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**C O N T E N T S**

<b><u>WITNESSES</u></b>	<b><u>DIRECT</u></b>	<b><u>CROSS</u></b>	<b><u>REDIRECT</u></b>	<b><u>RE CROSS</u></b>
Joseph R. Schadt				
By Mr. Russell	1539	--	--	--
By Mr. Kleppinger	--	1546	--	--
By Mr. Stewart	--	1559	--	--
By Mr. Zalcman	--	1562	--	--
By Mr. Caplan	--	1563	--	--
By Mr. Epstein	--	1574	--	--
By Ms. Moury	--	1581	--	--
By Mr. Burgraff	--	1583	--	--
By Mr. Simms	--	1587	--	--
Richard S. Shapiro				
By Mr. Kohler	1596	--	1641	--
By Mr. Kaplan	1597	--	--	--
By Mr. Rubin	--	1611	--	--
Stephen J. Baron				
By Mr. Kleppinger	1654	--	1672	--
By Mr. Nordstrom	--	1656	--	--
By Mr. Russell	--	1659	--	--
Jonathan S. Falk				
By Mr. Kaplan	1675	--	1700	--
By Mr. Kleppinger	--	1692	--	1702
Randall J. Falkenberg				
By Mr. Kleppinger	1716	--	1755	--
By Mr. Nordstrom	--	1720	--	--
By Mr. Kaplan	--	1731	--	1756

**E X H I B I T S**

<b><u>NUMBER</u></b>	<b><u>FOR IDENTIFICATION</u></b>	<b><u>IN EVIDENCE</u></b>
<b><u>Pennsylvania Power &amp; Light Statements</u></b>		
No. 8 (J.R. Schadt)	1539	1594
No. 8-R (J.R. Schadt)	1539	1594
No. 20-R (Falk)	1675	--

**EXHIBITS** (Continued)

<u>NUMBER</u>	<u>FOR IDENTIFICATION</u>	<u>IN EVIDENCE</u>
<b><u>Pennsylvania Power &amp; Light Exhibits</u></b>		
No. JRS-1 (J.R. Schadt)	1539	1594
No. JRS-1A (J.R. Schadt)	1539	1594
Nos. JRS-2 through 8 (J.R. Schadt)	1539	1594
JSF-1 (Falk)	1675	--
JSF-2 (Falk)	1680	--
JSF-3 (Falk)	1700	--
<b><u>PP&amp;L Cross Examination Exhibits</u></b>		
No. 7 (PP&L-Enron-39)	--	1598
<b><u>Enron Statements</u></b>		
No. 1.0 (Shapiro)	1596	1653
<b><u>IBEW Cross Examination Exhibits</u></b>		
No. 2 (R.S. Shapiro)	1612	1652
<b><u>PPLICA Statements</u></b>		
No. 1 (Baron)	1654	1673
No. 1R (Baron)	1654	1673
No. 1-S (Baron)	1654	1673
No. 2 (Falkenberg)	1715	1758
No. 2-S (Falkenberg)	1716	1758
No. 2-S Updated (Falkenberg)	1716	1758

25

E X H I B I T S (Continued)PPLICA Exhibits

1			
2			
3	↘	SJB-1 through 13 (Baron)	1654                      1673
4	↘	RJF-1 through 8 (Falkenberg)	1715                      1758
5	✓	RJF-9 through 16 (Falkenberg)	1716                      1758
6	↘	RJF-9 Revised (Falkenberg)	1716                      1758
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P R O C E E D I N G S

1  
2 ADMINISTRATIVE LAW JUDGE GEORGE M. KASHI: I'll call  
3 this proceeding back to order.

4 Does anybody want to report on last night's  
5 settlement discussions?

6 (No response.)

7 JUDGE KASHI: Then nobody wants to talk; okay. That  
8 being the case, let's call our first witness for this  
9 morning.

10 PP&L?

11 MR. RUSSELL: Thank you, Your Honor. PP&L calls  
12 Joseph R. Schadt.

13 JUDGE KASHI: Please raise your right hand and be  
14 sworn, sir.

15 **Whereupon,**

16 **JOSEPH R. SCHADT**

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

18 MR. RUSSELL: Your Honor, under our agreed-upon  
19 procedures I will simply identify Mr. Schadt's testimony and  
20 exhibits. PP&L Statement No. 8 is the direct testimony of  
21 Joseph R. Schadt, and accompanying that is Exhibit JRS-1.

22 PP&L Statement No. 8-R is the surrebuttal testimony  
23 of Joseph R. Schadt. Accompanying that are Exhibits JRS-1A  
24 and JRS-2 through 8.

25 JUDGE KASHI: So marked for purposes of

1 identification.

2 (Whereupon, the documents were marked as  
3 PP&L Statement No. 8, including Exhibit  
4 JRS-1, and PP&L Statement No. 8-R,  
5 including Exhibit Nos. JRS-1A and JRS-2  
6 through 8 for identification.)

7 DIRECT EXAMINATION

8 BY MR. RUSSELL:

9 Q. Mr. Schadt, do you have any corrections to your  
10 testimony or exhibits?

11 A. No, I do not.

12 MR. RUSSELL: Your Honor, with the foundation laid by  
13 agreement, PP&L moves into the record Statement No. 8,  
14 Statement No. 8-R, Exhibit JRS-1, Exhibit JRS-1A, and  
15 Exhibits JRS-2 through 8.

16 JUDGE KASHI: Subject to any timely motions and/or  
17 objections made, pending cross examination, that which has  
18 been marked and identified will be received into the  
19 evidentiary record.

20 MR. RUSSELL: Thank you.

21 Your Honor, we have some short oral rejoinder from  
22 Mr. Schadt.

23 JUDGE KASHI: I like the word "short."

24 (Laughter.)

25

1 BY MR. RUSSELL:

2 Q. Mr. Schadt, the surrebuttal testimonies of  
3 Mr. LaCapra and Mr. Kollen continue to discuss the merits of  
4 their asset value method versus PP&L's regulatory method for  
5 calculating stranded costs. Do you have any further  
6 comments on this issue?

7 A. Yes. I want to emphasize that, correctly  
8 applied, both methods produce the same result. Both methods  
9 must project generating plant revenues, operating costs, and  
10 capital expenditures over the remaining life of the  
11 generating plants. The only significant difference in the  
12 two methods is in their treatment of income taxes.

13 While either method can be used, I believe the PP&L  
14 regulatory method is better because it provides consistent  
15 treatment of generating plant and regulatory assets.

16 Under the OCA/PPLICA approach, generating plant is  
17 analyzed on an asset value basis, while regulatory assets  
18 are analyzed on a regulatory basis.

19 This use of two different methods can produce  
20 erroneous results unless proper adjustments are made. No  
21 such adjustments are required under the PP&L method, which  
22 uses a consistent approach throughout.

23 Q. You indicated that the only significant  
24 difference in the two methods is their treatment of income  
25 taxes. Do the OCA and PPLICA methods provide for the proper

1 treatment of income taxes?

2 A. No, they do not. There are at least two  
3 components to the proper calculation of income taxes, being  
4 current income taxes and taxes recoverable.

5 The key is to calculate each of these items over a  
6 consistent time period. PP&L does this by calculating each  
7 of these tax items over the remaining life of relevant  
8 generating assets, roughly 30 years.

9 OCA and PPLICA, on the other hand, calculate current  
10 income taxes related to return on plant assets over seven  
11 years, and calculate taxes recoverable over 30 years.

12 This is fundamentally inconsistent, and results in a  
13 significant understatement of stranded costs.

14 Q. Have the OCA and PPLICA correctly applied their  
15 asset value methods?

16 A. No, they have not. The goal of both methods  
17 should be to permit the utility to recover the book value of  
18 its investment in generation.

19 PP&L's method recovers that book value over the  
20 remaining life of the plants. The OCA/PPLICA method  
21 determines the price a willing buyer would pay for PP&L's  
22 generating plant today, and permits the recovery of the  
23 difference between that price and the net book value as a  
24 stranded cost.

25 Unfortunately, neither the OCA nor PPLICA's

1 application of the asset value method produces that goal.  
2 For example, Mr. Falkenberg's Surrebuttal Exhibit RJF-9A  
3 calculates a market value of PP&L's generating plant of \$2.6  
4 billion, adding \$200 million for inventory, and a  
5 recommended stranded cost recovery of another \$250 million.  
6 PPLICICA would allow PP&L a total recovery of approximately  
7 \$3.1 billion.

8           However, the book value of PP&L's plant is \$4.3  
9 billion, leaving PP&L about \$1.1 billion short of full  
10 recovery of book value. A similar result occurs under the  
11 OCA's proposal.

12           Q. Why does this shortfall occur?

13           A. Well, it occurs primarily because of their  
14 mishandling of deferred taxes. If the company were to sell  
15 its generating assets on January 1, 1999, for the market  
16 value estimated by either the OCA or PPLICICA, the associated  
17 deferred taxes would immediately reverse and become payable  
18 in 1999.

19           However, the OCA/PPLICICA method ignores this fact and  
20 treats deferred taxes as if they will not reverse upon the  
21 sale of related assets. As a result, they have  
22 significantly understate the company's actual stranded  
23 costs.

24           Q. Mr. LaCapra finds it hard to believe that the  
25 PP&L stranded generation cost claim exceeds the net book

1 value of PP&L's generating plant. Is Mr. LaCapra correct?

2 A. Absolutely not. Net book value is the cost of an  
3 asset minus its accumulated depreciation. The net book  
4 value of PP&L's generating plant, and associated materials  
5 and supplies, at January 1, 1999, is \$4.28 billion, not the  
6 \$3.25 billion cited by Mr. LaCapra.

7 PP&L's claim for generating plant stranded cost does  
8 not exceed its net book value. Mr. LaCapra is wrong.

9 Q. On surrebuttal, the OCA has revised its market  
10 price forecast, stranded cost calculation, and CTC  
11 collection proposals. Mr. LaCapra presents a revision to  
12 your financial calculation to reflect these changes on his  
13 Exhibit RLC-9. Do you have any comments on that exhibit?

14 A. Yes. This exhibit is misleading. Mr. LaCapra  
15 concludes from this exhibit that the financial effect of the  
16 OCA's proposal is similar to PP&L's proposal. This is  
17 simply not true.

18 Mr. LaCapra compares PP&L's proposal with the OCA's  
19 proposal under two different future scenarios. The PP&L  
20 column assumes PP&L's market price turns out to be right,  
21 but the OCA column assumes the OCA's market price turns out  
22 to the right. Obviously both future results cannot be true  
23 at the same time.

24 Mr. LaCapra has presented an apples to oranges  
25 comparison, which provides no meaningful basis for

1 comparison.

2 To demonstrate this, I recalculated the return on  
3 common equity under four scenarios for the company's  
4 generation function.

5 Under scenario one, the PUC adopts PP&L's proposal,  
6 and PP&L's market price is right. In that scenario the 1999  
7 return on common equity is 4.3 percent.

8 Under scenario two, the PUC adopts PP&L's proposal,  
9 but the OCA's market price turns out to be correct. And  
10 under that proposal, the results are somewhat better, but  
11 still not strong. The return on common equity is 7.1  
12 percent.

13 Under scenario three, the PUC adopts the OCA  
14 proposal, and the OCA market price turns out to be correct.  
15 In that scenario, the return on common equity is a negative,  
16 .3 percent.

17 Finally, under scenario four, the OCA proposal is  
18 adopted, and PP&L's market price turns out to be correct.  
19 The return on common equity drops to a negative 5.2 percent.

20 I should note that the results for 1999 are generally  
21 indicative of all years of the transition period. These  
22 results show that the company would be much worse off under  
23 the OCA's proposal.

24 The return on common equity is negative under both  
25 OCA scenarios. And even under the best case, if the PUC

1 adopts the PP&L case, and the OCA turns out to be right on  
2 the market clearing price, the return on common equity is  
3 only about seven percent, due to the rate cap.

4 Q. In his surrebuttal testimony, Mr. Kollen seeks to  
5 refute your presentation of a simple example to show that  
6 the PP&L regulatory method accurately calculates stranded  
7 costs. Do you have any response?

8 A. Yes. The only point of my example was to show  
9 that the PP&L regulatory method yields full recovery of a  
10 hypothetical \$150 investment in plant.

11 Mr. Kollen's counter example fails to produce this  
12 result. In fact, it only allows recovery of \$111.34. This  
13 is plainly shown on Exhibit LK-3.

14 And the place it's shown on that exhibit, Mr. Kollen  
15 has a beginning year investment which he identifies as  
16 \$111.34. And that's what his model goes through and  
17 calculates the return based on. But the original plant  
18 investment was \$150.

19 Thus, all Mr. Kollen has proven is that his method  
20 will deny the full recovery of plant investment.

21 Q. And finally, Mr. Kollen asserts in his rebuttal  
22 testimony that you actually failed to make the correction  
23 referenced in your rebuttal testimony for DOE assessment.  
24 Is this correct?

25 A. No. I specifically removed the DOE assessment

1 from the generation-related stranded cost, and left it in as  
2 a regulatory asset. The double counting error was clearly  
3 corrected. Mr. Kollen is simply wrong.

4 MR. RUSSELL: With that, Your Honor, Mr. Schadt is  
5 available for cross examination.

6 JUDGE KASHI: Thank you, sir.

7 Mr. Kleppinger?

8 MR. KLEPPINGER: Thank you, Your Honor.

9 **CROSS EXAMINATION**

10 BY MR. KLEPPINGER:

11 Q. Good morning, Mr. Schadt.

12 A. Good morning.

13 Q. My name is David Kleppinger, representing PP&L  
14 Industrial Customer Alliance.

15 In your rejoinder you made reference to  
16 Mr. Falkenberg's Exhibit RJF-9. Do you have that exhibit  
17 before you?

18 A. Yes, I do.

19 Q. And this is an exhibit to his surrebuttal  
20 testimony labeled RJF-9A; correct?

21 A. Correct.

22 Q. Do you dispute the production net plant of \$3.6  
23 billion as computed on this exhibit?

24 A. We have in our filing a slightly different  
25 production net plant. I believe what Mr. Falkenberg did was

1 convert it to what he believes is a PUC jurisdictional  
2 amount.

3 Q. You agree that the differences in our cases on  
4 the production net plant are relatively insignificant?

5 A. Yes, I do.

6 Q. Now, with respect to your comment on rejoinder  
7 that -- and I'll try to paraphrase it; this is a little  
8 difficult when we're going to move this quickly -- but I  
9 believe you indicated that there's a shortfall under RJF  
10 Exhibit 9 due to the treatment of deferred taxes. And you  
11 comment that if PP&L were to sell its generating assets on  
12 January 1, 1999, the deferred taxes would reverse and be  
13 payable at that point in time. Is that a fair  
14 characterization of what you said?

15 A. That's fair.

16 Q. Does PP&L have any plans to sell its generating  
17 assets on January 1, 1999?

18 A. To my knowledge, no, it does not.

19 Q. Next you discussed Mr. Kollen's Exhibit LK-3.  
20 And for this issue I'd like you to refer to page 13 of your  
21 rebuttal testimony.

22 A. Okay.

23 Q. In this example, did you assume that the company  
24 would pay income taxes on its stranded investment recovery?

25 A. Certainly.

1 Q. So, you would be treating revenues received under  
2 the CTC as income as opposed to a return of capital; is that  
3 correct?

4 A. Yes. However, it's important to note that for  
5 tax policy, CTC revenue is revenue. The IRS does not  
6 distinguish between the receipt of revenue as revenue, or  
7 whether it's return of capital. Those concepts are purely  
8 for book accounting purposes and have no impact on the  
9 calculation of income taxes.

10 Q. Well, isn't the issue for the IRS whether CTC  
11 revenue will be income, as a taxable income, as opposed to a  
12 revenue stream which is a return of capital?

13 A. No, that is not the issue for the IRS. For  
14 income tax policy, the way they do it is each fixed asset  
15 has a tax life. And that tax life will not be changed based  
16 upon the Commission's determination of CTC recovery. We  
17 have a fixed amount of tax appreciation that is not  
18 susceptible to change based on whether the Commission  
19 determines this revenue is a return of capital or CTC  
20 revenue or something else. It is purely revenue from a tax  
21 basis perspective.

22 Q. Can you tell me whether the IRS has ever  
23 confronted the issue of a competitive transition charge and  
24 treatment of the revenue under such a charge?

25 A. I'm sure they have, in other deregulation moves,

1 the telephone industry, the gas industry.

2 Q. Well, in the electric industry?

3 A. I don't believe the electric industry has made  
4 that step yet, no.

5 Q. Okay. Now, under the treatment that you would  
6 suggest for income related to the CTC, I take it then that  
7 under the approach of PP&L you would not be reducing the  
8 book value for the amount of recovery this Commission awards  
9 in stranded cost?

10 A. Would you mind repeating that question?

11 Q. It's probably more convoluted than it needs to  
12 be, I apologize.

13 Under PP&L's approach, would I be correct that the  
14 company, on its books, would not be reducing its book value  
15 of its generating plant by the amount that the Commission  
16 permits to be recovered through the CTC?

17 A. Okay. Well, it's very important to look at the  
18 components of the CTC when answering that question. And the  
19 accounting rules are not the same for each of the  
20 components.

21 For the regulatory asset portion and the NUG portion  
22 of CTC recovery, accounting rules are very clear that the  
23 company must amortize all of those assets as we're  
24 recovering CTC revenue. So those points are very clear.

25 In answer to your question, are the generation plant

1 assets; I'm not certain of the answer to that question at  
2 this time, and much is going to depend on the Commission's  
3 order, what they adopt as the final market clearing price to  
4 be used in the calculation.

5 The accounting rules are a bit different on the  
6 treatment of generation plant and whether you can accelerate  
7 the depreciation.

8 The company, I believe, would look at that and may  
9 ask the Commission for permission to accelerate depreciation  
10 and match a certain amount of CTC recovery. But I do not  
11 believe the company has made a final decision on that.

12 Q. And if the company hasn't made that final  
13 decision, I take it that the company's auditors have not  
14 made a determination as to whether or not it could issue an  
15 unqualified or a qualified accounting opinion on the  
16 company's treatment of book value after the Commission  
17 determines stranded cost; is that correct?

18 A. Well, the company would intend to prepare its  
19 external financial statements in accordance with generally  
20 accepted accounting principles, whatever result's actually  
21 determined. And so I'm fairly confident that when the  
22 company comes to that conclusion, our auditors will be  
23 comfortable with it and will issue an unqualified opinion.

24 Q. If the company pursues the avenue of reducing its  
25 book value by the amount of stranded recovery that the

1 Commission allows, would I be correct then that the  
2 depreciation line on your table at page 13 would be less  
3 than what you've reflected here?

4 A. No, you would not be correct.

5 Q. So, while your book value would go down due to  
6 the adjustment for stranded recovery, your depreciation  
7 would stay the same as if the book value had not been  
8 reduced?

9 A. Well, see, the way I believe it would happen in  
10 the scenario you're describing is that you're recovering --  
11 you're taking our \$150 of book plant and you're breaking it  
12 into two pieces, what you're calling stranded and non-  
13 stranded. And you're concluding that the stranded piece  
14 would be amortized over a shorter period, specifically the  
15 CTC recovery period. The unstranded piece would be  
16 amortized over the remaining book life of the asset.

17 So depreciation, the total depreciation for this  
18 plant asset would be \$150. Now, it's very possible in the  
19 scenario you described, more of the depreciation would occur  
20 during the seven-year transition period to match the actual  
21 revenue receipts of the company.

22 It would still be depreciation; you wouldn't just go  
23 in and write off this amount of plant, and then get CTC  
24 recovery over seven years. That would be a mismatch of  
25 expense and revenues. You would try and expense that

1 stranded plant over the same period you're recovering CTC  
2 revenues, presumably the seven-year transition period.

3 Q. And under that approach you would be taking  
4 depreciation on the expense portion of the plant that's  
5 being recovered under the CTC?

6 A. Yes. In essence, all you're doing is  
7 accelerating depreciation on the stranded piece. Instead of  
8 depreciating stranded plant over the book life of the asset,  
9 which in Susquehanna's case is 30 years, the remaining book  
10 life -- instead of depreciating the stranded plant over that  
11 30 years, you would depreciate it over the seven-year CTC  
12 recovery period. The unstranded piece you would continue to  
13 amortize or depreciate over the 30-year book life period.

14 Q. Mr. Schadt, are you generally familiar with the  
15 securitization provisions of the act that brought us here  
16 today?

17 A. Yes, I'm generally familiar with that.

18 Q. And if PP&L would proceed to securitize a portion  
19 of its stranded cost, then the collection of that stranded  
20 cost would be in the form of an ITC, or an intangible  
21 transition charge; is that correct?

22 A. That's correct.

23 Q. If the company would pursue securitization, would  
24 that change your treatment of depreciation in any way?

25 A. The accounting rules applicable to the

1 securitization are not as well set in stone as existing  
2 accounting rules, particularly because the electric utility  
3 industry, to my knowledge, has never to date implemented an  
4 actual securitization plan, with the exception of a very  
5 small thing that happened out west on a demand side  
6 management securitization.

7 But as far as recovering genuine stranded costs, I  
8 don't believe the accounting industry has actually addressed  
9 that question yet. When they do, though, I believe what  
10 will happen is that the stranded plant would be amortized  
11 over the same period that the ITC is collected. So that you  
12 would continue to have a good match of revenues and  
13 expenses.

14 Q. And would there be, under the securitization  
15 approach, a write-down of the book value of the asset?

16 A. Again, I am not certain of the answer to that, as  
17 these rules have not been tested yet by the financial  
18 community. And I'm unsure if that would take place  
19 immediately, but I believe it would happen over the period  
20 of securitization or the ITC amortization period.

21 Q. And without securitization, would the company be  
22 writing down the book value of the asset?

23 A. The answer to that question is guided by  
24 Statement of Financial Accounting Standards 121, the  
25 impairment of long-lived assets. And to properly answer

1 that question, you will need to know the final market  
2 clearing price that the Commission adopts, all of the other  
3 assumptions that are built into our stranded cost model,  
4 what the Commission finally adopts for those assumptions.  
5 What we would have to do then is run those assumptions  
6 through a FAS-121 test and determine whether, in fact, the  
7 assets are impaired. If they are impaired, FAS-121 requires  
8 a write-down; if they are not impaired, it precludes a  
9 write-down.

10 Q. And will this Commission have an opportunity to  
11 review the analysis that's undertaken as to whether or not  
12 there is, quote, "impairment," close quote, under FAS-121,  
13 to your knowledge?

14 A. To my knowledge they would.

15 Q. There is a proceeding in place post final order  
16 in this case for that, to your knowledge?

17 A. I am not aware of that. I know that the company  
18 has the opportunity to audit the books of the company every  
19 year, and does so. I would assume at least at that point  
20 that they could audit the FAS-121 calculation. I am unsure  
21 of the proceedings which will follow up these hearings.

22 Q. And other than the Commission's determination of  
23 market price, what other factors would be involved in  
24 conducting this impairment test?

25 A. Primarily, the impairment test is based on a few

1 factors. The book value of plant; that has already been  
2 defined, and that won't be subject to change. The market  
3 clearing price is the most important issue. The other  
4 important issues are the spending assumptions, what O&M will  
5 be, what capital expenditures will be. Those are the key  
6 inputs.

7 In addition, a key input is the discount rate. If  
8 you determine that the plant is impaired, then you must  
9 define a discount rate to use.

10 Q. And is that typically a before-tax or an after-  
11 tax discount rate?

12 A. I would have to go back and restudy the  
13 provisions of FAS-121 to be sure of the correct answer to  
14 that question.

15 Q. Now, in terms of your calculation of the  
16 company's future year revenue requirements under the  
17 regulatory method, you calculate those revenues on a before-  
18 tax basis; do you not?

19 A. That's correct.

20 Q. And you also calculate the company's future year  
21 projected market value on a before-tax basis; is that  
22 correct?

23 A. Would you repeat that part of the question,  
24 please?

25 Q. When you calculate the net present value of

1 PP&L's future year's projected market value, and then deduct  
2 that from the future year revenue requirement calculation,  
3 do you use a before-tax calculation in doing the market  
4 value projection?

5 A. I would state it slightly different than the way  
6 you did. What PP&L did was we calculated future year's  
7 revenues for the company's generation function, and we  
8 calculated the company's future year's revenue requirements  
9 for the generation function, and we discounted both of those  
10 streams using an after-tax discount rate.

11 Q. You discounted using an after-tax discount rate;  
12 but in terms of generating the revenue requirement for the  
13 company, those revenue requirements are stated on a before-  
14 tax basis?

15 A. That's correct. We grossed up the equity return  
16 for income taxes.

17 Q. And when you projected future year revenue  
18 requirements, was there any assumption you had to make on  
19 future income taxes?

20 A. Certainly.

21 Q. And did you assume those tax rates remained  
22 constant --

23 A. Yes, we did.

24 Q. -- or changed? At page 9 of your rebuttal  
25 testimony, you make the statement that the impact of

1 discounting exactly offsets the impact of calculating a  
2 return in investment, because the company used its cost of  
3 capital rate as the discount rate. And when you use  
4 discount rate there, I take it you're referring to an after-  
5 tax discount rate?

6 A. Yes, I am.

7 Q. Because that's what you used to discount?

8 A. Correct.

9 Q. And you reached that conclusion even though the  
10 revenues that were stated on the projection are calculated  
11 on a before-tax basis?

12 A. Yes. The very first line of the next paragraph,  
13 line 19, states that the only exception to that rule is the  
14 calculation and payment of income taxes.

15 Q. Now, your discussion of the financial results  
16 under the OCA and the PPLICCA positions, there were a couple  
17 of questions, I believe, Mr. Hill deferred to you.

18 A. Okay.

19 Q. And you may have answered that in your rejoinder,  
20 but I'm not sure. When you conducted the analysis that led  
21 to your conclusions on the financial impairment to the  
22 company, roughly at pages 27 to 29 of your testimony, did  
23 you assume for the company's revenue generation the  
24 company's market prices, or were you assuming the OCA's  
25 and/or PPLICCA's market prices?

FORM 2

1 A. Well, in the analysis I presented in my rejoinder  
2 we considered all of those scenarios. So in two scenarios  
3 we considered that the OCA's market price would be correct,  
4 which I believe was not too far off from PPLICA's, and in  
5 the other two scenarios we assumed that PP&L's market price  
6 would be correct.

7 Q. And in the rebuttal testimony it was PP&L's  
8 market prices; is that correct?

9 A. Well, but the trick there is, the rebuttal  
10 testimony was addressing the year 1999, one point in time.  
11 And in that year none of the three market prices were  
12 significantly different.

13 Q. Yes, I'm not looking for the trick, I'm just  
14 trying to figure out what you did in your rebuttal  
15 testimony, and which market price you actually used when you  
16 did the calculations that are shown on pages, I believe, 27.

17 A. Okay. Well, on page 25 -- okay, in answer to  
18 your question then; on page 23, when I went from -- okay,  
19 page 23, I went to a 1999 proforma income statement. So, on  
20 page 25, the first column is the 1999 proforma under PP&L's  
21 assumptions, and that would have assumed PP&L's market  
22 price.

23 Under the OCA column, the OCA adjustment there is a  
24 32 percent base rate reduction proposed in the rebuttal, in  
25 the original direct testimony by the OCA. So, when I got to

1 the OCA column, that's the OCA's market price.

2 So in the PP&L column I used the PP&L market price,  
3 in the OCA column I used the OCA market price.

4 Q. Okay. That's what I wanted to know.

5 MR. KLEPPINGER: Just a moment, Your Honor, I may be  
6 completed.

7 (Pause.)

8 MR. KLEPPINGER: Thank you, Mr. Schadt, that's all I  
9 have.

10 THE WITNESS: You're welcome.

11 JUDGE KASHI: Mr. Stewart?

12 MR. STEWART: Thank you, Your Honor.

13 **CROSS EXAMINATION**

14 BY MR. STEWART:

15 Q. Good morning, Mr. Schadt, my name is  
16 Todd Stewart, and I represent the Mid-Atlantic Power Supply  
17 Association.

18 I believe in your direct testimony, starting at page  
19 2, you state that you're applying the statutory requirements  
20 to the computation of stranded costs; is that correct?

21 A. Yes, it is.

22 Q. And in consideration of the statute when you did  
23 all these computations, is it your general understanding  
24 that the statute prohibited modification of the CTC once it  
25 had been established in this proceeding?

1           A. I know there are certain exception rules in the  
2 Customer Choice Act that did allow changes to the CTC, I  
3 believe, under very specific circumstances such as dramatic  
4 changes in tax rates and certain other provisions. So there  
5 were some exceptions to that.

6           Q. But was it your understanding that the statute  
7 prohibited modification --

8           MR. RUSSELL: Your Honor, I would object to  
9 continuing this line of questioning, for two reasons. It  
10 calls for a legal conclusion by Mr. Schadt, and it's outside  
11 the scope of his testimony. The design of the CTC itself  
12 was really with Mr. Kleha and Dr. Tierney and Mr. Krall.

13           JUDGE KASHI: Mr. Stewart?

14           MR. STEWART: Your Honor, the witness has testified  
15 in his direct testimony that he applied the statutory  
16 framework in several of these calculations, so he's already  
17 expressed his familiarity with the statute. And Mr. Kleha  
18 did defer this line of questioning to this witness, so I'm  
19 just trying to -- this is the last question. If he can  
20 answer this question --

21           JUDGE KASHI: The objection is overruled. Answer the  
22 question, sir.

23           BY MR. STEWART:

24           Q. Was it your understanding that the statute  
25 prohibited modification of the CTC? You said that the

1 statute allows -- there are certain instances where it  
2 allows for modification, but it was in certain extreme  
3 circumstances. But was it your understanding that the  
4 statute generally prohibited a modification of the CTC once  
5 it's established in this proceeding?

6 A. I believe if you exclude the unusual  
7 circumstances, my understanding was that the act did  
8 preclude changes to the CTC, other than in those unusual  
9 circumstances.

10 Q. Thank you. One last question. And maybe you can  
11 answer this if you can. But do you believe that from the  
12 perspective of a PP&L shareholder it would be in their best  
13 interests to get the largest amount of PP&L's generation  
14 assets, to recover that from the CTC or recover that from  
15 the market?

16 A. I believe that the company should be able to  
17 recover the book value of the plant assets either through  
18 the CTC or the market. As long as the company is able to  
19 recover that book value, I don't think the company cares  
20 whether it's through the market or through the CTC.

21 Q. Thank you.

22 MR. STEWART: That's all I have.

23 JUDGE KASHI: Thank you very much, sir.

24 Mr. Zalcman?

25 MR. ZALCMAN: Thank you, Your Honor.

## CROSS EXAMINATION

1  
2 BY MR. ZALCMAN:

3 Q. Mr. Schadt, my name is Fred Zalczman, I represent  
4 the Environmentalists in this case. And I have one limited  
5 line of cross examination intended to clarify how you derive  
6 the Pennsylvania jurisdictional percentage for purposes of  
7 calculating stranded costs.

8 Now, you indicate in Exhibit JRS-1 a derived  
9 jurisdictional split from Mr. Kleha; correct?

10 A. Mr. Kleha gave me the jurisdictional percentages.  
11 I did not derive those, Mr. Kleha did.

12 Q. So do you recall whether Mr. Kleha provided you  
13 with the entire horizon plan, horizon for jurisdictional  
14 splits, or did he give you simply the cost allocation study  
15 for the twelve-month period ending September 30th --

16 A. Yes, I do recall.

17 Q. -- of 1995?

18 A. What Mr. Kleha gave me was he gave me the  
19 jurisdictional allocators, which he suggested that I use for  
20 each category of stranded costs throughout each year of my  
21 stranded cost exhibit. He gave the jurisdictional  
22 percentages.

23 Q. So you have no idea how those were derived?

24 A. I have some idea.

25 Q. Can you elaborate on that?

1           A. Yes. To my understanding, what the  
2 jurisdictional allocators take into account is the unwinding  
3 of the company's bulk power contracts that were made several  
4 years ago with Jersey Central Power & Light, Atlantic City  
5 Electric, and Baltimore Gas & Electric. And additionally,  
6 it set aside a certain percentage of the company's  
7 generation, about four percent, for our municipal customers.

8           Q. Now, do you know whether the Commission has  
9 approved that methodology?

10           MR. RUSSELL: Your Honor, I object. Again, two  
11 reasons. It requires a legal conclusions; and it's really a  
12 subject area that's properly addressed by Mr. Kleha.

13           JUDGE KASHI: Sustained.

14           MR. ZALCMAN: Thank you. I won't pursue it any  
15 further.

16           Thank you, Your Honor. I have no further questions.

17           JUDGE KASHI: Mr. Caplan?

18           MR. CAPLAN: Thank you, Your Honor.

19                           **CROSS EXAMINATION**

20           BY MR. CAPLAN:

21           Q. Good morning, my name is Richard Caplan, and I  
22 represent a number of non-utility generators, the bulk of  
23 whom, if not all of them, have long-term power supply  
24 contracts with PP&L.

25           Did you have any involvement in the determination to

1 use for purposes of estimating the stranded costs associated  
2 with these non-utility generator contracts the assumption  
3 that output of these plants would continue to the end of the  
4 end of the contract term at the rates empirically determined  
5 for the period 1994 through 1996?

6 A. I did not have involvement in making that  
7 assumption. I reviewed it.

8 Q. I assume you reviewed it for reasonableness?

9 A. Yes.

10 Q. All right. Tell us how you did that. What was  
11 the test or tests that you used to determine that that was a  
12 reasonable assumption?

13 A. Well, the few things I did -- and I believe this  
14 is all included in my direct testimony -- was that we took a  
15 look and we saw that the capacity factors that are assumed,  
16 they were derived from the '94 through '96 average  
17 generation of the NUG plants. So that seemed to me to give  
18 the first test of reasonableness, that if we're assuming  
19 what's happened in the last three years, that didn't seem  
20 too unreasonable to me.

21 There were a few exceptions to that. There was a NUG  
22 that I believe had not come on line yet, and we assumed an  
23 80-percent capacity factor, since we didn't have anything  
24 else to assume.

25 There was another plant that I believe had some

1 operating problems early on, and then they got those  
2 resolved. And I believe we assumed their '96 average,  
3 because that got back onto what we considered a reasonable  
4 track.

5 Q. So, would it be fair to say that in that case,  
6 just for that one plant, you chose a year, rather than a  
7 three-year average, you chose one year, because you felt  
8 that that higher productivity was going to be more  
9 reflective of the performance of that plant over its entire  
10 contract life?

11 A. What we assumed was that those first two years  
12 were exceptions and that they were not normal operations.

13 Q. In other words, they were an aberration?

14 A. Correct.

15 Q. All right. Now, what was the capacity factor  
16 that was used by PP&L for determining the output of its own  
17 must-run plant?

18 A. I know for Susquehanna we used a 78-percent  
19 capacity factor. That too was based on the historic  
20 average. I am unsure of the capacity factors for our coal  
21 fire generation plants.

22 Q. Well, they weren't 90, were they?

23 A. I am unsure of that. The determination, the  
24 capacity factor, that would have been driven by demand, it  
25 would have followed through EGEAS, and Dr. Jones would be

1 able to answer that question far better than I could.

2 Q. All right. Now, are you familiar with the fact  
3 that a fair number of the non-utility generator plants with  
4 long-term contracts burn waste fuels?

5 A. Yes.

6 Q. And are you familiar with the fact that they use,  
7 in many cases, a technology with which PP&L is not  
8 intimately familiar; in other words, fluidized bed  
9 combustion?

10 A. I'm uncertain of what fuel pipes our engineering  
11 departments are real familiar with. That's not my area.

12 Q. Well, in order to determine over the useful life  
13 of these contracts -- which I gather have a general term of  
14 around 20 years; is that correct?

15 A. I believe that's generally correct.

16 Q. Would it be necessary to look at the O & M  
17 requirements of these plants over time in light of the fact  
18 that they use a technology which is not presently employed  
19 by PP&L in its own generation?

20 A. I suppose I assume that since the NUG signed a  
21 20-year contract that they anticipated fulfilling that 20-  
22 year contract. So I didn't find it necessary to go through  
23 a detailed analysis of each NUG's operating costs to  
24 determine whether it would be profitable to do that, to live  
25 up to their 20-year contract.

1 Q. Well, the contracts don't require them to  
2 maintain generating levels of 90 percent capacity; do they?

3 A. The contracts require PP&L to purchase their  
4 output.

5 Q. And that output could be 50 percent capacity;  
6 correct?

7 A. Well, while it could be, it would not appear to  
8 be in the NUG's interest for it to be a very low output,  
9 because they're going to get paid a far less amount of money  
10 than if it was at an 80- or 90-percent output.

11 Q. That's not my question. My question is: Isn't  
12 it correct, sir, that the contracts do not impose a minimum  
13 performance obligation on these non-utility generators over  
14 the life of the contract?

15 A. I am not intimately familiar with the contracts.  
16 But to my knowledge, that seems reasonable.

17 Q. All right. Would it be fair to say that PP&L  
18 made no assessment whatsoever that the likelihood that these  
19 plants would be able to maintain a 90-percent availability  
20 over the full term of their contracts without substantial  
21 capital infusion, that that evaluation was never done?

22 MR. RUSSELL: I object, Your Honor. That's not a  
23 question for Mr. Schadt. The capacity factors of the NUGs  
24 were developed by Mr. Krall. Mr. Schadt merely took that  
25 data, made a reasonableness test, not an in-depth analysis,

1 and then applied them in his stranded cost analysis.

2 MR. CAPLAN: Your Honor, if he knows what was done,  
3 if he as an accountant was asked to assess the  
4 reasonableness of the assumption underlying the financial  
5 position that he's espousing, it would seem to me reasonable  
6 to find out if he knows whether such a test was done.

7 JUDGE KASHI: No, I'm going to sustain the objection.  
8 If you want to try it some other way, go ahead.

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1 Q. You've answered a question already on cross to  
2 the effect that except for the most exceptional  
3 circumstance, it is your understanding that the CTC, once  
4 set by the Commission, remains sacrosanct for the time of  
5 recovery; is that correct?

6 A. That's correct.

7 Q. Therefore, there would be an incentive, would  
8 there not, on PP&L to defer mitigation efforts, in other  
9 words, efforts to reduce the CTC, until after the CTC amount  
10 were set by the Commission; isn't that so?

11 A. No, I don't think so.

12 Q. Why, if, in fact, there is no true-up procedure,  
13 as you understand it, in the statute, would it not be in  
14 PP&L's shareholders' best interest and in its management's  
15 best interest to delay mitigation efforts until the product  
16 of those efforts represented a windfall income stream to the  
17 company?

18 MR. RUSSELL: Your Honor, again, this is not Mr.  
19 Schadt's area. Mr. Hill, a senior executive at PP&L,  
20 testified on the company's past and future mitigation  
21 efforts, and this line of policy question on mitigation  
22 really was more properly directed to Mr. Hill than to Mr.  
23 Schadt.

24 JUDGE KASHI: Sustained.  
25

1 BY MR. CAPLAN:

2 Q. Let me ask you then about an effort for which we  
3 have conflicting testimony in the record. You are aware  
4 that PP&L has undertaken a proceeding before the Federal  
5 Energy Regulatory Commission in an attempt to change the  
6 certification of a particular non-utility generator in order  
7 to reduce the level of payments that would be payable under  
8 the contract to that generator over the life of the  
9 contract; is that correct?

10 A. That's correct.

11 Q. And there was a conflict between the testimony  
12 of two of the witnesses as to whether, in terms of  
13 calculating stranded costs, PP&L has assumed that the  
14 outcome of that litigation was positive for PP&L and its  
15 ratepayers or, in fact, was not; in other words, to your  
16 knowledge, in your calculation, did you assume that there  
17 would be a reduction over the term of the contract in  
18 payments to that particular non-utility generator as a  
19 consequence of the expected outcome from the FERC  
20 proceeding?

21 A. No, we did not include a reduction reflecting a  
22 positive outcome of that FERC proceeding.

23 Q. And it's your understanding, and, in fact, there  
24 has been prior testimony, has there not, that the change in  
25 payments to this single non-utility generator would be in

1 the neighborhood of \$10 million per year?

2 A. I'm not aware of the number that it would  
3 generate, but I'm sure it would generate savings.

4 Q. And it's your understanding that if the  
5 Commission approves the CTC and then the Federal Energy  
6 Regulatory Commission were to rule in PP&L's favor in this  
7 matter, that the company would be able to essentially reduce  
8 the amount that it had to pay to that particular NUG by  
9 whatever the amount that the Federal Energy Regulatory  
10 Commission would find appropriate; is that correct?

11 A. Could you repeat your question?

12 Q. Let me rephrase the question. Isn't it correct,  
13 sir, that if you receive stranded cost recovery for the full  
14 amount of the anticipated payments to that non-utility  
15 generator to the term of the contract, which is 2009, in  
16 other words, approximately 12 more years of payments, and  
17 those, just hypothetically, were to be subsequently reduced  
18 by \$10 million a year, in other words, approximately \$120  
19 million of total savings, that PP&L would basically be in a  
20 position to pocket that money because it essentially had  
21 already recovered it through the CTC?

22 A. The company has filed a stranded cost plan of  
23 \$4.6 billion, of which 4.0 is collectible under the rate  
24 cap. I believe if such an occurrence was to happen where  
25 our payments to this non-utility generator were in fact

1 reduced by the FERC, I believe that would simply reduce that  
2 \$600 million that our shareholders are already expected to  
3 eat.

4 Q. And if PP&L were to take steps to mitigate  
5 stranded costs subsequent to the action by the Commission  
6 approving the CTC recovery level, and that would in fact  
7 reduce stranded costs by, let's say, a billion dollars, what  
8 would happen to the excess recovery then?

9 A. The company has already built a billion dollars  
10 of future mitigation into our \$4.6 billion CTC claim. I  
11 find it highly unlikely that the company would be able to  
12 find another billion dollars of supposed mitigation, so I  
13 find that a very unlikely scenario.

14 Q. Let me ask you then a hypothetical question. To  
15 your knowledge, if you assume that the company would recover  
16 in the deregulated market substantially more income than its  
17 projections for purposes of calculating the CTC suggests,  
18 and, therefore, the CTC amount turned out to be over-funded  
19 as far as PP&L is concerned, in other words, PP&L, if it  
20 kept the entire proceeds, would accomplish a windfall, does  
21 the company have any plans to turn that money back to the  
22 ratepayers?

23 A. My projections, as I stated in my rejoinder  
24 testimony, demonstrate that even under the most optimistic  
25 of scenarios whereby the company is able to charge our full

1 today's rates through 2005, our rate of return through that  
2 entire transition period is going to approximate 7 percent,  
3 so I believe if we were able to recover any additional NUG  
4 dollars or find additional mitigation dollars, I believe it  
5 would take a tremendous amount of those types of dollars to  
6 get back to a double digit return.

7 Q. Let me just ask you one line of questions about  
8 this amount of CTC recovery for the non-utility generator  
9 contracts. Is it your understanding that the Commission has  
10 the discretion to award less than the amount that you  
11 request for non-utility generator contracts?

12 MR. RUSSELL: Your Honor, that really does require a  
13 legal conclusion based on a reading of the Act.

14 MR. CAPLAN: Let me rephrase the question to avoid  
15 the legal conclusion.

16 BY MR. CAPLAN:

17 Q. To your knowledge, in determining the stranded  
18 costs associated with the non-utility generator contracts,  
19 did you consider the basis of the price paid to these non-  
20 utility generators, in other words, how those prices were  
21 determined?

22 A. What we considered was that it was the contract  
23 price, so, no, I did not take it any further than that.  
24 That is the price dictated by the contract.

25 Q. Do you know if PP&L was responsible for

1 determining what that price was in the first instance?

2 A. I was not instrumental in developing those  
3 contracts. I would have to defer on that issue.

4 Q. So you have no knowledge of how those prices  
5 came to be?

6 A. I have no good knowledge of that.

7 MR. CAPLAN: I have no further questions of the  
8 witness.

9 JUDGE KASHI: Thank you very much, Mr. Caplan.

10 Mr. Epstein.

11 MR. EPSTEIN: Thank you, Your Honor.

12 **CROSS-EXAMINATION**

13 BY MR. EPSTEIN:

14 Q. Mr. Schadt, I'm Eric Epstein. I'm representing  
15 myself. How are you doing this morning?

16 A. Good, sir.

17 Q. Mr. Schadt, are you aware that the company is  
18 considering switching to a new fuel source at the  
19 Susquehanna Electric Steam Station?

20 MR. RUSSELL: Your Honor, objection; it's far outside  
21 Mr. Schadt's testimony.

22 JUDGE KASHI: Sustained. He doesn't have anything to  
23 do with that, Mr. Epstein.

24 BY MR. EPSTEIN:

25 Q. But didn't you calculate some of your costs

FORM 2

1 based on what the fuel expense would be at the Susquehanna  
2 Electric Steam Station?

3 A. I discussed with our nuclear department, I asked  
4 them to give me a projection of what our nuclear fuel  
5 expense would be, by year, and I accepted their modeling of  
6 nuclear fuel expenses throughout the book life of  
7 Susquehanna. I do not know how they derived specifically  
8 what types of fuels they use.

9 Q. But you basically took at the word of your  
10 company's nuclear department their projections for the fuel  
11 source assuming that the plant would operate for 40 years?

12 A. I assumed that the plant would operate through  
13 its remaining book life, which I think is about 27 years.  
14 The only additional test was I compared their projection for  
15 the early years, just the past two years, of nuclear fuel  
16 expense just to make sure it was not out of line. Further  
17 than that, I did no analysis.

18 Q. So the company really doesn't have any  
19 provisions in the event that Berwick would change fuel  
20 sources?

21 MR. RUSSELL: Your Honor, objection. Number one,  
22 it's not a proper question for Mr. Schadt, and, number two,  
23 there's no foundation for the conclusion in the question.  
24 The company may well have those sorts of contingencies  
25 within the nuclear department. Mr. Schadt simply didn't

1 inquire.

2 JUDGE KASHI: Sustained.

3 BY MR. EPSTEIN:

4 Q. Are you aware that those contingencies exist?

5 A. I am unaware.

6 Q. So basically, when you made your calculations,  
7 you took the department at its word, without knowledge of  
8 what kind of fuel is going to be burned at Berwick for the  
9 next 27 years?

10 A. We have Susquehanna.

11 Q. I tried to make it easier.

12 A. Okay. Berwick. Okay. Yes; that's correct.

13 Q. So, in other words, then, you don't know if  
14 there are any economic advantages or disadvantages to  
15 switching fuel; it's not a matter that you examined?

16 A. That is correct.

17 Q. To your knowledge, do you know any nuclear power  
18 plants that have operated for 40 years?

19 MR. RUSSELL: Your Honor, again, outside Mr. Schadt's  
20 testimony.

21 JUDGE KASHI: I understand it's outside his  
22 testimony, but he has formed his basis of opinion on the  
23 fact that it's going to be operating for 40 years. He has  
24 to have decided that on some kind of basis.

25 You can answer the question. The objection is

1 overruled.

2 THE WITNESS: To my knowledge, I don't believe that  
3 nuclear plants -- I do not know that there was any major  
4 nuclear plant constructed and in operation 40 years ago, to  
5 my knowledge, but I believe it's worth noting that in those  
6 last several years of Susquehanna's life, that is when the  
7 market revenues dramatically exceed the plant sustenance  
8 cost, so by continuing the operation through those 40 years,  
9 it reduces the stranded cost calculation.

10 BY MR. EPSTEIN:

11 Q. I understand that. Let me approach it another  
12 way. You're assuming that the plant will operate for its  
13 used and useful lifetime, which is 40 years.

14 A. For its book life; that's correct.

15 Q. Are you aware that other nuclear power plants  
16 throughout the country have been retired before their book  
17 life?

18 A. Certainly.

19 Q. Is there a contingency funding plan in the event  
20 that Susquehanna Electric Steam Station does not operate for  
21 its 40-year book life, which I guess at this point is 27  
22 more years?

23 A. Mr. Epstein, you said a contingency funding  
24 plan. Do you mean for nuclear decommissioning?

25 Q. Yes.

1           A.    The company's request will put the nuclear  
2 decommissioning funding -- we've requested that that be  
3 applied as a CTC for the wires company, so that if, in fact,  
4 Susquehanna was going to be prematurely closed, I believe  
5 that would be accounted for within that wires charge and  
6 that the wires charge for decommissioning should be adjusted  
7 accordingly.

8           Q.    Are you aware of any of the historic trends in  
9 nuclear decommissioning estimates that the company has  
10 rendered?

11          A.    I'm aware that they have, since the first -- I  
12 believe since the first nuclear decommissioning study, that  
13 they have dramatically increased in cost.

14          Q.    Are you aware that the prices from 1981 through  
15 1995 have increased by 553 percent?

16          A.    I knew the increase was dramatic. I'll take  
17 your analysis.

18          Q.    So you were aware that there was a dramatic  
19 increase and that the projections for nuclear  
20 decommissioning are somewhat fluid?

21          A.    Well, I believe it's worth noting that the early  
22 '80s were a period of very high inflation, in addition, so  
23 that I'm not sure whether that has something to do with it.  
24 That would tell me that it may be more likely that you see  
25 dramatic increases in nuclear decommissioning costs during

1 that decade than you would in the '90s, but I'm unable to  
2 project what future nuclear decommissioning costs would  
3 actually pan out to be.

4 Q. What I'm wondering, because I'm not sure, I  
5 think in the last base rate proceeding Mr. Jones was offered  
6 as a witness from the nuclear department, so, again, this  
7 might be out of your purview. The question is:  
8 technically, most nuclear power plants' capacity decline  
9 with age. Are you aware of that trend?

10 A. No, I'm really not.

11 Q. You're not. And the assumption is that nuclear  
12 capacity will be at 78 percent for the remaining life of the  
13 Susquehanna Electric Steam Station?

14 A. That is the assumption.

15 Q. So when we get to the last couple of years,  
16 you're still assuming that the plant will operate at at  
17 least 78 percent?

18 A. We're assuming that the plant will operate at an  
19 average of 78 percent over the remaining life of the plant.  
20 Now, whether that means it would be a little bit higher in  
21 the next, say, 15 years, and a little lower in the last 12,  
22 or a solid average of 78 percent, you know, obviously, over  
23 a 27-year period, some years are going to be higher and some  
24 are likely to be lower.

25 Q. I understand; especially when there is a

1 refueling outage --

2 A. Certainly.

3 Q. -- it's hard to maintain capacity.

4 And those figures are based on prior performance at  
5 Susquehanna Electric Steam Station?

6 A. That's correct.

7 Q. So then your fuel expenses -- and again, you may  
8 not know this -- relevant to the aging process, there hasn't  
9 been any accommodation for that?

10 A. I'm unable to answer your question.

11 Q. Again, because it's hard to find someone to  
12 cross on this particular issue, if I recall from the 1995  
13 rate proceedings, that's still the decommissioning plan  
14 you're utilizing now, the plan that was approved by the  
15 Commission in '95?

16 A. That is correct.

17 Q. Are you aware that during those proceedings,  
18 that the highest component of decommissioning costs was low  
19 level radioactive waste disposal?

20 A. I was not aware of that.

21 Q. At that time of the proceedings, Barnwell was  
22 not open as a nuclear waste facility, so the calculations  
23 presumed that Barnwell would not be open. My question to  
24 you: have the calculations been reconfigured now that  
25 Barnwell is not only open but PP&L utilizes Barnwell as a

1 low level radioactive waste facility?

2 MR. RUSSELL: Your Honor, Mr. Schadt did not examine  
3 that level of detail on the decommissioning estimate. I  
4 would object.

5 JUDGE KASHI: Do you understand that, Mr. Epstein.

6 MR. EPSTEIN: I understand he did that, but Mr.  
7 LaGuardia hasn't been offered as a witness, either, and I'm  
8 a little frustrated. If they're basing their presumptions  
9 on the 1995 plan, and they've asserted that the most  
10 expensive component is low level radioactive waste disposal,  
11 and that assumption is flawed, I think somebody from the  
12 company should be able to address the issue.

13 MR. RUSSELL: Your Honor, that study has not been  
14 challenged by testimony of any party in this proceeding.

15 JUDGE KASHI: I understand. The objection is  
16 sustained.

17 Go on, Mr. Epstein.

18 MR. EPSTEIN: That concludes my cross-examination,  
19 Your Honor.

20 JUDGE KASHI: Thank you very much, sir.

21 Ms. Moury.

22 MS. MOURY: Thank you, Your Honor.

23 **CROSS-EXAMINATION**

24 BY MS. MOURY:

25 Q. Good morning, Mr. Schadt. My name is Karen

1 Moury. I represent the Office of Small Business Advocate.

2 In your rebuttal testimony on page 18, line 15, this  
3 is where you state that the OSBA has submitted a stranded  
4 cost estimate of \$3.9 billion.

5 A. One moment, please.

6 (Witness perusing document.)

7 A. Yes.

8 Q. Then you go on to rely, at least in part, on  
9 that estimate to refute the stranded cost estimates  
10 presented by OCA and PPLICA; is that correct?

11 A. That is correct.

12 Q. Now, in arriving at the \$3.9 billion figure, am  
13 I correct that you simply subtracted Mr. Knecht's discount  
14 rate adjustment from PP&L's total stranded cost claim?

15 A. Yes. Mr. Knecht pointed out in his surrebuttal  
16 testimony that I should not have done that, that that simple  
17 subtraction was not what he was intending. He did quote  
18 \$3.9 billion in an exhibit, but I understand upon reading  
19 his surrebuttal testimony that that was simply to clarify  
20 the impact of his discount rate change. I would like to  
21 correct my rebuttal testimony to revise that; that that \$3.9  
22 billion was not a conclusive projection by the OSBA.

23 Q. So then you're revising your testimony  
24 essentially to delete that reference?

25 A. Yes.

1 MS. MOURY: Thank you.

2 That's all I have, Your Honor.

3 JUDGE KASHI: Thank you very much.

4 Mr. Burgraff.

5 MR. BURGRAFF: Thank you, Your Honor.

6 CROSS-EXAMINATION

7 BY MR. BURGRAFF:

8 Q. Mr. Schadt, good morning. My name is Craig  
9 Burgraff. I represent the Office of Consumer Advocate.

10 Actually, Mr. Schadt, most of my questions have  
11 already been answered, however, I would just like to take  
12 you back to your oral rejoinder for a minute, if I could.

13 A. Yes. If you could give me just one minute to  
14 find it. I seem to have messed it up.

15 (Witness perusing documents.)

16 A. Okay.

17 Q. Are you all set?

18 A. Yes.

19 Q. Now, I believe you gave a number of \$4.2 billion  
20 at January 1, 1999 representing the company's net book  
21 value, is that correct, of its generating assets?

22 A. That's correct.

23 Q. Am I correct that that number is based upon the  
24 company's jurisdictional allocators that were used in this  
25 case?

1 A. No. That is based on the book value of the  
2 company's assets as presented in Exhibit JRS-1.

3 Q. And that number, of course, is \$200 million  
4 higher than the proposed level of stranded cost recovery by  
5 the company in this case; is that right?

6 A. It's actually \$300 million higher. It was \$4.28  
7 billion.

8 Q. I'm sorry; 4.28. Thank you.

9 A. You're welcome.

10 Q. Now, you ran through some scenarios comparing  
11 different market price assumptions.

12 A. Sir, --

13 Q. In looking at your application of the Consumer  
14 Advocate's recommendation in this case, which recommendation  
15 did you rely upon for these numbers, the updated  
16 recommendation for stranded costs?

17 A. When I said the 4.28 versus the 3.25 billion  
18 that Mr. LaCapra mentioned?

19 Q. No. I'm sorry; I've switched gears. I'm  
20 looking at scenarios now on your financial analyses.

21 A. Okay.

22 Q. You gave the four scenarios.

23 A. May I clarify a point on your last question that  
24 I may not have said quite correctly?

25 Q. Certainly.

1           A.    When I said that the \$4.28 billion is \$300  
2 million higher than our stranded cost claim, I would like to  
3 point out that that stranded cost claim covered more than  
4 simply the book value of our generating plant. Our \$4.0  
5 billion stranded cost claim also included our NUG request  
6 and our regulatory asset request, so the excess over the  
7 generation plant portion, which is what relates to this  
8 4.28, is much higher than \$300 million.

9           Q.    That's correct.

10          A.    Okay. I'm sorry. Now, if you'd start out again  
11 on your question, I'll switch gears.

12          Q.    Sure. Switching to the four scenarios.

13          A.    Yes, sir.

14          Q.    In applying the Office of Consumer Advocate's  
15 recommendation, I assume you used the Consumer Advocate's  
16 updated recommendation; is that correct?

17          A.    That's correct.

18          Q.    Now, the return numbers that you gave, I was  
19 confused, are those overall return numbers or equity return  
20 numbers?

21          A.    Those are return on equity for the company's  
22 generation business.

23          Q.    As far as overall rates of return, do you have  
24 any numbers for those?

25          A.    No, I do not. We did not go back and

1 recalculate that number.

2 Q. However, on your chart on page 25 of your  
3 Statement No. 8-R, you do show an overall rate of return; is  
4 that correct?

5 A. Where was that, sir?

6 Q. Page 25 of your rebuttal.

7 A. Yes. I'd like to point out, though, that the  
8 reason for that difference was this chart simply took the  
9 company's 1996 PUC audited income statement that we  
10 submitted -- I'm not sure if it has been audited yet; it was  
11 our 1995 to the PUC. It presented our 1996 results of  
12 operations that have been audited by Price Waterhouse. We  
13 submitted this data to the PUC, and, as a simple proxy in my  
14 rebuttal testimony, I updated that; I assumed that that was  
15 pro forma applicable to 1999, as I explained in my rebuttal  
16 testimony why that seems reasonable. Those numbers were  
17 specifically calculated on the PUC income statement.

18 Now, when we got the surrebuttal from the OCA with  
19 the revised numbers, we didn't go back and revise that.  
20 Simply what we did was we updated our information on  
21 generation stranded costs as contained within my filed  
22 exhibit, so we did not go through all of these PUC  
23 calculations.

24 Q. Returning for a second to your discussion  
25 pertaining to FAS-121, when exactly is a plant impaired

1 under FAS-121?

2 A. A plant is impaired -- what FAS-121 requires you  
3 to do is it requires you to project what the future market  
4 revenues of an asset, what they will be. It also requires  
5 you to project what the operating type costs, sustenance  
6 costs, for that asset will be over its book life. You then  
7 compare the undiscounted sum of those amounts, and if the  
8 market revenues exceed the sustenance costs in total, you --  
9 first, you calculate that difference of market revenues over  
10 sustenance costs. If that difference exceeds the book value  
11 of a plant, it is not impaired. If it does not exceed it,  
12 it is impaired.

13 MR. BURGRAFF: That completes my cross. Thank you,  
14 Mr. Schadt.

15 THE WITNESS: You're welcome.

16 JUDGE KASHI: Thank you very much, Mr. Burgraff.  
17 Mr. Simms.

18 MR. SIMMS: Thank you, Your Honor.

19 **CROSS-EXAMINATION**

20 BY MR. SIMMS:

21 Q. Good morning, Mr. Schadt.

22 A. Good morning.

23 Q. My name is Johnnie Simms. I represent the  
24 Office of Trial Staff in this proceeding.

25 Mr. Schadt, I have a few questions for you on your

1 rebuttal testimony, but before I begin, you made a number of  
2 references in your rebuttal testimony, did you not, to the  
3 competition act and to certain cases? Do you recall that?

4 A. I certainly referred to the competition act. I  
5 don't recall referring to certain cases, but I may have.

6 Q. I guess my question to you: when you made those  
7 references in your testimony to the statute, were you doing  
8 so as an accountant?

9 A. I'm not sure I understand the question.

10 Q. Did you interpret the statute for purposes of  
11 your rebuttal testimony?

12 A. To the best of my ability, yes.

13 Q. To the extent I ask you questions about that, I  
14 want you to use, to the best of your ability, that you used  
15 in your rebuttal testimony.

16 A. Fair enough.

17 Q. Can we agree that for ratemaking purposes, there  
18 is a difference between amortization and normalization?

19 A. Yes, I believe -- I'm unclear on that  
20 difference, but I've read through the Trial Staff's  
21 surrebuttal testimony, and I have read their pointing out of  
22 the difference.

23 Q. Are you in agreement with the Trial Staff on  
24 those definitions and differences?

25 A. I believe that the assets that the company has

1 claimed in this proceeding as regulatory assets are, in  
2 fact, regulatory assets as determined by generally accepted  
3 accounting principles.

4 Q. My question goes to whether or not you agree  
5 from a ratemaking standpoint to the Trial Staff's position  
6 on normalization?

7 A. If what that means is that the company is not  
8 entitled to what you would call a normalized amount, no, I  
9 do not agree.

10 Q. Let me refer you to page 40 of your rebuttal  
11 testimony.

12 A. Okay.

13 Q. I'm referring you to lines 2 through 8. Do you  
14 see that?

15 A. Uh-huh.

16 Q. Now, you indicated, "based on the PUC's ruling."  
17 What case are you referring to, or what ruling?

18 A. The September 1995 rate decision.

19 Q. Now, in your rebuttal testimony you indicate  
20 that the 1994 rate case expense is to be amortized over a  
21 four-year period, do you not?

22 A. Yes, I do.

23 Q. Did you have an opportunity to review the  
24 Commission's order in that case?

25 A. I have before; I have not real currently, so I

1 could not clearly quote it.

2 MR. SIMMS: Your Honor, may I approach the witness?

3 JUDGE KASHI: Yes.

4 MR. SIMMS: For the purpose of the record, I'm  
5 showing the witness the Commission's order in the last PP&L  
6 rate case, and I'm showing him page 65.

7 JUDGE KASHI: Would you show it to counsel, first?

8 MR. SIMMS: Yes.

9 (Document shown to Counsel Russell.)

10 MR. RUSSELL: Thanks.

11 BY MR. SIMMS:

12 Q. Mr. Schadt, I'm going to show you the  
13 Commission's discussion on rate case expense. Could you  
14 read the first sentence in that decision?

15 (Document handed to witness.)

16 A. "PP&L seeks to normalize its rate case expense  
17 over a two-year period, although the OTS seeks a four-year  
18 period and DOD seeks a three-year period."

19 Q. Do you disagree that in that case the company  
20 sought to normalize its rate case expense and not amortize  
21 its rate case expense?

22 A. That is what that would imply. I would also  
23 agree, however, that the company did not make a claim for  
24 the expenses incurred in this proceeding, which I believe  
25 would have been additional rate case expenses that the

1 company could have claimed.

2 Q. That's could have, but did not; right?

3 A. We did not.

4 Q. And we're dealing with the company's filing;  
5 correct?

6 A. Pardon?

7 Q. We're dealing with the company's filing in this  
8 case; correct?

9 A. That is correct. ~~It simply seemed to me that we~~  
10 ~~were requesting a normalized~~

11 MR. SIMMS: Your Honor, I'm going to object. There's  
12 no question outstanding.

13 JUDGE KASHI: No question outstanding. Strike the  
14 witness' utterance.

15 BY MR. SIMMS:

16 Q. You make a reference, do you not, to Section  
17 28.10 of the competition act?

18 A. Could you tell me, please, where I made that  
19 reference?

20 Q. On page 35 and 36 of your rebuttal testimony.  
21 (Witness perusing document.)

22 A. Yes.

23 Q. Now, as I understand it, you have added an  
24 inflation adjustment to taxes other than income; is that  
25 correct?

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A. That is correct.

Q. Would I not be correct that in Section 28.10 there is no reference to inflation?

A. It does not specifically reference the term "inflation".

Q. As I recall Section 28.10, in fact, all of the provisions of the competition act, apply to all electric utilities in the Commonwealth, do they not?

A. I believe so.

MR. SIMMS: Your Honor, that concludes my cross-examination.

JUDGE KASHI: Thank you very much.

We're going to take a 15-minute recess at this particular point and come back and do redirect from PP&L. We stand in recess for 15 minutes.

(Recess.)

FORM 2

1 JUDGE KASHI: Back on the record.

2 Before we begin the redirect, there is an order  
3 presently being readied for faxing, and the order says  
4 something to the effect -- it's directed to all parties,  
5 it's directed to all counsel for parties, and it directs all  
6 parties to submit to lead counsel for their group their  
7 proposed settlement options by Thursday.

8 Lead counsel is then to communicate those settlement  
9 proposals to the company, coordinate them and submit them to  
10 the company by Friday. That should be flying around real  
11 soon.

12 MR. RUSSELL: Your Honor, we have no redirect for Mr.  
13 Schadt.

14 JUDGE KASHI: Thank you very much. You are excused,  
15 sir.

16 (Witness excused.)

17 JUDGE KASHI: That which has been marked and  
18 identified as PP&L Statement Nos. 8 and 8-R together with  
19 Exhibits JRS-1, JRS-1A and 2 through 8 are received into the  
20 evidentiary record, without objection?

21 (No response.)

22 JUDGE KASHI: Without objection.  
23  
24  
25

1 (Whereupon, the documents marked as  
2 PP&L Statements Nos. 8 and 8-R and  
3 PP&L Exhibits Nos. JRS-1 through  
4 JRS-8 were received in evidence.)

5 JUDGE KASHI: Mr. Kohler?

6 MR. KOHLER: Your Honor, we have somewhat of a  
7 logistical problem. Maybe I can set it forth for you. If  
8 you recall, Your Honor, Mr. Kaplan coordinating the  
9 schedule, and at Enron's request we moved Mr. Shapiro from  
10 Wednesday to Tuesday because that was the specific day he  
11 had been scheduled for per agreement of counsel.

12 Mr. Rubin was not in attendance when we did that,  
13 IBEW and the company being the only parties that have cross  
14 for Mr. Shapiro.

15 As agreed previously, I took responsibility for  
16 contacting Mr. Rubin regarding the change in schedule, and  
17 it was expected I think by everyone here that Mr. Schadt's  
18 testimony would take longer than it did and would likely  
19 fill the morning.

20 I did convey that to Mr. Rubin, that I expected that  
21 Mr. Schadt would fill the morning and that Mr. Shapiro might  
22 go on right after lunch. That was my best guess at the  
23 time. And Mr. Rubin indicated that he was fine with that  
24 and he would be there no later than lunchtime.

25 We are, at least from the matrix, way ahead of

1 schedule, and I don't see Mr. Rubin here. I'm not  
2 suggesting that he has done anything inappropriate or that  
3 he shouldn't have a right to cross Mr. Shapiro. I just  
4 raise it for Your Honor's consideration.

5 Mr. Shapiro is here. He is ready to take the stand,  
6 and it may be that PP&L is ready to cross-examine him.

7 JUDGE KASHI: Well, I don't want to put Mr. Shapiro  
8 on and have PP&L cross-examine and then wait until 1:30 to  
9 attend to Mr. Shapiro's cross by Mr. Rubin.

10 MR. KOHLER: Judge, as soon as it became clear that  
11 we were ahead of schedule, I had my office contact Mr.  
12 Rubin's office. I presume that either he left for  
13 Harrisburg or brought to his attention that we were ahead of  
14 schedule, so he could show up at any time.

15 JUDGE KASHI: Mr. Kleppinger, is Mr. Baron prepared  
16 to go?

17 MR. KLEPPINGER: They have not arrived yet, Your  
18 Honor. They are in transit from Atlanta -- well, Mr. Baron  
19 is. Mr. Falkenberg is coming from elsewhere.

20 JUDGE KASHI: All right, let's call Mr. Shapiro.

21 MR. KOHLER: Your Honor, Enron calls Mr. Shapiro.

22 JUDGE KASHI: Sir, would you raise your right hand to  
23 be sworn?  
24  
25

1 Whereupon,

2 RICHARD SHAPIRO

3 having been duly sworn, testified as follows:

4 MR. KOHLER: Your Honor, consistent with the  
5 procedures we are utilizing for this case, Mr. Shapiro has  
6 submitted pre-filed testimony on behalf of Enron on July 2,  
7 1997. That was marked as Enron Statement 1.0. It consists  
8 of seven pages, and I would ask that it be so marked.

9 JUDGE KASHI: So marked for purposes of  
10 identification.

11 (Whereupon, the document was marked  
12 as Enron Statement No. 1 for  
13 identification.)

14 DIRECT EXAMINATION

15 BY MR. KOHLER:

16 Q. Mr. Shapiro, do you have any changes to your  
17 testimony at this time?

18 A. No, I do not.

19 MR. KOHLER: Your Honor, I would move the admission  
20 of Enron Statement 1.0 subject to any timely motions and  
21 cross-examination.

22 JUDGE KASHI: Subject to any timely motions and/or  
23 objections made, pending cross-examination, that which has  
24 been marked as Enron Statement 1.0 will be received into the  
25 evidentiary record.

1 MR. KOHLER: The witness is available for cross.

2 JUDGE KASHI: Mr. Kaplan?

3 MR. KAPLAN: Thank you, Your Honor.

4 CROSS-EXAMINATION

5 BY MR. KAPLAN:

6 Q. Good morning, Mr. Shapiro. My name is Donald  
7 Kaplan. I'll be examining you this morning on behalf of  
8 Pennsylvania Power & Light Company.

9 Please turn to page 4 of your direct testimony.  
10 Actually, what I'd like to do is actually interrupt that  
11 flow and just take care of some old business.

12 We marked for identification Enron's supplemental  
13 response to Pennsylvania Power & Light Company Interrogatory  
14 No. 51 dated July 21, 1997, which you probably don't have  
15 before you, so I will supply you with a copy.

16 A. I do not.

17 Q. And Mr. Kohler as well.

18 (Documents distributed by counsel.)

19 Q. This is PP&L Cross-Examination Exhibit, for  
20 identification, No. 7.

21 (Pause.)

22 MR. KAPLAN: May I proceed, Your Honor?

23 JUDGE KASHI: Yes, please.

24 BY MR. KAPLAN:

25 Q. Mr. Shapiro, if you were asked this question,

1 would you give the same answer today?

2 A. Yes.

3 MR. KAPLAN: Thank you, Mr. Shapiro.

4 Pennsylvania Power & Light Company moves for  
5 admission into evidence PP&L Cross-Examination Exhibit  
6 No. 7.

7 JUDGE KASHI: It is received without objection.

8 (Whereupon, the document marked as  
9 PP&L Cross-Examination Exhibit  
10 No. 7 was received in evidence.)

11 BY MR. KAPLAN:

12 Q. Now, turning back to page 4 of your direct  
13 testimony, beginning at line 18, you describe the necessary  
14 conditions for equal access to essential facilities, the  
15 first part of your three part test for making competition a  
16 reality; is that correct?

17 A. That's correct.

18 Q. At line 23, you describe the actions taken by  
19 the Federal Energy Regulatory Commission with respect to  
20 open access in the natural gas business; is that correct?

21 A. That is correct.

22 Q. Enron is subject to these provisions; are they  
23 not?

24 A. The pipelines that are owned and operated by  
25 Enron are subject to those regulations.

1 Q. And as far as you know, Enron is complying with  
2 those provisions; is that correct?

3 A. To the best of my knowledge, Enron is in full  
4 compliance.

5 Q. Would you agree that the FERC's orders to which  
6 you refer provide the necessary elements to achieve true  
7 open access with respect at least to the natural gas  
8 industry?

9 A. With respect to the pipeline transportation  
10 component of the industry, I think I would agree with you  
11 that the regulations that have been promulgated by the  
12 Federal Energy Regulatory Commission have been adequate to  
13 the task of creating a competitive marketplace at the  
14 wholesale market level.

15 Q. Is it your view that the Commission should adopt  
16 comparable provisions to the natural gas provisions we  
17 discussed earlier with respect to the open and  
18 non-discriminatory access in the retail distribution of  
19 electric power?

20 A. I think Mr. Dirmeier, a witness for Enron,  
21 actually sponsored the testimony that went into detail on  
22 the code of conduct that we're recommending in this  
23 proceeding.

24 Conceptually, I think we have laid out some of the  
25 items that we believe must be promulgated here in the

1 context of the PP&L restructuring process.

2 Obviously, you are somewhat comparing apples to  
3 oranges in terms of the wholesale business or the pipeline  
4 transportation component of the natural gas business and the  
5 retail component of the electricity business which is what  
6 we're dealing with in the context of this process.

7 We have obviously proposed through Mr. Dirmeier's  
8 testimony a code of conduct that conceptually is consistent  
9 with what the Federal Energy Regulatory Commission did in  
10 the natural gas industry for pipelines, but obviously gets  
11 into more specific details and comes up with specific  
12 recommendations that are necessary in the context of the  
13 retail electricity business.

14 Q. Just to be specific, the provisions you're  
15 referring to in the gas industry are FERC Order No. 497,  
16 currently embodied in Part 161 of the Code of Federal  
17 Regulations?

18 A. Order 497 and probably some of the decisions  
19 that have been issued since by the FERC that have clarified  
20 and --

21 Q. Clarified those?

22 A. Yes.

23 Q. Now, Enron is also now subject to FERC Order  
24 No. 888 and 888-A as well as 889 and 889-A by virtue of its  
25 acquisition of Portland General Electric Company; is that

1 correct?

2 A. That is correct.

3 Q. Would you agree that these orders, at least at  
4 the federal wholesale level, meet the standard you set forth  
5 on pages 4 and 5 of your direct testimony?

6 A. Obviously I didn't get into in my testimony a  
7 direct comparison of 497 and 889. We have obviously  
8 recommended at the federal level -- and I can't do the  
9 specifics justice here today -- we have recommended  
10 strengthening of the code of conduct in 889 at the Federal  
11 Energy Regulatory Commission.

12 Q. Will you agree that Enron as an owner of  
13 Portland General Electric Company is currently complying  
14 with Orders 888, 888-A, 889 and 889-A, to the best of your  
15 knowledge?

16 A. To the best of my knowledge, Portland General is  
17 in compliance with the orders you just mentioned.

18 Q. Now, would you agree that if the Commission  
19 adopts orders comparable to FERC's electric power orders and  
20 their natural gas orders referred to above, that Enron will  
21 be able to compete successfully in the retail electricity  
22 business in Pennsylvania?

23 A. I think that the code of conduct that was  
24 reflected in Mr. Dirmeier's testimony is the type of code of  
25 conduct that's necessary to create the necessary environment

1 here for competition to be robust and for all the benefits  
2 of competition at the retail level to be delivered to  
3 consumers.

4 Q. Well, that's not really what I asked you. I  
5 asked you whether, if this Commission adopts provisions  
6 comparable to Order 497 and Order 888 and 889, Enron will be  
7 able to compete in the retail electricity business in  
8 Pennsylvania.

9 A. I don't believe -- I mean, again, you're  
10 comparing apples and oranges in terms of the wholesale part  
11 of the electricity business, the wholesale part of the  
12 natural gas business and what's required, and an affiliate  
13 code of conduct at the retail level.

14 I would say that unless you adopt the specific  
15 recommendations that are stated in Mr. Dirmeier's testimony,  
16 that you're going to fall short of the mark by just adopting  
17 the language that's reflected in 497 and 889 here in  
18 Pennsylvania.

19 Q. Is it your view that Enron will not be able to  
20 compete successfully unless all the details in Mr.  
21 Dirmeier's code of conduct are adopted?

22 A. I think it will limit the effectiveness of  
23 competition here in Pennsylvania.

24 Q. Excuse me. That's not the question I asked. I  
25 asked whether Enron would be able to compete successfully --

1 A. I think that it will --

2 Q. -- in Pennsylvania -- if I can finish the  
3 question -- even if not all of the detailed provisions of  
4 Mr. Dirmeier's proposed code of conduct are adopted.

5 A. Depending on how far short of the mark we fall,  
6 we end up at with respect to Mr. Dirmeier's recommendations,  
7 I think our ability to compete successfully -- and not just  
8 Enron's ability -- I think the ability of the competitive  
9 marketplace, retail electric competitive marketplace to  
10 function effectively in Pennsylvania will be diminished.

11 Q. Mr. Shapiro, we're going to take up all the time  
12 until Mr. Rubin gets here unless we limit your answers to my  
13 questions.

14 Now, we have on one hand the adoption -- and let me  
15 just see if we can sort of narrow this gap -- we have  
16 adoption of orders comparable to Order 888, 888-A and 497  
17 that the FERC has adopted with respect to the electricity  
18 and natural gas industries on one hand, and Mr. Dirmeier's  
19 more detailed proposals on the other.

20 If the Commission goes no further than the comparable  
21 provisions for the distribution of electricity than FERC has  
22 gone with respect to the transmission of electricity and  
23 natural gas, will Enron be able to compete successfully in  
24 Pennsylvania?

25 A. And I think I'm answering your question by

1 saying that our ability to compete successfully in  
2 Pennsylvania will be diminished.

3 Q. Let me put it this way: You still would intend  
4 to compete in Pennsylvania; is that correct?

5 A. I mean, our intention is to compete in  
6 Pennsylvania, but you're obviously taking one aspect of an  
7 entire market structural framework and asking me whether or  
8 not, if that decision is made in a less than optimal way,  
9 will we still compete.

10 And I think obviously it's going to diminish our  
11 ability compete, and I think it's also contingent on many  
12 other facets of the decision that will ultimately get made  
13 in this proceeding.

14 Q. My question was, do you intend to enter the  
15 market in Pennsylvania if the Pennsylvania Public Utility  
16 Commission adopts measures that go no further than Order 497  
17 and Orders 888 and 889?

18 MR. KOHLER: I think it's asked and answered a few  
19 times now, Your Honor. He's saying it's comparing apples  
20 and oranges. He has brought out the distinctions between  
21 wholesale and retail markets.

22 He has asked the question of number of ways. It has  
23 been asked a number of ways.

24 JUDGE KASHI: He has answered the question a number  
25 of ways, but I don't know that I have an answer as to

1 whether, if it doesn't go any farther than those specific  
2 orders, what happens.

3 MR. KOHLER: I think the answer, Your Honor, was that  
4 it depends what else is in the restructuring --

5 JUDGE KASHI: Let's let him answer. The objection is  
6 overruled.

7 THE WITNESS: I think we would have to evaluate our  
8 ability to compete in the Pennsylvania marketplace based on  
9 the entirety of the decision in this proceeding that's  
10 issued.

11 BY MR. KAPLAN:

12 Q. So you're not committed to enter into the  
13 Pennsylvania market?

14 A. We are extremely eager to bring the benefits of  
15 a competitive electric marketplace to consumers in  
16 Pennsylvania, and I trust that we will try to find a way to  
17 do so even in the face of a less than optimal regulatory  
18 decision.

19 Q. And indeed, Enron has made a major corporate  
20 determination to become the premier seller of electric  
21 energy at retail in the United States, haven't they?

22 A. That is a stated corporate objective, correct.

23 Q. And you are taking steps that any competitor  
24 would take, trying to break into new markets; is that  
25 correct?

1           A. I'm not exactly sure what you mean by "those  
2 steps."

3           Q. Well, for example, establishing brand name  
4 recognition.

5           A. We are in the process of establishing brand name  
6 recognition; that is correct.

7           Q. Presumably analyzing customers and their  
8 demands?

9           A. That is correct.

10          Q. Would you agree that Enron would also expect to  
11 price its electricity in such a manner as to facilitate its  
12 entry into those markets?

13          A. Consistent with our ability to earn a profit,  
14 obviously we would price electricity at a level that would  
15 enable us to enter the market.

16          Q. And that would probably mean initially offering  
17 some discounts, as any new entrant to a market would do?

18          A. I'm not sure what -- discounts off of what?

19          Q. Why don't we say, offer low prices that are not  
20 necessary meeting your profit objectives in the long run,  
21 but in the short run would establish your brand name, get  
22 customer recognition and expand market share?

23          A. I don't believe that it is the intent of the  
24 company to come into any marketplace with the intent of  
25 losing money.

1 Q. I understand that, in the long run you would  
2 agree with that; is that correct?

3 A. I would say even in the short run.

4 Q. But even in the short run, would you agree that  
5 you may have to price electricity at a price lower than you  
6 would like over the long run in order to establish brand  
7 name recognition, to obtain market share?

8 A. I'm not sure that is the case. I'm not sure I  
9 can answer that question definitively today one way or  
10 another, but I think in all likelihood we as a company would  
11 be quite reluctant -- I think what you're getting at in  
12 terms of buying market share by taking significant losses on  
13 the front end, I don't think that that's a viable entry  
14 strategy.

15 Q. You've characterized it as that. I didn't  
16 characterize it as that. I characterized it as offering  
17 lower prices -- well, let me characterize it -- offering  
18 lower prices than your competition and offering such things  
19 as perhaps special, one-time, short-term discount programs,  
20 things of that nature?

21 A. It is very likely that one of the products that  
22 we will try to bring into the marketplace is a lower priced  
23 product than our other competitors.

24 Q. Do you agree that Enron will not be alone in  
25 making those efforts, but will probably face stiff

1 competition?

2 A. I think, based on what we have seen in pilots  
3 around the country, that we're likely to have a great many  
4 competitors present here in Pennsylvania.

5 Q. And those would include both alternate suppliers  
6 and the existing utilities in Pennsylvania?

7 A. Alternative suppliers and hopefully utilities  
8 competing in the marketplace through non-regulated  
9 affiliates.

10 Q. Right. And you expect to see, in each of the  
11 service territories of the present utilities, the other  
12 utilities as competitors? For example, to clarify, you  
13 would expect as a possibility -- I don't know their specific  
14 plans -- that competing in PP&L's service territory, you  
15 will probably be competing not only against PP&L but PECO  
16 and perhaps GPU and Allegheny, et cetera?

17 A. We believe that non-regulated affiliates of the  
18 utilities should have every opportunity to compete here in  
19 Pennsylvania.

20 Q. And you expect that they will, don't you?

21 A. We have every expectation that they will.

22 Q. And would you agree that as long as everybody is  
23 playing by the same rules, Enron should have a reasonable  
24 chance of being successful in that effort to compete in  
25 Pennsylvania?

1           A.    So long as everyone is truly playing by the same  
2 rules, presumably our chances of success are no greater, no  
3 better than any other competitor in the marketplace.

4           Q.    And you expect to be able to match or beat  
5 incumbent utilities on price, service and variety of product  
6 offerings?

7           A.    That's what a competitive marketplace is all  
8 about, bringing lower prices, better service, innovative  
9 products to consumers.

10          Q.    And Enron expects to be able to do that?

11          A.    We have every expectation that we will do that  
12 successfully.

13          MR. KAPLAN: Thank you, Mr. Shapiro.

14          PP&L has no further questions.

15          JUDGE KASHI: Thank you very much.

16          MR. KOHLER: Do you want redirect now? I have some  
17 redirect. I can do it now or ---

18          JUDGE KASHI: Do you have an hour's worth of  
19 redirect?

20          MR. KOHLER: I'd be struggling to find an hour of  
21 redirect, Your Honor.

22          MR. KAPLAN: Your Honor, we would not object to  
23 taking an early, starting the lunch hour perhaps now and,  
24 since we did gain so much time this morning, we think that  
25 if we reconvene at 1:00, a little bit longer lunch hour, we

1 will be more efficient this afternoon.

2 JUDGE KASHI: Well, it might be more efficient, but  
3 it creates a problem for me.

4 MR. KAPLAN: I'm sorry, Your Honor.

5 JUDGE KASHI: I have things that have been scheduled  
6 for that particular hour.

7 MR. KAPLAN: Your Honor, I do think that we will  
8 certainly be able to reach and maybe even complete Mr.  
9 Falkenberg today, even if we do break now and reconvene at  
10 1:30. We do not contemplate significant, lengthy  
11 cross-examination for Mr. Baron. Mr. Falk we do not think  
12 will take very long.

13 JUDGE KASHI: I think I can rearrange some things.  
14 We will recess for lunch at this time and come back at 1:00,  
15 as opposed to 1:30. We will stand in recess until 1:00.

16 (Witness temporarily excused.)

17 (Whereupon, at 11:25 a.m., the hearing was adjourned,  
18 to be reconvened at 1:00 p.m., this same day.)  
19  
20  
21  
22  
23  
24  
25



1 I think in each of the, I guess, the seven delineated  
2 bullets, each of those create opportunities for consumer.  
3 But clearly, I think, your characterization, in that the  
4 primary ability to deliver those is going to be in the hands  
5 of suppliers, is correct.

6 Q. All right. So you're not suggesting that  
7 consumers would be able to aggregate loads for scheduling  
8 purposes, or reduce a utility's administrative costs  
9 directly; that's something a supplier would do?

10 A. That's correct.

11 MR. RUBIN: Your Honor, I would ask to have marked  
12 for identification as IBEW Cross Exhibit 2 a document that  
13 I'll proceed to identify further with the witness.

14 JUDGE KASHI: So marked for purposes of  
15 identification.

16 MR. RUBIN: Thank you, Your Honor.

17 (Whereupon, the document was marked as  
18 IBEW Cross Examination Exhibit No. 2  
19 for identification.)

20 BY MR. RUBIN:

21 Q. Mr. Shapiro, do you have a copy of IBEW Cross  
22 Exhibit 2 in front of you?

23 A. Yes, I do.

24 Q. Now, this is a response to an interrogatory that  
25 PP&L sent to Enron and that Mr. Reising answered on behalf

1 of the company.

2 Now, first, would I be correct that Mr. Reising is a  
3 consultant to Enron and not an employee of Enron?

4 A. That is correct.

5 Q. And I just want to make sure that what  
6 Mr. Reising says here actually reflects the opinion of your  
7 company. So I'll ask you that question. Does his answer  
8 accurately reflect the opinion of Enron?

9 MR. KOHLER: I don't believe he has a copy of the  
10 statute.

11 THE WITNESS: I do not.

12 JUDGE KASHI: Wait till counsel shows him a copy.

13 MR. KOHLER: I'm trying to find the right section,  
14 Your Honor.

15 (Pause.)

16 MR. KOHLER: The Commission shall require the  
17 unbundling; is that where we are?

18 MR. KLEPPINGER: Yes.

19 (Document handed to witness.)

20 THE WITNESS: Could you restate your question?

21 BY MR. RUBIN:

22 Q. Yes. I'm asking if the response that appears on  
23 IBEW Cross Exhibit 2 accurately reflects your opinion and  
24 the opinion of your company.

25 A. Yes, it appears to.

1 Q. So, being able to bill customers in any fashion  
2 that you choose and in any amount that you choose for  
3 distribution service is part of your vision for the electric  
4 industry in Pennsylvania?

5 A. We believe that competitive suppliers should have  
6 the opportunity, if the customer so chooses, to deliver a  
7 single bill to the consumer, representing the charges that  
8 have been agreed upon between the supplier and the consumer,  
9 that is correct.

10 Q. I'm not sure that you gave me a direct answer to  
11 my question. I'm asking if it is your opinion that you  
12 should be allowed to bill consumers in any manner that you  
13 choose and in any amount that you choose for electric  
14 distribution service.

15 MR. KOHLER: Your Honor, I think he answered it; as  
16 long as it was consistent with the agreement between the  
17 supplier and the customer.

18 JUDGE KASHI: I'm sorry, I didn't understand that.

19 MR. KOHLER: I think he answered it the first time.

20 JUDGE KASHI: I'm not sure. Let's do it again.

21 THE WITNESS: I guess I'll add one thing to my  
22 previous response, and that is, with respect to the actual  
23 content of the bill, we recognize that there is likely to be  
24 some regulation of the bill format. And clearly, to the  
25 extent that there is some prescribed format, at least in

1 part, clearly Enron would be in compliance in the provision  
2 of the bill with any of those types of requirements.

3 BY MR. RUBIN:

4 Q. Excuse me; I have a few additional questions for  
5 you. And in these questions, or at least in many of them, I  
6 will use the term "electric distribution service." And by  
7 that term I am referring to services provided by PP&L as the  
8 electric distribution utility, excluding revenue cycle  
9 service.

10 Before we go any further, do you understand what I  
11 mean by the term "electric distribution service" as I'm  
12 going to be using it?

13 A. I think I do, but I guess I would ask you to --  
14 I'm not sure that we have an agreed-upon definition of what  
15 you're backing out; and presumably what you're backing out  
16 are revenue cycle services. So, perhaps you could define  
17 those services for me.

18 Q. Well, I will define them as I believe several  
19 witnesses from your company have defined them, to include  
20 meter reading, billing and customer service. Do you think  
21 there's anything I've left out of that?

22 A. I think that's sufficient for the purpose of  
23 this.

24 Q. Now, in your opinion, and in the opinion of your  
25 company, should you be able to charge different rates for

1 electric distribution service to customers who receive the  
2 same class of service?

3 A. And again, let me just make sure I understand  
4 your terminology. The electric distribution service is more  
5 or less the wires function. It's not the revenue cycle  
6 services that you just described.

7 A. As I'm using it here, yes.

8 MR. KOHLER: I'm going to object; only because it  
9 occurred to me the witness is confused because there is on  
10 foundation. The line of questioning may be appropriate, and  
11 I think Mr. Rubin was referring to --

12 JUDGE KASHI: He didn't seem confused to me.

13 MR. KOHLER: Well, that's fine, Your Honor, he can  
14 answer.

15 JUDGE KASHI: Okay.

16 MR. KOHLER: I think there's a foundation necessary.  
17 What Mr. Rubin is referring to is Enron's proposal as to  
18 agency, and he's asking the questions in that context.

19 JUDGE KASHI: Are you testifying now?

20 MR. KOHLER: Well, I think that's the foundation he  
21 needs before he can get to these questions.

22 JUDGE KASHI: Mr. Rubin, are you satisfied with  
23 Mr. Kohler's request for a foundation; which he's already  
24 laid?

25 (Laughter.)

1 BY MR. RUBIN:

2 Q. Mr. Shapiro, do you have any trouble  
3 understanding what we're talking about here?

4 A. Why don't you restate the question.

5 Q. All right. Would it be easier if I use the term  
6 "wires charge"? Would that make it clearer, what I'm  
7 talking about?

8 A. That's fine, that's fine.

9 Q. All right. Now, in your opinion, and in the  
10 opinion of Enron, should you be allowed to charge different  
11 rates for the wires charge to customers who receive the same  
12 class of service?

13 A. Well, our intention is to purchase the wires  
14 service on behalf of customers in an agency relationship as  
15 their agent. And what we would be actually charging the  
16 consumer for, whatever services we would be providing them  
17 in a competitive marketplace, would be a function of the  
18 agreement reached between the customer and the supplier,  
19 whether it be Enron or another supplier.

20 Q. Well, and when you say it would be a function of  
21 the agreement you reached with the customer, would it be  
22 correct that you would reach, or you may reach, different  
23 agreements with different customers, which would result in  
24 different customers paying different rates for the same  
25 service?

1           A. Given that not all customers are similarly  
2 situated, have different electricity requirements, different  
3 needs, I think that it's very likely that there will be some  
4 differentiation in terms of the price that's proposed to  
5 various customers.

6           Q. And would I be correct that, again, under your  
7 proposal, PP&L would receive the same amount of revenue for  
8 these distribution charges or wire charges from every  
9 customer that it serves; some customers would pay PP&L  
10 directly, and in other cases you would be paying PP&L on  
11 behalf of the customer?

12           A. As agent for the customer, that's correct.

13           Q. Is it your opinion, and the opinion of Enron,  
14 that this Commission should oversee or review the amount  
15 that you charge your customers, who you're acting as agent  
16 for, for these wire charges or distribution charges?

17           A. We fully expect that there will be some degree of  
18 oversight of competitive electric providers here in  
19 Pennsylvania and around the country. I think, however, if I  
20 understand your question correctly, that is, whether or not  
21 the Pennsylvania Commission should regulate the charges that  
22 are agreed upon between us and the ultimate consumer, the  
23 answer is that is a price that is going to be agreed upon in  
24 a competitive marketplace, it's going to be a function of  
25 the various choices, the multitude of choices that consumers

1 have available to them. And absent some demonstration of  
2 fraud, the answer is, no.

3 Q. Is it your opinion, and the opinion of your  
4 company, that you could charge a customer more than PP&L's  
5 tariffed rate for electric distribution service, or wires  
6 service?

7 A. Well, it's theoretically possible that a customer  
8 could agree to pay a premium over what they're currently  
9 paying for bundled electric services if they believe that  
10 they're receiving some premium in return for the services  
11 that are being delivered to them. And let me give you an  
12 example.

13 Q. I'm sorry; before you give me the example, you  
14 answered about bundled electric service, and my question was  
15 referring only to the charges for distribution service. I  
16 want to make sure we're on the same wavelength.

17 A. Well, I think it's very difficult to answer that  
18 question in the context of just distribution service,  
19 because customers are going to be looking for a package of  
20 services, generally speaking, from electric service  
21 providers. And they're going to be looking at the full sort  
22 of array of services and products that are being delivered  
23 to them by a particular supplier or suppliers, and then  
24 measuring them against what they may be offered by the  
25 affiliate of the incumbent utility, or what may be the

1 default service option that they have available to them.  
2 And there are going to be a variety of factors that  
3 determine whether or not they choose to receive service from  
4 another provider, and if they're willing to pay a premium,  
5 what they're getting in return for that premium.

6 Q. All right. Now, part of that package of services  
7 you're talking about is distribution service; is that right?

8 A. That is one component of the overall service that  
9 would be provided to every electricity consumer, that's  
10 correct.

11 Q. And again, in your understanding, under your  
12 vision or proposal that you're making to this Commission,  
13 would PP&L be the only company that is allowed to own,  
14 operate, maintain and repair the distribution services  
15 within its service territory?

16 A. The monopoly wires functions we're talking about;  
17 is that correct?

18 Q. Yes.

19 A. Generally speaking, I think that that is correct.  
20 I mean, there clearly is the potential for some competition  
21 around the margins for the provision of those services. But  
22 generally speaking, if we're talking about the monopoly  
23 wires function, I think your assumption is correct.

24 Q. And what I'm asking you is, for that piece of the  
25 service that we're both in agreement that only PP&L will

1 provide, would you be allowed to charge more than PP&L's  
2 tariffed rate?

3 A. And again, the answer is, I can't conceive of a  
4 marketplace in which a customer would pay a premium for just  
5 the distribution services that they can get at a certain  
6 price under a tariff, if they were to buy that directly from  
7 the distribution service provider. The only way that I can  
8 conceive of a consumer paying a premium above, let's say, a  
9 default service option that might be available to them, is  
10 if they believe that they've being delivered some services  
11 or some products that are worthy of them paying a higher  
12 price.

13 JUDGE KASHI: Do you really believe that,  
14 Mr. Shapiro?

15 THE WITNESS: Yes. In fact, the example that I was  
16 going to get to -- and clearly, the market will perhaps  
17 either bear this out or not, but green energy, or renewable,  
18 or energy that comes from renewable resources, there is  
19 polling that's been done by many that have indicated that  
20 consumers are willing to pay a small premium over their  
21 current rates for the knowledge that the energy that's being  
22 bought on their behalf is coming from renewable energy  
23 resources.

24 JUDGE KASHI: Do you believe that by the time it's  
25 unbundled and repackaged by everybody else, that the

1 consumer's going to have any idea what he's really paying  
2 for in those packages?

3 THE WITNESS: I think the answer is yes. I mean,  
4 he's clearly going to have a benchmark against which to  
5 assess.

6 JUDGE KASHI: Are you familiar with the  
7 telecommunications industry?

8 THE WITNESS: Yes.

9 JUDGE KASHI: Do you believe that the consumers out  
10 there, in purchasing services at a premium or no premium,  
11 know what it is they're getting and what they're paying for?

12 THE WITNESS: I think they know that they're paying a  
13 whole lot less for long distance telecommunications services  
14 than they did pre the AT&T divestiture. In fact, somewhere  
15 on the order of 50 to 70 percent less. I think consumer  
16 intuitively know that.

17 JUDGE KASHI: And they know that there are packages  
18 out there that they can get on local long distance calling  
19 that are cheaper than other packages, and yet they still go  
20 for the more expensive packages?

21 THE WITNESS: And they make that decision for many  
22 reasons, including comfort with --

23 JUDGE KASHI: Primarily because they understand what  
24 they're doing?

25 THE WITNESS: I think the vast majority of consumers

1 understand the significance of their decisions, their buying  
2 decisions, in the telecommunications marketplace.

3 JUDGE KASHI: I personally find that incredible, sir.  
4 I mean, I just do. Consumer Reports puts out information on  
5 cellular phones that in the markets throughout the entire  
6 United States that the packages that are being sold by MCI  
7 are twice the amount of any local caller, da-da, da-da,  
8 da-da, this, that and the other, and MCI is taking the  
9 market, as oppose to the others; and they're being provided  
10 the same service.

11 And you want me to accept that that's the credible  
12 understanding of the consumer out there who knows what it is  
13 he's doing, as opposed to some rash judgment based upon some  
14 kind of slick advertising or some perception that he gets or  
15 some misunderstanding of the packages, to what it is that  
16 he's actually getting?

17 THE WITNESS: I don't believe -- I mean, not being  
18 personally familiar with the MCI approach to charging double  
19 for the same service, I don't think that that's a  
20 sustainable commercial strategy. I think that eventually  
21 consumers will figure out that they're paying a significant  
22 premium for the same service that's available for a lesser  
23 price in the market.

24 JUDGE KASHI: That is exactly my point, some day they  
25 will figure it out.

1 I'm sorry to interrupt you.

2 MR. RUBIN: Thank you, Your Honor.

3 BY MR. RUBIN:

4 Q. Mr. Shapiro, under your agency concept, would the  
5 supplier be the only point of contact that the customer  
6 would have concerning its electric service?

7 A. I think we have -- I think the answer to that is,  
8 no, that there would still be a point of contact with the  
9 distribution company, particularly with respect to  
10 emergencies that might arise with respect to the delivery of  
11 their electric service.

12 Q. If, for example, there were an outage, would the  
13 customer call you as the customer's agent, or would the  
14 customer contact PP&L directly?

15 A. Well, I guess there's a couple of answers to  
16 that. One is, with many customers, assuming that we have  
17 the ability to delivery a meter of their choice, one of the  
18 functionalities of many of the high technology meters that  
19 are available is an outage detection service that would  
20 immediately communicate that the outage has occurred, to the  
21 distribution company, so that they could get the necessary  
22 people and equipment out to the location.

23 We would expect, absent that kind of technology being  
24 deployed on a household, or on a commercial location, that  
25 the consumer would then have two choices available to them.

1 One is to contact their electric competitive service  
2 provider, or to contact the distribution company with  
3 respect to the nature of the outage.

4 Q. And just so I understand the first part of your  
5 answer where you talked about meters that could provide  
6 outage detection service. Would an outage be communicated  
7 to the supplier or to PP&L?

8 A. It's our hope -- and I know Mr. Jacobson was our  
9 primary witness on this issue; and I'm not sure whether he  
10 actually had the opportunity to get into this issue. The  
11 hope is that by developing open architecture communications  
12 standards, which I'm not intimately familiar with, that that  
13 information would be conveyed to the distribution company at  
14 the same time that it's being conveyed to the competitive  
15 supplier.

16 Q. If a customer had difficulty paying his or her  
17 bill, would that problem come to you or to PP&L? Again,  
18 under your agency concept.

19 A. Under the agency concept, I imagine that the non-  
20 payment problem would get communicated to both entities, and  
21 both entities would have remedies available to them.

22 Q. Now, I'm getting a little confused here. As I  
23 understood the agency concept, the customer would not even  
24 know that PP&L was in the picture. They would get a bill  
25 from Enron every month, it would either include as a

1 separate line item, or rolled into some other charges, the  
2 distribution fee. Is that correct? Is that what you  
3 envision with an agency concept, that you would be the  
4 electric provider, at least on paper, for the customer?

5 A. We would be the entity providing a single bill  
6 reflecting all their electric service charges, that is  
7 correct.

8 Q. So, under that kind of an arrangement, why would  
9 the customer ever contact PP&L directly instead of  
10 contacting you as the customer's agent?

11 A. Well, we would do everything to make it worth  
12 their while to come to us and only us with respect to any  
13 problems that they may have with respect to their electric  
14 service.

15 I think we recognize, however, that there probably  
16 will continue to be some type of default call center that's  
17 available within the distribution company, so that if the  
18 customer wants to exercise the choice of calling the  
19 distribution company directly, perhaps with respect to an  
20 outage of service, that they would have that choice  
21 available to them. We would try our best to provide a  
22 quality of service that would not make that necessary.

23 Q. Okay. So, just so I understand, even though you  
24 would be the customer's agent, you're suggesting that that  
25 would not be an exclusive arrangement and that the customer

1 could deal directly with PP&L, rather than having to deal  
2 only through you?

3 A. With respect to, let's say, an outage -- and I'm  
4 not sure I could give you a definitive yes to that question,  
5 because I'm not sure of everything that you're talking  
6 about. But let's take it in the context of an outage.

7 At least for some transitional period, it's our  
8 expectation that the distribution company will continue to  
9 provide that service and that the customer would have the  
10 option in the event of an outage to call either their  
11 competitive service provider or the distribution company.

12 Q. All right. Now let's go to my second example  
13 where the customer is having difficulty paying his or her  
14 bill.

15 Would they be required to deal exclusively with you,  
16 as the agent, or would they have the option of dealing with  
17 you or with PP&L, or would they be required to deal with  
18 both of these separately to take care of this payment  
19 problem?

20 A. Well, clearly, we would encourage them to deal  
21 with us in resolving any payment problems that may exist  
22 between us and them.

23 And obviously, in the context of -- much of this is  
24 sort of undefined in terms of how the rules ultimately end  
25 up and what the respective remedies are that are available

1 to competitive service providers and distribution companies.  
2 We may only have the opportunity to end the service that  
3 we're providing to them. It's not our expectation that we  
4 would have the ability to actually physically terminate  
5 service to a customer.

6 So that in the event that we were to end our service  
7 to them, presumably they would default to whatever the  
8 default service option is, and then the payment problem  
9 would become the responsibility of whomever the default  
10 service provider is.

11 Q. Again, I thought I understood you, then you said  
12 something that made me wonder if I understood or not. Are  
13 you saying that even though you would be the customer's  
14 agent, that you would not have the ability to terminate all  
15 electric service to the customer?

16 A. Let me ask you what you mean by terminate.

17 Q. Well, you used --

18 A. Is it a physical --

19 Q. -- the term in your answer.

20 A. Well, and I explained it by saying termination  
21 meaning physical disconnection of service.

22 Q. Okay. Let me ask you a slightly different  
23 question then. Am I correct that some of the more automated  
24 electric meters allow for what would be called virtual  
25 disconnection; that is, a disconnection of electric service

1 that does not require anyone to physically visit the  
2 premises and physically disconnect the meter?

3 A. I don't know the answer to that question.

4 Q. When you just used the term "physical  
5 disconnection of service," what were you referring to?

6 A. The actual severing of electric service to a  
7 residence of business, as opposed to the discontinuation of  
8 a particular service that might be provided by Enron or  
9 another competitive service supplier.

10 Q. All right. I think I'm starting to understand  
11 again. Are you saying that Enron as the supplier of the  
12 electric generation service would be allowed to terminate  
13 electric generation service to a customer? And that is  
14 something that you intend to do if the need arises?

15 A. That's correct.

16 Q. Okay. And when you were talking about physical  
17 disconnection of service, you were talking about a complete  
18 elimination of electric service to that customer; is that  
19 correct?

20 A. That's correct.

21 Q. So in the event that Enron ends its relationship  
22 with a customer and no longer provides generation service to  
23 the customer, then it would be up to the customer to find  
24 another generation supplier; is that right?

25 A. Right; or revert to whatever the default service

1 option may be, and whoever the default service provider  
2 might be.

3 Q. All right. Now, in that situation, if Enron were  
4 also providing these agency services to the customer so that  
5 you were doing everything for the customer, what would  
6 happen? And what would happen if you terminated your  
7 relationship with the customer as the generation supplier?  
8 Where would the customer go to get all these other services  
9 you were providing to them?

10 A. Well, I'm not sure that, not knowing what the  
11 actual contract would look like, and not being the person  
12 who would be writing such a contract, I'm not sure what all  
13 the specific provisions of that agency agreement would be.

14 But my expectation is it wouldn't be a whole lot  
15 different from the scenario that we just described. For  
16 non-payment of services in a non-agency context, there would  
17 obviously be the ability of a service supplier to  
18 discontinue that service to a customer; and presumably in an  
19 agency arrangement, for non-payment of the various services  
20 that are being provided, there would be a provision in there  
21 that would allow discontinuation of that agency arrangement.

22 The same thing would happen, however, with respect  
23 to the customer, they would revert back, presumably, to a  
24 default service option, or would go out and seek another  
25 supplier, either a generation service supplier in a

1 non-agency context, or would seek another competitive  
2 service supplier in an agency context.

3 Q. Mr. Shapiro, on page 6 of your testimony, I guess  
4 it's roughly on lines 4 through 14, this is part of your  
5 discussion of this agency concept.

6 You state that in your opinion, suppliers should be  
7 allowed to arrange for delivery services for their customer.  
8 And just so I understand that, by delivery services, you're  
9 talking about the wires services that we'd been referring to  
10 earlier; is that right?

11 A. That's correct.

12 Q. I'm having a little bit of trouble understanding  
13 this concept, too. Right now we have a system where the  
14 buyer of electric service, the end use customer, pays for  
15 delivering that service to the customer; is that right?

16 A. Could you state that again? I sort of lost you  
17 in the middle of the question.

18 Q. Yes, it was a confusing question. I apologize  
19 for that.

20 The system that we have right now is set up where the  
21 buyer of electricity pays to deliver the electricity to the  
22 customer, to the buyer; is that right?

23 A. In today's system, a buyer of electricity pays  
24 the monopoly utility a bundled rate for a bundle of  
25 services, some of which are competitive, some of which are

1 monopoly functions.

2 Q. And first, I think we agreed earlier that under  
3 whatever system arises here, PP&L will be the exclusive  
4 provider of wires services within its service territory; is  
5 that right?

6 A. Generally speaking, I think that's correct.

7 Q. And once we hit January 1, 1999, are you  
8 suggesting that there should be two different options;  
9 option one is that a customer pays the deliver charge in  
10 order to have electricity delivered to the customer, and  
11 option two would be that the electricity supplier pays the  
12 deliver charge, so that it can bundle that charge in with  
13 other services that it wants to sell to a customer?

14 A. I think what we have proposed in one of our other  
15 witnesses' testimony is actually a three bill option, that  
16 each consumer would have the ability to receive a single  
17 bill from the distribution company, which would include the  
18 competitive supplier's charges.

19 The second option would be the opportunity to receive  
20 separate bills from the distribution company and the  
21 competitive supplier for their respective services.

22 Or, a consumer would have the ability to receive a  
23 single bill from the competitive supplier reflecting the  
24 services that are being provided by the distribution  
25 company.

1 Q. All right. I'm not focusing here on the bill,  
2 I'm focusing on who pays PP&L for the service. And my  
3 question is: Would there be two different options -- I'll  
4 tell you what, let me take a step back.

5 This delivery charge we're talking about would be  
6 like buying a postage stamp at the post office; wouldn't it?  
7 Somebody has to pay to deliver the mail.

8 A. That's correct.

9 Q. And right now we have a system where the person  
10 who puts something into the postal system is the one who  
11 pays the charge most of the time. You put a stamp on the  
12 envelope, so you have paid the charge to send something out  
13 into the system; is that right?

14 A. I think that's generally right, although with the  
15 proliferation of folks like Mail Boxes, etcetera, I think  
16 that -- I'm not sure that that explanation fits. I think  
17 there are other entities oftentimes in the middle that are  
18 providing those services and are actually paying the  
19 delivery company, the delivery company in your example being  
20 the postal service.

21 Q. And that's kind of where I was heading with this.  
22 Is this the kind of system you're talking about, where there  
23 would be options? In some options the person receiving  
24 electricity would have to pay a delivery charge every month  
25 directly to PP&L, and in other circumstances the person

1 sending electricity, trying to sell it to the customer,  
2 could cover that delivery charge. You would pay PP&L  
3 directly, and the customer just gets a rate from you, and  
4 the customer may not know what's included in it.

5 Q. Well, you've added lots of stuff there at the end  
6 of your question. I think I would generally agree with you  
7 that the customer would have choices available to them as to  
8 how they would pay for their distribution services, as to  
9 how they would pay for all of their electric services.

10 Q. And these different options for paying for  
11 distribution services would all be available in the  
12 marketplace, under your proposal? And none of them would be  
13 required; customers and suppliers could choose whichever  
14 ones they want?

15 A. That is correct.

16 Q. And a customer could switch back and forth  
17 between options?

18 A. Within whatever constraints are built into the  
19 rules with respect to switching. That is, I think, one of  
20 the cornerstones of this restructuring process, to give  
21 customers choices.

22 Q. And again, so I'm sure that I understand your  
23 proposal, you are suggesting that when Enron or another  
24 supplier pays PP&L for these delivery services, you would  
25 then be allowed to charge the customer any amount for the

1 provision of those services? You wouldn't be limited to  
2 just charging exactly what you paid to PP&L?

3 A. That is correct, within the constraints of the  
4 marketplace, there would -- providers are going to find  
5 different ways to differentiate themselves. Many are going  
6 to be low-cost providers, many perhaps will be premium  
7 service providers.

8 But if a customer desires -- let's say, let's take an  
9 office building as an example. If it's in the best  
10 interests of an office building to get a single bill each  
11 month, \$1,000 or \$10,000, whatever that amount is, without  
12 any delineation of what the various components are, but that  
13 represents a significant reduction, or a reduction of some  
14 magnitude from what they're currently paying for their  
15 electric services, and there are lots of other things  
16 attached to that service in terms of retro-fitting of  
17 equipment, that should be an option that's available to  
18 consumer. If that works for them and it's agreed upon by  
19 them and their competitive service provider, that should be  
20 an option that's out there.

21 Q. So, as the supplier then you would, under this  
22 proposal, you would have the option of discounting delivery  
23 service for some customers but not for others? Again, if  
24 that's what the marketplace required?

25 A. Well, it would obviously be part of an overall

1 package of services that are being delivered to the  
2 customer.

3 Presumably, competitive service providers are not  
4 going to be in this business of losing money on every  
5 customer that they serve. And if we're paying PP&L or any  
6 other distribution company a tariffed rate for their  
7 distribution services, we're not going to be in the business  
8 long if we're providing those services at a discount off of  
9 the charge that we're paying to the distribution company and  
10 obviously not making it up elsewhere.

11 But what form what takes is going to be, again,  
12 between the competitive service providers and the customer.  
13 And the key is providers. You're going to have folks  
14 competing. And the marketplace is not going to allow  
15 somebody to come in and charge a premium for a service or a  
16 package of services without delivering something in return  
17 for that premium.

18 Q. You spoke a moment ago about, say you're serving  
19 an office building, and how you might want to build that  
20 office building.

21 Under the agency concept that you're proposing, if  
22 every tenant in that off building signed up with Enron to  
23 provide service, and agreed that Enron would be that  
24 tenant's agent for electric service, let's assume  
25 hypothetically that there were a problem with the delivery

1 of electricity to that building; say there were several  
2 outages during a month. Would Enron have the right to make  
3 any changes in the distribution facilities that were serving  
4 that building?

5 A. Obviously you've given me sort of an incomplete  
6 question in terms of not knowing exactly what's causing the  
7 variety of outages.

8 But getting, I guess, to the latter part, the  
9 question, I can't conceive of a situation where we would  
10 have the ability to unilaterally go in and modify the  
11 distribution facilities. Clearly we would become, as part  
12 of our customer service arrangement with that customer, we  
13 would be their advocate in going to the distribution company  
14 and trying to work out a facilities-based solution to  
15 whatever the problem may be.

16 Q. All right. And if you were unable to receive  
17 satisfaction from the distribution utility, I assume from  
18 the answer you just gave that you would not be able to take  
19 matters into your own hands?

20 A. I think that's correct. Obviously there would be  
21 avenues such as this forum before which to bring those types  
22 of problems if, in fact, a distribution company is not  
23 responding adequately to the customer's needs.

24  
25

1 Q. And if that were to happen, your customers might  
2 blame you for the problem and end their relationship with  
3 you, and there would be nothing you could do about it?

4 A. That is conceivable. There are going to be  
5 certain decisions that are going to be within the purview of  
6 the monopoly wires company, and I guess I tend to believe  
7 that they're going to try to find solutions that assist the  
8 customer in resolving problems that may exist on the  
9 distribution system. I don't think the distribution  
10 companies, once properly structured and once properly  
11 incentivized, will choose to make decisions that are adverse  
12 to customers unless there's some overriding engineering  
13 reason for doing so.

14 Q. Under your agency concept, who would the  
15 distribution utility's customer be? Would it be the end-  
16 user or would it be Enron?

17 A. In an agency arrangement the customer of record  
18 would become the competitive service supplier. And,  
19 frankly, those kinds of situations, as far as I understand  
20 it, exist today where customers of electric and gas  
21 utilities have arranged for agency relationships and have  
22 established someone else, another entity, as the customer of  
23 record. It could be some type of real estate management  
24 company; it could take a number of forms. But this is not a  
25 new concept, it's done today.

1 Q. Do you know if it's done today in Pennsylvania?

2 A. I do not know.

3 MR. RUBIN: Thank you, Mr. Shapiro.

4 That's all I have for this witness, Your Honor.

5 JUDGE KASHI: Thank you.

6 Mr. Shapiro, there's a couple questions that may or  
7 may not be within your purview, you may or may not have any  
8 answers, and if you don't, you just tell me that.

9 THE WITNESS: I'll tell you.

10 JUDGE KASHI: Do you have any idea what the  
11 percentage of illiterate adults there are in Pennsylvania?

12 THE WITNESS: I don't have any --

13 JUDGE KASHI: Do you have any idea what the  
14 percentage of functionally illiterate adults there are in  
15 Pennsylvania?

16 THE WITNESS: I do not know that percentage for  
17 Pennsylvania.

18 JUDGE KASHI: Do you have any idea what the  
19 percentage of households receiving electricity in  
20 Pennsylvania are run by people over 75 years old?

21 THE WITNESS: I don't know the actual percentage.

22 JUDGE KASHI: Thank you. I said I didn't know  
23 whether you would or wouldn't.

24 THE WITNESS: I have some approximate notion of what  
25 those percentages might be, but I don't have any specific

1 numbers to provide you.

2 JUDGE KASHI: What would your approximate notions of  
3 those types of things be?

4 THE WITNESS: In terms of which?

5 JUDGE KASHI: Of any of my questions.

6 THE WITNESS: Going back through the categories?

7 JUDGE KASHI: Well, the illiterate adult portion of  
8 Pennsylvania.

9 THE WITNESS: I've seen illiteracy numbers on a  
10 national basis in the order of 10 to 15 percent,  
11 functionally illiterates being somewhat higher than that.  
12 I've seen different numbers, and often times, depending on  
13 the advocacy group that's advancing them, you have different  
14 perceptions.

15 JUDGE KASHI: Those people, as high as 40 percent,  
16 would tell you that the adult population is functionally  
17 illiterate.

18 THE WITNESS: Functionally.

19 JUDGE KASHI: All right. I just thought maybe in  
20 what you were doing here, that those ideas may have crossed  
21 your mind and that you would have had opportunity to look at  
22 those types of things.

23 Redirect? Do you want a minute, two minutes?

24 MR. KOHLER: Yes, sir.

25 JUDGE KASHI: Everybody stand easy.

1 (Discussion off the record.)

2 JUDGE KASHI: Back on the record.

3 Redirect, Mr. Kohler.

4 MR. KOHLER: Thank you, Your Honor.

5 **REDIRECT EXAMINATION**

6 BY MR. KOHLER:

7 Q. Mr. Shapiro, just some clarifying questions. Do  
8 you have an expectation that within an agency arrangement,  
9 whether Enron would expect to offer a bundled or an  
10 unbundled product?

11 A. I think it's our expectation that customers are  
12 generally going to desire a package of services, rebundled,  
13 so for the vast majority of consumers, I think it would take  
14 that form.

15 Q. In pricing those services, would Enron seek to  
16 provide a lower price than the customer currently pays for  
17 that product?

18 A. I think, again, for the vast majority of  
19 customers, the price is going to be less than they're  
20 currently paying for their electric services.

21 Q. Would it be Enron's plan or would it be  
22 necessary in your view to assign that discount to one  
23 component of that product or another?

24 A. I think that, generally speaking, the answer is  
25 no. Consumers are going to be looking for an understandable

1 bill that explains to them in relatively, again,  
2 understandable terms what they're paying for the services  
3 they're receiving, so I wouldn't expect that you would have  
4 a 12-line component bill, but a single line representing  
5 what they're paying and the fact that it represents a  
6 savings off of what they're currently paying.

7 Q. Would that bill provided by Enron be subject to  
8 regulatory requirements?

9 A. We fully expect that there will be some  
10 regulatory requirements built around a bill that a  
11 competitive supplier would provide.

12 Q. Now, you answered some questions about service  
13 to payment troubled customers and what might happen if there  
14 was non-payment of a bill. In a situation where Enron  
15 discontinued service to a given customer and that customer  
16 either went to another supplier or went back to the default  
17 provider, what would happen to the arrearages that accrued  
18 while that customer was being served by Enron?

19 A. We would be responsible for the arrearages that  
20 existed at the time the customer was discontinued.

21 Q. It's been a while now, but do you recall Mr.  
22 Kaplan's cross-examination regarding Portland General and  
23 Enron's compliance with FERC orders?

24 A. I do.

25 Q. Is Portland General also in the process of

1 restructuring its electric business?

2 A. Yes, it is. Portland General --

3 MR. KAPLAN: I object, Your Honor. This is beyond  
4 the scope of my cross-examination.

5 MR. KOHLER: Your Honor, I think it's right in line  
6 with the scope of cross.

7 MR. KAPLAN: I asked only about their wholesale  
8 business.

9 MR. KOHLER: But I think Mr. Kaplan was trying to  
10 draw analogies between their wholesale business and the  
11 retail business; that was the distinction that we were  
12 drawing, not that he was drawing.

13 MR. KAPLAN: Not between Portland General's retail  
14 business, but between the wholesale business of Portland  
15 General, the wholesale business of Enron, and the retail  
16 business of PP&L in Pennsylvania. What Portland General is  
17 doing in the State of Oregon, subject to the regulation of  
18 the Oregon Public Utility Commission, is of no interest in  
19 this proceeding. It may be of some interest to my partners  
20 in Portland, but not in this proceeding.

21 MR. KOHLER: Your Honor, I think it clearly was in  
22 the scope of cross.

23 JUDGE KASHI: I agree. I also agree with Mr. Kaplan  
24 that we're not too interested in what's going on in  
25 Portland, but I think it's within the scope of the cross,

1 and I'm going to overrule your objection. But I don't know  
2 where you're going to go with it, Mr. Kohler.

3 MR. KOHLER: This is going to be a very short line.

4 JUDGE KASHI: All right. Because, like I say,  
5 Portland is Portland.

6 BY MR. RUBIN:

7 Q. Is Portland General also in the process of  
8 restructuring its electric business?

9 A. Yes. Portland, at the request of the Oregon  
10 Commission, filed a pilot program for about 15 percent of  
11 its load on August 1 of this year, and on September 2, next  
12 Tuesday, will be filing a full restructuring proposal that  
13 would give all consumers in the service areas choice by the  
14 end of 1998.

15 Q. In your view, are those restructuring proposals,  
16 both pilot and permanent, consistent with applicable FERC  
17 orders?

18 A. Yes.

19 Q. Can you briefly describe some of the elements of  
20 PGE's restructuring?

21 A. Yes. Just very briefly, it provides competition  
22 for all competitive services, generation, metering, billing,  
23 customer care services. It establishes the distribution  
24 company as purely a wires company, with the relationship,  
25 the customer relationship, of the distribution company being

1 exclusively with energy service providers. It also, in the  
2 context of the discussion we had this morning, puts in place  
3 an affiliate code of conduct that goes beyond the affiliate  
4 code of conduct that's part of Order 889 and Order 497.  
5 Because of the unique attributes of a retail marketplace, it  
6 ensures the complete separation --

7 MR. KAPLAN: Your Honor, --

8 JUDGE KASHI: Wait one second. I'm having a problem  
9 here, because as I recall the testimony -- and I may be  
10 wrong, and the record will speak for itself -- this morning,  
11 on cross-examination by Mr. Kaplan, the witness was asked  
12 about, specifically, 497, 888 and 889, and he told us that  
13 he didn't have what it took to tell us about those orders.

14 MR. KOHLER: I think he testified, if I recall, Your  
15 Honor, that he generally accepted the philosophy behind  
16 those orders, but that he thought additional safeguards were  
17 necessary in a retail market. I don't think he testified  
18 that he was not familiar with them.

19 MR. KAPLAN: But, Your Honor, he gave his answer this  
20 morning. I asked specifically -- if you look at his  
21 testimony, page 4, I asked specifically about this first  
22 point, "equal non-discriminatory access to essential  
23 facilities by competing suppliers." That's the heart of the  
24 FERC Order 888 and the heart of the Order 497. That's all I  
25 asked about. He gave me an answer. He slipped in a little

1 bit more this morning. He can't do redirect on his own  
2 cross answer.

3 JUDGE KASHI: I'm in agreement with that, sir.

4 MR. KOHLER: I'll end my redirect at this point.

5 JUDGE KASHI: All right. Thank you very much, sir.

6 If there's no follow-up from any of the parties,  
7 unfortunately, I think the Judge has a question.

8 I was confused, sir, in response to I forget whose  
9 question it was now, but you were asked about the packaging  
10 that the competitive entities would be doing, and that it  
11 was your understanding -- and this is where I got confused,  
12 because you talked about the consumers being able to  
13 purchase packages and that the packages most assuredly were  
14 going to be less expensive than the service that they were  
15 receiving at the current time. Do you recall that? Do you  
16 recall saying that?

17 THE WITNESS: Could you state that again? I'm not  
18 sure I followed the entire thread of the question.

19 JUDGE KASHI: You were questioned about Enron and the  
20 other competitors putting together packages that would be  
21 provided to service the consumers, and that it was your feel  
22 that the consumers would pick and choose among those various  
23 packages, and that in some way that whatever package they  
24 were going to get, that that would be less expensive for  
25 them than, and you then said, the service that they are

1 currently receiving. Is that correct?

2 THE WITNESS: Yes. I think --

3 JUDGE KASHI: All right. Well, here's where you lose  
4 me. The service that they are currently receiving is, in  
5 fact, the unbundled service being provided by PP&L; is that  
6 correct?

7 THE WITNESS: Well, today, if you're comparing it to  
8 today, consumers are paying a rate per kilowatt-hour for a  
9 number of services that are bundled together, and I think  
10 what I was saying or trying to say was that in a competitive  
11 marketplace, the vast majority of consumers are going to  
12 expect to see a reduction in their electric bills, in their  
13 total electric bills. In order for competitive suppliers to  
14 earn the right to serve them, the vast majority of consumers  
15 are going to expect, in return, a reduction in their  
16 electric bills from what they are today.

17 JUDGE KASHI: That's correct. The question is: in  
18 the packages that they're receiving, what do we do to  
19 compare the service that they are receiving in the package  
20 to the service that they were receiving prior to the  
21 unbundling?

22 THE WITNESS: So you're talking about today versus --  
23 how would you compare what a consumer is receiving a year or  
24 two years from now versus what they're receiving today?

25 JUDGE KASHI: Well, it was your answer, sir, that I'm

1 trying to understand. Your answer was that the packages  
2 were going to be less expensive than the service they were  
3 receiving, and I thought, when you said "they were  
4 receiving," I expected that to have been now. I mean that's  
5 how I read that. I don't know if that's what you intended,  
6 but that's what I thought you meant. What I'm trying to  
7 figure out is: what are they going to get in the packages  
8 as opposed to what they are getting in the packages?

9 THE WITNESS: There are going to be a variety of ways  
10 that consumers determine a proper assessment of what they're  
11 receiving in the future versus what they were receiving  
12 under today's structure. One way would be a straight out  
13 comparison as to: your bill in 1997 during the month of  
14 July was this, with Enron serving you, your bill is this.  
15 That could come about as a result of a per unit reduction in  
16 the cost of energy, it could come about as a result of a  
17 smart meter being put on someone's home and incentivizing  
18 them to utilize energy at a less expensive time of day. How  
19 the reduced bill occurs for a particular consumer is going  
20 to be a function of the services and products that we and  
21 others will provide to them.

22 JUDGE KASHI: And the bottom line is that you expect  
23 that it won't make a difference to them as long as their  
24 bottom line is less than what it was?

25 THE WITNESS: Again, it's going to vary by consumer

1 to consumer, but I think that many consumers are going to be  
2 looking at the bottom line in terms of whether or not  
3 they're seeing a reduction in their bill in a competitive  
4 environment, or an offer that's put on the table by us or  
5 another competitive supplier, versus what they could get in  
6 a default service option and versus what they might have  
7 been receiving under today's regulated structure.

8 JUDGE KASHI: I, quite frankly, still don't  
9 understand the nature of the billing and the metering that's  
10 going to take place that's going to indicate to people where  
11 it is they're talking about saving money, because if we're  
12 talking about the products, we all know how much of the bill  
13 the product is, so the ultimate bill has got to do with a  
14 lot of other services that are going to be in that package,  
15 and I'm not sure at the present time, from what I'm hearing,  
16 how the folks are going to be able to compare the various  
17 services. When you start talking about giving them a smart  
18 meter and all the rest of that kind of stuff, and if the  
19 smart meter costs more than what it's costing them at the  
20 present time, do we still tell them, "Well, wait a minute,  
21 you're saving money; take a look at what the energy  
22 component of this bill is"?

23 THE WITNESS: Again, I think it's going to be -- for  
24 us to be successful in the marketplace, we're going to have  
25 to deliver something of value to consumers. Many consumers

1 are going to value a reduction in their overall bill, and  
2 how we deliver that is going to take various forms. It  
3 could be in the form of helping them to modify their energy  
4 usage during certain times of the day. It could be by  
5 helping to finance certain energy efficiency improvements to  
6 their home or business. It could take the form of coming in  
7 and retrofitting boilers in an office building and  
8 delivering the commodity for less cost. I think ultimately  
9 perhaps the difficulty in comparing it to today is that  
10 there are going to be a multitude of new services, new  
11 products, that are going to be delivered to consumers in  
12 different ways that are going to create value propositions  
13 for consumers or they won't fly for long. I think because  
14 there's always been this sort of one size fits all mentality  
15 under the current monopoly structure, I think it's difficult  
16 for all of us to conceive of the various forms that service  
17 and the new products will take in a competitive marketplace,  
18 but that, in fact, is, frankly, the beauty of a competitive  
19 marketplace, because it's going to deliver -- a supplier  
20 will not succeed unless it's delivering a value proposition  
21 to a consumer and is able to articulate what that value  
22 proposition is.

23 JUDGE KASHI: I will note that my telephone bill, by  
24 virtue of the services that have been offered to me, is  
25 nowhere near what my telephone bill used to be, it's just

1 not even close, and yet, as you testified this morning, long  
2 distance rates are going down. I can call Brazil for things  
3 like you couldn't believe, and I can call India. All the  
4 friends that I have that are Indian that have people still  
5 over there, they're just jumping up and down, we went from  
6 \$8.00 a minute down to \$2.50 a minute, and they're just  
7 going to think that's wonderful. But when we're getting  
8 ready to tell Pennsylvanians that they're going to save 10  
9 percent on their bill, I just wonder how honest that is.

10 THE WITNESS: There are various ways to get there.  
11 You can do a simple reduction in the bundled service rate,  
12 and that could end up being a component of a particular  
13 restructuring proceeding, but if you stay on a default  
14 service and you buy electricity exactly the way you did in  
15 the past, you'll pay 9 cents a kilowatt-hour instead of 10  
16 cents. That's one way to get to a 10 percent savings that I  
17 think consumers would be able to understand. Then there are  
18 going to be additional value propositions that competitive  
19 service providers are going to be forced to deliver if  
20 they're going to succeed in the marketplace. It could take  
21 the form of an additional reduction in the commodity price  
22 per kilowatt-hour, it could take the form of a provider  
23 coming in and putting a meter on a home that helps a  
24 consumer modify the usage of their energy so that they're  
25 buying it in the middle of the night when it's 3 cents

1 instead of 3:00 in the afternoon when it's 5 cents. There  
2 are various ways beyond what might take the form of some  
3 sort of a regulated 10 percent reduction that consumers are  
4 going to be able to receive additional value through the  
5 delivery of electric services.

6 JUDGE KASHI: Thank you, sir.

7 THE WITNESS: Thank you.

8 JUDGE KASHI: Did you want to follow on that at all?

9 MR. KOHLER: No.

10 JUDGE KASHI: You're excused, sir.

11 THE WITNESS: Thank you.

12 (Witness excused.)

13 MR. RUBIN: Your Honor, excuse me. Before we move  
14 on, I neglected to move my exhibit, so I would move IBEW  
15 Cross Exhibit No. 2.

16 JUDGE KASHI: Received without objection.

17 (Whereupon, the document marked as  
18 IBEW Cross-Examination Exhibit No. 2  
19 was received in evidence.)

20 JUDGE KASHI: That which has been marked and  
21 identified as Enron Statement 1.0 is received into the  
22 evidentiary record, without objection?

23 (No response.)

24 JUDGE KASHI: Without objection.  
25

1 (Whereupon, the document marked as  
2 Enron Statement No. 1.0 was received  
3 in evidence.)

4 JUDGE KASHI: That one gave me a headache. Not Mr.  
5 Shapiro; that whole line of questioning gave me a headache.  
6 I don't understand it.

7 All right, Mr. Baron or PPLICA, you're about ready to  
8 go?

9 MR. KLEPPINGER: Your Honor, PPLICA would call Mr.  
10 Baron at this point.

11 MR. KOHLER: Your Honor, I was on the matrix as  
12 having cross for Mr. Baron. I don't.

13 JUDGE KASHI: That makes me happy.

14 MR. KLEPPINGER: Did that remove the headache, maybe?

15 JUDGE KASHI: No. It's not as good as two Motrin,  
16 but it'll get there.

17 Would you raise your right hand and be sworn, sir?

18 Whereupon,

19 **STEPHEN J. BARON**

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

21 JUDGE KASHI: Please be seated, sir.

22 MR. KLEPPINGER: Thank you, Your Honor. Consistent  
23 with the agreement of counsel, we would like to have marked  
24 for identification PPLICA Statement No. 1, the direct  
25 testimony and exhibits of Stephen Baron, which consists of

1 the text as well as Exhibits SJB-1 through SJB-13.

2 JUDGE KASHI: So marked for purpose of  
3 identification.

4 (Whereupon, the documents were marked  
5 as PPLICA Statement No. 1 and PPLICA  
6 Exhibits Nos. SJB-1 through SJB-13  
7 for identification.)

8 MR. KLEPPINGER: We would also like to have marked as  
9 PPLICA Statement No. 1R the rebuttal testimony of Mr. Baron.

10 JUDGE KASHI: So marked for purpose of  
11 identification.

12 (Whereupon, the document was marked  
13 as PPLICA Statement No. 1R for  
14 identification.)

15 MR. KLEPPINGER: We would finally like to have marked  
16 as PPLICA Statement No. 1-S the surrebuttal testimony of  
17 Stephen Baron.

18 JUDGE KASHI: So marked for purpose of  
19 identification.

20 (Whereupon, the document was marked  
21 as PPLICA Statement No. 1-S for  
22 identification.)

23 DIRECT EXAMINATION

24 BY MR. KLEPPINGER:

25 Q. Mr. Baron, are there any corrections to make to

FORM 2

1 Statement No. 1, 1R or 1-S at this time?

2 A. Yes. I have one correction to make to Statement  
3 1 on page 11, at lines 17 and 18. I previously identified  
4 this in a data response, but it is not in the record. The  
5 last sentence which begins with "As discussed by PPLICA  
6 witness Kollen," et cetera, should be replaced in its  
7 entirety by the following sentence: "For the purposes of  
8 this analysis, we have utilized PP&L's cost of capital  
9 recommendation." The numbers shown on my original testimony  
10 are correct, and those are PP&L's numbers.

11 MR. KLEPPINGER: Thank you, Mr. Baron.

12 Your Honor, at this time I would move for the  
13 admission of PPLICA Statement No. 1, along with Exhibits  
14 SJB-1 through 13, PPLICA Statement 1R, and PPLICA Statement  
15 1-S.

16 JUDGE KASHI: Subject to any timely motions and/or  
17 objections pending cross-examination, that which has been  
18 marked and identified will be received into the evidentiary  
19 record.

20 MR. KLEPPINGER: Thank you, Your Honor. Mr. Baron is  
21 available for cross-examination.

22 JUDGE KASHI: Mr. Hladik?

23 (No response.)

24 JUDGE KASHI: I'm saying somebody's name wrong.  
25 Allegheny?

1 MR. NORDSTROM: Yes.

2 CROSS-EXAMINATION

3 BY MR. NORDSTROM:

4 Q. Good afternoon, Mr. Baron. My name is Paul  
5 Nordstrom and I represent Allegheny Power.

6 A. Good afternoon.

7 Q. Mr. Baron, in your testimony you propose a  
8 \$47 million adjustment to PP&L's stranded cost recovery to  
9 effect a partial sharing of costs by the company's  
10 shareholders; is that correct?

11 A. That's correct.

12 Q. This adjustment is essentially a disallowance of  
13 the equity return on the unamortized balance of generation  
14 stranded costs as those costs are recovered through the CTC;  
15 is that correct?

16 A. That's correct.

17 Q. This adjustment is appropriate, in your opinion,  
18 to arrive at a just and reasonable level of recovery from  
19 ratepayers; is that right?

20 A. Yes; that is my position.

21 Q. Would you turn to page 15 of your direct  
22 testimony, please?

23 A. I have that.

24 Q. Now, in the answer that begins at the middle of  
25 the page and goes to the bottom, you are describing there

1 the steps that are required to arrive at a just and  
2 reasonable level of stranded cost recovery; is that right?

3 A. Yes.

4 Q. And you state, beginning at line 10, that with  
5 respect to generation stranded costs, the Competition Act  
6 first requires the Commission to consider whether or not the  
7 utility has undertaken reasonable mitigation efforts before  
8 then quantifying and determining a just and reasonable level  
9 of stranded costs. Is that the essence of your testimony?

10 A. That's part of my testimony.

11 Q. Is it your understanding that the Competition  
12 Act was intended to encourage utilities to engage in  
13 mitigation?

14 A. My interpretation would be that it did encourage  
15 utilities to engage in mitigation.

16 Q. Is it your opinion that a utility's success in  
17 mitigating its stranded costs should be considered in  
18 determining a just and reasonable level of stranded cost  
19 recovery?

20 A. I would agree that that could be considered,  
21 yes.

22 Q. Could you explain to me how it might be  
23 considered?

24 A. I think it would have to be a qualitative  
25 determination. Certainly, if the utility presents specific

1 quantified evidence that shows that certain actions on their  
2 part were responsible for stranded cost reduction, and it  
3 was quantified, obviously, that evidence could be  
4 considered. It's speculative in terms of how I, as a  
5 witness, would recommend that be used. It would depend on  
6 the facts at hand in the case.

7 Q. Is it your opinion that, as a matter of  
8 appropriate regulatory policy, the decision-maker should  
9 consider the successful efforts of one utility to mitigate  
10 its stranded costs and perhaps allow it a better result at  
11 the end of the case than a utility that failed to mitigate  
12 stranded costs?

13 A. Given my understanding of the Competition Act  
14 that the first step in the development of stranded costs is  
15 to mitigate all possible stranded costs, or to the extent  
16 possible, I'd say mitigation is a requirement, and failing  
17 to do so would result in perhaps a greater disallowance of  
18 stranded costs on the part of the Commission, or should.  
19 Now, to the extent that that essentially means, if you've  
20 gone one step beyond, that might affect the ultimate level  
21 of a just and reasonable determination of generation  
22 stranded costs, that may be reasonable.

23 MR. NORDSTROM: Your Honor, I have no more questions.

24 JUDGE KASHI: Thank you very much.

25 Mr. Kaplan.

1 MR. RUSSELL: Mr. Russell this time.

2 CROSS-EXAMINATION

3 BY MR. RUSSELL:

4 Q. Good afternoon, Mr. Baron.

5 A. Good afternoon.

6 Q. My name is Paul Russell. I'm representing PP&L  
7 in this case.

8 If you would turn your attention to page 9 of your  
9 direct testimony, at lines 17 to 20, you're discussing your  
10 Exhibit SJB-2, which shows a summary of PPLICCA's recommended  
11 stranded cost allowance; am I correct?

12 A. Yes.

13 Q. Am I correct that Exhibit SJB-2 reflects  
14 stranded regulatory assets on a revenue requirements basis?

15 A. Yes.

16 Q. Am I further correct that that exhibit shows  
17 stranded generating costs, but those costs are not shown on  
18 a revenue requirements basis?

19 A. Those costs are on a revenue requirements basis,  
20 assuming that it was going to be paid by ratepayers on day  
21 one of the transition period. To the extent that, in  
22 reality, the recovery of those stranded generation costs are  
23 going to be recovered through a CTC over time, there would  
24 be a return on the uncollected amounts, and that return  
25 would provide an equity, a debt return and associated taxes.

1 So there would be an adjustment in the calculation of the  
2 accrual of CTC revenues, but if the payment were actually  
3 made on day one of the transition period, it would  
4 essentially cover all of the costs, and in that sense, I've  
5 characterized that, I believe, in my testimony as being on a  
6 revenue requirement basis.

7 Q. But that characterization aside for a minute,  
8 the computation or determination of stranded generating  
9 plant is done on an asset basis?

10 A. Right. Okay. In terms of contrasting to PP&L's  
11 methodology, the methodology that's used by Mr. Falkenberg  
12 and the results of which are presented on SJB-2 is an asset-  
13 based approach to the calculation of stranded generation  
14 costs, not a lost revenue approach, which is the way I would  
15 characterize PP&L's method.

16 Q. If you would turn to page 10, still in your  
17 direct, looking at lines 4 to 8, am I correct that PPLICA's  
18 analysis indicates that the market value for PP&L's  
19 generating plants will be approximately \$186 million less  
20 than their net balance on PP&L's books?

21 A. That's correct.

22 Q. Is this relatively small difference driven in  
23 large part by PPLICA's estimate of future market prices?

24 A. Yes. I would characterize it that way; yes.

25 Q. Would you agree, to the extent that actual

1 market prices are less than PPLICCA's estimate in this  
2 proceeding, PP&L may not be able to recover its stranded  
3 generation costs?

4 A. If the Commission were to adopt our  
5 recommendation that stranded generation costs were \$186  
6 million on a total company basis, and that's premised on our  
7 market price forecast, and if, further, as I understand your  
8 question or hypothetical, if market prices ultimately were  
9 not that high, then stranded costs, everything else being  
10 equal, would have been higher had we known that market  
11 prices did not actually come out that high. On the other  
12 hand, if market prices were higher than we expected, it  
13 would be the reverse, stranded costs would have actually  
14 been lower than \$186 million.

15 Q. Under the hypothetical that we're discussing, if  
16 market prices in fact turn out to be less, then PP&L  
17 actually will have lost its ability to recover stranded  
18 generation costs?

19 A. I think the answer is yes, and that's true of  
20 our methodology, that's true of PP&L's methodology or any  
21 methodology that utilizes a projection of market prices. To  
22 the extent those market prices overstate the actual market  
23 prices that materialize or understate the actual market  
24 prices that materialize, it would have had an effect on  
25 stranded costs on a present value basis. That's the nature

1 of this type of analysis. The same would be true using  
2 PP&L's filing. If market prices turn out to be less than  
3 PP&L believes them to be, PP&L, according to its  
4 calculations, would not recover its stranded costs that it  
5 believes it deserves. On the other hand, if market prices  
6 turn out to be at the level that we're projecting, PP&L  
7 would substantially over-collect stranded costs.

8 Q. Looping back to a question of just a couple  
9 minutes ago, am I correct that under PPLICA's analysis the  
10 vast majority of PP&L's stranded costs would be recovered  
11 through market rates and only a relatively small amount,  
12 approximately \$186 million, would be recovered through the  
13 CTC?

14 A. I would not agree with your characterization. I  
15 think perhaps I can clarify your question to something that  
16 I can agree with. Of the total generation component of  
17 PP&L's rates, we're assuming that a large amount or some  
18 amount will be recovered in the market price component that  
19 PP&L will get when it sells electricity at competitive  
20 rates. The other portion of the generation portion of  
21 current rates would be recovered through stranded costs. I  
22 think that was a slightly different characterization than  
23 how you characterized it or stated it.

24 Q. That's fine, with just one final clarification.  
25 As you recharacterized, you talked about PP&L would recover

1 a large amount of its stranded through market price, and  
2 then you kind of restated and said "some amount." Could you  
3 tell me which it is in your opinion?

4 A. I haven't calculated the amount. Again, I  
5 disagree with your characterization. I think your question  
6 was PP&L would recover a large amount of its stranded costs  
7 through the market price, and that's not, in my opinion, a  
8 correct characterization. There's a generation component of  
9 PP&L's rates currently based on embedded revenue  
10 requirements and average fuel cost. That is going to be  
11 essentially disaggregated into a market piece and a stranded  
12 piece, and, obviously, the higher the market price  
13 assumption that one makes, the greater the percentage of  
14 that generation component of the rate will be recovered  
15 through market sales, competitive market sales. I haven't  
16 calculated the relative percentages in terms of dollars, so  
17 how I characterize it, I'd say that given the amount of  
18 stranded costs that we are recommending for recovery  
19 associated with generation assets, it's a relatively small  
20 proportion of the total asset value of PP&L's generating  
21 assets.

22 Q. Thank you.

23 Turning to page 16, still in your direct, the answer  
24 that begins on line 11 and continues through the end of the  
25 page, you're discussing the need to be consistent with

1 previous Commission precedent. My question: are you aware  
2 of any Commission decision which found that any portion of a  
3 PP&L generating plant investment was imprudently incurred?

4 A. I am not aware of that, no. I'm not aware of  
5 any findings in any case that I've been in, and I've been in  
6 a few cases, probably, since 1984. That's not to say it  
7 didn't occur, I'm just not aware of it.

8 Q. Are you aware of any PUC decision which found  
9 any portion of a PP&L generating plant investment not used  
10 and useful on economic grounds as distinguished from  
11 reliability grounds?

12 A. My recollection was that in the case of the  
13 Susquehanna units, they were found to be not used and useful  
14 on the basis of excess capacity. I don't recall any  
15 disallowance, and, again, I just don't recall, based on an  
16 economic excess capacity basis, if that's what you're  
17 referring to.

18 Q. Turning to page 19 of your direct, beginning at  
19 the top of that page, you're discussing the Commission's  
20 responsibility to apply a just and reasonable standard; is  
21 that correct?

22 A. Yes.

23 Q. Do you believe that application of that just and  
24 reasonable standard requires some adjustment or discount  
25 from the total calculated level of stranded costs in every

1 case?

2 A. My view would be that the standard would not  
3 necessarily require such an adjustment, but that such an  
4 adjustment would be appropriate, certainly, in a situation  
5 like this, as I'm recommending, in this case a relatively  
6 modest disallowance relative to PP&L's total stranded cost  
7 claim. However, I don't think I would characterize that as  
8 an absolute requirement in order to arrive at a just and  
9 reasonable rate.

10 Q. So to just follow up, hypothetically, there  
11 could be a situation where there would be a just and  
12 reasonable award of stranded costs without a discount or an  
13 adjustment?

14 A. It's certainly possible, yes.

15 Q. On page 26 of your direct testimony, at lines 11  
16 to 14, you discuss PPLICA's proposal regarding  
17 reconciliation of the CTC, and my only question here:  
18 wouldn't you agree that your proposal regarding CTC  
19 reconciliation would essentially leave that issue unresolved  
20 for as long as seven years?

21 A. The testimony on page 26 talks about our  
22 position with respect to the -- I assume you're talking  
23 about the extension beyond a seven-year period in terms of  
24 CTC recovery. Our position is, and my testimony supports  
25 this position, that that determination should not be made in

1 this case, but rather should be made at such time as there  
2 is substantial evidence that the company would not be  
3 allowed to recover all of its authorized stranded costs,  
4 Commission-authorized stranded costs, during the seven-year  
5 period. To that extent, you could characterize it as an  
6 element of uncertainty. However, based on the analytical  
7 framework that we've used in this case, and that PP&L has  
8 used, the determination of stranded costs will be made in  
9 this proceeding; it will not be subject to revision if  
10 market prices change over time. What we're talking about in  
11 this extension issue is simply sufficient sales revenue to  
12 recover the allowed stranded costs that the Commission  
13 authorized in this case. So I consider -- as I discussed  
14 elsewhere in my testimony, we've estimated that based on our  
15 stranded cost estimate, PP&L would recover its stranded  
16 costs in approximately a year, so it doesn't look to us like  
17 the seven-year period is a real problem or an issue at all.

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1 Q. Turning to page 43 of your direct, lines 4 to 6  
2 where you are discussing PP&L's proposed customized CTC,  
3 could you tell me, would PPLICA object if PP&L were to  
4 withdraw its proposal to offer a customized rate design?

5 A. No. As a matter of fact, I believe in my  
6 surrebuttal testimony, I so stated that we believe -- our  
7 main position is that such a customized proposal should not  
8 under any circumstance be mandatory for commercial and  
9 industrial customers as proposed by PP&L.

10 In my direct testimony at page 43, I stated that it  
11 would be appropriate to offer it as an option to those  
12 customers.

13 PP&L in its rebuttal responded that it believed that  
14 would result in self-selection bias, and at that point I  
15 stated that our position is, A, we recommend the Commission  
16 reject the mandatory proposal, and if PP&L doesn't offer the  
17 optional, that would be appropriate as well.

18 Q. On page 46 of your direct at lines, particularly  
19 14 to 16, you're discussing appropriate CTC for an  
20 interruptible customer that elects to shop in the  
21 marketplace.

22 My question goes to a slightly different issue but  
23 related. Assume that a customer previously served on Rate  
24 Schedule LP-5 no longer qualifies for service under that  
25 rate schedule and transfers to Rate Schedule LP-4, has a

1 smaller load, for example.

2 Would it be your testimony that that customer, who  
3 has transferred from LP-5 to LP-4 during the transition  
4 period should continue to pay the CTC rate contained in Rate  
5 Schedule LP-5, that customer's original schedule for  
6 service?

7 A. No, just like I wouldn't recommend that a  
8 residential customer that adds a new addition to his house  
9 and increases his usage or installs some energy efficiency  
10 equipment and decreases his usage would be required to pay a  
11 CTC based on the historic maximum level.

12 The nature of rate schedules is such that customers  
13 basically would pay the charges associated with the rate  
14 schedule they're taking service on.

15 I make in my mind a very large distinction between  
16 that concept and the issue that I'm addressing in my  
17 testimony regarding interruptible service.

18 Q. Maybe my question wasn't clear. I wasn't really  
19 going to the level of CTC payments as driven by the level of  
20 the customer's usage.

21 I'm trying to identify, as a customer moves from one  
22 rate schedule to another, would it be your opinion that the  
23 per unit CTC from the original rate schedule would still be  
24 applicable because, if I understand your testimony, that was  
25 where the customers incurred the cost?

1           A.    No.  That was how I understood your question,  
2 and my answer was no.  And again, it goes to the nature of  
3 rate schedules.

4           Likewise, an LP-4 customer that moves to LP-5 because  
5 they increase their usage would end up paying a higher CTC  
6 presumably because they're going to be using more  
7 electricity based on the LP-5 schedule, and the CTC would be  
8 based on the new schedule.

9           That's the nature of rate schedules, that rates are  
10 not designed for individual customers with take-or-pay  
11 contract provisions.

12           But I do wish to contrast that concept to the issue  
13 at hand with respect to interruptible service, in which I'm  
14 arguing and I believe appropriately that interruptible  
15 customers who stay on the PP&L system and continue to buy  
16 electricity during the transition period from PP&L would pay  
17 a transition charge associated with that rate.

18           That's PP&L's proposal.  My testimony concerns what  
19 happens to that customer if they choose to leave the system  
20 for the purpose of taking part in the competitive  
21 marketplace.

22           They should pay the same CTC as they would had they  
23 remained on the system, and I see a big distinction between  
24 that concept and the question you raised with regard to my  
25 testimony.

1 Q. But isn't it true that that interruptible  
2 customer under PP&L's proposal is now being served on a  
3 different rate schedule, a firm rate schedule and should pay  
4 the CTC associated with that rate schedule?

5 A. An interruptible customer, which --

6 Q. That has elected to shop and then return.

7 A. Well, not return, but elected to shop for the  
8 purposes of their generation component of their rate?

9 Q. That's correct.

10 A. With respect to the services that PP&L is  
11 providing, distribution, perhaps transmission services,  
12 those services are identical to both customers.

13 With respect to the generation component of the rate,  
14 that reflects -- the customer would pay the market price for  
15 that. With respect to the CTC that's premised on PP&L's  
16 stranded costs, my argument is they should pay the same  
17 price for that as well, whether or not they leave.

18 There is simply no distinction with respect to  
19 stranded costs between an interruptible customer that  
20 chooses to buy distribution and transmission from PP&L but  
21 production from another entity versus an interruptible  
22 customer that buys distribution and transmission from PP&L  
23 and production resources from PP&L. With respect to the  
24 stranded cost issue, they're identical.

25 Q. Finally, Mr. Baron, if you would look at

1 page 59, still in your direct, lines 1 to 4 where you're  
2 suggesting a pro rata adjustment to subscribers' nominated  
3 load in the event a class is oversubscribed, would your  
4 proposed pro rata adjustment be performed on a once-and-done  
5 basis?

6 A. I'm not sure -- maybe you could explain. I  
7 think I understand what you're saying, but I want to make  
8 sure I understand. When you say "once and done" --

9 Q. Well, within the first phase of the transition  
10 period where a third of the customers can shop, if it turns  
11 out that a particular class is oversubscribed as of 1/1/99  
12 and a pro rata adjustment is required, would it be done just  
13 that one time or would customers have an opportunity to sign  
14 up throughout the year of 1999 and thereby necessitating  
15 additional pro rata adjustments throughout that year?

16 A. We were envisioning that it would be done one  
17 time, that customers would nominate an amount of load during  
18 the subscription period, the company would aggregate that,  
19 determine whether there is an oversubscription and then make  
20 the adjustment. Otherwise, there would be too much  
21 uncertainty, I think.

22 Q. And to make that one-time adjustment work, there  
23 would need to be a firm cut-off for customers to sign up to  
24 participate in, in my example, the first phase of  
25 competition; is that right?

1           A.    Yes.  I believe, in order for it to work  
2 effectively, that would be the case.

3           MR. RUSSELL:  I have nothing else.  Thank you.

4           JUDGE KASHI:  Thank you very much, sir.

5           Redirect?

6           MR. KLEPPINGER:  Just briefly, Your Honor.

7                               REDIRECT EXAMINATION

8           BY MR. KLEPPINGER:

9           Q.    Mr. Baron, Mr. Russell asked you a few questions  
10 regarding an LP-5 customer that would transfer to Rate  
11 Schedule LP-4.  Do you recall that line of questioning?

12          A.    Yes.

13          Q.    And is it your understanding that LP-4 and LP-5  
14 are both firm rate schedules?

15          A.    Yes, that's correct.

16          Q.    So would the character of service that the  
17 customer is taking from PP&L change by moving from Rate  
18 LP-5 to LP-4?

19          A.    No, no.  Presumably, it would only be due to  
20 changes in some usage level, but the character of service  
21 would be identical.

22          Q.    And under PP&L's proposal in this case, would it  
23 be your testimony that by causing the customer to transfer  
24 from the IS-T or the IS-P rate schedule when they exercise  
25 their right of direct access to the LP-5 or LP-6 rate

1 schedule, that it would effectively be a change in the  
2 character of that customer's service?

3 A. Yes. The company would effectively reclassify  
4 that customer from interruptible to firm.

5 MR. KLEPPINGER: Thank you. That's all I have, Your  
6 Honor.

7 JUDGE KASHI: Thank you very much.

8 No follow-up on that?

9 (No response.)

10 JUDGE KASHI: You are excused, sir. Thank you very  
11 much.

12 (Witness excused.)

13 JUDGE KASHI: That which has been marked and  
14 identified as PPLICA Statement No. 1, 1-R, 1-S and the  
15 attendant exhibits, SJB-1 through 13, will be received into  
16 the evidentiary record, without objection?

17 (No response.)

18 JUDGE KASHI: Without objection.

19 (Whereupon, the documents marked as  
20 PPLICA Statements Nos. 1, 1-R and  
21 1-S and PPLICA Exhibits Nos. SJB-1  
22 through SJB-13 were received in  
23 evidence.)

24 JUDGE KASHI: Mr. Falk for PP&L? Do you wish to call  
25 your next witness?

1 (Pause.)

2 JUDGE KASHI: Let's take a minute.

3 (Pause.)

4 JUDGE KASHI: I have a question in my ever-increasing  
5 interest in settling this matter, because I would like to  
6 see competition come to Pennsylvania as quickly as possible.

7 The question is whether or not the parties who are  
8 having problems with themselves are talking as opposed to  
9 just the parties talking to PP&L.

10 I mean, from what I've seen in the testimony and what  
11 I've seen in some of the cross that's coming out, some of  
12 the parties have some problems between themselves I think  
13 that are causing ultimate problems to this Gordian knot, and  
14 I would hope that those parties are talking to each other as  
15 opposed to just thinking about this in terms of "us and  
16 PP&L." Enough said.

17 Would you raise your right hand and be sworn, sir?  
18 Whereupon,

19 JONATHAN S. FALK  
20 having been duly sworn, testified as follows:

21 JUDGE KASHI: Mr. Kaplan?

22 MR. KAPLAN: Thank you, Your Honor.

23 Your Honor, I would like to identify for the record  
24 PP&L Statement No. 20-R, the rebuttal testimony of Jonathan  
25 S. Falk, a statement of some 24 pages.

1 JUDGE KASHI: So marked for purposes of  
2 identification.

3 (Whereupon, the document was marked  
4 as PP&L Statement No. 20-R for  
5 identification.)

6 MR. KAPLAN: And I would also like to identify  
7 Exhibit JSF-1.

8 JUDGE KASHI: So marked for purposes of  
9 identification.

10 (Whereupon, the document was marked  
11 as PP&L Exhibit No. JSF-1 for  
12 identification.)

13 DIRECT EXAMINATION

14 BY MR. KAPLAN:

15 Q. Do you have any corrections in that testimony?

16 A. I do not.

17 MR. KAPLAN: Your Honor, at this time, PP&L would  
18 like to move for the admission into the record of PP&L  
19 Statement 20-R and Exhibit JSF-1.

20 JUDGE KASHI: Subject to any timely motions and/or  
21 objections, pending cross-examination, that which has been  
22 marked as PP&L Statement 20-R and Exhibit JSF-1 will be  
23 received into the evidentiary record.

24 MR. KAPLAN: Your Honor, we do have some rejoinder.

25 JUDGE KASHI: Short rejoinder?

1 MR. KAPLAN: Well, Your Honor, I don't want to  
2 characterize it as "short." It will not be the longest  
3 rejoinder we've had, but I think it will become obvious why  
4 I cannot characterize it as short when I begin the  
5 examination. It will not be lengthy, but I do not want to  
6 promise its being very short.

7 BY MR. KAPLAN:

8 Q. Good afternoon, Mr. Falk. Have you read Mr.  
9 Falkenberg's surrebuttal testimony?

10 A. Yes.

11 Q. Have you had the opportunity to examine Mr.  
12 Falkenberg's model?

13 A. Yes.

14 Q. When did you get Mr. Falkenberg's model?

15 A. One week after my rebuttal testimony was filed.

16 Q. Have you examined the various points you made in  
17 light of Mr. Falkenberg's surrebuttal and your study of his  
18 model?

19 A. Yes, I have. My rebuttal testimony contained  
20 five direct and two indirect criticisms of Mr. Falkenberg's  
21 model.

22 The direct criticisms involved his treatment of  
23 maintenance scheduling, capacity addition scheduling,  
24 repowering --

25 MR. KLEPPINGER: Just one moment. If we're going to

1 be reading, let's at least read slowly.

2 JUDGE KASHI: Okay.

3 THE WITNESS: Fair enough.

4 MR. KLEPPINGER: For me and the reporter.

5 JUDGE KASHI: It's getting late in the day, and our  
6 note-taking capacity diminishes.

7 THE WITNESS: Fair enough.

8 JUDGE KASHI: If you could just slow it down just a  
9 little.

10 THE WITNESS: Okay.

11 The direct criticisms involved his treatments of  
12 maintenance scheduling, capacity addition scheduling,  
13 repowering, unserved energy and unit sizes.

14 The indirect criticisms involved the non-commercial  
15 nature of his model and its failure to treat overbuilding  
16 appropriately. In no case do I believe Mr. Falkenberg's  
17 responses past muster.

18 BY MR. KAPLAN:

19 Q. Please start with his direct criticisms. How  
20 does Mr. Falkenberg reply to your complaint that his model  
21 treats maintenance improperly?

22 A. He makes two arguments. The first one is that  
23 maintenance is not as deferable as Dr. Jones and I make it  
24 out to be.

25 And this seems to me to miss the point that to the

1 extent maintenance is deferable, his model is obviously  
2 overstating prices. So we agree that the model is flawed.  
3 We now simply disagree on the impact.

4 In addition, I couldn't disagree more with his  
5 assumption about the impact of competition on maintenance  
6 scheduling.

7 The fact that it's scheduled now one way doesn't  
8 necessarily imply about how it will be scheduled in the  
9 future.

10 With all due respect to the operating history of the  
11 regulated people and the talented people in PJM, as my  
12 colleague, Fred Kahn, pointed out, if we knew where the  
13 savings were going to be before we went down this path, we  
14 could have just commanded that they occur.

15 The second argument he makes is that the effect is  
16 small. He does this, though, in a curious fashion. As you  
17 may recall, his model spreads maintenance over the nine  
18 months of the year that are outside of the 84 days in which  
19 PJM essentially forbids maintenance.

20 He says, "Well, I spread it out over the whole year  
21 and it didn't have much effect." What I wanted him to do  
22 was not crowd it that way but to crowd it further into the  
23 six months of the year encompassing the spring and the fall.

24 Indeed, the fact that the PJM winter peak is very  
25 close to the PJM summer peak suggests that that is really

1 not a very good way to test the proposition of whether or  
2 not this has a big impact, because in fact he is now going  
3 to push some maintenance into periods that are very close to  
4 the summer peak, anyway.

5 He is pushing them out of periods that were close to  
6 the summer peak, namely the winter peak, into the summer  
7 peak. So it's not a very good test of whether or not you  
8 could have done better scheduling maintenance by moving more  
9 and more of it into the spring and the fall. In any case,  
10 he acknowledges that his model mishandles maintenance.

11 Q. What about additions?

12 A. Mr. Falkenberg asserts that at his prices, no  
13 one will build new units in excess of the 18 percent reserve  
14 margins.

15 He still hasn't demonstrated that result. Indeed,  
16 there's ample evidence that Mr. Falkenberg's prices would  
17 lead to substantial new entry.

18 In fact, his capacity prices alone are virtually  
19 guaranteed to provide new entry. Even if we were to believe  
20 that the capital cost of new oil-fired CTs were fixed at a  
21 real \$300 a kilowatt, and using Mr. Falkenberg's real fixed  
22 charge rate, his capacity prices alone would guarantee a new  
23 entrant profits.

24 Q. Have you prepared an exhibit demonstrating this  
25 point?

1 A. Yes, I have.

2 MR. KAPLAN: Your Honor, at this time, we would like  
3 marked Exhibit JSF-2, a two-page document consisting of a  
4 chart and a graph.

5 JUDGE KASHI: So marked for purposes of  
6 identification.

7 (Whereupon, the document was marked  
8 as PP&L Exhibit No. JSF-2 for  
9 identification.)

10 MR. KAPLAN: It's actually a graph and a chart, not a  
11 chart and a graph.

12 BY MR. KAPLAN:

13 Q. Please proceed, Mr. Falkenberg.

14 A. The numbers that underlie the chart that's on  
15 page 1 are on page 2, but essentially the blue bars are the  
16 capacity prices out of Mr. Falkenberg's original testimony.  
17 The gray or brown bar are the capacity prices in his revised  
18 surrebuttal exhibit.

19 All I've done is compared them with a very simple  
20 calculation, which is to take a \$300 CT, assuming that the  
21 real fixed charge rate is 13.34 percent and that inflation  
22 is 3.11 percent, which are all from his testimony, and  
23 simply inflated that number out. And you can see it in the  
24 numbers inflated year by year.

25 On the second page, I've shaded in any year in which

1 the price for that capacity exceeds what in any real world  
2 application would have to be the maximum sustainable price  
3 of that capacity, because if it ever got over that number,  
4 someone could simply build or even rent a CT and make money.

5 So you can see certainly in his direct testimony and  
6 later in his surrebuttal, there are substantial periods of  
7 very high excess.

8 I just want to point out that in doing this this way,  
9 I'm giving no credit for energy at all. That is, I am  
10 assuming this unit absolutely never runs, so it never makes  
11 any money at all in the energy market. I have burdened it  
12 with a \$5.00 amount for fixed O&M, which I think is surely  
13 adequate in this world and is definitely adequate in the  
14 future world with increased improvements.

15 I've assumed no technical progress at all, and I'm  
16 giving Mr. Falkenberg in this calculation his inflation rate  
17 for where these prices are going.

18 Q. This exhibit covers combustion turbines. What  
19 about combined cycle units?

20 A. Well, Mr. Falkenberg indicates in his original  
21 testimony that he adds, whichever is cheaper, combined  
22 cycles or combustion turbines.

23 Since in the original testimony he only added  
24 combined cycle units, now he does add combustion turbines at  
25 some periods early, although he says later he only adds

1 combined cycle units.

2 Since combined cycle units are cheaper by his lights  
3 than combustion turbines, if combustion turbines are making  
4 money, combined cycles must be making lots and lots of  
5 money.

6 Q. What about his comments on repowering?

7 A. Well, he makes two assertions. The first one is  
8 that repowered plants are probably inferior to new plants in  
9 energy costs, and his second point is that if repowering is  
10 a good option, it should be a good option at the PP&L  
11 retired units.

12 Well, the first point I think is just misguided. The  
13 question is not whether repowered units are inferior to new  
14 units. I think they probably are.

15 After all, Mr. Falkenberg adds the same number of  
16 units in his model whether a unit is repowered or not.  
17 What's important is that repowering lowers the energy cost  
18 of existing units, a proposition which is of course  
19 undeniable, and lowering the cost of existing units would  
20 lower the marginal energy prices in Mr. Falkenberg's model.

21 Consequently, he has to agree that his prices are  
22 overstated and, further, there's no clear indication that  
23 repowering would lower stranded costs significantly for the  
24 PP&L unit.

25 After all, to repower, you have to invest new

1 dollars, new dollars that aren't covered by any stranded  
2 charges or anything like that, and you have to earn all that  
3 money back before you make any cutback in the stranded cost  
4 number.

5 Finally, for PP&L's case specifically, most of PP&L's  
6 stranded costs aren't in units that anybody can repower. I  
7 mean, nobody thinks you can repower, for example, the  
8 Susquehanna station. The stranded costs lie in other things  
9 like the NUG contracts, it lies in regulatory assets which  
10 are simply not subject to any of these repowering  
11 advantages.

12 Q. Now, how about his comments on unserved energy?

13 A. Well, first, Mr. Falkenberg concedes the force  
14 of the point because he re-estimates his model and drops the  
15 amount of unserved energy by 20-fold.

16 He then claims that the effect of this is negligible  
17 because I ignored the dynamic nature of his modeling, and he  
18 describes this by saying that a reduction in the peak price  
19 of energy simply results in a nearly countervailing increase  
20 in the price of capacity.

21 But if you'll compare his result, you'll see no such  
22 effect is actually going on when he actually does this.  
23 Note what happens. In fact, his capacity prices are even  
24 lower than they were in the original run that he did, and  
25 his energy prices are actually no lower at all. So I'm not

1 exactly sure how he's claiming to get to where he's going  
2 from what he says he's doing.

3 Furthermore, it couldn't work that way. Remember,  
4 his capacity payments are essentially already at the limit  
5 of where they could go.

6 If we lower the price that energy receives, there  
7 can't be a countervailing ability to raise capacity prices  
8 because they should be limited by the \$300 oil-fired CT.

9 When we lower the price of energy in the top 100  
10 hours by altering the supply conditions and nothing else,  
11 somehow mysteriously the off-peak energy prices somehow are  
12 seeming to rise because we're getting back to the same price  
13 result we were getting to before. I simply can't think of a  
14 reasonable explanation for that result.

15 Q. Could you now turn to his indirect criticisms?  
16 What about your claim that non-commercial models are  
17 untrustworthy?

18 A. Well, first Mr. Falkenberg says that the  
19 simplicity of his model is a virtue, and he's right, but  
20 only so long as his model doesn't contain biases.

21 I guess my view on this is, complexity is needed  
22 where it's needed, and that simple isn't a substitute for  
23 accurate.

24 But next, he defends his model on the grounds that  
25 commercial models have been run badly by PECO and that

1 West Penn used a model with logic errors.

2 And I certainly admit that using an accurate model  
3 badly is no substitute for using an inaccurate model well,  
4 although the proof is in the pudding. Obviously, it could  
5 come out either way. Since both sides are making errors,  
6 it's just a question of which one wins.

7 I'll also concede that it's impossible to demonstrate  
8 that any model, EGEAS, Mr. Falkenberg's or anybody else's,  
9 doesn't contain errors. They almost surely do contain some  
10 errors that we just haven't found yet. But since this does  
11 include Mr. Falkenberg's model, I don't think I'm conceding  
12 too much.

13 Next, he contrasts the crucible of competition, which  
14 was my phrase, with the trial by ordeal. And if  
15 Mr. Falkenberg weren't so wedded to the regulatory process,  
16 he'd know how poorly regulation fares in this comparison.

17 I've sold dispatch models commercially, and  
18 differences in dispatch and the price and the commitment of  
19 units that would be glossed over in two seconds in a  
20 regulatory proceeding lead to weeks of meetings, rewrites,  
21 your model against my model out in the real world, in a  
22 never-ending process because it doesn't have deadlines or  
23 time limits, and people are sitting there with as much  
24 knowledge as you have about the problem, sitting there  
25 questioning you for weeks about what's going on.

1 I just don't think, with all due respect to the  
2 regulatory process, that it matches the crucible of  
3 competition, if that's the test that we want to set up.

4 Next, he gives us the bottom line of a number of  
5 benchmarking studies. All of his benchmark studies which he  
6 presents here are I think completely inadequate, because I  
7 think, at least as I can tell, all of them seem to be based  
8 on the total production cost of the system.

9 And it's true he gets those to within a percent or  
10 so, but I think virtually any model will get total  
11 production costs within a percent or so.

12 After all, you have so many units out there. A lot  
13 of them are base load units. You know exactly how much  
14 they're going to cost, so you're going to get those exactly  
15 right.

16 And so to get just the total production cost  
17 percentage right is I think just not a very interesting  
18 exercise or test of a model, and he admits that because he  
19 goes through his next three pages talking about how the  
20 right thing to predict is marginal costs, and I agree with  
21 him completely there.

22 JUDGE KASHI: Before you go any further, I want to  
23 take the afternoon recess at this particular point. It's  
24 3:00. We'll return at 3:15.

25 MR. KLEPPINGER: Your Honor, we will most likely need

1 a break to prepare cross on this extensive rejoinder.

2 JUDGE KASHI: I understand that.

3 MR. KLEPPINGER: And I would also request at this  
4 time that, prior to the initial break that you asked that we  
5 take now, that we be provided a copy of the written  
6 materials that Mr. Falk is clearly reading from.

7 JUDGE KASHI: It doesn't make sense for you not to  
8 have it. Could we get it? The man's got, what, 20 pages  
9 there in front of him?

10 MR. KAPLAN: No, not quite. It's very widely spaced.

11 THE WITNESS: It was seven when I wrote it.

12 MR. KAPLAN: And we will make an effort to produce a  
13 clean copy of the material for Mr. Kleppinger.

14 JUDGE KASHI: Can we do that now, and then I can just  
15 add to the recess and we can go until 3:30, and then you  
16 won't have to take another one, Mr. Kleppinger?

17 MR. KLEPPINGER: I'm not sure what's left.

18 MR. KAPLAN: We are close to the end. We probably  
19 have about another five minutes.

20 MR. KLEPPINGER: If there's not much left, a  
21 half-hour should be adequate, Your Honor.

22 JUDGE KASHI: We will recess for a half-hour. You're  
23 going to get a copy for him of what he's got. We'll come  
24 back and finish the five minutes. So we stand in recess  
25 until 3:30.

1 (Recess.)

2 JUDGE KASHI: Going back on the record.

3 Mr. Kaplan, do you want to continue with your  
4 rejoinder of Mr. Falk?

5 MR. KAPLAN: Thank you, Your Honor.

6 BY MR. KAPLAN:

7 Q. Mr. Falk, what about Mr. Falkenberg's  
8 benchmarking of CTs and other marginal units with actual  
9 usage in 1995?

10 A. There are three fundamental errors with his  
11 approach. First, he criticizes EGEAS for failing to produce  
12 power from units which will in fact be retired by 1999.

13 Second, he uses one year without any notion of  
14 whether that year was typical, and without fully  
15 investigating the situation, I conclude that it's not.

16 Third, he defends the dispatch of those units without  
17 any notion of whether or not the dispatch was optimal or in  
18 merit order.

19 To the first point, Cromby 2, Delaware 7 and 8 and  
20 the Schuylkill 1 units are scheduled for pre-1999  
21 retirement. What's surprising is that Mr. Falkenberg  
22 projects profitable operations from units which system  
23 planners have decided are not worth the effort.

24 Second, the particular outage pattern and weather  
25 patterns for 1995 determine the system characteristics for

1 1995.

2 Nineteen ninety-five was a hot year, and capacity  
3 factors for almost all the units he cites were much lower in  
4 1991 than in 1995. And I certainly don't have any way of  
5 figuring out which one is more typical.

6 In addition, some of those plants may have operated  
7 for local reliability reasons, which would make the  
8 Falkenberg results just fortuitous.

9 Third, a competitive functioning spot market should  
10 simply have better overall results through its open access  
11 and ability to bring in other supplies when it's needed,  
12 which is already an adjustment Mr. Falkenberg claims to have  
13 made. Benchmarking just isn't as easy as Mr. Falkenberg  
14 contends it is.

15 Q. What about his overbuilding points?

16 A. I don't think he has given any substantive  
17 answer. First he says that my colleague Lou Guth's  
18 wait-and-see metric means there won't be any overbuilding,  
19 and I think he's just wrong about that.

20 Second, he says that overbuilding probabilities, if  
21 it actually happens, would simply raise the discount rate,  
22 increasing the price of power.

23 And he's right about the discount rate effect, but I  
24 think he's wrong about whether or not it will increase the  
25 price of power.

1           And finally, he insists that overbuilding  
2 probabilities are symmetric without any consideration of the  
3 mechanism which I proposed.

4           Q.    Please explain.

5           A.    Well, investments in real options, which is what  
6 Mr. Guth's testimony is about, do increase discount rates,  
7 that is people have hurdle rates for projects in excess of  
8 their cost of capital, and we all agree on that.

9           But once a unit is constructed, the capital costs are  
10 sunk and form no part of the market price. This is very  
11 similar actually to the heat rate issue. Once committed,  
12 the marginal and not the average heat rate determines the  
13 price.

14           What still hasn't been demonstrated anywhere that  
15 I've seen is that an equity investor, even with hefty  
16 discount rates, wouldn't construct merchant plant if he  
17 believed Mr. Falkenberg's estimates or in fact believed  
18 estimates higher than Mr. Falkenberg's estimates.

19           If Mr. Falkenberg believes his estimates are  
20 unbiased, then if we had independent analysts out there  
21 looking at the answer of, what are market prices, then half  
22 of them ought to find market prices higher than Mr.  
23 Falkenberg and half of them lower.

24           Even if Mr. Falkenberg is absolutely right on  
25 average, all the people who are convinced that the prices

1 are going to be higher have no reason not to go out there  
2 and build.

3 Of course, when they do so, there will be too much,  
4 even if Mr. Falkenberg's projection of demand and things  
5 like that happen to be right.

6 Once too much capacity is out there, we find  
7 ourselves exactly back in the situation we're in right now:  
8 overcapacity, too much capacity chasing too little load, and  
9 capacity prices drop to a floor which is roughly equal to  
10 the fixed O&M of a plant.

11 Of course, when that happens, some investors are  
12 going to lose money. But of course, some investors losing  
13 money is exactly what the high hurdle rate point was about.

14 The high hurdle rate is sort of a penalty for your  
15 optimism. It suggests that once everything shakes out, on  
16 average, after the things that work out and the things that  
17 don't work out all average out, you'll be right back to the  
18 expected rate of return that you started with in the first  
19 place.

20 Note, there's no corresponding problem on the down  
21 side. Those 250 analysts who found price lower than  
22 Mr. Falkenberg's just didn't build anything. When they  
23 didn't build anything, there was no symmetric problem.

24 There's always people who are going to be more  
25 optimistic than the average, and they're going to be the

1 ones building. The ones less optimistic than the average  
2 just aren't in the problem.

3 Q. Does this complete your rejoinder testimony?

4 A. Yes, it does.

5 MR. KAPLAN: Thank you, Your Honor. At this time, we  
6 would like to move into the record Exhibit JSF-2.

7 JUDGE KASHI: Subject to any timely motions and/or  
8 objections made, pending cross-examination, it will be  
9 received into the evidentiary record.

10 MR. KAPLAN: Thank you, Your Honor. Mr. Falk is  
11 available for cross-examination.

12 JUDGE KASHI: Mr. Kleppinger?

13 MR. KLEPPINGER: Thank you, Your Honor.

14 CROSS-EXAMINATION

15 BY MR. KLEPPINGER:

16 Q. Good afternoon. My name is David Kleppinger and  
17 I represent the PP&L Industrial Customer Alliance.

18 Now, Mr. Falk, you only submitted rebuttal testimony  
19 in this case, correct?

20 A. That's correct.

21 Q. At what point were you retained by PP&L for  
22 purposes of this proceeding?

23 A. It was sometime in the middle of July.

24 Q. Which would have been after the preparation and  
25 filing of PP&L's direct case in this proceeding?

1 A. I assume so.

2 Q. Now, you I believe reference in your testimony  
3 that NERA, the company that you work for, also has an  
4 electric market model.

5 A. They do.

6 Q. And was that model utilized by PP&L in this  
7 proceeding?

8 A. No.

9 Q. Is that a commercially available model?

10 A. Absolutely.

11 Q. So it can be purchased from NERA?

12 A. Absolutely.

13 Q. What's the cost of purchasing the NERA electric  
14 model?

15 A. We have not really settled on the firm price.  
16 We've sold it now three times, and we sort of customize the  
17 price to what it looks like the people want to use it for.  
18 It's different if you want to use it in-house or you want to  
19 let us run it. It depends on how much service we give you  
20 with it.

21 I can't really give you a price. I just can't give  
22 you one, I guess.

23 Q. If we would have wanted to use it in this  
24 proceeding as PPLICA, what kind of price would you have  
25 offered it to us for?

1           A.    You only want to use it for this proceeding and  
2 didn't want to keep it thereafter?

3           Q.    Right.

4           A.    Oh, probably \$150,000.

5           Q.    Now, does the NERA electric model determine the  
6 market price of capacity based on the modeling itself?

7           A.    Yes.

8           Q.    And would the NERA model employ the analyst's  
9 judgment in modifying the market price for capacity that's  
10 produced by the model?

11          A.    They would if they were projecting competitive  
12 market prices, but I mean, I would suggest that any analyst  
13 not use the raw output, if that's what you're saying.

14                But it will produce an output that someone could use  
15 as the price of capacity.

16          Q.    My point is whether it would produce the output  
17 for market price capacity. You're saying it would?

18          A.    It would produce such a price.

19          Q.    To your knowledge, does the NERA electric market  
20 model develop the mathematical relationship between market  
21 energy prices and market capacity prices?

22          A.    I don't know what you mean by the question.  
23 There is a relationship. It's embedded in the equations  
24 that are in the model.

25          Q.    That's the right answer. Whether the question

1 was right or not, that was the answer I was wanting to hear.

2 Would you expect that the NERA electric market model  
3 would produce market prices that are sufficient to justify  
4 capacity additions when they are needed by having the prices  
5 at least cover the cost of that new capacity?

6 A. In the NERA model, all capacity -- I'm sorry.  
7 The prices that come out of the NERA market model are such  
8 that no additional capacity is justified.

9 Q. So, from that, can I conclude that the model  
10 then produces a result that is always at optimum?

11 A. When I run it right.

12 Q. Would you agree with me that if a model is  
13 demonstrated to have flaws which clearly tend to understate  
14 the level of future prices and thus overstate the amount of  
15 stranded cost, that the Commission should view that model as  
16 inappropriate for use in the case?

17 A. I think that to the extent that those biases  
18 can't be corrected, sure.

19 Q. I'd like to turn to Exhibit JSF-2. As capacity  
20 would be added, would you agree that the price in the market  
21 should decline?

22 A. Not necessarily.

23 Q. If there is excess capacity in the system, why  
24 would price not decline?

25 A. Well, if there is excess capacity in the system,

1 going from no excess capacity to excess capacity would  
2 definitely lead to a decline in prices.

3 Q. Now, I'm trying to understand the sources of the  
4 data that you've included in JSF-2, and the column that  
5 you've labeled "Direct 1", that was extracted directly from  
6 Mr. Falkenberg's direct testimony?

7 A. That's correct.

8 Q. And the column labeled "Surrebuttal 2" was  
9 extracted directly from Mr. Falkenberg's surrebuttal  
10 testimony as revised?

11 A. That's correct.

12 Q. Now, the column that's labeled "Maximum  
13 Sustainable", how was that column computed?

14 A. Again, the first number in there is 300 times  
15 .1334 plus 5. Every subsequent column is the column before  
16 it -- every subsequent row is the row before it times  
17 1.0311.

18 Q. And the 300 per kW number was taken from  
19 Mr. Falkenberg's prior testimony, correct?

20 A. That's correct, as was the .1334 and the 3.11.

21 Q. Now, the number that would not have been would  
22 have been the, I believe you called it \$5.00 assumption for  
23 fixed O&M on a combustion turbine; is that correct?

24 A. That's correct.

25 Q. Now, as part of the preparation for this case,

1 you had reviewed, had you not, the EGEAS runs that were  
2 provided by PP&L to support its claim in the case?

3 A. I talked to people about those runs. I  
4 certainly didn't review the runs myself.

5 Q. Do you know what the assumed O&M, fixed O&M on a  
6 combustion turbine assumption was for purposes of Dr. Jones'  
7 utilization of the EGEAS runs?

8 A. I do not.

9 Q. Would you agree subject to check that the  
10 assumed fixed O&M for a CT was \$9.00 per kW in the EGEAS  
11 runs?

12 A. That's certainly possible.

13 Q. If in fact the \$9.00 was used, would that mean  
14 that the maximum sustainable column in Exhibit JSF-1 would  
15 be, at least in the first year, \$4.00 higher than what you  
16 have included in your exhibit?

17 A. To the extent that it's correct, that would be  
18 true in 1997.

19 Q. And would you agree that if we then ran that out  
20 beginning with \$49.02 in 1997 with the same escalations that  
21 you have employed, that the maximum sustainable column would  
22 always be sufficient to cover the costs of capacity shown in  
23 the first two columns?

24 A. I guess I would say I haven't done that  
25 calculation, and I wouldn't think that would be the right

1 calculation, but it might come to that result.

2 Q. And the reason you wouldn't think it right, you  
3 would dispute what the fixed O&M number should be? You used  
4 five and the EGEAS runs used nine?

5 A. That would be a reason, yes.

6 Q. Now, do you know what the fixed O&M assumption  
7 for a CT was that was used by Mr. Falkenberg in the  
8 preparation of his surrebuttal and direct testimony?

9 A. I was not certain, no.

10 Q. Would you agree, subject to check, that Mr.  
11 Falkenberg's starting point for 1997, instead of \$45.02, was  
12 \$46.94?

13 A. That may be.

14 Q. Will you agree to that subject to check?

15 A. I'll agree to anything subject to check.

16 Q. And if you then escalate the \$46.94, again under  
17 the same assumptions that you have escalated the \$45.02,  
18 would you agree with me that the maximum sustainable column,  
19 again subject to check, would be sufficient to support the  
20 investments in capacity as shown in the "Direct 1" column  
21 and the "Surrebuttal 2" column on Exhibit JSF-2?

22 A. I guess what I would want to do, before I did  
23 that, if that happened, I guess I'd then want to investigate  
24 a lot further.

25 I'd then want to start to look at what the energy

1 savings were out of these units. I'd then start to look at  
2 other questions like, if that's true, how come these aren't  
3 the units that are being added? How come you're adding CCs  
4 which are even cheaper than that?

5 But if all that were true -- that could well be true,  
6 but that's just the analytical path I'd begin to go down.

7 Q. Okay. But in terms of the integrity of this  
8 model that's been used and the assumptions you have used to  
9 prepare JSF-2, would you agree that the model maintains its  
10 integrity in the sense that the maximum sustainable column  
11 would be sufficient to support the investments in capacity?

12 A. There is a fixed O&M number that will justify  
13 any maximum sustainable -- that will justify any set of  
14 capacity prices.

15 Q. And you agree that either the EGEAS number of  
16 \$9.00 or the Falkenberg number that begins, the total number  
17 is \$46.94, would be sufficient to do that, again subject to  
18 check?

19 A. Subject to check.

20 MR. KLEPPINGER: Thank you, Mr. Falk. That's all the  
21 questions I have.

22 JUDGE KASHI: Thank you very much, Mr. Kleppinger.

23 Mr. Caplan?

24 MR. CAPLAN: I have no questions, Your Honor.

25 JUDGE KASHI: That works for me.

1 Redirect?

2 MR. KAPLAN: If we could just have a minute, Your  
3 Honor?

4 JUDGE KASHI: Surely.

5 (Pause.)

6 JUDGE KASHI: On the record.

7 Redirect, sir?

8 MR. KAPLAN: Your Honor, we don't have copies of  
9 this, but I would like the following exhibit -- we will  
10 supply copies -- marked Exhibit RJF-3. I'm going to  
11 describe it. I wanted to show it to counsel.

12 It is Pennsylvania Power & Light Company Response to  
13 Interrogatories of the Office of Consumer Advocate, Set III,  
14 corrected response, July 25, 1997, No. 74.

15 JUDGE KASHI: So marked for purposes of  
16 identification.

17 (Whereupon, the document was marked  
18 as PP&L Exhibit No. JSF-3 for  
19 identification.)

20 MR. KLEPPINGER: Might I review it?

21 MR. KAPLAN: It should be JSF-3, not RJF.

22 REDIRECT EXAMINATION

23 BY MR. KAPLAN:

24 Q. Now, Mr. Falk, having reviewed that  
25 interrogatory answer, could you tell us what fixed cost

1 charge was used in the EGEAS runs?

2 A. It appears that \$5.28 was used.

3 Q. Does the figure of \$9.00 appear on that  
4 interrogatory answer?

5 A. It does, but it applies to a combined cycle  
6 unit.

7 Q. Thank you. Now, Mr. Falk, to the extent that a  
8 model consistently overstates the price of energy and  
9 thereby understates stranded costs, it should also be  
10 rejected by the Commission; do you agree with that  
11 statement?

12 A. Absolutely.

13 Q. Now, you were asked about when you were  
14 retained. Do you recall when the direct testimony of  
15 intervenors was filed in this case?

16 A. I just don't know.

17 Q. Will you accept subject to check it was filed on  
18 July 2, 1997?

19 A. I have no reason to doubt it.

20 Q. Do you understand why you were retained?

21 A. Yes, I do. I was retained to look at the  
22 Falkenberg model which PP&L had not previously seen and was  
23 unfamiliar with.

24 Q. Do you understand that another model has been  
25 used in this case by intervenors?

1 A. Yes, ENPRO.

2 Q. And do you understand why your assignment was  
3 limited to the Falkenberg model rather than the ENPRO model?

4 A. Yes, because the ENPRO model is a commercially  
5 derived model that I think people have broad familiarity  
6 with and could be purchased and exercised, and nobody wanted  
7 to pay me to do that.

8 MR. KAPLAN: Thank you. That's all the redirect we  
9 have, Your Honor.

10 JUDGE KASHI: Thank you very much.

11 MR. KLEPPINGER: Just a little, Your Honor.

12 JUDGE KASHI: Excuse me?

13 MR. KLEPPINGER: I need to cross on the additional  
14 exhibit.

15 JUDGE KASHI: Yes, sir.

16 RE-CROSS-EXAMINATION

17 BY MR. KLEPPINGER:

18 Q. Now, earlier, Mr. Falk, you indicated that you  
19 had not reviewed the detail of the EGEAS runs performed in  
20 this case and submitted through the testimony of Dr. Jones;  
21 is that correct?

22 A. That is still correct.

23 Q. So while this exhibit that has been identified  
24 indicates that the fixed O&M charge of \$9.00 per kW was  
25 applied to combined cycles as opposed to combustion

1 turbines, you have not verified whether in fact the EGEAS  
2 runs that were provided in this case used the \$9.00 for both  
3 the combined cycle and the combustion turbine?

4 A. No. If they used the \$9.00 for the combustion  
5 turbine, they overstated the market prices and will have  
6 understated stranded costs, and that's I guess an error  
7 they'll have to live with.

8 Q. And you did not review the EGEAS runs to verify  
9 that in fact they did that; is that correct?

10 A. No, I didn't.

11 Q. And in your review of Dr. Jones's corrected  
12 response which is OCA Set III-74, this response in and of  
13 itself does not indicate, does it, Mr. Falk, that the \$5.28  
14 fixed O&M for CTs was in fact used in the EGEAS runs?

15 A. Again, whatever rate was used in the EGEAS runs,  
16 it seems to me, if it was \$5.00, they were probably pretty  
17 close to right. If it was \$9.00, then they understated  
18 stranded costs. I don't know what they in fact did, though.

19 MR. KAPLAN: Your Honor, Mr. Kleppinger's question is  
20 correcting the veracity of the interrogatory answer  
21 submitted by Pennsylvania Power & Light Company.

22 First of all, this witness is not in a position to  
23 ascertain or confirm that. Secondly, I believe a little  
24 statement of some of the history of the procedures in this  
25 case of what happened with respect to the data submitted by

1 PP&L might elucidate on this problem.

2 We, as Your Honor understands and recalls, we  
3 submitted a protective order to Your Honor for signature.  
4 In order to give the parties confidential information as  
5 soon as possible, we voluntarily agreed to treat an  
6 agreement to follow that order if parties signed the  
7 protective order and the agreement and submitted the  
8 certificates called for under the protective order.

9 JUDGE KASHI: I understand.

10 MR. KAPLAN: We did not receive such certificates  
11 from anybody, either expert or client or counsel, from  
12 PPLICA until well into July, and I believe it was after this  
13 July date.

14 We then provided them all of the information. I  
15 think, to the extent that PPLICA perhaps went on the  
16 original interrogatory answer and not the corrected one is  
17 not our fault. It is their fault for not responsively  
18 signing the protective agreement and obtaining the  
19 information as it came.

20 Certainly this witness can add nothing to this  
21 subject. And also, to the extent that Mr. Kleppinger  
22 believes that we have made runs using one number and  
23 answered an interrogatory with another number, I would like  
24 him to state what proof he has on the record, and to make an  
25 offer of that proof and we can deal with that issue.

1 MR. KLEPPINGER: Very well. We will be pleased to do  
2 that. We have the disk that was provided under the  
3 confidentiality order that clearly shows that the \$9.00 was  
4 used in the EGEAS run. Now, if we want to play this game,  
5 let's play it. Otherwise, let's get the right answer on the  
6 record and identify that the fixed O&M charge that was used  
7 in the EGEAS runs that form the basis of the market prices  
8 in this case was \$9.00 for the CTs.

9 JUDGE KASHI: So we have a conflict here.

10 MR. KAPLAN: It has nothing to do with this witness.

11 JUDGE KASHI: I understand.

12 MR. KLEPPINGER: You supplied this as an exhibit for  
13 this witness, so it does --

14 MR. KAPLAN: Because you suggest in your --

15 JUDGE KASHI: Gentlemen --

16 MR. KLEPPINGER: You've put it into the record with  
17 this witness, not with Dr. Jones.

18 JUDGE KASHI: I understand that. So the question is,  
19 how do we get the right number into the record without this  
20 witness. And I'm suggesting that we bring, is it Dr. Jones,  
21 back.

22 MR. KAPLAN: Well, the question, Your Honor, is not  
23 so much what's on that disk. The question is how PPLICA  
24 handled the information they were provided.

25 JUDGE KASHI: No, I don't think so. I think it's

1 what information was provided to them.

2 MR. KAPLAN: I think the answer is what runs were  
3 done in EGEAS, not how they -- they got information and we  
4 made corrections and they got additional information. How  
5 they handled and monitored that information is the issue,  
6 and we cannot be responsible for how they handle that  
7 information. We can only be responsible for the runs  
8 actually used in EGEAS.

9 They may have gotten that information and they may  
10 have subsequently gotten that correction and did nothing  
11 about it.

12 MR. KLEPPINGER: The point, Your Honor, is to try to  
13 get in the record of this case the right answer. And the  
14 right answer is, which fixed O&M number was used in the  
15 EGEAS runs that form the basis of the market prices -- that  
16 is one of the key issues in this case -- for the combustion  
17 turbines.

18 JUDGE KASHI: I agree, Mr. Kleppinger. So how do we  
19 do that?

20 MR. KAPLAN: We will go back and check what we did,  
21 and we would also like to -- we may have to do a little  
22 discovery as to PPLICA's treatment of the discovery that has  
23 been provided to them.

24 JUDGE KASHI: Mr. Kleppinger, your suggestion for  
25 getting it in, sir?

1 MR. KLEPPINGER: We can provide what we received as a  
2 response to OCA Set III, No. 75, which came subsequent to  
3 the OCA-III-74, that tells us that the \$9.00 was used in the  
4 EGEAS runs that form the market prices in this case for  
5 PP&L's case. We can use Mr. Falkenberg to do that.

6 MR. KAPLAN: Well, the first thing we can do, Your  
7 Honor, is we can make a copy of that diskette.

8 MR. KLEPPINGER: We got it from you, so you would  
9 have it, but --

10 MR. KAPLAN: No. We want a copy of that diskette  
11 right now, without putting it in the computer again.

12 JUDGE KASHI: Wait, wait, wait.

13 MR. KLEPPINGER: I don't want to violate any of the  
14 protective agreement that this was provided to Mr.  
15 Falkenberg under.

16 JUDGE KASHI: That's what -- I'm trying to figure  
17 this one out.

18 MR. KAPLAN: The company can make a copy of the  
19 company's own confidential information that it provided, and  
20 we will be happy to put it right in that computer and make a  
21 disk copy of that diskette.

22 JUDGE KASHI: Mr. Kleppinger, do you understand that?

23 MR. KLEPPINGER: I'm sorry, I missed that, Your  
24 Honor. I apologize.

25 JUDGE KASHI: What Mr. Kaplan is proposing, to not

1 violate the confidentiality, is to take the diskette right  
2 this minute, put it in their computer, and make a copy right  
3 here, this minute, period.

4 MR. KLEPPINGER: That's fine.

5 JUDGE KASHI: Does that work for you?

6 MR. KLEPPINGER: Yes.

7 JUDGE KASHI: Okay. All right, Mr. Kaplan.

8 For God's sakes, don't anybody erase that.

9 (Laughter.)

10 MR. KLEPPINGER: Let the record show, Your Honor,  
11 that I am providing to counsel for PP&L a disk that we were  
12 provided as OCA Set III, Question 75-A.

13 MR. KAPLAN: Well, let's do it -- we don't want to  
14 hold up the proceeding while we're doing it. I would just  
15 ask that the diskette not be -- we can keep it out here and  
16 we can do it at the adjournment, provided this is not placed  
17 in a computer again, if that's agreeable to Mr. Kleppinger.

18 JUDGE KASHI: You lost me there. You want to hold on  
19 it, don't put it into the computer until --

20 MR. KAPLAN: Well, I don't want to hold the  
21 proceedings up while we do this.

22 JUDGE KASHI: How long are we talking about, two  
23 seconds?

24 MR. KAPLAN: No, we're talking probably more, about  
25 three or four minutes to do it properly.

1 JUDGE KASHI: Let's do it properly. Let's do it now.  
2 I don't want that laying around anywhere. We'll take a  
3 recess for the three minutes that's necessary to make that  
4 copy.

5 (Recess.)

6 JUDGE KASHI: Back on the record.

7 There have been various proposals that have been made  
8 by the parties since the disk which was provided has been  
9 copied by the company and there appears to be the inability  
10 to match the files. There are proposals as to how to handle  
11 the evidentiary problem created by this, specifically as to  
12 what numbers in fact were used in the runs. The company is  
13 proposing to provide further information to substantiate  
14 what in fact they believe was used in the runs, and at this  
15 time Mr. Kleppinger is objecting to the piece of evidence,  
16 the interrogatory that was submitted by PP&L as a cross-  
17 examination exhibit -- I forget what it was.

18 MR. KAPLAN: Mr. Kleppinger made the objection, and,  
19 Your Honor, if I may rise to the objection?

20 JUDGE KASHI: Sure.

21 MR. KAPLAN: Mr. Falk testified that the number of  
22 \$5.00 was his own independent judgment because he could not  
23 find Mr. Falkenberg's number, and he chose a number that he  
24 felt was reasonably appropriate to use, and he based his  
25 analysis on that number. That was his testimony.

1 JUDGE KASHI: I'm going to sustain the objection  
2 before you go any further, counsel. I'm going to sustain  
3 the objection because I think that we can do this in a much  
4 cleaner way than trying to do it with this particular piece  
5 of paper that's going to create just an untoward burden in  
6 the record to begin with and divert our attention from  
7 what's really going on, and that is the point of what's the  
8 O&M that was used in the EGEAS runs, and that's the only  
9 thing. I don't want to get into who struck John and who  
10 said this and who said that. That's why I think if we leave  
11 that out, we're going to be better off.

12 MR. KAPLAN: Your Honor, I don't want to argue too  
13 long, but I think there is an important issue here. The  
14 issue is not for this witness' testimony, what was in the  
15 runs, the issue of this witness' testimony is whether the  
16 runs made by Mr. Falkenberg were reasonable. That's the  
17 sole issue this exhibit went to. This exhibit goes to that  
18 issue. He testified that when he tested those runs against  
19 some very simple assumptions with data he either took from  
20 Mr. Falkenberg or provided himself, without reference to the  
21 company's data, that those tests -- against those tests, Mr.  
22 Falkenberg's model showed problems. That was the sole issue  
23 here. The issue is not the company's runs, the issue is Mr.  
24 Falkenberg's runs. He's a rebuttal witness on Mr.  
25 Falkenberg. He did not review EGEAS. He did not seek to

1 take data from EGEAS. He sought to take data either from  
2 Mr. Falkenberg or, where he could not find that data, his  
3 own judgment. It solely goes to Mr. Falkenberg's model, it  
4 does not go to the company's model, and that's the only  
5 purpose for which it's offered. We are perfectly happy to  
6 stipulate that we are not offering it to support any of the  
7 company's information, simply as an exhibit directed toward  
8 Mr. Falkenberg's model.

9 JUDGE KASHI: So you're saying that you're not  
10 offering it for the truth or veracity of the information  
11 that in fact is contained therein, but merely for the  
12 judgment that Mr. Falk made on Mr. Falkenberg's runs based  
13 on that?

14 MR. KAPLAN: Right. It goes totally to the operation  
15 of Mr. Falkenberg's model and the exercise of judgment that  
16 Mr. Falkenberg made. That is the sum total of that exhibit.  
17 It is a narrow exhibit. It has nothing to do with the truth  
18 of a \$5.00 charge within the company's runs at all.

19 JUDGE KASHI: Mr. Kleppinger.

20 MR. KLEPPINGER: Your Honor, if counsel is willing to  
21 stipulate that the fixed O&M number for combustion turbines  
22 that was utilized to prepare JSF-2 is in fact lower than the  
23 fixed O&M charge rate that Mr. Falkenberg used for CTs and  
24 that the company used in its EGEAS runs, I have no objection  
25 to this exhibit.

1 MR. KAPLAN: Can you restate the request? Can you  
2 restate that, repeat it?

3 MR. KLEPPINGER: Sandy, give it a shot.

4 (Whereupon, the reporter read from the record, as  
5 requested.)

6 MR. KAPLAN: If I may have 30 seconds, Your Honor?

7 JUDGE KASHI: Sure.

8 (Pause.)

9 MR. KAPLAN: Your Honor, we are willing to, in a  
10 counter offer, stipulate that the exhibit does not speak to  
11 the numbers used in EGEAS, it only speaks to Mr. Falk's  
12 evaluation of Mr. Falkenberg's model. I will state for the  
13 record, Your Honor, that we have never received any  
14 information in Mr. Falkenberg's output runs as to what  
15 prices he was using for CT, and that is one of the problems;  
16 we have absolutely no clue.

17 MR. KLEPPINGER: That's not good enough, Your Honor,  
18 because at the meeting held July 18 with Mr. Falk and with  
19 representatives from ERG, that information was available and  
20 not requested on site. Secondly, the purpose of this  
21 exhibit is to discredit Mr. Falkenberg's model. I  
22 understand the purpose; I think we all understand the  
23 purpose. However, an O&M assumption was used by Mr. Falk to  
24 create this exhibit. That O&M assumption is different and  
25 lower than that used by Mr. Falkenberg and that used by the

1 company in the EGEAS runs to support their market prices.  
2 That's the problem. So I can't agree to the counter offer.

3 MR. KAPLAN: Your Honor, I don't think Mr. Kleppinger  
4 wants to go down the road about when we obtained information  
5 that we requested, because we requested Mr. Falkenberg's  
6 model on July 9, I believe. We obtained it --

7 MR. KLEPPINGER: And I think the Judge said he didn't  
8 want to hear that anyway.

9 MR. KAPLAN: -- four weeks later, after we filed our  
10 rebuttal testimony. We never had a chance to bring it to  
11 Your Honor because we kept on getting promises that we were  
12 to receive the model, and we kept on never getting it. Mr.  
13 Kleppinger's office promised we'd get the model, Mr.  
14 Falkenberg then would refuse to turn it over, posing one  
15 burden over another obstacle over another obstacle, and we  
16 did not receive it until finally we absolutely demanded it  
17 in lieu of going to Your Honor.

18 JUDGE KASHI: I'm not going to let the exhibit in.  
19 You're going to have to come back and demonstrate with runs  
20 as to what the figures actually were, and if at that time  
21 that is demonstrated, you can again attempt, through Mr.  
22 Falk, to put that in.

23 MR. KAPLAN: Then, Your Honor, I make an on-the-  
24 record data request, which I hesitate to formulate standing  
25 on my feet, but I will have to, Mr. Kleppinger, by the time

1 we leave here today, of precisely the information we want  
2 from Mr. Falkenberg, and we would hopefully get it tonight.

3 JUDGE KASHI: I don't know about tonight. I'm sure  
4 we'll get the information as quickly as possible.

5 Mr. Kleppinger.

6 MR. KLEPPINGER: I don't know what the request is  
7 yet, Your Honor.

8 JUDGE KASHI: You're going to use your best efforts.

9 MR. KLEPPINGER: Your Honor, if the request is to  
10 see, for their own eyes, and verify the fixed O&M numbers  
11 Mr. Falkenberg used on the combustion turbines, we can show  
12 that to them right now.

13 JUDGE KASHI: Nobody has formulated a data request.  
14 All I'm saying is we're all going to use our best efforts to  
15 get this evidentiary problem taken care of so that we can  
16 proceed. I mean, what's a two-week hearing without at least  
17 one evidentiary problem?

18 MR. KAPLAN: Your Honor, I would propose, subject to  
19 our right to recall Mr. Falk, which we may do in light of  
20 all this information, that we move on to the next witness.

21 JUDGE KASHI: All right. We'll do that. We will not  
22 formalize the record on the statements or anything else like  
23 that because he is subject to recall.

24 MR. KAPLAN: Thank you.

25 (Witness excused.)

1 JUDGE KASHI: Mr. Falkenberg, sir, would you raise  
2 your right hand and be sworn?

3 having been duly sworn, testified as follows:

4 Whereupon,

5 RANDALL J. FALKENBERG

6 having been duly sworn, testified as follows:

7 MR. KLEPPINGER: Thank you, Your Honor. In  
8 accordance with the agreement of counsel in this case, we  
9 would like to identify for the record as PPLICA Statement  
10 No. 2 the direct testimony and exhibits of Randall J.  
11 Falkenberg. The exhibits are labeled as RJF-1 through  
12 RJF-8.

13 JUDGE KASHI: So marked for purpose of  
14 identification.

15 (Whereupon, the documents were marked  
16 as PPLICA Statement No. 2 and PPLICA  
17 Exhibits Nos. RJF-1 through RJF-8  
18 for identification.)

19 MR. KLEPPINGER: We also would like to have marked  
20 for identification purposes as PPLICA Statement No. 2-S the  
21 surrebuttal testimony and exhibits of Randall J. Falkenberg,  
22 again with the exhibits being labeled as Exhibits RJF-9  
23 through 15.

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

FORM 2

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(Whereupon, the documents were marked as PPLICA Statement No. 2-S and PPLICA Exhibits Nos. RJF-9 through RJF-15 for identification.)

MR. KLEPPINGER: And finally, Your Honor, we had distributed last week an updated PPLICA Statement No. 2-S to the surrebuttal testimony and exhibits of Randall J. Falkenberg. We would like to have that to be marked for identification as PPLICA Statement No. 2-S Update 8/22/97, and that also includes Exhibit RJF-9 Revised.

JUDGE KASHI: So marked for purpose of identification.

(Whereupon, the documents were marked as PPLICA Statement No. 2-S Update and PPLICA Exhibit RJF-9 Revised for identification.)

**DIRECT EXAMINATION**

BY MR. KLEPPINGER:

Q. Mr. Falkenberg, are there any additions or corrections to these statements that you'd like to make at this time?

A. Nothing material.

MR. KLEPPINGER: Your Honor, with that I'd like to move for the admission of PPLICA Statement No. 2 and the accompanying exhibits, PPLICA Statement No. 2-S and the

1 accompanying exhibits, and PPLICA Statement 2-S Update and  
2 the accompanying exhibit.

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

7 MR. KLEPPINGER: Your Honor, we have very brief  
8 additional testimony by Mr. Falkenberg given your ruling the  
9 other day on the Exhibit STJ-28 that was a revision to the  
10 original rebuttal testimony of Dr. Jones.

11 BY MR. KLEPPINGER:

12 Q. Mr. Falkenberg, have you had an opportunity to  
13 review Exhibit STJ-28aR?

14 A. Yes, I have.

15 Q. Have you verified what modifications have been  
16 made by Dr. Jones to this exhibit in comparison to the  
17 original Exhibit 28?

18 A. Yes, I have.

19 Q. Could you summarize those modifications for us?

20 A. Well, I believe that Dr. Jones changed his  
21 capacity factor figures, he did correct the heat rate, he  
22 increased the market energy price substantially, and he may  
23 have made a few other minor adjustments.

24 Q. Does the revised exhibit change any of the  
25 conclusions and other criticisms that you included in your

FORM 2

1 surrebuttal testimony with respect to this exhibit?

2 A. There's nothing that changes in the way of  
3 conclusions because of this exhibit. Dr. Jones did adjust  
4 the capacity factors; he took the capacity factors out of  
5 the EGEAS run, from what I can tell. I believe he still has  
6 improperly applied these capacity factors, because the EGEAS  
7 runs are based on the summer ratings of the units, are  
8 what's shown in EGEAS, so the capacity factors that are  
9 computed based on that are based on the summer rating. So  
10 to the extent that he hasn't used the summer rating, but  
11 he's used a 59 degree rating, I believe that his estimates  
12 of generation for these units would be overstated.

13 Second of all, Dr. Jones did increase his revenue.  
14 His explanation of it was that the units would have lower  
15 capacity factors, I guess, than he thought previously, and  
16 that he wasn't any longer utilizing Mr. Knecht's  
17 calculation, he now had a different calculation. To my  
18 knowledge there is no evidence in the record as to support  
19 those figures. Having said that, I believe that if I were  
20 to have had this information at the time that I filed my  
21 surrebuttal testimony, it wouldn't have changed any of my  
22 conclusions; I still would have made the other adjustments  
23 that I made. I might or might not have accepted all of the  
24 higher revenue that Dr. Jones shows here.

25 Furthermore, this exhibit really only corresponds --

1 this exhibit deals with the question of whether or not Dr.  
2 Jones' market prices are sufficient to pay for the cost of  
3 new capacity. I had two sets of exhibits that dealt with  
4 that question, my Exhibits 11a and b, and my Exhibits 13a  
5 and b. These modifications that Dr. Jones made here to the  
6 revenues would only be applicable to my Exhibit 13a and b.  
7 If Dr. Jones is right, then that would mean that I would  
8 have somewhat higher revenue; however, I don't believe that  
9 that effect would be enough to change the conclusions in my  
10 exhibits. It wouldn't affect my Exhibits Nos. 11a and b  
11 because I used a different revenue forecast for those anyway  
12 based on a higher cost unit than even Dr. Jones uses here.  
13 So had I had this exhibit earlier, I obviously wouldn't have  
14 made the criticisms about the heat rate inputs; I don't  
15 believe it would have changed my calculations or my end  
16 results.

17 MR. KLEPPINGER: Thank you, Your Honor. That's all I  
18 have unless in your judgment, Your Honor, it would be useful  
19 for Mr. Falkenberg to testify to the fixed O&M number he  
20 used on CTs.

21 JUDGE KASHI: No. Let's get that straight the other  
22 way.

23 MR. KLEPPINGER: Very well. The witness is available  
24 for cross-examination.

25 JUDGE KASHI: Mr. Nordstrom.

1 MR. NORDSTROM: Thank you, Your Honor.

2 CROSS-EXAMINATION

3 BY MR. NORDSTROM:

4 Q. Good afternoon, Mr. Falkenberg. My name is Paul  
5 Nordstrom, and I represent Allegheny Power.

6 A. Good afternoon.

7 Q. Mr. Falkenberg, your testimony in this  
8 proceeding is that PP&L, PECO and GPU should use consistent  
9 market price assumptions and a consistent methodology in  
10 computing stranded costs; is that correct?

11 A. That's correct.

12 Q. And the reason for this is that all three  
13 utilities are located in the PJM pool and would face  
14 virtually the same market prices; is that correct?

15 A. Yes.

16 Q. I take it by the same reasoning, that utilities  
17 that are not in PJM would not necessarily have to use the  
18 same market price assumptions or the same stranded cost  
19 methodologies as PECO, PP&L and GPU.

20 A. Well, I can agree with the first part of that  
21 question in that the market prices would be different in  
22 different markets. Now, with respect to the second part of  
23 the question, the methodology I think would probably be the  
24 same. You don't change methodologies just because market  
25 prices change.

1 Q. In forecasting electricity prices, that is a  
2 very complex endeavor, is it not?

3 A. I believe so.

4 Q. And forecasting of market electricity prices  
5 involves in part the forecasting of fuel prices; is that  
6 correct?

7 A. Or accepting a fuel price forecast.

8 Q. And similarly, the forecasting of fuel prices is  
9 a complex endeavor; is that right?

10 A. That's correct.

11 Q. And fuel prices have proven to be notoriously  
12 difficult to predict; is that correct?

13 A. I think I read that somewhere, yes.

14 Q. Now, you've been in the electricity industry  
15 approximately 20 years by your resume; is that correct?

16 A. That's correct.

17 Q. And can you recall predictions that oil prices  
18 would reach \$100.00 a barrel?

19 A. Yes.

20 Q. And that didn't happen, did it?

21 A. No.

22 Q. What is the approximate price of oil today?

23 A. I would say somewhere around \$20.00 a barrel.

24 Q. Can you recall predictions that our nation was  
25 running short of natural gas reserves?

1 A. Yes.

2 Q. And that didn't happen, did it?

3 A. Not yet.

4 Q. Well, in fact, we discovered we have an  
5 abundance of natural gas now, don't we?

6 A. I don't have any testimony in here regarding the  
7 supply of natural gas.

8 JUDGE KASHI: Yes, but it goes to your credibility,  
9 sir.

10 THE WITNESS: I'm sorry. Could you restate the  
11 question?

12 BY MR. NORDSTROM:

13 Q. In fact, we've discovered we have an abundance  
14 of natural gas, don't we?

15 A. As I understand it now, there is an abundance of  
16 natural gas.

17 Q. There's not an abundance of natural gas; is that  
18 your testimony?

19 A. I said as I understand it now, there is an  
20 abundance of natural gas.

21 Q. Excuse me. Can you recall predictions that  
22 nuclear power would be too cheap to meter?

23 A. I cannot recall those, actually, because that  
24 was generally made in the early '70s before I got into this  
25 industry. I can certainly say that I read a lot about

1 those.

2 Q. There were such predictions?

3 A. I believe that there were, yes.

4 Q. But that didn't happen either, did it?

5 A. Unfortunately, not.

6 Q. In fact, nuclear power plants are among our most  
7 uneconomic assets, are they not?

8 A. That's right. Meter makers are perfectly  
9 protected.

10 Q. I'm sorry. Could you repeat your answer?

11 A. Meter makers have nothing to worry about.

12 Q. Can you recall predictions that future utility  
13 avoided costs would justify long-term contracts demanded by  
14 co-generators?

15 A. I can recall some that were done by APS that  
16 were quite wrong that you may be referring to.

17 Q. By APS, who is APS?

18 A. Allegheny Power Service.

19 Q. There were predictions made by Allegheny Power  
20 and there were predictions made by others.

21 A. That's correct.

22 Q. That is correct?

23 A. Yes.

24 Q. And to a large extent, those predictions proved  
25 to be untrue, did they not?

1 A. That's correct.

2 Q. And in fact, many NUGs are also quite  
3 uneconomical these days; is that right?

4 A. That's correct.

5 Q. Is it true that the energy industry has really  
6 missed the mark on some very important projections over the  
7 years?

8 A. Well, I don't know if I can talk about the  
9 entire energy industry, but I can certainly say the electric  
10 utility industry has missed the mark quite often.

11 Q. And here we are again in this proceeding trying  
12 to make major decisions as to the disposition of billions of  
13 dollars of costs based on market prices out 20 years or  
14 more; is that basically true?

15 A. That's correct.

16 Q. Now, the market price of the commodity,  
17 electricity, that we are trying to predict in this  
18 proceeding is itself driven to a large extent by the market  
19 price of another commodity, fuel oil, which is so difficult  
20 to predict; is that correct?

21 A. That's correct.

22 Q. And further, the market in which we are trying  
23 to predict these prices in, the electricity market, is a  
24 relatively new and immature market; is that correct?

25 A. Well, the competitive market certainly is a new

1 and immature market, yes.

2 Q. I'm sorry?

3 A. I would say the competitive market is certainly  
4 a new and immature market.

5 Q. And we are trying to predict electricity prices  
6 in the competitive market; is that right?

7 A. That's correct.

8 Q. And because this market is new and immature, we  
9 all have to speculate just a bit as to how that market will  
10 function when it develops; is that right?

11 A. Well, I think that the choice of the term  
12 "speculate" or "speculation" is probably not the best. I  
13 think we have to make informed judgments about that and  
14 logical choices.

15 Q. But no one really knows now in fact how the  
16 market is going to work.

17 A. I think that's true.

18 Q. Is it true that of some of the other industries  
19 that have been deregulated, they have come up with some  
20 rather wild pricing schemes for consumers?

21 MR. KLEPPINGER: Can you be a little more specific?

22 BY MR. NORDSTROM:

23 Q. Let me give you an example. The airline  
24 industry; is it true that it is possible for a person  
25 attempting to buy an airline ticket, a round-trip airline

1 ticket between the east coast and the west coast, to be able  
2 to pay \$300.00 for that ticket on one day, but on the very  
3 next day, to buy the same ticket for the same flight on the  
4 same airplane and the same seat, to pay \$1,800?

5 A. I think that's correct. I don't know if it is  
6 entirely correct to characterize it as the same seat and the  
7 same -- there are differences in conditions that apply that  
8 do lead to different types of prices.

9 Q. But the question is basically correct?

10 A. There is a difference in the quality of service.  
11 For someone who can stay over a weekend and come and go on  
12 certain times, that isn't the same quality of service as  
13 someone who wants to be able to come and go when they want  
14 to come and go.

15 Q. Is there any cost relationship between the  
16 differences in those two tickets from an airline's point of  
17 view?

18 A. I couldn't identify any.

19 Q. Is it true that it is sometimes cheaper to buy  
20 two round-trip tickets, use two of the four legs of those  
21 tickets, discard the other two of the four legs of those  
22 tickets, cheaper to do that than to buy a single round-trip  
23 ticket to the same destination?

24 A. Actually, Mr. Kollen of our firm is a lot more  
25 experienced at those types of arrangements than I am.

1 Q. He's an expert in those?

2 A. I believe that there are a lot of ways in which  
3 people have managed to figure out ways to game the system.

4 Q. Before the airline industry was deregulated, was  
5 anyone predicting such wild pricing schemes?

6 A. I really don't know.

7 Q. Returning to electricity, there are, as I  
8 understand it, a number of major variables besides the cost  
9 of fuel and the uncertainties involved in the immature and  
10 yet developing electricity market that we can't predict now  
11 with certainty that would ultimately affect the market price  
12 of electricity; is that correct?

13 A. I would agree with that.

14 Q. Let me suggest several of those to you, and can  
15 you tell me whether they are such variables? Environmental  
16 compliance costs.

17 A. I just want to make sure I understand the  
18 question. You're asking whether or not it is predictable as  
19 to what levels those will be in the future and how those  
20 would affect the cost of electricity or the price of  
21 electricity?

22 Q. I'm saying the variables that I will list are  
23 variables that we do not now know with certainty how they  
24 will be in the future and, therefore, they will affect the  
25 market price of competitive energy in a way that we do not

1 know now.

2 A. Okay. I agree with that.

3 Q. Environmental compliance costs, you would agree?

4 A. Yes.

5 Q. The future demand for electricity.

6 A. I agree that that is somewhat uncertain.

7 Q. The time when new capacity will be needed.

8 A. That is somewhat uncertain.

9 Q. The rate at which new players will jump into the  
10 market.

11 A. I believe that is probably more uncertain.

12 Q. The cost of their new capacity.

13 A. I believe that is somewhat uncertain.

14 Q. The efficiency of the new plants.

15 A. I believe that is somewhat uncertain.

16 Q. Future interest rates.

17 A. Pretty uncertain.

18 Q. Are there any other major variables you can  
19 think of that we could add to that list?

20 A. Well, I think there are probably lots of  
21 variable fuel prices. I don't know if you covered that one  
22 or not.

23 Q. We did mention fuel prices earlier.

24 A. Those would certainly be factors.

25 Q. All these variables would tend to add to the

1 uncertainty as to the ultimate projection of market  
2 electricity prices; is that right?

3 A. I agree.

4 Q. Is it true that the farther out we project as a  
5 general matter, the more these variables will tend to  
6 increase the uncertainty of our projections?

7 A. I would agree with that.

8 Q. You certainly would agree it is impossible to  
9 predict long-term future market electricity prices with  
10 certainty?

11 A. You are asking if I would agree that it is  
12 impossible to predict long-term market electricity prices  
13 with certainty?

14 Q. Yes.

15 A. I think it is probably impossible so long as  
16 human beings don't have perfect foresight to ever predict  
17 anything with certainty. That's why we call it prediction  
18 instead of a fact. Things that have not yet happened are  
19 not facts.

20 MR. KAPLAN: Your Honor, I hesitate to rise except  
21 Mr. Nordstrom's client has a proposal for a variable CTC in  
22 their case. This is our case. We can go on and on  
23 supporting his proposal; but if he would like to examine Mr.  
24 Falkenberg in their case, why don't they do it in their  
25 case, not in our case? That's clearly the point where he's

1 driving at.

2 MR. NORDSTROM: Your Honor, I'm virtually at the end  
3 of my rope, and I think we can wrap up momentarily.

4 JUDGE KASHI: All right. It might be something I  
5 like in this case.

6 MR. NORDSTROM: I suspect it might.

7 MR. KLEPPINGER: Don't press your luck.

8 MR. NORDSTROM: I won't.

9 BY MR. NORDSTROM:

10 Q. Given the uncertainty involving the various  
11 variables we discussed about forecasting the future  
12 electricity prices, if a utility were to develop a  
13 legitimate way to calculate its stranded costs on the basis  
14 of actual rather than projected market conditions and were  
15 actually willing to do that, shouldn't such a method be  
16 permitted as a matter of regulatory policy?

17 MR. KLEPPINGER: Now I'll object, Your Honor. There  
18 is no such proposal in this case to that effect.

19 JUDGE KASHI: Sustained.

20 MR. NORDSTROM: Your Honor, I have no further  
21 questions.

22 JUDGE KASHI: Thank you very much.

23 Mr. Kaplan.

24

25

1 MR. KAPLAN: Thank you very much.

2 CROSS EXAMINATION

3 BY MR. KAPLAN:

4 Q. We've met informally, but my name is  
5 Donald Kaplan. I'll be examining you this afternoon on  
6 behalf of Pennsylvania Power & Light Company,  
7 Mr. Falkenberg.

8 A. Good afternoon.

9 Q. If we can clear up a little bit of the mystery,  
10 what was the fixed charge rate you used for CTs in your  
11 model?

12 A. Well, I think you just asked for the fixed charge  
13 rate, which was 13.34 percent. That's the real fixed charge  
14 rate.

15 Q. All right. I mean the fixed O & M.

16 A. The fixed O & M in 1997 was \$6.94. And I  
17 escalated it 3.11 percent until the year 2015, and then at  
18 3.56 percent from 2015 and beyond, in conjunction with the  
19 EIA forecast for inflation.

20 Q. So the 3.114, to be precise -- or, 3.11 percent  
21 to 2015?

22 A. And then 3.56 percent after that.

23 Q. After that.

24 A. And that can be seen, I believe, just by looking  
25 at my exhibits.

1 Q. Okay. Now, what rate did you use for a combined  
2 cycle turbine?

3 A. Fixed O & M?

4 Q. Yes.

5 A. I remember that the 1995 dollar value -- the  
6 value in 1995 dollars was about \$17 a kw year.

7 Q. Excuse me?

8 A. About \$17 a kw year. Plus I added in an  
9 allowance for a couple dollars for capital additions and --

10 Q. By a couple, you mean two?

11 A. I would have to check that. And have added in an  
12 additional allowance for A & G, which was in the range of a  
13 dollar and a half to two dollars.

14 Q. So, it's my understanding then with respect to  
15 the combustion turbine, you used neither the \$9.00 figure,  
16 which you state was on the disk, or the \$5.28 figure which  
17 is shown in response to the interrogatory, Interrogatory No.  
18 74, OCA Set III.

19 A. I agree those were PP&L's numbers. I wouldn't  
20 have any necessary reason to use those, I would have used my  
21 own.

22 I just want to clarify one thing, though.

23 Q. Excuse me.

24 A. I just want to clarify the \$6.94 --

25 Q. Hold it.

1 JUDGE KASHI: Hold it, hold it.

2 BY MR. KAPLAN:

3 Q. I have a question.

4 A. I didn't get to finish answering.

5 JUDGE KASHI: Wait a minute. We're not going to go  
6 this way. Answer the questions.

7 BY MR. KAPLAN:

8 Q. So you used neither \$5.28 nor \$9.00; is that  
9 correct?

10 A. No, I didn't.

11 Q. You exercised your own judgment and chose a  
12 different number?

13 A. That's correct.

14 Q. And you would agree that the higher the number  
15 for fixed O & M, the higher the capacity price?

16 A. Not necessarily. At least not for combustion  
17 turbines.

18 Q. Now, would you agree, Mr. Falkenberg, that,  
19 putting aside the issue of model construction and model  
20 application, that the finding of the projected price of  
21 electricity over the forecast period is largely driven by  
22 the inputs?

23 A. I would agree.

24 Q. Would you also agree that among those inputs, by  
25 far the most important is the real price of fuels and the

1 impact of inflation on the price of fuels?

2 A. I don't know that I would agree with that,  
3 because I haven't done that analysis. I'd say that's a very  
4 important variable.

5 Q. You would not necessarily agree that they are  
6 among the most important?

7 A. Well, the capacity cost, for example, is very  
8 important.

9 Q. Would you agree that in making a forecast of fuel  
10 prices and making a forecast of inflation, that it is  
11 generally better to have more data than less data?

12 A. I guess that more data's always better than less  
13 data.

14 Q. Would you also agree that with respect to the  
15 price of fuel, the choice of the proper forecast is an  
16 important factor?

17 A. Yes.

18 Q. And would you also agree that with respect to  
19 expected inflation, that the choice of the proper forecast  
20 of inflation is an important factor?

21 A. Yes.

22 Q. Would you also agree that if one were looking at  
23 regulatory proceedings to determine whether a model had been  
24 endorsed or verified in that proceeding, that one would need  
25 to know the facts of the individual proceedings and how the

1 model was used precisely?

2 A. Yes.

3 Q. Now, you would agree that your model, as well as  
4 EGEAS, does not model efficiency gains in the production of  
5 energy from power plants such as combined cycles or  
6 combustion turbines?

7 A. Well, I think, if I understand your question, the  
8 answer's yes.

9 Q. Would you agree that neither your model nor EGEAS  
10 models the impact of the competitive process on the  
11 efficiency and the production of energy?

12 A. Neither my model nor the EGEAS model made any  
13 explicit assumptions about what you might call the invisible  
14 hand benefits where generators become more efficient, or  
15 that sort of thing.

16 Q. And would you agree that with respect to  
17 scheduling maintenance in a competitive market, the owners  
18 of generation will seek to schedule maintenance at times  
19 they suspect the prices are going to be low on a seasonal  
20 basis?

21 A. They will do so at times when they suspect prices  
22 will be low. However, whether prices will actually be as  
23 low as they suspect, is something that they're going to have  
24 some difficulty in predicting.

25 And the other problem is that sometimes generating

1 units do go down for reasons unexpectedly, and then it is  
2 determined that that's a reasonably good time to go ahead  
3 and finish some maintenance.

4 If you look at the maintenance schedule for any  
5 utility, and I've looked at lots of them, you see planned  
6 maintenance that avoids summer seasons and winter peaks and  
7 that sort of thing. But you see that in reality maintenance  
8 generally occurs in all of those months.

9 Q. But you would agree that planned maintenance in a  
10 competitive market is probably most advisable in the spring  
11 or the fall when the prices are lower?

12 A. I would agree that that would be the time when  
13 most people would attempt to do it. But then if everybody  
14 did it at those times, it might well be that you drive the  
15 price up so high that it's counterproductive and that  
16 there's nothing to be gained by doing that.

17 Q. You haven't tested your model to determine that;  
18 have you?

19 A. No, I haven't.

20 Q. Would you agree that in your model, you modeled  
21 maintenance to be scheduled in all but the 84 days that the  
22 PJM prohibits maintenance?

23 A. That's correct.

24 Q. And you scheduled it evenly throughout that  
25 period?

1 A. That's correct.

2 Q. Now, the 84 days were selected to comply with PJM  
3 rules; is that correct?

4 A. Yes.

5 Q. The 84 days of exclusion, just to be precise?

6 A. Yes.

7 Q. Now, those rules have been in place for several  
8 years; do you know?

9 A. I don't know how long they've been in place. I  
10 know that that is also part of the supporting company's  
11 proposal for the current PJM restructuring that's before the  
12 FERC.

13 Q. But they're not a new proposal just recently  
14 introduced, as far as you know?

15 A. Not to my knowledge.

16 Q. In fact, as far as you know, they were probably  
17 developed several years ago; is that correct?

18 A. I would not want to speculate.

19 Q. Now, you would agree that until very recently,  
20 PJM utilities were essentially fully essentially fully  
21 vertically, integrated, regulated utilities operating in  
22 both regulated wholesale and retail markets?

23 A. Yes.

24 Q. And would you also agree that in a competitive  
25 market the incentive to properly scheduled maintenance is

1 greater than in a regulated market?

2 A. I think if you don't schedule your maintenance  
3 efficiently in a regulated market you could well be  
4 criticized in a regulatory process and have costs  
5 disallowed. I don't know if that's a greater incentive than  
6 the possibility of trying to make more money on market  
7 prices or not.

8 Q. Would you agree that the same incentive to  
9 schedule maintenance correctly is very much related to the  
10 incentives to price electricity more efficiently, or to  
11 achieve lower electricity prices, that the legislature  
12 probably had in mind in passing the Customer Choice Act?

13 A. I really don't --

14 MR. KLEPPINGER: That calls for a conclusion of what  
15 the intent of what the legislature was. That's really  
16 beyond this witness.

17 JUDGE KASHI: I was going to say, if he can determine  
18 what the intent of the legislature is --

19 (Laughter.)

20 MR. KAPLAN: I will withdraw the question, Your  
21 Honor. I admit that it's probably calling upon this  
22 witness, or indeed any witness, to speculate.

23 BY MR. KAPLAN:

24 Q. Will you agree that one of the benefits of  
25 competition is obviously to achieve greater efficiency of

1 operations in our productive resources?

2 A. That one of the benefits?

3 Q. Yes.

4 A. I believe competition will promote efficiency. I  
5 think that there's other benefits, broader choices for  
6 customers, that sort of thing.

7 Q. And you would agree that to the extent that such  
8 an intent on the part of the legislature could be  
9 ascertained, that where it is economically appropriate to  
10 deregulate markets, that society should seek to do so?

11 A. Yes, I would agree. I think that the kinds of  
12 efficiency gains that I think of most often are things like  
13 not building nuclear plants instead of building combined  
14 cycle or combustion turbine units instead, that sort of  
15 thing.

16 Q. But those competitive incentives would spread  
17 throughout the entire range of choices that a power producer  
18 would make?

19 A. I would agree.

20 Q. Including maintenance?

21 A. I would agree.

22 (Pause.)

23 Q. Mr. Falkenberg, would you agree that one way that  
24 generating facilities make money, i.e. make returns to their  
25 fixed costs and the cost of capital, is by selling energy at

1 a price above their marginal cost of operation?

2 A. Well, I believe that's the assumption of the  
3 competitive market, yes.

4 Q. And would you agree that in determining whether  
5 to invest in a generation facility, an investor would look  
6 not only at the stream of capacity payments, but also to  
7 contributions to margin they would expect to make when  
8 prices are above their marginal cost of operation?

9 A. I would agree as a matter of principle that  
10 that's true. However, I would certainly discount that  
11 concept for units that run with very low capacity factors  
12 and that have very widely fluctuating degrees of operation.  
13 Investors are going to do projections, they're going to use  
14 models to do that. The output of combustion turbines, for  
15 example, and various models in these types of energy savings  
16 that you're talking about, are dependent on the model, and  
17 the assumptions, more than anything else.

18 For example, in the PECO case, the GE MAPS --

19 MR. KAPLAN: Your Honor --

20 THE WITNESS: -- model produced no savings.

21 MR. KAPLAN: Your Honor, I am not interested in the  
22 PECO case.

23 MR. KLEPPINGER: It's an explanation to the question  
24 that was asked, however.

25 MR. KAPLAN: He answered the question long ago, sir.

1 JUDGE KASHI: Yes, I think so.

2 BY MR. KAPLAN:

3 Q. Mr. Falkenberg, I want you to assume the  
4 following. Assume that Mr. Kleppinger, as he frequently is,  
5 is a very successful advocate, and he convinces the  
6 Commission to reject PP&L's proposal to interruptible  
7 customers choosing alternate suppliers --

8 JUDGE KASHI: I didn't hear that last part.

9 BY MR. KAPLAN:

10 Q. That interruptible customers choosing alternate  
11 suppliers pay CTC associated with LP-4 or LP-5 rates. Do  
12 you have that assumption in your head?

13 A. I think so.

14 Q. Okay. Now, with that assumption, would you  
15 recommend that members of the PP&L Industrial Customer  
16 Association, on whose behalf you're testifying today, signed  
17 long-term power supply contracts based upon the energy and  
18 capacity prices to which you have testified at this  
19 proceeding?

20 A. Yes. If I understand everything about those rate  
21 schedules, which I can't say that I do. I think Mr. Baron  
22 is a better witness on rate schedule type issues in this  
23 particular case.

24 Q. Well, the basic assumption, just so it's clear,  
25 is that, if they do sign such contracts, they pay no more

1 stranded costs than they would as an industrial customer.

2 MR. KLEPPINGER: I'm sorry, you trailed off.

3 BY MR. KAPLAN:

4 Q. That if they do sign a contract with an alternate  
5 supplier, their CTC payments do not change as a result of  
6 leaving PP&L. That is the basic assumption.

7 And with that in mind, will you --

8 A. I just want to -- what you're asking me is, if  
9 the PPLICA members were able to sign contracts that required  
10 them to pay the CTC at the LP-4 or LP-5 rate, would I  
11 recommend --

12 Q. No. Let me correct you. No. They would  
13 continue to pay the CTC they would have paid had they not  
14 left PP&L.

15 A. Okay, okay.

16 Q. What you said is what we want. I'm saying what  
17 Mr. Kleppinger wants.

18 MR. KLEPPINGER: Mr. Kaplan, if we could just clarify  
19 for Mr. Falkenberg's benefit. You're talking about the CTC  
20 that's contained in the unbundle interruptible tariff  
21 submitted by PP&L?

22 MR. KAPLAN: That's right.

23 MR. KLEPPINGER: Okay.

24 BY MR. KAPLAN:

25 Q. Now, with that in mind, sir, would you recommend

1 that members of PPLICA sign long-term power supply contracts  
2 at the energy and capacity prices recommended in your  
3 testimony?

4 A. I really can't say if I know the answer to that.  
5 And the problem is, I would have to look at those rates and  
6 what the -- I guess what I would say is this, if it will  
7 help. I think my forecast would be a reasonable basis for  
8 PPLICA members to use to determine the attractiveness of  
9 various contract offers. Whether they select the PP&L rate  
10 or some other rate, I can't tell you that I'm sure about  
11 that because I don't know what the rate structure is. As I  
12 said, Mr. Baron is our rate structure witness.

13 Q. One second. We seem to have misplaced your  
14 testimony.

15 MR. KAPLAN: Bear with me a second, Your Honor.

16 (Pause.)

17 BY MR. KAPLAN:

18 Q. If you could turn to page 49 of your surrebuttal  
19 testimony.

20 A. Yes, I have that.

21 Q. Now, here you provide a list beginning on the  
22 bottom of page 49, going over to the top of page 50, of what  
23 you term benchmark studies in regulatory proceedings; is  
24 that correct?

25 A. Yes.

1 Q. Now, isn't it true that you nowhere state in your  
2 testimony precisely what the absolute percentage difference  
3 represented in your last column means?

4 A. That's correct.

5 Q. That's true?

6 A. I think I didn't state what I meant exactly by  
7 absolute percent difference.

8 Q. Can we turn to Exhibit RJF-14?

9 A. Okay.

10 Q. And page 2.

11 A. I have it.

12 Q. Okay. Now, here we have a page that shows LGE  
13 system production costs; is that correct?

14 A. That's correct.

15 Q. Now, this is out of one of the cases listed at  
16 page 49?

17 A. That's correct.

18 Q. That's a 1988 case, LGE case; is that true?

19 A. I believe that's right, yes.

20 Q. Okay. Now, would you agree that what was being  
21 measured here were total system production costs?

22 A. It says production costs include fuel, O & M and  
23 purchase power expense.

24 Q. So that's total production costs?

25 A. I believe so, yes.

1 Q. Okay. Now, you note in your testimony at page  
2 50, line 12 that the most important test is not getting the  
3 total production cost right, but getting incremental cost  
4 correct; is that true?

5 A. For this application, I believe that that's what  
6 I said. But let me just verify exactly what page you're on  
7 again. Page 50, line 12?

8 Q. Page 50, line 12.

9 A. Well, I think I said that I believe the most  
10 logical place to start would be to examine how the  
11 respective models do in predicting the actual generation of  
12 marginal units for this particular application. For other  
13 types of applications such as those referenced in this  
14 table, I think total production cost was a good indicator.

15 Q. Okay. But are all the other applications in this  
16 table total production cost?

17 A. I believe they are.

18 Q. I see. Thank you. Now, let's turn to Exhibit  
19 No. 15, page 2 of 2.

20 A. Okay, I have it.

21 Q. Now, this is your attempt to benchmark your  
22 prediction of 1995 versus actual results of 1995; is that  
23 correct?

24 A. It's a comparison of predicted generation for '95  
25 versus the generation for a set of what's called marginal

1 units.

2 Q. Now, would you agree that the number of hours  
3 that you run a combustion turbine would have an impact on  
4 the incremental cost of energy, and hence the market price  
5 of electricity?

6 A. It would have an impact on the market price of  
7 energy, but it wouldn't necessarily have a direct impact on  
8 the overall market price, because if a combustion turbine  
9 runs more hours in a simulation in my modeling, it will  
10 serve to reduce the capacity charge or capacity credit. And  
11 so, there is sort of a washing out effect of that. It isn't  
12 very sensitive to those results.

13 Q. Now, will you please turn to page 1 of Exhibit  
14 RJF-15?

15 A. Yes.

16 Q. And here you show that all PP&L's combustion  
17 turbines had an output of 23 gigawatt hours in 1995; is that  
18 correct?

19 A. That's correct.

20 Q. And your model predicted 46 and 57 gigawatt  
21 hours; is that correct?

22 A. That's correct, depending upon the scenario.

23 Q. And would you agree, 36 gigawatt hours is 50  
24 percent greater than 23, at least 50 percent greater than  
25 23; and 47 is more than twice as greater as 23 gigawatt

1 hours?

2 A. That's correct. The point of this exhibit wasn't  
3 that the model was perfect, but just that it was a lot  
4 closer than the EGEAS model.

5 Q. Even if EGEAS ran the combustion turbine to zero,  
6 wouldn't zero be closer to 23 than 36 or 47 -- than 47  
7 gigawatt hours?

8 A. Well, 23 is closer to 36 than it is to zero. And  
9 it is farther from 47 than it is to zero, but percentage-  
10 wise it's a whole lot closer.

11 Q. Now, would it surprise you to know that in 1992  
12 PP&L's combustion turbines produced only eight gigawatt  
13 hours?

14 A. It wouldn't surprise me. Reserve margins were a  
15 lot higher a couple of years ago.

16 Q. So, there are year-to-year differences is that  
17 probably should be examined; is that true?

18 A. I only had one year of historic data to look at,  
19 1995, and I was satisfied with the result. I would like to  
20 look at every single year from the beginning of time on end,  
21 but there's a limit.

22 Q. But you only examined 1995?

23 A. That's correct.

24 Q. Now, let's talk about 1995. 1995 predated FERC  
25 Order 888; is that correct?

1 A. Yes.

2 Q. The year 1995.

3 A. That's correct.

4 Q. It also predated the reforms in the PJM  
5 interconnection; is that correct?

6 A. That's correct.

7 Q. Is it your understanding that in 1995 PJM was  
8 still compensating dispatched generation on a split savings  
9 basis?

10 A. Yes.

11 Q. And also in 1995, PJM was still largely operating  
12 as a combination of fully regulated utilities at wholesale  
13 and retail; is that also correct?

14 A. That's correct.

15 Q. Would you agree that the incentives of regulated  
16 utilities operating in a fully regulated environment, in  
17 which open access transmission is not required, are  
18 substantially different from the incentives of generation  
19 operators operating in an open access world subject to fully  
20 competitive pricing?

21 A. Yes.

22 Q. Now, wouldn't you agree, in selecting the  
23 appropriate fuel price forecast, that the use of, to use in  
24 a model, involves an exercise of judgment?

25 A. Yes.

1 Q. Would you agree that in selecting the appropriate  
2 inflation rate to use in connection with modeling future  
3 energy prices also requires an exercise of judgment?

4 A. Yes.

5 Q. Would you agree that interpreting the results of  
6 a model is also an exercise in judgment?

7 A. Yes.

8 Q. Would you agree that the design of your model,  
9 for example, in choosing simplicity over complexity, also  
10 involves an exercise of judgment?

11 A. That's correct.

12 Q. And would you agree that the entire modeling  
13 exercise of future energy prices involves a great deal of  
14 judgment?

15 A. I would agree with that to a certain limit.

16 Q. Would you agree that in assessing the judgment  
17 involved in producing future energy prices, the background  
18 of the individual exercising that judgment is an important  
19 and relevant consideration?

20 A. I guess I'd agree with that. I'm not sure what  
21 you mean by background, but --

22 Q. Work experience, forecasting experience.

23 A. Okay.

24 Q. Now, EIA's fuel forecast relies heavily on DRI's  
25 inflation projection; is that correct?

1 A. I'm not aware that that's the case. I know that  
2 the DRI and EIA inflation forecasts are quite similar. I'm  
3 not quite sure if EIA actually adopted the DRI figures or  
4 not.

5 Q. But you haven't detected any significant  
6 difference in their forecasts?

7 A. No.

8 Q. Now, would you agree that you have not reviewed  
9 in detail DRI's assumptions regarding inflation?

10 A. No.

11 Q. Would you agree that you haven't reviewed in  
12 detail EIA's assumptions for inflation?

13 A. No.

14 Q. You haven't reviewed them?

15 A. I use the EIA figures that were presented, I  
16 didn't do an in-depth analysis of whether those figures were  
17 better than somebody else's or worse.

18 Q. All right. So you did not analyze the inflation  
19 assumptions?

20 A. I utilized them, I didn't analyze them.

21 Q. You did not question them?

22 A. I did not question them.

23 Q. Now, have you yourself made a separate fuel  
24 forecast?

25 A. I don't quite follow what you're asking. I don't

1 believe so in this particular proceeding. I did in EPI --

2 Q. Okay. Do you regularly make forecasts of gas or  
3 oil prices?

4 A. I generally do not.

5 Q. Now, you read the testimony of Mr. Smith in this  
6 proceeding; is that correct?

7 A. Yes.

8 Q. And his surrebuttal testimony?

9 A. Actually, I take that back. I'm not sure if I  
10 actually read all of his testimony in this proceeding, and I  
11 didn't read his surrebuttal. I did read some of his direct  
12 testimony.

13 Q. Are you aware that he updated his forecast to use  
14 a more recent DRI forecast?

15 A. I am aware of that, yes.

16 Q. And you did not choose to do the same; is that  
17 true?

18 A. I did not use the DRI forecast, no.

19 Q. You did not choose to update your forecast in  
20 light of additional DRI or EIA data; is that true?

21 A. I did not.

22

23

24

25

1 Q. You understand that EIA updated its short-term  
2 forecast; is that correct?

3 A. It updated the short-term forecast; and from Dr.  
4 Jones' revised exhibit, it doesn't appear that things  
5 changed very much, and it certainly didn't produce any long-  
6 term forecasts, which is what I was using anyway.

7 Q. Mr. Falkenberg, do you regard the Kennedy and  
8 Associates model as proprietary?

9 A. Yes.

10 Q. And indeed, you regard it as a trade secret; is  
11 that correct?

12 A. That's correct.

13 Q. Indeed, you're reluctant to release your model  
14 for detailed examination; is that true?

15 A. I am reluctant to release it because I am  
16 concerned about losing the value that we've invested in it.

17 Q. But you are in fact reluctant to release it for  
18 detailed examination; is that true?

19 A. I have released it in this particular  
20 proceeding.

21 Q. And you did in fact release that model one week  
22 ago Tuesday; is that correct?

23 A. I believe I e-mailed it to Mr. Falk on Sunday,  
24 August 10.

25 Q. But without the password; is that correct?

1           A.    The instructions made it very clear how to go  
2 about getting the password.

3           Q.    But until he had that password, he couldn't open  
4 your model; is that correct?

5           A.    He could open it. He just couldn't get answers.

6           Q.    Now, would you please turn to page 10, line 3 of  
7 your surrebuttal testimony?

8           A.    Okay.

9           Q.    Would you agree that if you had used the 1995  
10 EIA base price of \$2.10 instead of the \$2.04 that you did  
11 use, the result of that would have been a reduction in your  
12 finding of PP&L's stranded costs?

13          A.    If I had used the \$2.10 instead of the \$2.04, I  
14 would have, yes, had a lower stranded cost, I believe.

15          Q.    And you would agree that you made that decision  
16 because you sought a result that in your view would minimize  
17 controversy; is that correct?

18          A.    I believe I said that I thought it was a  
19 reasonable number that I used the \$2.04 and that I thought  
20 by using that and sticking with it I would minimize  
21 controversy.

22          Q.    So you looked at the results and you thought it  
23 was reasonable?

24          A.    I thought it was reasonable from the start.

25          Q.    But you looked at the results and used those

1 numbers because you thought they were reasonable.

2 A. I looked at the results and I determined that  
3 the number I used originally was reasonable, yes.

4 Q. And in fact, it was the number that you had in  
5 mind all along; is that correct?

6 A. It was the number that I computed from historic  
7 data.

8 Q. Now, when you looked at the results, you  
9 exercised judgment; is that correct?

10 A. That's correct.

11 MR. KAPLAN: One second, Your Honor.

12 (Pause.)

13 MR. KAPLAN: Thank you, Mr. Falkenberg. Your Honor,  
14 as a result of some on-the-spot editing, we are done at this  
15 time with this examination.

16 JUDGE KASHI: Thank you very much, sir.

17 Do you need some time, Mr. Kleppinger?

18 MR. KLEPPINGER: Just a little bit, Your Honor. I  
19 shouldn't be much.

20 JUDGE KASHI: Five minutes?

21 MR. KLEPPINGER: Five is good.

22 JUDGE KASHI: Five minutes.

23 (Recess.)

24 JUDGE KASHI: Back on the record.

25 Redirect, Mr. Kleppinger?

1 MR. KLEPPINGER: Thank you, Your Honor. This will be  
2 painfully brief.

3 REDIRECT EXAMINATION

4 BY MR. KLEPPINGER:

5 Q. Mr. Falkenberg, Mr. Kaplan's cross-examination  
6 at the very end focused on page 10 of your surrebuttal  
7 testimony.

8 A. Yes.

9 Q. And in his questioning he asked about certain  
10 results. When you were answering those questions, were you  
11 interpreting the word "result" as being the price per MMBtu  
12 of gas that you were using in your study?

13 A. Yes.

14 Q. It was not a result that was going to be the  
15 product of the use of that price, namely the ultimate  
16 stranded costs in the case?

17 A. No, I never computed that.

18 Q. So the judgment you applied was to use an actual  
19 1995 natural gas price for the PJM out of the 1995 FERC Form  
20 1; is that correct?

21 A. That's correct. I just calculated the total  
22 average price.

23 Q. And that was a lower gas price than the EIA base  
24 price?

25 A. That's correct.

1 MR. KLEPPINGER: That's all I have, Your Honor.

2 JUDGE KASHI: Thank you very much, sir.

3 MR. KAPLAN: Your Honor, I need to just clarify one  
4 thing.

5 JUDGE KASHI: All right.

6 **REXCROSS-EXAMINATION**

7 BY MR. KAPLAN:

8 Q. Mr. Falkenberg, could you read the two sentences  
9 beginning on line 3 to the end of that paragraph out loud?

10 A. "Had I used the EIA figure, I would have  
11 decreased PP&L's stranded costs by an amount that is more  
12 than all the above cited adjustments combined. I did not do  
13 so in order to minimize controversy, and because I believed  
14 the original figure was reasonable."

15 Q. So you made a judgment that use of the figure  
16 you used would not further decrease PP&L's stranded costs,  
17 as I understand it.

18 A. The figure I used was the 2.04, and by keeping  
19 that, I kept the stranded costs constant.

20 Q. But what I'm trying to understand is what does  
21 that have to do with the rest of that paragraph, minimizing  
22 controversy?

23 A. I just thought that it would be considered bad  
24 form to come in with a different gas price assumption in the  
25 surrebuttal phase than I used in the direct phase.

1 Q. Because it would have changed the stranded  
2 costs; is that correct?

3 A. Yes, it would have.

4 Q. So you did have stranded costs in mind when you  
5 made that judgment.

6 A. Well, obviously, it would affect the result, but  
7 that isn't what I'm saying here. I just said that the \$2.04  
8 was reasonable. I think that the model and the inputs, it's  
9 very sensitive to the natural gas price assumption.

10 Q. In making your judgment to minimize controversy,  
11 you had the impact on stranded costs in mind, is that  
12 correct, as one of the factors you considered?

13 A. Actually, I had the impact on the hearing,  
14 because I would have to answer questions about why I chose  
15 2.10 versus 2.04 and that sort of thing. I would have had  
16 the same set of questions with different answers.

17 MR. KAPLAN: No further questions, Your Honor.

18 JUDGE KASHI: Thank you. Nothing further. The  
19 witness is excused.

20 (Witness excused.)

21 JUDGE KASHI: That which has been marked and  
22 identified as PPLICA Statement 2, 2-S, 2-S Updated and RJF-1  
23 to 8, 9 to 15 and 9-Revised are received into the  
24 evidentiary record without objection.

25 (No response.)

1 JUDGE KASHI: Without objection.

2 (Whereupon, the documents marked as  
3 PPLICA Statements Nos. 2 and 2-S and  
4 2-S Updated and Exhibits RJF-1  
5 through RJF-15 and RJF-9 Revised  
6 were received in evidence.)

7 JUDGE KASHI: Tomorrow looks very short, and I'm  
8 wondering is it possible if we can add the two Thursday  
9 witnesses Guth and Moul onto Wednesday's schedule? The  
10 reason that I'm asking for that is because I'm directing the  
11 Intervenors to come together on Thursday afternoon after the  
12 hearing; and so therefore, if I can cut short Thursday's  
13 date, it will give them more of an opportunity. Is that a  
14 possibility?

15 MR. RUSSELL: Your Honor, can we go off the record  
16 for a scheduling discussion?

17 JUDGE KASHI: Off the record.

18 (Discussion off the record.)

19 JUDGE KASHI: Back on the record.

20 If there is nothing further other than putting on the  
21 record the start time of 10:00 tomorrow morning, we will  
22 recess until 10:00 a.m.

23 Thank you very much, counsel Have a good evening.  
24  
25

1 (Whereupon, at 5:50 p.m., the hearing was adjourned,  
2 to be reconvened at 10:00 a.m., Wednesday, August 27, 1997,  
3 in Harrisburg, Pennsylvania.)

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9 C E R T I F I C A T E

10 I hereby certify, as the stenographic reporter, that  
11 the foregoing proceedings were taken stenographically by me,  
12 and thereafter reduced to typewriting by me or under my  
13 direction; and that this transcript is a true and accurate  
14 record to the best of my ability.

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