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FORM 2

P R O C E E D I N G S

1
2 JUDGE CHESTNUT: This is the hearing scheduled at
3 docket A-110550F0160. For the record, let me state that I'm
4 Administrative Law Judge Marlane R. Chestnut.

5 Let's go off the record for a second here.

6 (Discussion off the record.)

7 JUDGE CHESTNUT: Let's go back on the record.

8 I will note the following appearances for the record:
9 Thomas Niesen representing Philadelphia Gas Works, Kenneth
10 Mickens representing the Office of Trial Staff, David
11 Kleppinger representing the City of Philadelphia and PAIEUG,
12 Jessie Dillon representing the PPL Companies, Donald Kaplan
13 also representing the PPL Companies, Megan Troy representing
14 the PPL Companies, Kent Murphy and Paul Bonney representing
15 PECO Energy Company, Susan Shinkman representing DEP.

16 Who's Ms. Shinkman?

17 (Ms. Shinkman indicating.)

18 JUDGE CHESTNUT: Okay. Sharon Webb representing
19 OSBA.

20 Ms. Webb?

21 (Ms. Webb indicating.)

22 JUDGE CHESTNUT: Okay. Tanya McCloskey and Aron
23 Beatty representing the Office of Consumer Advocate.

24 Is it Mike Naeve. I can't even read this writing.
25 I'm sorry.

1 MR. NAEVE: It's Naeve, Your Honor.

2 JUDGE CHESTNUT: Naeve; okay. And Wyatt Estes?

3 MR. ESTES: It's Matt.

4 JUDGE CHESTNUT: Oh, my goodness. I'm sorry.

5 MR. ESTES: That's my handwriting, Your Honor. I
6 apologize.

7 JUDGE CHESTNUT: I'm sorry. I see it now. Also
8 representing PECO.

9 Dan Clearfield representing PSE&G.

10 Is there anybody who hasn't signed this and wants to
11 be recognized at this point?

12 (No response.)

13 JUDGE CHESTNUT: Okay. Let's take care of the
14 housekeeping items first. I know there are a number of
15 parties -- let's talk about stipulations that have been
16 reached regarding I guess the admission of exhibits and
17 cross-examination.

18 Mr. Murphy, do you want to address that?

19 MR. MURPHY: Yes, Your Honor. We've reached in the
20 past day two stipulations concerning the cross-examination
21 of various witnesses. The first is with Philadelphia Gas
22 Works and the second is with the City of Philadelphia.

23 Philadelphia Gas Works plans to admit into the record
24 certain data requests, and we're going to stipulate to that
25 admission in exchange for their waiver of cross-examination

1 of Dr. Hieronymus and Dr. Morris, and that would be subject
2 to our ability, the Joint Applicants' ability to perform
3 redirect on the cross-examination witnesses and the
4 Philadelphia Gas Works' ability then to cross-examine our
5 witness on those exhibits.

6 With regard to the City of Philadelphia, Witness
7 Tumar Alexander will not be presenting testimony on behalf
8 of the City of Philadelphia; and as result Geraldine
9 Brockman from the Joint Applicants will also not be
10 submitting testimony.

11 In addition, the City will be redacting certain
12 provisions of the testimony of Kent Miller, and I take it
13 that Mr. Kleppinger will be providing a copy of that for the
14 court reporter when it's available.

15 MR. KLEPPINGER: Yes. I hope to present the redacted
16 version to the reporter tomorrow.

17 JUDGE CHESTNUT: Okay. Thank you.

18 MR. MURPHY: And, also, we will not be cross-
19 examining the City of Philadelphia Witness Kent Miller.

20 JUDGE CHESTNUT: Okay. Does anybody have any comment
21 or anything they want to say about those stipulations?

22 MR. NIESEN: If Your Honor pleases, in regard to the
23 agreement with Philadelphia Gas Works, I just would want to
24 point out that we would reserve the opportunity to address
25 the redirect that might be done by the Joint Applicants with

1 Dr. Carpenter tomorrow when he's here.

2 JUDGE CHESTNUT: I don't know what you mean by that,
3 but you know that the Joint Applicants open and close. So
4 there's not going to be endless rounds of responsive
5 testimony, if that's what you have in mind.

6 MR. MURPHY: Your Honor, in addition to what Mr.
7 Niesen said, I failed to add that with their right to do
8 that, we would be performing our oral rejoinder after Dr.
9 Carpenter's testimony tomorrow.

10 JUDGE CHESTNUT: Okay. Sounds okay to me.

11 Mr. Kleppinger?

12 MR. KLEPPINGER: Your Honor, I'm not sure if Mr.
13 Murphy indicated this, but part of the understanding that
14 the City reached with the company is that the limited cross-
15 examination we had submitted in our grid for the PECO
16 witnesses, we would not be cross-examining Witnesses
17 O'Brien, Morris, Hieronymus, and Crowley. We had indicated
18 slight cross for them.

19 JUDGE CHESTNUT: So you'll have no cross for them;
20 okay.

21 MR. KLEPPINGER: Just for your planning purposes and
22 the shortness of the hearing that that facilitates.

23 JUDGE CHESTNUT: Great.

24 MR. KAPLAN: Your Honor, I have a question of Mr.
25 Murphy with respect to his last statement on the oral

1 rejoinder. Would Dr. Hieronymus come back tomorrow to do
2 that oral rejoinder?

3 MR. MURPHY: No. We would do the oral rejoinder
4 through Dr. Morris.

5 MR. KAPLAN: Okay. So Dr. Hieronymus would not be
6 returning?

7 MR. MURPHY: That's correct.

8 MR. KAPLAN: Thank you.

9 JUDGE CHESTNUT: Would it be today?

10 MR. MURPHY: Dr. Hieronymus will be doing his oral
11 rejoinder today.

12 MR. KAPLAN: Today. But after Dr. Carpenter
13 testifies tomorrow, that would be Dr. Morris?

14 MR. MURPHY: Dr. Morris.

15 MR. KAPLAN: Thank you.

16 JUDGE CHESTNUT: I thought Dr. Morris was scheduled
17 for today.

18 MR. MURPHY: His cross-examination is scheduled for
19 today, Your Honor.

20 JUDGE CHESTNUT: Okay. That's okay with me as long
21 as it's all right with you guys in terms of how we proceed
22 here, but I would like us to go in an orderly fashion,
23 though.

24 Anything else then about the stipulations?

25 MR. DILLON: Your Honor, is this the point in time

1 when you'd like the parties to admit the testimony which is
2 not going to be cross-examined?

3 JUDGE CHESTNUT: I was going to get to that. That
4 was going to be my next question. So we can get to that now
5 if you want, sure.

6 Do you want to get started then?

7 MR. DILLON: I'd be happy to, Your Honor. PPL has --

8 JUDGE CHESTNUT: Hold on a second. Did you send me
9 an e-mail? I think you did. I think I did get something of
10 yours. Let me get that first.

11 (Pause.)

12 MR. KAPLAN: We sent you an e-mail with the
13 statements.

14 JUDGE CHESTNUT: So it's the direct and surrebuttal
15 of Dr. Kalt?

16 MR. DILLON: That's correct. At this time, Your
17 Honor, we have to distribute to the court reporter copies of
18 the following statements which will be admitted by
19 stipulation: PPL Statement No. 1, the direct testimony of
20 Dr. Joseph P. Kalt, as well as Exhibit Nos. JPK-1 through
21 JPK-11.

22 Also, at this time, we have to distribute to the
23 court reporter copies of PPL Statement No. 1-SR, the
24 surrebuttal testimony of Joseph P. Kalt, and, in addition to
25 that, Exhibit Nos. JPK-12 through JPK-14.

1 We have additional copies if Your Honor would like an
2 additional copy at this time.

3 JUDGE CHESTNUT: Not if it's the same as the copy
4 that I received previously.

5 MR. DILLON: It is, indeed, the same, Your Honor.

6 JUDGE CHESTNUT: Okay. All right. So, PPL
7 Statements 1 and 1-SR and Exhibits JPK-1 through 14 are
8 admitted.

9 MR. DILLON: Thank you, Your Honor.

10 JUDGE CHESTNUT: I assume there's no objection.

11 (No response.)

12 JUDGE CHESTNUT: Okay; just to be sure.

13 (Whereupon, the documents were
14 marked as PPL Statements Nos. 1 and
15 1-SR and PPL Exhibits Nos. JPK-1
16 through JPK-14 for identification,
17 and were received in evidence.)

18 JUDGE CHESTNUT: Okay. Anybody want to go next?

19 MR. MICKENS: I'll go, Your Honor.

20 JUDGE CHESTNUT: Okay; OTS.

21 MR. MICKENS: Your Honor, I've given two copies to
22 the court reporter of a document that I would like to be
23 admitted without cross-examination by stipulation.

24 Prior to doing that, let me just state for the record
25 that OTS is withdrawing OTS Statement No. 2 and OTS Exhibit

1 No. 2.

2 JUDGE CHESTNUT: Well, you're not actually
3 withdrawing it, because it was never filed.

4 MR. MICKENS: It has been distributed, so just for
5 informational purposes.

6 JUDGE CHESTNUT: So we're talking Statements 1 and 3
7 then and associated exhibits?

8 MR. MICKENS: That's right. I'll indicate what's
9 being submitted. OTS Statement No. 1, OTS Exhibit No. 1,
10 OTS Statement No. 3, OTS Exhibit No. 3.

11 JUDGE CHESTNUT: Wait, wait. Just a second, please.
12 (Pause.)

13 JUDGE CHESTNUT: I'm sorry. That was 1 and 3. Then
14 what were you going to go onto? 1-S?

15 MR. MICKENS: Yes; OTS No. 1-SR, OTS Statement No.
16 3-SR, OTS Statement 2-SR. And that is a redacted version
17 from what was distributed. And OTS Exhibit No. 3-SR.

18 JUDGE CHESTNUT: Okay. They're all admitted,
19 obviously.

20 (Whereupon, the documents were
21 marked as OTS Statement Nos. 1, 3,
22 1-SR, 2-SR, 3-SR and OTS Exhibits
23 Nos. 1, 3, and 3-SR for
24 identification, and were received
25 in evidence.)

1 JUDGE CHESTNUT: I'm not clear. Is 2-SR withdrawn?

2 MR. MICKENS: No. 2-SR is being admitted.

3 JUDGE CHESTNUT: The only thing you're withdrawing is
4 Statement 2 then and the associated exhibit?

5 MR. MICKENS: And Exhibit No. 2.

6 JUDGE CHESTNUT: Right.

7 MR. MICKENS: Now, would you like a copy of the
8 redacted version of OTS 2-SR?

9 JUDGE CHESTNUT: Yes.

10 (Document handed to Judge Chestnut.)

11 JUDGE CHESTNUT: Thank you.

12 MR. MICKENS: Are those documents admitted, Your
13 Honor?

14 JUDGE CHESTNUT: Yes, they are.

15 MR. MICKENS: Thank you.

16 JUDGE CHESTNUT: Thank you, Mr. Mickens.

17 Okay. Anybody want to volunteer to go next?

18 MS. SHINKMAN: I will, Your Honor.

19 JUDGE CHESTNUT: Okay.

20 MS. SHINKMAN: Your Honor, my name is Susan Shinkman.
21 I represent the Department of Environmental Protection, and
22 I'm here to move for the admission of DEP Statement No. 3,
23 the testimony of Daniel Desmond; and DEP will not be moving
24 for the admission of any other testimony.

25 JUDGE CHESTNUT: Okay. You're statement is admitted.

1 (Whereupon, the document was marked
2 as DEP Statement No. 3 for
3 identification, and was received in
4 evidence.)

5 MS. SHINKMAN: Thank you.

6 JUDGE CHESTNUT: Anybody want to go next? Ms.
7 McCloskey?

8 MS. McCLOSKEY: Your Honor, we'd like to do ours
9 either tomorrow or on Monday. There are some redactions
10 that need to be made to some of our testimony.

11 JUDGE CHESTNUT: That's fine. Anybody else want to
12 do this tomorrow? Yes.

13 MS. WEBB: Good morning, Your Honor. Sharon Webb on
14 behalf of the OSBA. I'm giving the court reporter copies of
15 OSBA Statements 1, 2, 3 and 4, which is the direct,
16 rebuttal, surrebuttal, and supplemental testimony of our
17 witness, Brian Kalcic.

18 JUDGE CHESTNUT: Hold on just a second, please. 1,
19 2, 3 and 4.

20 MS. WEBB: Additionally --

21 JUDGE CHESTNUT: Are any of those redacted?

22 MS. WEBB: I have included a list of the redactions
23 with the testimony. I also have copies for the parties and
24 for Your Honor.

25 JUDGE CHESTNUT: Okay. Obviously, the documents are

1 admitted.

2

(Whereupon, the documents were

3

marked as OSBA Statements Nos. 1,

4

2, 3 and 4 for identification, and

5

were received in evidence.)

6

JUDGE CHESTNUT: Let me just clarify that the

7

redactions are not because it involves proprietary material?

8

MS. WEBB: No, Your Honor.

9

JUDGE CHESTNUT: So I'm assuming that unless

10

something is marked proprietary, it's going to be treated as

11

non-proprietary for filing purposes. Okay.

12

Does anybody else want to go today?

13

MR. MURPHY: Your Honor, Joint Applicants will go

14

today. We have a list of exhibits here that are similar to

15

what we provided to Your Honor yesterday, and I propose that

16

I just read through the ones that we're planning to admit

17

through stipulation.

18

JUDGE CHESTNUT: Okay.

19

MR. MURPHY: Two copies of each of these statements

20

and exhibits have been provided to the court reporter, and

21

they include the merger application filed February 4th, 2005

22

along with Exhibits A, B, C and D to that application; PECO

23

Statement No. 1, PECO Statement No. 2, along with Exhibits

24

WDA-1, WDA-2, 3, 4, 5 and 6; PECO Statement No. 1-R, along

25

with --

1 JUDGE CHESTNUT: Wait. Let me find that. Okay.

2 MR. MURPHY: Along with Exhibits DPO-1, 2, 3, 4, 5
3 and 6; and 6 was provided on August 24th in the errata that
4 we provided. PECO Statement No. 2 --

5 JUDGE CHESTNUT: Excuse me. During a break, see if
6 you have a copy of that for me. I could not find that
7 August 24th submission.

8 MR. MURPHY: The errata?

9 JUDGE CHESTNUT: Yes.

10 MR. MURPHY: Okay.

11 JUDGE CHESTNUT: I assume the errata has been picked
12 up in your revised testimony, but if there's anything else
13 such as that exhibit, let me have it.

14 MR. MURPHY: Yes.

15 JUDGE CHESTNUT: Okay.

16 MR. MURPHY: PECO Statement No. 2-R; PECO Statement
17 No. 4-R, along with the Exhibits LC-1, 2, 3, 4, 5 and 6;
18 PECO Statement No. 5-R, the rebuttal testimony of M. Bridget
19 Reidy, along with Exhibits BR-1 and 2; PECO Statement No.
20 6-R; PECO Statement No. 7-R, along with Exhibits BDC-1, 2, 3
21 and 4; PECO Statement No. 8-R, along with Exhibit WJP-1;
22 PECO Statement No. 10-R, the rebuttal testimony of Jeff
23 Benjamin, along with Exhibit JAB-1; PECO Statement No. 11-R,
24 along with Exhibits JRM-1, JRM-2 and JRM-3; PECO Statement
25 No. 12-R; PECO Statement No. 1-DQ; PECO Statement No. 12-DQ;

1 PECO Statement No. 13-DQ; the Joint Petition for Settlement
2 that was filed on September 13th, 2005; and PECO Statement
3 No. 1-S, which was circulated on September 14th, 2005.

4 JUDGE CHESTNUT: Thank you. Those documents are all
5 admitted.

6 (Whereupon, the documents were
7 marked as Joint Application, PECO
8 Statements Nos. 1, 2, 1-R, 2-R,
9 4-R, 5-R, 6-R, 7-R, 8-R, 10-R,
10 11-R, 12-R, 1-DQ, 12-DQ, 13-DQ,
11 1-S, Joint Petition for Settlement,
12 and PECO Exhibits A, B, C, D,
13 WDA-1, WDA-2, WDA-3, WDA-4, WDA-5,
14 WDA-6, DPO-1, DPO-2, DPO-3, DPO-4,
15 DPO-5, DPO-6, LC-1, LC-2, LC-3,
16 LC-4, LC-5, LC-6, DR-1, DR-2,
17 BDC-1, BDC-2, BDC-3, BDC-4, WJP-1,
18 JAB-1, JRM-1, JRM-2, JRM-3 for
19 identification, and were
20 received in evidence.)

21 JUDGE CHESTNUT: Anybody else?

22 (No response.)

23 JUDGE CHESTNUT: Okay. Then --

24 MR. MURPHY: Your Honor, if I might approach the
25 bench?

1 JUDGE CHESTNUT: Sure.

2 MR. MURPHY: I'm providing to you a copy of the
3 August 24th letter that had the errata.

4 JUDGE CHESTNUT: I didn't get this, and we looked
5 through the file.

6 Are there any other procedural housekeeping matters
7 to address?

8 (No response.)

9 JUDGE CHESTNUT: Okay. Where are we in terms of
10 witnesses for today then? Are we still going to go with, I
11 assume, Dr. Hieronymus?

12 MR. MURPHY: Your Honor, I believe today's cross-
13 examination and presentation of testimony is limited to Dr.
14 Hieronymus and Jack Crowley and Dr. Morris.

15 JUDGE CHESTNUT: They are the three who are listed.
16 Are you going to present them individually or as a panel?

17 MR. BONNEY: Individually, Your Honor.

18 JUDGE CHESTNUT: Do you have a preference in terms of
19 who goes first?

20 MR. BONNEY: Dr. Hieronymus first, Your Honor.

21 JUDGE CHESTNUT: Okay.

22 (Pause.)

23 JUDGE CHESTNUT: Good morning, Dr. Hieronymus. Would
24 you raise your right hand, please?

25 **Whereupon,**

WILLIAM H. HIERONYMUS

having been duly sworn, testified as follows:

JUDGE CHESTNUT: Please sit down and give and spell your name for the record.

THE WITNESS: My name is William H. Hieronymus, H-i-e-r-o-n-y-m-u-s.

JUDGE CHESTNUT: Go ahead.

DIRECT EXAMINATION

BY MR. NAEVE:

Q. Dr. Hieronymus, would you please provide the court with your title?

A. I'm a Vice President of CRA International.

Q. And what is your address?

A. 200 Clarendon Street, T-33, Boston, Massachusetts, 02116.

Q. Do you have before you Joint Applicants' Statements PECO -- or PECO Statement 3, Exhibits WHH-1 and 1-A, and Statement 3-R, Exhibit WHH-2, and Statement 3-DQ?

A. I'm sorry; the latter?

Q. Statement 3-DQ.

A. Actually, I don't, but I'm sure if it becomes relevant, you can provide it to me.

Q. Were these statements and exhibits prepared under your direct control and supervision?

A. Yes, they were.

1 JUDGE CHESTNUT: Excuse me. Do you have an extra
2 copy of Statement 3?

3 MR. BONNEY: Yes, Your Honor.

4 (Document handed to Judge Chestnut.)

5 BY MR. NAEVE:

6 Q. Dr. Hieronymus, are the responses to the
7 questions and those statements true and correct to the best
8 of your information and belief?

9 A. Yes, they are.

10 Q. If I were to ask you the same questions today,
11 would you give the same responses?

12 A. I would.

13 MR. NAEVE: Your Honor, I move for admission of PECO
14 Statement 3, Exhibits WHH-1, WHH-1-A, Statement 3-R and
15 Exhibit WHH-2, and Statement 3-DQ.

16 JUDGE CHESTNUT: Any objection?

17 MR. KAPLAN: Your Honor, we received last night
18 sometime very late redacted versions of these statements.

19 My first inquiry is what version are we seeking to
20 admit into evidence?

21 MR. NAEVE: We're seeking to admit the redacted
22 version.

23 MR. KAPLAN: Your Honor --

24 JUDGE CHESTNUT: Is it redacted or revised, because
25 they're not the same?

1 MR. NAEVE: It is redacted and revised.

2 JUDGE CHESTNUT: Okay.

3 MR. KAPLAN: Your Honor, we have endeavored last
4 night and this morning to determine whether there was
5 anything in that redacted version which we either would find
6 objectionable or perhaps exceeded what we understand is the
7 reason for the redaction or not.

8 I would like to reserve objection given the lateness
9 of the time we received them. However, I am willing to
10 reserve with a time limit. In other words, if we do not
11 inform Your Honor by the opening of hearings tomorrow, our
12 objection is withdrawn.

13 JUDGE CHESTNUT: You're going to have to remind me.

14 MR. KAPLAN: We will do so, Your Honor.

15 JUDGE CHESTNUT: Okay. And I assume that's only to
16 Statement 3-R?

17 MR. KAPLAN: Only the one that was redacted.

18 JUDGE CHESTNUT: Okay.

19 MR. NIESEN: And if Your Honor pleases, on behalf of
20 Philadelphia Gas Works, I make the same reservation. And I
21 guess just for the record to be clear, what has been marked
22 as Statement 3-R is what is captioned in the upper right-
23 hand corner "PECO Statement No. 3-R (Revised)?"

24 MR. NAEVE: That's correct.

25 MR. NIESEN: And it's my understanding also, and

1 perhaps it can be confirmed on the record, that the
2 revisions to 3-R do not affect and are not intended to
3 affect Dr. Hieronymus' testimony concerning Dr. Carpenter.

4 MR. NAEVE: That is correct, Your Honor.

5 JUDGE CHESTNUT: Okay.

6 MR. NAEVE: The redactions are intended to remove
7 references to testimony which has been withdrawn.

8 MR. KAPLAN: So the same statement on the record, Mr.
9 Naeve, would apply to Dr. Kalt's testimony?

10 MR. NAEVE: That's correct.

11 MR. KAPLAN: Thank you.

12 JUDGE CHESTNUT: So, are you still reserving your
13 right to object or not?

14 MR. KAPLAN: I take Mr. Naeve's word very seriously,
15 Your Honor. However, responsibly, I must continue my
16 reservation until --

17 JUDGE CHESTNUT: How about if I admit it
18 conditionally?

19 MR. KAPLAN: That would be acceptable to us, Your
20 Honor.

21 JUDGE CHESTNUT: Okay; subject to your right to raise
22 it tomorrow morning.

23 MR. KAPLAN: Very good. Thank you, Your Honor.

24 MR. NIESEN: And mine, also, Your Honor, if you
25 would.

1 JUDGE CHESTNUT: Okay.

2 MR. NIESEN: Thank you.

3 JUDGE CHESTNUT: So that's 3, 3-R and 3-DQ and
4 associated exhibits. Okay.

5 (Whereupon, the documents were
6 marked as PECO Statements Nos. 3,
7 3-R, 3-DQ and PECO Exhibits Nos.
8 WHH-1 and WHH-1-A and WHH-2 for
9 identification, and were received
10 in evidence.)

11 JUDGE CHESTNUT: Is he available for cross-
12 examination or do you have anything further?

13 MR. NAEVE: Yes, Your Honor. At this point, I'd like
14 to conduct oral rejoinder examination of Dr. Hieronymus.

15 JUDGE CHESTNUT: Okay.

16 BY MR. NAEVE:

17 Q. Dr. Hieronymus, I'd like to turn your attention
18 to page 18 of Dr. Kalt's surrebuttal testimony, and, in
19 particular, I'd like you to focus on lines 1 through 7.

20 A. I have it.

21 Q. At this point in his surrebuttal, Dr. Kalt
22 introduces a new basis for his proposition that FTRs should
23 be allocated on the -- the imports should be allocated on
24 the basis of FTRs, and he say in effect that FTRs create an
25 incentive for the Merger Parties to withhold generation

1 because their FTRs will increase in value --

2 MR. KAPLAN: Your Honor, Mr. Naeve is starting to
3 characterize and give impressions as to what the testimony
4 is, and I think if he intends to ask Dr. Hieronymus about
5 this testimony, he should ask Dr. Hieronymus what his
6 impressions are and what he thinks --

7 JUDGE CHESTNUT: I agree 100 percent. All you need
8 to do is refer the witness to the portion you want him to
9 comment on.

10 MR. NAEVE: All right, Your Honor.

11 BY MR. NAEVE:

12 Q. Dr. Hieronymus, would you respond to the
13 statements made by Dr. Kalt pertaining to incentives to
14 withhold created by FTRs?

15 A. Sure. Previously, Professor Kalt had talked
16 about FTRs giving you the right to sink generation control
17 and treated it like it was a physical right, which it is
18 not, and I so stated.

19 Now he's saying that no, no; the reason why you need
20 to take them into account is because holding an FTR creates
21 an incentive to increase a price in the market that the FTR
22 goes into that would not be present if you didn't have the
23 FTR. That's what I think he's saying.

24 I'm sorry. I've lost the question as to whether that
25 was all you were asking.

1 Q. What is your reaction to Dr. Kalt's statement?

2 A. Well, I think once you start talking about
3 incentives, you have to take into account the fact that FTRs
4 -- the grandfathered FTRs that he's talking about
5 principally go with load; and so if you're going to take
6 into account the incentive effects of FTRs, you need to take
7 into account the parallel incentive effects of having load,
8 and it's important that you do that properly.

9 Q. For clarification purposes, Dr. Hieronymus,
10 would you define what an FTR is?

11 A. An FTR is the right to receive the amount of
12 congestion between the two points. So an FTR is point to
13 point. So you might have an FTR from Keystone to some point
14 in New Jersey, for example; and to the extent there is
15 congestion between Keystone and New Jersey, you get paid the
16 amount of that congestion 24/7 times the quantity of FTRs
17 that you hold.

18 So it has entirely to do with the value of
19 congestion. Conversely, for example, it has nothing to do
20 with the right to import generation, and the value of the
21 FTR is the same whether you're a generator or a marketer or
22 whatever. It's just the difference between those two prices
23 each and every hour.

24 Q. Could you elaborate on your statement about the
25 incentive effects of FTRs and load?

1 A. Well, if I have -- suppose I have a thousand
2 megawatts of load and a thousand megawatts of generation in
3 PJM East. I'm sorry; a thousand megawatts of FTRs into PJM
4 East. If the price goes up in PJM East by my having done
5 something or for whatever reason by, say, a dollar, my FTR
6 becomes more valuable by a dollar, and that's the incentive
7 effect that Professor Kalt is talking about.

8 But my cost of serving load also goes up by a dollar;
9 and to the extent those two are paired, then the incentive
10 effect is washed out. I have the load. I have the FTR.
11 Having load means I have less incentive to increase prices
12 because I'm not selling that amount in the market. I may
13 indeed even be buying that amount. Having FTRs increases
14 the incentive. They're related.

15 Q. Now, are all FTRs paired with load?

16 A. No. You can also buy FTRs in the annual
17 auction, but I don't know what to do with those, because
18 they're only annual. I don't know what's going to be held
19 in 2006 or 2007 or 2008 that acquired through the auction
20 even if, as Dr. Kalt asserts, there's a higher degree to the
21 AARs that give rise to the grandfathered FTRs.

22 Q. So which FTRs are associated with load?

23 A. It's the so-called grandfathered FTRs.

24 Q. How does one receive a grandfathered FTR?

25 A. I'm sorry?

1 Q. How does one receive a grandfathered FTR?

2 A. Initially, they were allocated back on the basis
3 of 1998 positions, if you like, but if PECO, for example,
4 loses load, then the load serving entity that acquires that
5 load automatically acquires a pro rata share of all the good
6 FTRs, all the ones that have positive rather than negative
7 values.

8 Q. Did Dr. Kalt account for the offsetting
9 incentive effects of serving load for the FTRs of carrying
10 the load?

11 A. No. The analysis -- my analysis that Professor
12 Kalt modified was what's called an economic capacity
13 analysis under the FERC merger policy guidelines, and that
14 analysis doesn't look at load at all. It doesn't look at
15 various things that might give you incentives or
16 disincentives. It simply looks at your generation position.

17 Q. Is there a type of analysis that would account
18 for these incentive effects?

19 A. Yes, there is. FERC requires two kinds of
20 analyses, and they're both in my FERC testimony. Economic
21 capacity looks at the generation or the long-term contracts
22 in control to determine your share of the market; and in
23 terms of transmission allocation, if I have a physical right
24 to bring generation from my own remote generator into the
25 relevant market, that gets treated as if it is, to use

1 Professor Kalt's words, sunk into that market. So it gets
2 allocated as if it were in that market, but, of course,
3 there are no such rights in PJM.

4 The purpose, as I understand it, of economic capacity
5 analysis is to look at the ability to increase prices. I
6 can increase prices by withholding generation. I can
7 withhold generation that's within the market. That's
8 straightforward enough. But FERC is also concerned about
9 generation that's not within the confines of the market to
10 the extent that there is transmission capability to come in,
11 and so there is a well settled way of dealing with this, and
12 that's the way I dealt with it, which is to allocate the
13 transmission capability into the market on a pro rata basis
14 to all the generators who have economic generation outside
15 the market that can reach it.

16 Available economic capacity analysis is the analysis
17 that looks at your incentive to increase prices as distinct
18 from your ability, and the principal difference ordinarily
19 is that parties' -- not just Applicants, but other parties
20 -- load commitments are subtracted from their generation in
21 order to look at what they call available economic capacity,
22 and then they look at that market, which is, in effect, the
23 wholesale market, to say how much -- how important are the
24 merged parties in that market; what incentive do they have
25 to increase prices in that market.

1 So that's the market or that's the analysis, the
2 available economic capacity analysis, that keys into the
3 issue of incentives that Professor Kalt is now pointing to
4 when he's talking about how he thinks FTRs should be
5 treated.

6 MR. KAPLAN: Your Honor, I would object to any
7 further questions along these lines as beyond the scope of
8 the surrebuttal testimony and ask that the last answer be
9 stricken, and let me explain why. The process of filing
10 testimony and rebuttal and surrebuttal narrows the scope.
11 Dr. Kalt was specifically responding to Dr. Hieronymus'
12 economic capacity analysis; in fact, alternate tables of his
13 economic capacity analysis were put in. There was no
14 discussion of Dr. Kalt of the available economic capacities
15 in the passages we're referring to, nor was that the subject
16 of the surrebuttal testimony on this point. Dr. Hieronymus,
17 on the other hand, has just given us a long explanation of
18 another test, of another test that FERC does employ, but
19 that is not what Dr. Kalt was talking about, he was talking
20 about the errors Dr. Hieronymus made in doing his economic
21 capacity analysis, which is clearly one of the tests that
22 FERC applies. So I think we're going down a road which is
23 going to take us far afield of the written testimony,
24 surrebuttal testimony, and is clearly beyond the purpose of
25 what I understand is a very limited scope rejoinder.

1 JUDGE CHESTNUT: Do you have a response?

2 MR. NAEVE: Your Honor, in his direct testimony
3 Dr. Kalt focused more on physical ability to move power into
4 the PJM east market and he analogized having FTRs as giving
5 a physical ability to move. In his surrebuttal testimony
6 Dr. Kalt introduced a new concept, and that new concept was
7 FTRs create a new incentive to raise prices, and
8 Dr. Hieronymus is testifying as to the type of analysis FERC
9 does to measure incentives as opposed to measure ability to
10 influence prices. And indeed, and I'll read directly from
11 Dr. Kalt's testimony --

12 JUDGE CHESTNUT: That's not necessary. Thank you.

13 MR. NAEVE: He in effect says an analysis should be
14 done of incentives. Dr. Hieronymus has prepared an exhibit,
15 an available economic capacity analysis pursuant to FERC
16 guidelines, but including the FTRs to look at incentives
17 under available economic capacity, which is the methodology
18 FERC uses to measure incentives as opposed to ability, and
19 we would like to discuss that.

20 JUDGE CHESTNUT: I'm a little concerned because I
21 think Dr. Hieronymus is directly responding to Dr. Kalt's
22 contention, but I really hope it's not going much further.

23 MR. KAPLAN: And I would object to any new tabular
24 analysis. We have not had an opportunity to --

25 JUDGE CHESTNUT: Yes. I think that's inappropriate

1 at this point in the proceeding. If you have that you could
2 have provided it --

3 MR. NAEVE: Actually, Your Honor, we could not have
4 responded to the incentive argument with tabular evidence,
5 because Dr. Kalt didn't raise that incentive argument in his
6 testimony. He raised it for the first time in the last
7 piece he filed. Had he raised it originally, we would have
8 been able to --

9 JUDGE CHESTNUT: I'm not talking about originally,
10 I'm talking about in his surrebuttal testimony. It's always
11 been the process here that oral rejoinder is very brief and
12 limited because the parties really don't have a chance to
13 think about it before they prepare their cross. If you want
14 to take a short break and review that, I would be --

15 MR. KAPLAN: Your Honor, we think it's entirely
16 inappropriate. We have made every effort to conduct
17 thorough discovery, we conducted a deposition. If we want
18 to take a week break, or two week break, to permit us to
19 reopen the deposition of Dr. Hieronymus and conduct
20 discovery on the tables they're about to present, and then
21 also have an opportunity for further written testimony,
22 maybe that might be acceptable, but I don't think that's
23 what the Applicants had in mind here. This is entirely
24 beyond the scope of what is normally done. Now, I'm not new
25 to Pennsylvania proceedings, and I have never seen this

1 myself, anything quite so extensive properly admitted on
2 rejoinder.

3 JUDGE CHESTNUT: Well, it's hard for me to discuss
4 this because I don't know what your tables contain or how
5 detailed they are or what kind of time is required for you
6 and Dr. Kalt to review them. It may be that they're pretty
7 obvious to experts.

8 MR. KAPLAN: Well, it took us somewhere about eight
9 weeks to get responses to our initial discovery on the
10 initial tables presented. This is not simple.
11 Dr. Hieronymus' model is quite complex, the underlying data
12 is quite complex. The assumptions used in assigning and
13 determining available capacity, as Dr. Hieronymus has
14 admitted in his own testimony, are very difficult, and
15 there's a great deal of judgment involved. This is entirely
16 inappropriate. We really would have to adjourn these
17 proceedings and maybe resume in a month.

18 JUDGE CHESTNUT: Well, that's not going to happen. I
19 think we all know that.

20 MR. KAPLAN: I understand, Your Honor. That's why I
21 think the simpler course here is to restrict Dr. Hieronymus
22 to proper rejoinder under Pennsylvania practice.

23 MR. NAEVE: Your Honor, a couple of points. The
24 first is, had Dr. Kalt not held back this argument until the
25 surrebuttal testimony, we would have been able to submit

1 this evidence in response to his statement, and it's
2 somewhat unfair to the Applicants for him to introduce a new
3 concept in that testimony and then not allow us to respond
4 to it, doing the type of analysis which he himself says
5 needs to be done.

6 Might I suggest that we go through this analysis, and
7 then when we attempt to move it into evidence, if Mr. Kaplan
8 objects at that point --

9 JUDGE CHESTNUT: I'm not sure if I like that.
10 Dr. Kalt's surrebuttal was served at the end of August, so
11 Dr. Hieronymus had plenty of time to review it before now.

12 MR. NAEVE: That's correct, but this is our first
13 opportunity to respond to it, Your Honor.

14 JUDGE CHESTNUT: Well, no. I'm saying that you could
15 have prepared the tables and provided them to PPL prior to
16 the hearing so that they and their experts would have had a
17 chance to review them, instead of waiting till now to do it.
18 In fact, I'm kind of surprised because there was always kind
19 of a good faith understanding when it came to oral rejoinder
20 that you would try and accommodate the other parties, that
21 you would provide a written outline, if possible, or
22 whatever.

23 Do you have the tables? Did you provide them to PPL
24 yet?

25 THE WITNESS: He has them. I don't.

1 MR. NAEVE: We have them right here, Your Honor.

2 MR. KAPLAN: Your Honor, there's a couple other
3 things that need to be said here. First of all, they did
4 not object when -- if, in fact, they claim Dr. Hieronymus
5 raised a new concept, they should have objected that it was
6 beyond the scope of --

7 JUDGE CHESTNUT: Are you talking about Dr. Kalt?

8 MR. KAPLAN: Dr. Kalt raised a new concept. I'm
9 sorry, Your Honor.

10 -- that it was beyond the scope of proper surrebuttal
11 evidence. They did not. That's number one.

12 Number two, Dr. Hieronymus is well aware, as an
13 expert in antitrust law, that incentive and ability are
14 clearly part of the test upon which you determine a
15 monopoly. This is not new. We did not introduce a new
16 concept, we simply referred to common antitrust terms which
17 have been extant for 50, 60, 70, 80 years.

18 JUDGE CHESTNUT: Well, if that's true then, wouldn't
19 you expect that there would be a response to Dr. Kalt's
20 surrebuttal testimony?

21 MR. KAPLAN: Well, Dr. Hieronymus, in his rebuttal
22 testimony, talked about, at page 22 -- this is I believe his
23 Statement No. 3-R, page 22 --

24 JUDGE CHESTNUT: Of his rebuttal?

25 MR. KAPLAN: In his rebuttal.

1 -- lines 10 through 14, and I read, "At best, this
2 suggests that ARR's" -- and ARR's are a precursor to FTR's,
3 Your Honor.

4 JUDGE CHESTNUT: Okay.

5 MR. KAPLAN: -- "should be reflected in an available
6 economic capacity analysis, but not an economic capacity
7 analysis. As I explained in my supplemental testimony,
8 however, Applicants' additional mitigation commitments
9 reduce the incremental available economic capacity to zero
10 (actually, negative) in all but one instance." He did in
11 fact already respond. He was aware of exactly what Dr. Kalt
12 was talking about. This is a red herring.

13 JUDGE CHESTNUT: Well, unless I'm not understanding
14 this, that is the subject of your oral rejoinder, isn't it?

15 MR. NAEVE: Our oral rejoinder goes to the issue of
16 incentives, pointing out merely that Dr. Kalt previously had
17 not objected to Dr. Hieronymus' approach because of the
18 incentive effects, and Dr. Hieronymus did not do an analysis
19 of the incentive effects because it was not an issue raised
20 previously by Dr. Kalt. Now that Dr. Kalt has raised the
21 incentive issue, Your Honor, we feel we should be allowed to
22 respond to it.

23 JUDGE CHESTNUT: Respond to it briefly.

24 Are you ready to move on from this?

25 MR. NAEVE: Yes, Your Honor.

1 JUDGE CHESTNUT: I'm not going to strike the answer,
2 but if you are planning on presenting any kind of tables or
3 exhibits, I'm going to direct you to give them to PPL now.
4 And if you want a short break to review them, --

5 MR. NAEVE: We have one other, Your Honor, so why
6 don't we take a break here and --

7 JUDGE CHESTNUT: Why don't we take a break now then.

8 MR. KAPLAN: Thank you, Your Honor.

9 (Recess.)

10 JUDGE CHESTNUT: All right, we took a break so that
11 the parties could discuss the oral rejoinder being given by
12 Dr. Hieronymus.

13 Do you want to tell me where you are with that?

14 MR. NAEVE: Actually, Your Honor, with respect to the
15 exhibit that we were proposing to introduce, we will
16 withdraw that exhibit.

17 JUDGE CHESTNUT: Okay. Good.

18 MR. NAEVE: But I would like to ask Dr. Hieronymus
19 one further question on this issue.

20 BY MR. NAEVE:

21 Q. Dr. Hieronymus, you did prepare an available
22 economic capacity analysis; is that correct?

23 A. Yes.

24 MR. KAPLAN: Again, Your Honor, objection. I object
25 to any testimony about available economic capacity analysis.

1 It's beyond the scope of the surrebuttal.

2 JUDGE CHESTNUT: I thought you folks discussed this
3 and worked it out.

4 MR. NAEVE: Actually, we were giving Mr. Kaplan time
5 to review the exhibit. We didn't discuss this particular --

6 MR. KAPLAN: We did not respond on the surrebuttal to
7 Dr. Hieronymus' available economic capacity analysis. It
8 had nothing to do with it.

9 MR. NAEVE: They did, Your Honor, suggest that the
10 incentive effects of FTRs should be factored in, and our
11 point is, which this is our first opportunity to make that
12 point, it should be factored into the available economic
13 capacity analysis, not the economic capacity analysis.

14 MR. KAPLAN: And they've already made that point in
15 the rebuttal testimony.

16 JUDGE CHESTNUT: That sounds okay to me.

17 BY MR. NAEVE:

18 Q. Dr. Hieronymus, let's turn to another subject
19 here. I'd like to direct your attention to Dr. Kalt's
20 surrebuttal testimony on page 9, in particular lines 1
21 through 3.

22 JUDGE CHESTNUT: I'm sorry; what page was that?

23 MR. NAEVE: It's page 9, Your Honor.

24 JUDGE CHESTNUT: Of the direct or the --

25 MR. NAEVE: No, of the surrebuttal. And I'm focusing

1 his attention on lines 1 through 3.

2 (Pause.)

3 BY MR. NAEVE:

4 Q. Have you had a chance to read that,
5 Dr. Hieronymus?

6 A. Yes, I have. I'm sorry.

7 Q. Do you have any comments on the proposed
8 strategy by Dr. Kalt for raising prices for the nuclear
9 divestiture auction?

10 A. This raises, in the first instance, the question
11 of whether withholding to increase spot prices increases
12 long-term contract prices, which is an issue I've looked at
13 both in this proceeding, in a somewhat peripheral context,
14 looking at the supply curves, and also elsewhere, and I
15 think it's important, before you start speculating about
16 this possibility, to consider the unlikelihood that it would
17 be economic and the unlikelihood that you'd get away with it
18 and the substantial penalties you would incur if you got
19 caught.

20 MR. KAPLAN: Your Honor, I move the answer be
21 stricken. This is beyond the scope of the surrebuttal. If
22 you read clearly the sentence as quoted by Dr. Kalt, it says
23 that next month or two's forward prices. Forward prices, as
24 Dr. Hieronymus well knows, are different from spot prices.

25 JUDGE CHESTNUT: Are they? Yes or no, one word.

1 THE WITNESS: Yes, it is true that forward prices are
2 different than spot prices.

3 JUDGE CHESTNUT: Okay. Then restrict yourself to
4 responding directly to the surrebuttal.

5 THE WITNESS: I'll try, Your Honor.

6 JUDGE CHESTNUT: And if you're doing that, you need
7 to explain it so I understand it.

8 THE WITNESS: Okay; fine. I appreciate that.

9 BY MR. NAEVE:

10 Q. Dr. Hieronymus, will you respond to the
11 statement made by Dr. Kalt here and the proposed strategy?

12 A. Dr. Kalt appears to be saying that applicants
13 can somehow or another withhold capacity in order to affect
14 -- let me get the term accurate here -- in order to elevate
15 next month or two's forward prices. The problem with that
16 statement is what withholding does is affect the prices in
17 the market that you're affecting by withholding. The
18 markets in PJM are day ahead and real time spot prices.
19 There is no PJM market for one month forward, two month
20 forward prices. There is no effect of withholding
21 generation per se on one month forward, two month forward
22 prices. There is an effect of withholding generation on
23 spot prices.

24 Q. What's your opinion of his proposed strategy?

25 A. Well, in order for it to work, the mechanism

1 inherently has to be withholding generation, which
2 inherently has to have its effect on affecting spot prices
3 in order to have any effect on any price. And so when we
4 talk about so-called -- what's the language again --
5 elevating the next month or two month forward prices, the
6 mechanism by which you do this has to be the effect that you
7 have from withholding generation on the spot market, and
8 that's a policed market, so you can't do what Professor Kalt
9 is saying directly, you have to do it by mediation through
10 your effect on the spot market.

11 Q. And do you believe such a strategy would be
12 effective?

13 A. No.

14 Q. Why not?

15 JUDGE CHESTNUT: Didn't he just explain why not?

16 THE WITNESS: I think, Your Honor, the question he's
17 asking is whether the strategy of affecting the spot price,
18 thereby affecting the short-term forward price, thereby
19 affecting the long-term forward price, would be effective.

20 MR. KAPLAN: Your Honor, I agree with you, it was
21 asked and answered, and not only that, I suppose I should
22 reserve for cross-examination the serious factual errors
23 that Dr. Hieronymus just made, statements which I believe he
24 will retract once he's reminded of them.

25 JUDGE CHESTNUT: Well, you could have discussed that

1 during your break, too, and saved us all some time here. I
2 understand what you said, but I really do think you should
3 wrap it up very shortly, if you can.

4 BY MR. NAEVE:

5 Q. If the Applicants were to carry out such a
6 policy, do you anticipate that they would successfully
7 achieve higher prices in the forward market?

8 A. Well, that's the point of it, that's what
9 Professor Kalt is asserting might happen.

10 Q. And do you expect that they would?

11 A. No.

12 Q. Let's turn to another issue. I'm going to
13 direct your attention to page 12 of Dr. Kalt's surrebuttal
14 testimony.

15 JUDGE CHESTNUT: Do you have much more, Mr. Naeve?

16 MR. NAEVE: I'm sorry, Your Honor?

17 JUDGE CHESTNUT: Do you have many more issues after
18 this one?

19 MR. NAEVE: This is the last issue.

20 JUDGE CHESTNUT: Okay.

21 BY MR. NAEVE:

22 Q. Page 12, and in particular the paragraph
23 beginning on line 7 and running through line 10 on page 13.

24 A. I have it.

25 Q. Could you please provide your response to

1 Dr. Kalt's suggestion that perhaps FE Penelec should also,
2 on occasions, be excluded from the PJM Classic market.

3 A. Yeah. I think he may or may not have missed the
4 point of what I was trying to say, but what I was trying to
5 say is that if you look at his own depiction of prices in
6 2004 at different nodes in PJM and outside of PJM, not only
7 is it the case that FE and Penelec have essentially the same
8 price, they're properly considered to be in the same market
9 with PP&L, as is PEPCO, and in that sense APS is no
10 different than FE Penelec in that it properly is considered
11 in the market, which is, if you like, east of AEP and west
12 of the PJM East interface, that part which is added to PJM
13 East when PJM East is not itself constrained away, more
14 properly stated. That was really the point I was trying to
15 make. And it would be just as improper to exclude FE
16 Penelec as it is improper to exclude PPS.

17 Q. Have you prepared an exhibit to illustrate this
18 point?

19 A. Yes, I have. It just simply based off
20 Dr. Kalt's exhibit.

21 MR. NAEVE: Your Honor, we have not given Mr. Kaplan
22 a chance to review this exhibit, we have not discussed it.
23 I would ask Mr. Kaplan if he objects to the admission of
24 this.

25 MR. KAPLAN: Yes, Your Honor, I do object. The

1 exhibit is a response to Dr. Kalt's direct testimony. The
2 exhibit appeared in Dr. Kalt's direct testimony as JPK
3 No. 2. Your Honor will see that exhibit as JPK No. 2. If
4 Dr. Hieronymus wanted to redo JPK No. 2, that should have
5 been done on July 29.

6 JUDGE CHESTNUT: What is this proposed exhibit? I'm
7 looking at JPK-2.

8 MR. NAEVE: Your Honor, this is a three-page exhibit.
9 It is derived exclusively from all the information on that
10 exhibit. It is the response to the assertion that Dr. Kalt
11 made in his surrebuttal testimony that FE Penelec should
12 perhaps also be excluded from the PJM Classic market. It's
13 a three-page exhibit. There's no information on this
14 exhibit that's not contained in Dr. Kalt's exhibit, and
15 indeed, the first page of this three-page exhibit is merely
16 Dr. Kalt's exhibit for purposes of reference.

17 MR. KAPLAN: Your Honor, --

18 JUDGE CHESTNUT: Are you moving it in now?

19 MR. NAEVE: Yes, Your Honor.

20 JUDGE CHESTNUT: What do you want to have it marked
21 as?

22 MR. NAEVE: I'd like it marked Exhibit WHH-3.

23 (Whereupon, the document was marked
24 as PECO Exhibit No. WHH-3 for
25 identification.)

1 JUDGE CHESTNUT: Let me take a look at it.

2 I assume you're still objecting?

3 MR. KAPLAN: Yes. Your Honor, I think we have the
4 process here entirely backwards. There are two times when
5 something like this could come in, first as part of
6 Dr. Hieronymus' rebuttal testimony that was submitted in
7 July. If they chose not to do it there, what they should
8 have done is not waived their testimony of Dr. Kalt and
9 presented it to Dr. Kalt as a cross-examination exhibit. If
10 they had taken Dr. Kalt's chart as a cross-examination
11 exhibit and said, "Well, if we made these three changes,
12 doesn't this show x, y and z," that might be proper cross-
13 examination and I would not object, but not as direct
14 testimony, direct testimony by their own witness, long after
15 the time when it should have been presented. This was
16 again, as I say, this was an exhibit to Dr. Kalt's testimony
17 submitted on June 28 as Exhibit No. 2. There are two times
18 to respond, one, in the rebuttal testimony on July 29, or
19 two, in cross-examination of Dr. Kalt. Dr. Kalt was made
20 available to them; he was available until noon yesterday.
21 They have decided to waive and agreed not to cross-examine,
22 and I think that they've waived their opportunity to use
23 this.

24 MR. NAEVE: Your Honor, --

25 MR. KAPLAN: They can argue in words on the brief

1 anything -- they can do anything they want to do with these
2 numbers on the brief.

3 MR. NAEVE: Your Honor, there's no new information
4 here. All we're doing is responding to Dr. Kalt's assertion
5 that there should be perhaps a different market definition,
6 an assertion he made in his surrebuttal testimony, and that
7 would be a market that looks like PJM Classic but excluding
8 not only AP but excluding FE Penelec, and that's the purpose
9 of these exhibits.

10 MR. KAPLAN: And you had every opportunity in the
11 world to ask Dr. Kalt about his contention if he had come to
12 testify tomorrow.

13 MR. NAEVE: Your Honor, this would be the first time
14 we had an opportunity to respond on the record to that
15 assertion.

16 JUDGE CHESTNUT: It is a little awkward here. I
17 think it would have been an appropriate cross-examination
18 exhibit for Dr. Kalt, because you're asking him to basically
19 revise his own exhibit in light of this additional factor.
20 But on the other hand, I can't see that you're -- you did
21 have this agreement in terms of presenting Dr. Kalt and not
22 having him come. I find myself really caught here, because
23 like I said, I really feel that this really isn't all that
24 appropriate an exhibit, but on the other hand, you do have
25 the right to open and close, so I don't know if Dr. Kalt

1 could have really responded directly to this. I'm going to
2 let it in, although I do have some concerns.

3 MR. KAPLAN: Thank you.

4 JUDGE CHESTNUT: I really don't feel that you're all
5 that disadvantaged by it, but I do think it's marginally
6 inappropriate. So I will allow it's admission.

7 (Whereupon, the document marked
8 as PECO Exhibit No. WHH-3 was
9 received in evidence.)

10 BY MR. NAEVE:

11 Q. Dr. Hieronymus, looking at Exhibit WHH-3, were
12 you again using this exhibit to respond to Dr. Kalt's
13 assertion that FE Penelec as well as Allegheny Power should
14 not belong in PJM Classic market?

15 A. Sure. As you've indicated, the first page has
16 no new information on it, it's simply Professor Kalt's
17 exhibit, and the prices and the nodes on the second page are
18 identical to what they were in his exhibit. All I've done
19 here is try to explain why it is that PJM pre-2004, as
20 opposed to PJM pre-2004 minus FE Penelec and minus AP, is an
21 appropriate geographic market.

22 Very briefly, if you look at the difference between
23 AEP and the four utilities to its right, it's quite
24 substantial. If you look at the difference from the four
25 utilities to its right and the utilities in the east zone,

1 the differences are quite substantial. But if you look at
2 PPL, Professor Kalt's client, as the swing bus of PJM pre-
3 2004 excluding the east, you see that each of these
4 utilities that he's considered in this table are within less
5 than two dollars of that price, which is two or three
6 percent. So compared to looking at the exclusion of AEP or
7 looking at having to consider the east zone as a separate
8 zone, these guys really are in the same market.

9 Q. What does page 3 of your exhibit show?

10 A. All I'm trying to show on page 3 is that the
11 kinds of price differences one sees within this contested
12 area, that area that does or doesn't include APS and does or
13 doesn't include FE Penelec, are no greater than, in fact,
14 somewhat less than the price differences that we get in PJM
15 East, which is an uncontested appropriate geographic market.

16 MR. NAEVE: Your Honor, that's the extent of our oral
17 rejoinder. I would move Exhibit WHH-3 into the record.

18 JUDGE CHESTNUT: I thought I already admitted it, but
19 if I haven't, then I will.

20 MR. KAPLAN: My objection was noted.

21 JUDGE CHESTNUT: Certainly.

22 MR. NAEVE: Dr. Hieronymus is available for cross-
23 examination.

24 JUDGE CHESTNUT: Do you want to take a short break
25 before you do this?

1 MR. KAPLAN: Yes, if we could just have a second.

2 JUDGE CHESTNUT: Why don't we take like a five minute
3 break.

4 (Recess.)

5 JUDGE CHESTNUT: We'll go back on the record.

6 Mr. Kaplan, are you ready?

7 MR. KAPLAN: Thank you, Your Honor.

8 **CROSS-EXAMINATION**

9 BY MR. KAPLAN:

10 Q. Good morning, Dr. Hieronymus.

11 A. Good morning, Mr. Kaplan.

12 Q. I'll be examining you today on behalf of PECO
13 Companies. I'd like to go back to Exhibit WHH-3 which was
14 just recently introduced into evidence and which you
15 discussed with your counsel. These prices depicted here are
16 average over the year peak prices; is that correct?

17 A. Yes. That's what Professor Kahn asserts and I
18 have no reason to dispute it -- Professor --

19 Q. Kalt?

20 A. Kalt, sorry.

21 Q. Another noted economist.

22 And they're also zonal average prices as well?

23 A. Yes, that's correct.

24 Q. Now, you said earlier on your rejoinder that
25 there was no forward market in the PJM.

1 A. There's no PJM forward market.

2 Q. You mean there's no organized PJM forward
3 market; is that correct?

4 A. Run by PJM, yes.

5 Q. Right. There is an active, in fact, informal
6 forward market?

7 A. Sure.

8 Q. And you haven't done any studies, have you, to
9 determine what portion of PJM transactions go through the
10 spot market versus other kinds of transactions?

11 A. Not as such. I would anticipate that there are
12 far more longer term transactions, for example, hedge
13 contracts underlying the New Jersey BJS auction, than there
14 are spot transactions.

15 Q. Let's turn to your surrebuttal testimony, or
16 your testimony in general. In conducting your analysis of
17 market shares and the Herfindahl-Hirschmann Index --
18 otherwise known as HHI, which we're going to use in the
19 future, index -- and you used that proprietary model to
20 conduct your analysis which appeared in your testimony; is
21 that correct?

22 A. I used a proprietary model, yes.

23 Q. And the name of that model is the CASm model,
24 correct?

25 A. Yes, that's correct.

1 Q. I'd like to take a look at one of your exhibits
2 to understand what the model does for us. If we could turn
3 to Exhibit J-18 --

4 MR. KAPLAN: -- which is attached to, Your Honor,
5 Statement 1-A; do I have that correct, Mr. Murphy?

6 JUDGE CHESTNUT: What is that? You have to tell me
7 what that is.

8 MR. KAPLAN: That is the supplemental FERC testimony.

9 JUDGE CHESTNUT: Is that WHH-1A?

10 MR. KAPLAN: WHH-1A. Now --

11 JUDGE CHESTNUT: I'm sorry, did you have a page
12 reference?

13 MR. KAPLAN: No, it's Exhibit J-18, which is attached
14 to that, and that's a one-page exhibit.

15 BY MR. KAPLAN:

16 Q. Now, let's take a look here at the first group
17 of numbers at the top of the page, and those are your
18 analyses of market shares and HHI calculations for PJM East;
19 is that correct?

20 A. For economic capacity, that's correct.

21 Q. For economic capacity. Now, the abbreviations
22 in the left column, these are different market conditions;
23 is that correct?

24 A. Yes.

25 Q. For example, S_SP1 would be super peak; is that

1 correct?

2 A. Summer super peak, yes.

3 Q. Thank you. And SH_OP would be shoulder off-
4 peak; is that correct?

5 A. Yes, that's correct.

6 Q. Now, in the next column we have prices
7 representing prices for wholesale energy during those market
8 conditions; is that correct?

9 A. Yes.

10 Q. And now, these prices are not calculated by the
11 model; is that correct?

12 A. That is correct.

13 Q. Rather, their input is based upon your
14 evaluation of the appropriate price in each of the market
15 conditions?

16 A. Yes.

17 Q. Thus, the prices were not developed by your
18 program but are based upon observations and judgment?

19 A. Yes.

20 Q. Is it also correct that you did not run any
21 alternate market concentration analysis based upon another
22 set of prices other than those shown on Exhibit J-18?

23 A. Not to my recollection.

24 Q. Now, as I understand how the model works, it
25 determines how much generation is available in each relevant

1 market under each set of market conditions; is that correct?

2 A. Yes.

3 Q. And once the generation is identified, you
4 calculate the market share based on who owns or who has
5 contracted for the generation; is that correct?

6 A. Yes.

7 Q. And the HHI is simply the sum of the squares of
8 the market shares; is that correct?

9 A. Yes.

10 Q. Now, there's another element that factors into
11 market shares in addition to generation and that's imports;
12 is that correct?

13 A. Well, I was including imports within the context
14 of generation, but yes.

15 Q. Now, in order to accurately determine market
16 shares, you need to allocation those imports among market
17 participants; is that correct?

18 A. Yes.

19 Q. Now, the model also allocates imports; is that
20 correct?

21 A. Yes.

22 Q. And it uses a squeeze-down method?

23 A. That's correct, a proration.

24 Q. And under that squeeze-down method, you
25 determine the economic generation outside of the market and

1 the ownership of that generation and allocate transmission
2 import capacity into the market based upon the ownership
3 shares of generation outside of the market capable of being
4 imported into the market; is that correct?

5 A. That's approximately correct. It's a little
6 more complicated than that in that we start further out. We
7 then have transmission interfaces that constrain how much
8 can come in from further out, and then we cascade toward the
9 market, so that we don't simply take all the generation in
10 the eastern interconnect. It's mostly generation that's
11 only one interface out, some that's two interfaces out,
12 maybe a little that's three interfaces out.

13 Q. And when you get to that last hurdle, so to
14 speak, you've got capacity and ownership, and that's how you
15 basically do the allocation before you go over the last,
16 let's for example, the PJM East constraint?

17 A. That's correct, yes.

18 Q. Now, you agree that the import capability into
19 PJM East is constrained; is that correct?

20 A. Sometimes.

21 Q. And that there's a limit --

22 A. Three percent of the time.

23 Q. But there is a limitation on the amount that can
24 be simultaneously imported into PJM East?

25 A. Yes.

1 Q. And that import capability is approximately
2 7,300 megawatts; is that correct?

3 A. That's the number I used. It turns out that PJM
4 actually allocates more FTRs across that interface than
5 7,300, but not much more, so it's about 7,300.

6 Q. And that amount would continue under, would be
7 roughly the same, approximately the same under all market
8 conditions?

9 A. Yes.

10 Q. Now, import capability, if you do turn to
11 Exhibit J-18, and let's look at the column that says market
12 size. And that was the total generation available to the
13 market during those economic conditions; is that correct?

14 A. It's the total which was economic at those
15 prices. It was located within PJM East to take the top
16 block plus imports that also were economic at those prices.

17 Q. Plus imports, okay. So if we're assuming we
18 have about 7,300 megawatts of import capability and we look
19 at the S_SP1, which is summer super peak, approximately one-
20 fifth of that market or 20 percent was accounted for by
21 imports; is that correct?

22 A. Yes.

23 Q. And then if we go for example to shoulder off-
24 peak, there, imports were half the market, roughly?

25 A. I'm not certain, frankly. Certainly no more

1 than -- the only reason I hesitate is I wouldn't know
2 without going back and looking at computerized workpapers
3 whether we were able to utilize the full import capability.
4 But I wouldn't be surprised if we could, so on that
5 hypothetical, it would be about half.

6 Q. Just as an aside, for locational purposes, the
7 City of Philadelphia is in the PJM East Market; is that
8 correct?

9 A. Yes.

10 Q. Now, is it true that you do not know precisely
11 what market shares your program allocated to various market
12 participants of the import capability into PJM East?

13 A. I didn't when I did my deposition, and I don't
14 have the numbers with me. It's knowable.

15 Q. Is it true that at the time you conducted the
16 analysis upon which your testimony is based, that you had
17 not examined the results of how your program allocated
18 imports into PJM East?

19 A. I'm sorry, I don't understand the question.

20 Q. At the time you did your testimony in this case,
21 either your --

22 A. I understand that part of it. I don't
23 understand what you mean by "examined the results."

24 Q. You had not examined the results of how imports
25 were allocated among market participants.

1 A. If your question is, had I computed how many
2 megawatts are allocated to each market participant, the
3 answer is no, I hadn't.

4 Q. Now, is it also true that if you wanted to know
5 the market shares that your model allocated to various
6 market participants of import capability into PJM East, it
7 could be determined only with extreme difficulty?

8 A. That's what I told you on depo. I've since
9 learned it's not extreme difficulty. Dr. Kalt did it, and
10 I've been able to do it subsequently.

11 Q. Dr. Kalt in his testimony did not use the
12 squeeze-down method; is that correct?

13 A. That's correct.

14 Q. He used ownership of FTRs as we discussed
15 earlier; is that correct?

16 A. Yes.

17 Q. Now, would you agree that the value of an FTR
18 across the PJM interface increases if the price in the PJM
19 East market increases relative to the price outside of the
20 PJM market?

21 A. Yes. More formally, if the price difference
22 between the two end-points of the point-to-point FTR
23 increases, the value of the FTR increases.

24 Q. Is it also true that at the time you did your
25 testimony, you had not looked at or studied historical

1 ownership of FTRs across the eastern interface?

2 A. That is correct.

3 Q. Would you agree that you have not conducted any
4 sensitivity analysis of using some other method other than
5 the squeeze-down method on the results of your market
6 analysis?

7 A. That's a bit unfair, because you just excluded
8 it.

9 Q. Would you agree that you have not done any
10 sensitivity analysis to some other method of allocating, to
11 calculating market shares and HHIs by using some other
12 method of allocating imports into PJM East?

13 A. Well, I don't know how to respond to that other
14 than what I did. The answer is yes, I have, and that's
15 precisely what was just excluded from the record.

16 Q. On economic capacity analysis?

17 A. You didn't ask me that. The answer on economic
18 capacity is no.

19 Q. Thank you. And the question was intended to be
20 limited to economic capacity analysis. I apologize that I
21 left those words out.

22 Now, if you could turn to page 23 of your rebuttal
23 testimony, which is Statement WHH-2 -- actually, it's
24 Statement 3-R; is that correct, not WHH, Statement 3-R?

25 A. Yes.

1 Q. Right, I stand corrected. Now, at this point in
2 your testimony, you relied upon the FERC order in this case
3 in rejecting the PJM Classic as a relevant market; is that
4 true? I'm looking at lines 25 to 29 where you quoted.

5 A. Well, that's what I'm talking about at this
6 particular part, yes.

7 Q. Now, the FERC order in turn relied on the PJM
8 Market Monitor report that was prepared by the PJM Market
9 Monitor at the request of the regulatory authorities in New
10 Jersey; is that correct?

11 A. I can't answer that. In some places, they
12 relied on that. I don't know whether they relied on it for
13 this particular conclusion. I don't have the order with me.

14 Q. Well, I'm reading this. Do you know what they
15 were referring to when they said PJM MMU report?

16 A. No, I don't. I don't know whether they're
17 talking about the 2004 State of the Market Report or the one
18 that was done for the BPU.

19 Q. You do quote extensively from the FERC order,
20 however?

21 A. Yes.

22 Q. And you studied it extensively?

23 A. Yes.

24 Q. Have you read the MMU report?

25 A. Yes.

1 Q. Do you agree that the PJM Market Monitor -- and
2 by "this report," I'm referring to the report prepared for
3 the regulatory authorities in New Jersey about the impacts
4 of the merger on competition -- do you agree that the Market
5 Monitor does not discuss the PJM Classic energy market at
6 all?

7 A. I don't recollect.

8 Q. I don't recollect that he did?

9 A. I don't at this point in time recollect whether
10 he did. I recall he looked at the east, west and central
11 interfaces and some other things within the east. I don't
12 recollect him having looked at PJM Classic, but I may be
13 wrong.

14 Q. It's also true he didn't look at the pre-2004
15 market that you analyzed; is that correct?

16 A. Yeah, I think he just looked at the interfaces.

17 Q. Just looked at the interfaces, okay. Now, would
18 you agree, Dr. Hieronymus, that the PJM western interface is
19 marked by constraints over major transmission lines in west
20 central Pennsylvania?

21 A. Rarely, but yes.

22 Q. But that is the line of the west interface?

23 A. Sorry? .

24 Q. I didn't ask you how often. I asked you, is the
25 PJM West interface delineated or defined by key transmission

1 lines in west central Pennsylvania?

2 A. Oh, I'm sorry. Yes, it is.

3 Q. Would you agree that most of PJM's load is east
4 of the western interface?

5 A. Yes.

6 Q. PJM Classic's load is west -- would you agree
7 that most of PJM Classic's load is west of the PJM western
8 interface?

9 A. Yes, classic or pre-2004. It would be true of
10 both.

11 Q. Now, another constraint frequently cited is the
12 Beddington-Black Oak constraint, is the constraint on the
13 Beddington-Black Oak line; is that correct?

14 A. I'm not sure I had a question there.

15 Q. Another constraint that is frequently mentioned
16 in PJM on a transmission line is the constraint on the
17 Beddington-Black Oak line; is that correct?

18 A. That is correct.

19 Q. And if you could look at your recently admitted
20 exhibit which is WHH-4 --

21 A. Three, I believe.

22 JUDGE CHESTNUT: Three. It was marked four.

23 BY MR. KAPLAN:

24 Q. And just look at the first page of that, and can
25 you tell us, looking at this chart, where that line is

1 located? What two bubbles does it connect, two circles?

2 A. Best of my recollection, it's -- what are marked
3 here AEP and PEPCO.

4 Q. And do you agree that the Beddington-Black Oak
5 line has been called by the PJM Market Monitor as the most
6 constrained interface in PJM?

7 A. Yes.

8 Q. Now, do you also agree that you have not
9 analyzed economic capacity of the merger in the PJM Classic
10 market?

11 A. That's not true.

12 Q. You did analyze the PJM Classic market?

13 A. Yes.

14 Q. Did you analyze it at the time you submitted
15 your testimony?

16 A. No.

17 Q. Is it discussed in any of your testimony?

18 A. No.

19 Q. If we could please turn to --

20 MR. KAPLAN: One second, Your Honor.

21 (Pause.)

22 THE WITNESS: Actually, if I could correct a previous
23 answer?

24 BY MR. KAPLAN:

25 Q. If there's something you stated that is not

1 correct, please do so.

2 A. Yeah. I do believe that I discussed the
3 analysis of the PJM Classic market in Exhibit 3-R.

4 Q. In response to Dr. Kalt's rebuttal testimony?

5 A. Yes.

6 Q. Yes, Dr. Kalt's direct testimony.

7 A. Whichever.

8 Q. PPL Statement No. 1.

9 A. Yes.

10 Q. All right. The testimony submitted on June
11 28th, okay. Back to Exhibit J-28, now, this exhibit shows
12 your analysis of post-mitigation impact of the merger on the
13 PJM East market; is that correct?

14 A. One moment.

15 Q. Oh, I'm sorry.

16 (Witness perusing document.)

17 A. It is one such analysis. There were actually
18 two.

19 Q. Right. Well, I was going to ask you about this
20 one.

21 A. Actually, there were three.

22 Q. The heading here says, new purchaser
23 assumptions. I understand new purchaser assumptions, you
24 assume the four largest non-affiliated companies -- not
25 affiliated with the merging companies -- in PJM East each

1 capture one-quarter of the real divestiture of assets; is
2 that correct?

3 A. The divested fossil, yes, that's correct.

4 Q. Now, the actual megawatts of capacity needed to
5 be divested in order to achieve the HHI results shown in
6 Exhibit J-28 is shown in the last column under "megawatt
7 summer equivalent;" is that correct?

8 A. Just give me a moment.

9 (Pause.)

10 A. Yes.

11 Q. And then just to clarify, the column that says
12 "mitigation megawatts" is simply the megawatts available to
13 the market after generation outages; is that correct?

14 A. Yes.

15 Q. Now, in PJM East, the applicants are proposing
16 to divest 2,400 megawatts of virtual divestiture; is that
17 correct?

18 A. Yes.

19 Q. Now, you can look at J-28 during peak and
20 off-peak market conditions during the shoulder months.
21 Either all or almost all of the divestiture relied upon
22 would be virtual divestiture; is that correct?

23 A. I'm sorry, which periods?

24 Q. During peak and off-peak market conditions
25 during the shoulder months, the last two lines on Exhibit

1 J-28.

2 A. Well, the virtual divestiture in shoulder
3 periods, to the best of my recollection, it says here,
4 1,950, so yes, in these periods that are low-priced when the
5 coal units are on maintenance, it's substantially nuclear
6 (phonetic) -- nuclear, I'm sorry. I'm sounding like our
7 President.

8 (Laughter.)

9 Q. Now, where more than 2,400 megawatts of
10 divestiture are required for mitigation, the mitigation plan
11 relies on real divestiture, is that correct, the real sale
12 of assets?

13 A. I don't want to be pejorative about it. It
14 relies on the outright sale of fossil assets.

15 Q. Where the title to the facility passes to the
16 buyer?

17 A. That's correct.

18 Q. Now, in calculating the number of megawatts
19 required to mitigate market power that would result from the
20 merger, did you have any specific generation in mind?

21 A. I had in mind price categories of generation
22 which track to particular generating units, but I didn't
23 have a unique set in mind, if that's your question.

24 Q. And would you agree that you simply totalled the
25 number of megawatts, assuming that some combination of units

1 that were economic at the various price ranges here shown in
2 the second column of Exhibit J-28 would add up to the
3 correct number of megawatts for each set of market
4 conditions? Is that correct?

5 A. Well, I don't think I'm disagreeing with you.
6 Let me just state it a little differently. I computed the
7 number of megawatts that would have to be divested coming up
8 from the bottom of the prices and assumed that for each of
9 those price levels, that number was divested from units that
10 had that price characteristic.

11 Q. But you didn't, for example, go through and see
12 if there was some combination of units to be divested that
13 would actually come up with the precise number of megawatts?

14 A. Oh, you mean, as in 3,300 megawatts at a
15 particular time period?

16 Q. Yes.

17 A. No. But I did insure that there were sufficient
18 assets in the pool of potentially divestible assets to meet
19 the criteria.

20 Q. Is it your understanding that the applicants
21 will make the final determination of which units they intend
22 to sell as part of their divestiture plan?

23 A. That's my understanding.

24 Q. Is it also your understanding that --

25 A. Let me --

1 Q. I'm sorry.

2 A. Let me correct that. They will make the
3 candidate decision, which then will be subject to FERC
4 review as to whether FERC regards it as sufficient from a
5 market power perspective.

6 Q. But FERC will only consider what they propose?

7 A. Well, initially, I presume so. I don't know
8 whether the proceeding will allow others to comment on why
9 it should be some other set. I frankly don't know. I don't
10 know how FERC will handle it.

11 Q. Is it your understanding that, for example, in
12 order to meet their obligations to divest generating units
13 to meet market power concerns during the summer peak period,
14 applicants could divest a unit that is just barely economic
15 at \$55, choosing to retain a unit of much lower cost?

16 A. Yes, at least from my perspective.

17 Q. But it's also true that a unit at \$30 or even
18 \$20 would also provide mitigation during that same summer
19 peak period?

20 A. Yes.

21 Q. And when I was saying summer peak, I was
22 referring to S_P on Exhibit J-28.

23 A. Okay.

24 Q. Just for the clarity of the record.

25 Would you agree that the primary logic of virtual

1 divestiture is not price discipline but to reduce the
2 incentive on the merged entity to withhold capacity from the
3 market?

4 A. Well, that's my perspective based on the fact
5 that -- I don't know what you mean by "not price
6 discipline," but it certainly is the case, I would regard
7 nuclear units as poor candidates for being withheld. And so
8 why do you care about them? Presumably the reason you care
9 about them is because they're units that give you, you know,
10 if you retain the economic value of them, they go into your
11 calculus as to whether you want to do something with other
12 units.

13 Q. Now, you also agree that the buyers in the
14 virtual divestiture auctions will not have any say as to how
15 the units are run; is that correct?

16 A. Physically? No, no.

17 Q. They won't determine maintenance schedules, for
18 example?

19 A. Not directly. I mean, obviously, the
20 contractual rights that they have and the costs pertinent
21 thereto will weigh on how EEG decides to do its maintenance
22 scheduling, but in the sense that, do they get to say, "I
23 want you to start maintenance on February 16th," the answer
24 is no, they can't.

25 Q. Can we turn to Exhibit J-12? This was an

1 exhibit to your direct testimony submitted to FERC, and I
2 believe this is an exhibit, WHH-1, that's your direct
3 testimony, and this is an exhibit to that direct testimony.

4 A. Okay, I'm there.

5 Q. Is it your understanding that only some of the
6 units listed on this page but not all of the units will be
7 made available as part of the divestiture plan?

8 A. More accurately, I'm aware that the companies
9 have not committed to making all of them available.

10 Q. Dr. Hieronymus, if an entity with market power
11 were seeking to exercise that market power to raise price,
12 one way he could do so would be to choose not to run
13 generation; is that correct?

14 A. To physically withhold generation --

15 Q. Yes.

16 A. -- that it controls, yes.

17 Q. And would it also be true that the price
18 increase resulting from physically withholding generation
19 would take place regardless of whether a generator was
20 temporarily taken out of service or permanently taken out of
21 service?

22 A. Well, at least in the short run. In the longer
23 run, if permanently taken out, they may affect somebody
24 else's decisions about to build, but the short run impact
25 doesn't distinguish between whether it's down temporarily or

1 down permanently.

2 Q. Would you agree, Dr. Hieronymus, that to the
3 extent that an entity has market power, it can exercise that
4 market power and increase price by withholding capacity from
5 the market of any unit that is economic at the competitive
6 price?

7 A. Withholding any unit that is competitive at the
8 price from the market should have essentially an identical
9 effect. My only cavil is, you say "can." That kind of
10 presumes, "can get away with." But I don't think that was
11 the intent of your question.

12 Q. And just to put some numbers on it, if the price
13 were \$55.00, for example, if I was holding any unit that is
14 economic at \$55.00, or less than \$55.00, an entity with
15 market power could increase the price above \$55.00?

16 A. Yes. It's not clear it would be profitable, but
17 it would be physically possible.

18 Q. But it would not be necessary for that entity
19 with market power to withhold a unit that is economic at a
20 much lower price?

21 A. It wouldn't be necessary, you mean in lieu of
22 withholding one with a price below market but nearer market?

23 Q. Yes.

24 A. Yes, that's correct.

25 Q. And it would be probably more profitable to

1 withhold one that's nearer the market price than one that's
2 much lower?

3 A. Generally speaking.

4 Q. Dr. Hieronymus, do you agree that the price of
5 electric power under long-term contracts is largely based on
6 the expectation of buyers at the time that the contracts are
7 entered into?

8 A. Buyers and sellers.

9 Q. Dr. Hieronymus, in a situation in which there
10 are retail price caps imposed upon electric utilities, such
11 as in Pennsylvania -- and I'm speaking here specifically of
12 PECO, and I believe there are price caps in other
13 jurisdictions in Pennsylvania -- would you agree that the
14 impact of an exercise of market power at wholesale would be
15 to disadvantage competitive retail suppliers of generation?

16 A. It would depend.

17 Q. Would you agree that if retail customers have
18 the option of returning to their default supplier that is
19 price capped, an increase in wholesale prices could squeeze
20 the profits, or actually eliminate the profits, of
21 competitive retail suppliers?

22 A. It could. It depends on whether the competitive
23 supplier is hedged either physically, by owning generation,
24 or financially, by having forward hedged his position.

25 MR. KAPLAN: Your Honor, if I could just have a

1 moment to make sure I've covered everything?

2 JUDGE CHESTNUT: Certainly.

3 (Pause.)

4 MR. KAPLAN: Thank you, Your Honor. We have no
5 further questions.

6 JUDGE CHESTNUT: Mr. Niesen, do you have any cross
7 for Dr. Hieronymus?

8 MR. NIESEN: If Your Honor pleases, what I have is an
9 exhibit that I would like to identify and offer into the
10 record. It's a response to PGW Set VI, Interrogatory No. 1,
11 for which Dr. Hieronymus is the responsible witness.

12 JUDGE CHESTNUT: What is it marked as?

13 MR. NIESEN: I would like to have it marked as PGW
14 Exhibit No. 1.

15 JUDGE CHESTNUT: Shall we call it Cross-Examination
16 Exhibit 1?

17 MR. NIESEN: Yes, Your Honor.

18 (Whereupon, the document was marked
19 as PGW Cross-Examination Exhibit
20 No. 1 for identification.)

21 MR. NIESEN: And if Your Honor pleases, the
22 understanding is that the exhibit will be identified,
23 offered into the record, and with that, PGW has no cross-
24 examination for Dr. Hieronymus. I would offer into the
25 record PGW Cross-Examination Exhibit No. 1.

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JUDGE CHESTNUT: Any objection?

MR. NAEVE: No, Your Honor.

JUDGE CHESTNUT: The document is admitted then.

(Whereupon, the document marked
as PGW Cross-Examination Exhibit
No. 1 was received in evidence.)

JUDGE CHESTNUT: I don't think anybody else indicated
they had cross-examination for Dr. Hieronymus. The City of
Philadelphia, but you're not, right?

MR. KLEPPINGER: Right. That was part of the
stipulation, Your Honor.

JUDGE CHESTNUT: Redirect?

MR. NAEVE: Your Honor, might we have just a brief
recess?

JUDGE CHESTNUT: Sure.

(Recess.)

JUDGE CHESTNUT: Are you ready?

MR. NAEVE: Yes, Your Honor. I have four areas I'd
like to redirect on.

REDIRECT EXAMINATION

BY MR. NAEVE:

Q. Dr. Hieronymus, Mr. Kaplan asked you about the
western interface and constraints across the western
interface. Do you have anything more you'd like to add to
that?

FORM 2

1 MR. KAPLAN: Your Honor, I think he has to be a
2 little bit more specific.

3 JUDGE CHESTNUT: Yes. Just to clarify, not really to
4 supplement.

5 BY MR. NAEVE:

6 Q. Dr. Hieronymus, would you clarify how frequently
7 constraints occur across the western interface?

8 A. Well, the Market Monitor Report said that in
9 2004 it was 63 hours, which was a substantial decline from
10 the previous year, so it's less than 1 percent of the time.

11 Q. Mr. Kaplan also asked you about the Beddington-
12 Black Oak constraint. Is that part of the western
13 interface?

14 A. No, it isn't.

15 Q. Mr. Kaplan asked you if you analyzed the PJM
16 Classic market. Did you do that? I believe you said you
17 did.

18 A. Yes, I did. I think the analysis is part of the
19 record as Mr. Kalt's Exhibit 11 to his second testimony,
20 whatever that is.

21 Q. What did you find?

22 A. I found that you could pass or fail it depending
23 on how large the buyers were who bought the divested
24 capacity if you used the PJM Classic market. If you had
25 large buyers, you would get modest screen failures, if you

1 had smaller buyers, you wouldn't.

2 Q. And then finally, Dr. Hieronymus, again,
3 Mr. Kaplan asked you if you did a sensitivity analysis of
4 the effects of the FTRs and the FTR allocation, and you
5 answered that you did; is that correct?

6 A. Yes.

7 MR. NAEVE: Your Honor, since Mr. Kaplan opened the
8 subject, I would like again to offer Dr. Hieronymus'
9 analysis of the effects of FTRs on his economic capacity
10 analysis.

11 MR. KAPLAN: Your Honor, it was economic capacity,
12 not available economic capacity. I asked him if he had done
13 it at the time he submitted his testimony; he said no. And
14 the point of my analysis was purely and simply that
15 Dr. Hieronymus submitted his testimony without conducting
16 such a sensitivity analysis.

17 MR. NAEVE: Well, --

18 JUDGE CHESTNUT: Wait; wait. Let me make sure I
19 understand this. Your questions went to available --

20 MR. KAPLAN: Economic.

21 JUDGE CHESTNUT: Just economic.

22 MR. KAPLAN: Economic capacity.

23 JUDGE CHESTNUT: And you're asking him about
24 available economic capacity?

25 MR. NAEVE: I believe, Your Honor, Mr. Kaplan simply

1 asked, "Did you do a sensitivity analysis pertaining to the
2 effects of FTRs?" and Dr. Hieronymus said, "Yes, I did."
3 Then Mr. Kaplan said, "Let me correct my question; make that
4 for economic capacity," and he also corrected his question
5 to say "at the time of your direct testimony," obviously, to
6 avoid this subject.

7 JUDGE CHESTNUT: If he corrected it, then I'm not
8 going to allow it.

9 MR. NAEVE: Thank you, Your Honor. That's all.

10 JUDGE CHESTNUT: Recross?

11 MR. KAPLAN: No, Your Honor.

12 JUDGE CHESTNUT: Thank you very much, Dr. Hieronymus.
13 You're excused.

14 (Witness excused.)

15 JUDGE CHESTNUT: Off the record.

16 (Discussion off the record.)

17 JUDGE CHESTNUT: We'll go back on the record.

18 Raise your right hand, please.

19 **Whereupon,**

20 **JOHN R. MORRIS**

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

22 JUDGE CHESTNUT: Please sit down and give and spell
23 your name for the record.

24 THE WITNESS: My name is John Morris, M-o-r-r-i-s.

25 JUDGE CHESTNUT: Go ahead.

DIRECT EXAMINATION

1
2 BY MR. ESTES:

3 Q. Dr. Morris, by whom are you employed?

4 A. I'm employed by Economist, Incorporated.

5 Q. What's your position at Economist, Incorporated?

6 A. I'm a principal at Economist, Incorporated.

7 Q. Do you have before you PECO Statement 11-R and
8 Exhibits JRM-1 through JRM-3?

9 A. Yes, I do.

10 MR. ESTES: Your Honor, I believe two copies of the
11 statement and exhibits have been provided to the reporter,
12 and you should have it.

13 JUDGE CHESTNUT: I have it.

14 MR. ESTES: I don't believe there were any redactions
15 to this testimony, so this should be as was submitted to
16 you.

17 BY MR. ESTES:

18 Q. Can you identify what PECO Statement 11-R is,
19 Dr. Morris?

20 A. PECO Statement 11-R is my prepared rebuttal
21 testimony on behalf of PECO Energy Company.

22 Q. Was this statement and these exhibits prepared
23 by you or under your supervision?

24 A. Yes, they were.

25 Q. And if asked the questions in your statement,

1 would you give the same answers?

2 A. Yes, I would.

3 Q. And are those answers true and correct to the
4 best of your knowledge?

5 A. Yes, they are.

6 MR. ESTES: Your Honor, I would move for the
7 admission of PECO Statement 11-R and Exhibits JRM-1 through
8 JRM-3.

9 JUDGE CHESTNUT: Any objection?

10 (No response.)

11 JUDGE CHESTNUT: The documents are admitted.

12 MR. ESTES: I think, Your Honor, we stated this
13 before, but just to be clear, we are going to do oral
14 rejoinder on Dr. Morris tomorrow after Dr. Carpenter
15 testifies.

16 JUDGE CHESTNUT: Okay.

17 MR. ESTES: With that understanding I would tender
18 him for cross-examination.

19 JUDGE CHESTNUT: So I assume you reserve your right
20 to cross on the oral rejoinder till he actually gives it
21 tomorrow; right?

22 MR. NIESEN: Yes, Your Honor.

23 JUDGE CHESTNUT: Does anyone have any questions
24 otherwise for Dr. Morris?

25 MR. DILLON: No, Your Honor.

1 JUDGE CHESTNUT: Mr. Niesen, you had something?

2 MR. NIESEN: Only to mark and offer my exhibit,
3 Your Honor.

4 JUDGE CHESTNUT: Okay.

5 MR. NIESEN: If Your Honor pleases, I'd like to have
6 marked for identification several of Dr. Morris' responses
7 to PGW interrogatories, and with your permission I'd like to
8 have that marked as PGW Cross-Examination Exhibit No. 2.
9 May that be so identified?

10 JUDGE CHESTNUT: Yes.

11 (Whereupon, the document was marked
12 as PGW Cross-Examination Exhibit
13 No. 2 for identification.)

14 MR. NIESEN: I've given two copies to the court
15 reporter.

16 JUDGE CHESTNUT: Don't forget to pre-mark them before
17 you give me them to make sure that they're right.

18 MR. NIESEN: Sure. If Your Honor pleases, we would
19 offer into evidence PGW Cross-Examination Exhibit No. 2, and
20 with the admission of that document, we have no cross-
21 examination for Dr. Morris.

22 JUDGE CHESTNUT: Any objection?

23 MR. ESTES: No objection, Your Honor, provided that
24 we can ask a couple of questions on redirect about this. It
25 should be less than five minutes.

1 JUDGE CHESTNUT: It will be admitted subject to
2 whatever you want to do here.

3 MR. ESTES: No objection then, Your Honor.

4 JUDGE CHESTNUT: Then the document is admitted.

5 (Whereupon, the document marked
6 as PGW Cross-Examination Exhibit
7 No. 2 was received in evidence.)

8 MR. ESTES: May I go forward with my redirect?

9 JUDGE CHESTNUT: Yes. I'm not even sure what to call
10 this, so I guess redirect is the best thing.

11 **REDIRECT EXAMINATION**

12 BY MR. ESTES:

13 Q. Dr. Morris, let's look at the first page of PGW
14 Cross-Examination Exhibit No. 2. Am I correct that this is
15 a discovery response that you made to PGW?

16 A. Yes, it is.

17 Q. Now, your response is that you had no documents,
18 data or other materials responsive to a statement you made
19 in your rebuttal testimony.

20 MR. ESTES: I don't know, Your Honor, do you want me
21 to read that statement into the record?

22 JUDGE CHESTNUT: Not in the least. I don't even want
23 you to read his answer here. If you could just refer him to
24 it, that would be great.

25 MR. ESTES: I only mentioned that to set up my next

1 question.

2 BY MR. ESTES:

3 Q. Could you explain what your statement was based
4 on if it was not based on documents, data or other
5 materials?

6 MR. NIESEN: If Your Honor pleases, I don't mind him
7 explaining if the statement is based on opinions or his
8 judgment, but I don't think the offering of the question,
9 which was simply does he have any documents, and his answer
10 leaves open the door for an extended discussion of what his
11 opinions or judgments might be. I have no objection if it's
12 going to simply be, "I had no documents, but my testimony is
13 based on my opinion and my judgment," but beyond that I
14 think it's beyond the scope of the cross-examination and
15 beyond the limited nature of the question.

16 JUDGE CHESTNUT: Well, Dr. Morris, you've been
17 warned. What kind of answer were you going to give here?
18 You're not going to restate your conclusions, are you?

19 THE WITNESS: No.

20 MR. ESTES: That wasn't the intent of the question.

21 JUDGE CHESTNUT: I didn't think so.

22 THE WITNESS: I was going to say what I relied upon.

23 JUDGE CHESTNUT: Okay. That's fine.

24 BY MR. ESTES:

25 Q. So what did you rely upon for that statement?

1 A. I relied upon my experience. I've been studying
2 and consulting in the gas and electric industries for 20
3 years now. I've spoken to a lot of electric generators and
4 a lot of natural gas pipeline operators, and based upon my
5 experience there's a number of gas-fired generators, those
6 ones that most need firm capacity, that do have firm
7 contracts. Also, for this matter I spoke to some of the gas
8 operations people and they indicated that on specifically
9 the PSEG system there were some firm sales contracts for
10 electric generators.

11 Q. We can skip over the next page, but if you turn
12 to the third page of this exhibit, again you have a
13 discovery response that says that you did not rely upon
14 documents, data or other materials for your statement, and
15 I'd like you to explain what the statement was based on.

16 A. The statement was based upon interviews I had
17 with officials from PECO and PSEG about their practices for
18 filling storage.

19 Q. Let's turn to the next page.

20 JUDGE CHESTNUT: Are we going to go through all of
21 these like that?

22 MR. ESTES: This is the last one, Your Honor.

23 JUDGE CHESTNUT: Okay. Because I could see another
24 stipulation maybe being appropriate here.

25 MR. ESTES: If it was any more than that, I would

1 agree, but I think this will be short. Actually, I don't
2 think I have any questions on this, so I will end my
3 redirect here.

4 JUDGE CHESTNUT: Are you done in terms of --

5 MR. ESTES: That's all I have, Your Honor.

6 JUDGE CHESTNUT: Mr. Niesen, do you have any recross,
7 I guess?

8 MR. NIESEN: I do not, Your Honor.

9 JUDGE CHESTNUT: Thank you very much, Dr. Morris.
10 You're excused.

11 (Witness excused.)

12 JUDGE CHESTNUT: Mr. Crowley, would you stand,
13 please, raise your right hand?

14 **Whereupon,**

15 **JACK CROWLEY**

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

17 JUDGE CHESTNUT: Please sit down and give and spell
18 your name for the record.

19 THE WITNESS: Jack Crowley, C-r-o-w-l-e-y.

20 **DIRECT EXAMINATION**

21 BY MR. BONNEY:

22 Q. Mr. Crowley, by whom are you employed?

23 A. I am employed by Exelon Generation Power Team
24 and I have the title of Director of Regulatory Affairs for
25 Power Team.

1 Q. Do you have before you a document that's been
2 marked PECO Statement No. 9-R Revised, the rebuttal
3 testimony of Jack Crowley?

4 A. Yes.

5 Q. Was this testimony prepared by you or under your
6 direction and supervision?

7 A. Yes.

8 Q. If I were to ask you the questions set forth in
9 this document, would your answers be the same as contained
10 therein?

11 A. Yes.

12 Q. And are those answers true and correct to the
13 best of your knowledge?

14 A. Yes.

15 MR. BONNEY: Your Honor, at this time I would move
16 the admission of PECO Statement No. 9-R Revised into the
17 record.

18 JUDGE CHESTNUT: Any objection?

19 MR. KAPLAN: Yes, Your Honor, the same objection we
20 had earlier to Dr. Hieronymus. We received, actually,
21 Mr. Crowley's testimony later than Dr. Hieronymus' testimony
22 last night and it, in fact, does reflect some rewriting in
23 addition to simple redactions. We will agree that it can be
24 admitted subject to our ability to challenge that admission
25 if we believe that it's improperly redacted or the testimony

1 is substantially changed.

2 JUDGE CHESTNUT: Okay. I'll let it in on that basis.

3 (Whereupon, the document was marked
4 as PECO Statement No. 9-R Revised
5 for identification, and was received
6 in evidence.)

7 JUDGE CHESTNUT: By the way, Mr. Bonney, I printed
8 off your revised testimony that you sent last night. That
9 didn't have exhibits, so if you could provide me with a copy
10 at some point of those statements, I'd appreciate it. Thank
11 you.

12 MR. BONNEY: Will do, Your Honor.

13 MR. NIESEN: Your Honor, I would like to make the
14 same reservation concerning the testimony.

15 JUDGE CHESTNUT: Okay.

16 MR. BONNEY: Your Honor, Mr. Crowley is available for
17 cross-examination.

18 JUDGE CHESTNUT: Mr. Kaplan.

19 MR. KAPLAN: Thank you, Your Honor.

20 **CROSS-EXAMINATION**

21 BY MR. KAPLAN:

22 Q. Mr. Crowley, when the Exelon Power Team decides
23 to bid a unit into the PJM market, under normal operating
24 conditions does it consult with the Market Monitor?

25 A. No.

1 Q. Does it consult the Market Monitor regarding the
2 price it's going to bid that unit at?

3 A. No.

4 Q. And it doesn't consult with the Market Monitor
5 with respect to whether or not it's going to operate a unit,
6 does it?

7 A. No. We are required, as a designated capacity
8 resource, to bid that unit in.

9 Q. To bid the unit into the market?

10 A. Yes.

11 Q. But that can be anything up to \$1,000; is that
12 correct?

13 A. That's the cap in PJM, that's correct, the price
14 cap.

15 MR. KAPLAN: Thank you, Your Honor. That's all we
16 have.

17 JUDGE CHESTNUT: Any redirect?

18 MR. BONNEY: No, Your Honor.

19 JUDGE CHESTNUT: Thank you very much, Mr. Crowley.
20 You're excused.

21 (Witness excused.)

22 JUDGE CHESTNUT: I think that's the end of our
23 witness line-up for today. I guess I want to be sure I have
24 this clear. Tomorrow is Dr. Carpenter and Dr. Morris;
25 right?

1 MR. BONNEY: That's correct, Your Honor.

2 JUDGE CHESTNUT: And then I'm not sure about Monday.
3 Dr. Miller, is there any cross for him?

4 MR. BONNEY: No, Your Honor. My understanding is the
5 only witness that will be cross-examined on Monday is
6 Mr. White on behalf of PGW.

7 JUDGE CHESTNUT: Okay. Now, Mr. Ogden, did you want
8 to --

9 MR. OGDEN: Yes, Your Honor. If I might just mark
10 and move our First Energy Company's testimony and exhibits.
11 First, I've distributed to the court reporter and I
12 previously distributed to the parties and Your Honor copies
13 of the following documents, which I would ask to have marked
14 as Met-Ed/Penelec/Penn Power Statement No. 1;
15 Met-Ed/Penelec/Penn Power Statement No. 2, Appendix A, and
16 Exhibits RAD-1 through RAD-4, inclusive; Met-Ed/Penelec/Penn
17 Power Statement No. 3, Appendices A, B and C, and Exhibits
18 3-A and 3-B; and Met-Ed/Penelec/Penn Power Statement No.
19 1-S-1; and Met-Ed/Penelec/Penn Power Statement No. 3-S. May
20 those be so marked?

21 JUDGE CHESTNUT: Yes.

22 (Whereupon, the documents were marked
23 as Met-Ed/Penelec/Penn Power
24 Statement No. 1; Met-Ed/Penelec/Penn
25 Power Statement 2 with Appendix A

FORM 2

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and Exhibits RAD-1 through RAD-4;
Met-Ed/Penelec/Penn Power Statement
3, with Appendices A, B and C and
Exhibits 3-A and 3-B;
Met-Ed/Penelec/Penn Power Statements
Nos. 1-S-1 and 3-S for
identification.)

MR. OGDEN: By previous stipulation, I believe it is
agreed that they will be moved into the record without
objection.

JUDGE CHESTNUT: Okay; the documents are admitted.
(Whereupon, the documents marked
as Met-Ed/Penelec/Penn Power
Statement No. 1; Met-Ed/Penelec/Penn
Power Statement 2 with Appendix A
and Exhibits RAD-1 through RAD-4;
Met-Ed/Penelec/Penn Power Statement
3, with Appendices A, B and C and
Exhibits 3-A and 3-B;
Met-Ed/Penelec/Penn Power Statements
Nos. 1-S-1 and 3-S were received in
evidence.)

JUDGE CHESTNUT: Is there anything further then
before we adjourn for today?

(No response.)

1 JUDGE CHESTNUT: It looks like tomorrow should be a
2 relatively short day. Do you want to start at 9:00 or do
3 you want to start at 10:00? Nine is fine with me, but if
4 you want more time in the morning, that's okay.

5 MS. McCLOSKEY: Your Honor, speaking for those of us
6 who may be able to go home tonight and then travel back on
7 the train, a 10:00 start or slightly later would be best.

8 JUDGE CHESTNUT: Shall we say 10:00?

9 MS. McCLOSKEY: The train gets in about 9:35.

10 JUDGE CHESTNUT: So we'll start at 10:00 or when you
11 get here.

12 Okay, then. Thank you very much. This hearing is
13 adjourned.

14 (Whereupon, at 11:25 a.m., the hearing was adjourned,
15 to be reconvened at 10:00 a.m. on Friday, September 23,
16 2005, in Philadelphia, Pennsylvania.)

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C E R T I F I C A T E

I hereby certify, as the stenographic reporter, that the foregoing proceedings were taken stenographically by me, and thereafter reduced to typewriting by me or under my direction; and that this transcript is a true and accurate record to the best of my ability.

COMMONWEALTH REPORTING COMPANY, INC.

By: John A. Kelly

John A. Kelly
Certified Verbatim Reporter

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FORM 2