



## 1 APPEARANCES (Continued):

2 DAVID WERSAN, Esquire  
3 IRWIN POPOWSKY, Esquire  
4 1425 Strawberry Square  
5 Harrisburg, Pennsylvania 17120  
6 (For the Office of Consumer Advocate)

7 DAVID M. KLEPPINGER, Esquire  
8 McNees, Wallace & Nurick  
9 100 Pine Street  
10 Harrisburg, Pennsylvania 17108  
11 (For Philadelphia Area Industrial Energy Users  
12 Group)

13 J. THOMAS MORRIS, Esquire  
14 Reed, Smith, Shaw & McClay  
15 1600 Avenue of the Arts Building  
16 Philadelphia, Pennsylvania 19107  
17 (For SEPTA and Amtrak)

18 MARK WIDOFF, Esquire  
19 129 State Street  
20 Harrisburg, Pennsylvania 17101  
21 (For University of Pennsylvania and  
22 Utility Users Group)

23 CHARLES RAINEY, Esquire  
24 15th Floor  
25 Municipal Services Building  
1101 Market Street  
Philadelphia, Pennsylvania 19107  
(For City of Philadelphia)

PAMELA FOA, Esquire  
One Reading Center  
Philadelphia, Pennsylvania 19107  
(For City of Philadelphia)

ROGER E. CLARK, Esquire  
P.O. Box 8010  
Harrisburg, Pennsylvania 17105  
(For Governor's Energy Council)

MARTHA BUSH, Esquire  
237 South Melville Street  
Philadelphia, Pennsylvania 19139  
(For ENRACO)

C O N T E N T S

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

<u>WITNESSES</u>	<u>DIRECT</u>	<u>CROSS</u>	<u>REDIRECT</u>	<u>RECROSS</u>
Gregory A. Palast				
By Mr. Rainey	2566		2634	
By Mr. MacGregor		2569	--	2638
		2631		
By Ms. Chestnut		2623		2642
By Mr. Kleppinger		2624		
By Mr. Clark		2626		
By Ms. Bush		2629		
Thomas E. Knudsen				
By Mr. Wersan	2655	--	--	--
Dennis P. Dougherty				
By Ms. Chestnut	2657		2701	
By Mr. Hall		2660	--	2703

E X H I B I T S

<u>NUMBER</u>	<u>FOR IDENTIFICATION</u>	<u>IN EVIDENCE</u>
<u>City of Philadelphia Statement</u>		
✓ No. 2 (Palast)	2566	2568
<u>OCA Statement</u>		
✓ No. 7 (Knudsen)	2655	2656
<u>Staff Statement</u>		
✓ No. DPD-1 (Dougherty)	2658	2660
<u>Staff Exhibits</u>		
✓ Nos. DPD-1 through DPD-30 (Dougherty)	2658	2660
<u>PECO Exhibit</u>		
✓ No. 4 (IR-PECO-III-1 through IR-PECO-V-4)	2662	2662

P R O C E E D I N G S

1  
2 ADMINISTRATIVE LAW JUDGE JOSEPH MATUSCHAK: This is  
3 the time and place set for the further hearing in the matter  
4 of the Pennsylvania Public Utility Commission, et al. versus  
5 Philadelphia Electric Company, Docket No. R-850152.

6 Are there any preliminary matters before we proceed  
7 with the witnesses?

8 MS. CHESTNUT: Yes, Your Honor.

9 Staff has outstanding a motion to strike certain  
10 supplemental testimony filed by Philadelphia Electric Company.  
11 Your Honor had indicated that there would be oral argument  
12 on that motion this morning.

13 JUDGE MATUSCHAK: Are you ready to proceed with that,  
14 Mr. MacGregor?

15 MR. MacGREGOR: No, Your Honor. This is the first  
16 I've heard that there had been an indication that there would  
17 be oral argument on that matter this morning.

18 MS. CHESTNUT: Your Honor, perhaps I could inquire  
19 as to when the company proposed to have the oral argument.  
20 I would like to know, because the testimony on this issue  
21 is tomorrow with cross-examination scheduled for February  
22 26. If we are to have time to supply additional testimony  
23 in order not to prejudice the company I would deem it  
24 obvious that we should have the oral argument as soon as  
25 possible so that Your Honor can issue a ruling.

1 MR. MacGREGOR: That's fine with the company. I  
2 believe the Judge indicated last week that he wasn't going  
3 to be rushed into a decision on this matter. We would be  
4 prepared to argue the matter tomorrow.

5 JUDGE MATUSCHAK: We will hear you, then, tomorrow  
6 morning.

7 MR. RAINEY: Your Honor, there is another preliminary  
8 motion. I have handed to Your Honor and all parties two  
9 letters in response to letters which I received from Dr.  
10 Jay Calvert as well as Mr. John Stillman with respect to  
11 the availability of Mr. Shinnar and other matters.

12 I spoke to Mr. Calvert by telephone this morning and  
13 he informed me that he would talk to his consultants about  
14 meeting with Dr. Shinnar on Monday, February 10, which is a  
15 date which is feasible to the City of Philadelphia as well  
16 as to Dr. Shinnare. It is our hope that we will be able to  
17 resolve that particular matter.

18 I would also like to note that a letter was received  
19 from Mr. John Stillman, in it he had mentioned the date of  
20 February 10th as a date that might be acceptable.

21 So Dr. Shinnar is available on that date. However,  
22 as I stated last week in hearings, Dr. Shinnar, as a result  
23 of having had to change his schedule, which was originally  
24 one in which he would be doing work for the World Bank  
25 next week, he has changed his schedule so that he's doing

1 that this week. He is unavailable this week. However,  
2 he will be available, as I said, on the 10th, and we hope  
3 we can resolve that matter.

4 JUDGE MATUSCHAK: Very well. Counsel will  
5 cooperate with each other and try to resolve that matter.

6 MR. MacGREGOR: Yes, Your Honor. Mr. Calvert will  
7 be coming over later this morning and see if he can't  
8 resolve that situation.

9 JUDGE MATUSCHAK: Mr. MacGregor and Mr. Wersan,  
10 do the parties wish to argue the petition or the motion  
11 in limine of PECO against certain witnesses? When do you  
12 wish to argue that matter?

13 MR. WERSAN: Your Honor, the OCA has not asked for  
14 oral argument. If you would like it we would certainly go  
15 ahead with such argument.

16 MR. MacGREGOR: Your Honor, we would like either  
17 oral argument or a chance to file a written response. Can  
18 I get back to you at a break later this morning on that?

19 JUDGE MATUSCHAK: Yes.

20 MR. RAINEY: We are ready, Your Honor.

21 Whereupon,

22 GREGORY A. PALAST  
23 having been duly sworn, testified as follows:  
24  
25

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

JUDGE MATUSCHAK: You may proceed.

MR. RAINEY: Thank you, Your Honor.

DIRECT EXAMINATION

BY MR. RAINEY:

Q. Mr. Palast, would you state your full name and business address for the record, please?

A. My name is Gregory A. Palast, P-a-l-a-s-t, of Union Associates, 64 Second Avenue, New York, New York 10003.

Q. And, Mr. Palast, for whom are you testifying in this proceeding?

A. I am testifying at the request of the City of Philadelphia.

Q. Mr. Palast, do you have before you a document entitled "Testimony and Exhibits of Gregory A. Palast"?

A. Yes, I do.

Q. And does that document contain 79 pages of testimony and 15 pages of exhibits?

A. Yes, it does.

MR. RAINEY: Your Honor, I would like to have this document marked for identification purposes as City Statement No. 2.

JUDGE MATUSCHAK: The motion is granted.

(Whereupon, the document was marked as City of Philadelphia Statement No. 2 for identification.)

1 BY MR. RAINEY:

2 Q Mr. Palast, was City Statement No. 2 prepared  
3 by you or under your direct supervision?

4 A Yes, it was.

5 Q Mr. Palast, at this time do you have any  
6 corrections, deletions, revisions or additions which you  
7 would like to make to City Statement No. 2?

8 A Other than typographical errors, which I need  
9 not review because they are obvious, I would note two  
10 corrections.

11 On page 24 of the prepared testimony the answer to  
12 the first complete question, the last sentence of that  
13 answer, eight lines down from the top of the page, reads,  
14 "The company's plan will raise a typical residential  
15 bill, non-heating, to \$941 per year." That should be  
16 corrected to read, "The company's plan will raise a typical  
17 500 kilowatt hour per month residential bill to \$996 per  
18 year in 1989."

19 My second note is not so much a correction but just  
20 to note that since I originally drafted this testimony there  
21 has been one change which may affect this discussion. So I  
22 would just note briefly, Section 5 of my testimony, beginning  
23 at page 36, discusses proposed changes in Financial Accounting  
24 Standards Board Statement 71. The draft was based upon the  
25 testimony of Company Witness Mr. Farling and the AICPA issues

1 paper which he discussed. Since the drafting of this  
2 testimony the FASB has issued an exposure draft for Statement  
3 71. I have reviewed the exposure draft and certain other  
4 documents in the past couple of weeks; after that review  
5 I have not changed my conclusions. The basic points I  
6 make in the testimony and the conclusions I reach remain  
7 unchanged.

8 Q. Mr. Palast, with those additions and corrections  
9 is the testimony that you have submitted and exhibits true  
10 and correct to the best of your knowledge, information and  
11 belief?

12 A. Yes, it is.

13 Q. Mr. Palast, if I were to ask you today the  
14 questions contained in City Statement No. 2 would your  
15 answers be the same as contained herein?

16 A. Yes.

17 MR. RAINEY: Your Honor, at this time I would like  
18 to move for the admission into evidence of City Statement  
19 No. 2 subject to any timely motions or objections raised by  
20 any party to these proceedings.

21 JUDGE MATUSCHAK: Under those conditions the motion  
22 is granted.  
23

24 (Whereupon, the document marked  
25 as City of Philadelphia State-  
ment No. 2 was received in  
evidence.)

1 MR. RAINEY: Your Honor, Mr. Palast is available  
2 for cross-examination.

3 JUDGE MATUSCHAK: Mr. MacGregor.

4 MR. MacGREGOR: Thank you, Your Honor.

5 CROSS-EXAMINATION

6 BY MR. MacGREGOR:

7 Q Good morning, Mr. Palast.

8 A Good morning.

9 Q Mr. Palast, first, as a preliminary matter  
10 with respect to your correction on page 24 of your testimony  
11 could you provide us with the workpapers which you used to  
12 determine that revised calculation?

13 A For your information, in providing the work-  
14 papers to the company I believe that I gave the company the  
15 calculations for that figure.

16 Q For the \$996 figure?

17 A Yes. However, it is very simple and I could  
18 give that to you, if you want me to, very quickly now.

19 Q No, that's fine.

20 Mr. Palast, referring, first, to page one of your  
21 testimony, at the bottom, you state that you hold an MBA  
22 from the University of Chicago; is that correct?

23 A That is correct, sir.

24 Q Do you also hold an undergraduate degree from  
25 that institution?

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

A. Yes, I do.

Q. And when was that degree received?

A. I believe -- that's a difficult question to answer. I began my graduate work before completing my undergraduate work and I was, I think, granted -- the college granted me a degree in 1974, about 12 years ago.

Q. In what area of study was that degree granted?

A. I don't know because I didn't complete my undergraduate education. I went straight into graduate school. They gave me the degree and I'm not sure what they put down, but I believe that on the degree it states business.

Q. So you're telling me that you don't know what academic area your undergraduate degree was awarded in?

A. Sir, I began graduate school before completing my undergraduate education so that --

Q. Do you hold an undergraduate degree?

A. Yes, I do.

Q. You just don't know in what area?

A. I believe that the record -- that they stated it was a business degree.

Q. I take it, then, to the best of your knowledge you do not hold an academic degree in accounting?

A. Well, an MBA incorporates accounting, sir.

Q. Do you hold an undergraduate degree in accounting

1 to the best of your knowledge?

2 A. Unless you consider the assignment of the  
3 business credential as an academic degree in accounting.

4 Q. Are you a Certified Public Accountant, Mr.  
5 Palast?

6 A. No, I'm not.

7 Q. Are you a Chartered Financial Analyst?

8 A. No.

9 Q. Are you a member of the Federation of Financial  
10 Analysts?

11 A. No.

12 Q. Now, upon receiving your MBA in 1976 am I correct  
13 that you taught economics between 1976 and 1979 in the  
14 Department of Labor Studies at Indiana University?

15 A. Yes, sir. I taught collection and use of  
16 economic data, I taught economic issues and I also taught  
17 collective bargaining.

18 Q. And this is within the Department of Labor  
19 Studies; is that correct?

20 A. That's correct.

21 Q. Were you a faculty member of the Department of  
22 Economics at Indiana University?

23 A. No, sir.

24 Q. Now, in 1980 am I correct that you were employed  
25 as an economist for the New York State Assembly Subcommittee

on Public Power?

1  
2 A. Yes, sir.

3 Q. And you state in your testimony that this  
4 Subcommittee has oversight responsibility for the Power  
5 Authority of the State of New York?

6 A. Yes, it does.

7 Q. And by "oversight" do you mean the normal type  
8 of oversight exercised by a legislative subcommittee?  
9 Is that correct?

10 (Pause.)

11 Q. Does the Subcommittee establish the rates for  
12 PASNY?

13 A. To answer your first question, it is normal  
14 oversight authority in the sense that I had to review all  
15 legislation proposed by or proposed to the Power Authority  
16 as its regulatory powers in addition to maintaining a  
17 continuing working relationship with them to carry out a  
18 legislative mandate.

19 Q. The Subcommittee is not the body that establishes  
20 the rates for PASNY; is that correct?

21 A. No.

22 Q. What body does establish those rates?

23 A. The public authority in effect established its  
24 own rates.

25 Q. Now, in 1981 and '82 you stated you were

1 Executive Director of the New York State Legislative  
2 Committee on Science and Technology; is that correct?

3 A. It's the New York State Legislative Commission.  
4 It's like a super committee of both houses of the  
5 legislature.

6 Q. Am I correct in understanding that this  
7 commission is essentially an advisory body that prepares  
8 studies and reports and reviews legislation on behalf of  
9 the New York State General Assembly?

10 A. No. It is a bi-cameral body that provides  
11 information to both houses, though most of our time was  
12 concentrated on the New York State Assembly side. In addition  
13 to advising, we drafted and initiated legislation and  
14 developed -- because we had a larger staff than any other  
15 committee of the legislature we had a depth of expertise  
16 which we could apply to certain areas, and we concentrated  
17 in the energy and utilities field for the most part.

18 Q. But am I correct that the essential role of the  
19 commission was to provide information and support to the  
20 New York Legislature?

21 A. That was our charter mandate, to provide  
22 information, to draft legislation, to review legislation, to  
23 provide policy analysis and, in addition, we did represent  
24 the state legislature in regulatory matters before the  
25 utility commission.

1 Q. But the commission itself has no independent  
2 regulatory authority over public utilities or any other  
3 body for that matter; is that correct?

4 A. We could pass bills. We could not set rates.  
5 That was left to the PSC.

6 Q. The commission could pass bills?

7 A. The commission would pass upon bills, draft  
8 bills and pass them through to the legislature.

9 Q. Now, you're currently employed by Union  
10 Associates; is that correct?

11 A. That is correct.

12 Q. And one of your principal responsibilities at  
13 Union Associates has been to present testimony in public  
14 utility rate proceedings; is that correct?

15 A. That is one of the functions I perform.

16 Q. Mr. Palast, have you ever been employed as an  
17 officer or employee of a public utility?

18 A. No.

19 Q. Have you ever been an employee or decision-  
20 maker for a federal or state regulatory agency charged with  
21 the responsibility for establishing public utility rates?

22 A. Yes. I was a consultant to the Missouri  
23 Public Service Commission.

24 Q. No, I said employee or decision-maker. Other  
25 than as a consultant.

1 A. Other than as a consultant, no.

2 Q. Have you ever been employed by a public  
3 accounting firm, other than as a consultant?

4 A. No.

5 Q. Have you ever been an officer or employee of  
6 an investment banking firm?

7 A. Yes. I have worked with investment banking  
8 firms, but not as an employee.

9 Q. Now, as we previously discussed, Mr. Palast, one  
10 of your areas of responsibility at Union Associates has been  
11 the presentation of testimony in public utility rate  
12 proceedings; is that correct?

13 A. That is one of the tasks. The main task is  
14 research and analysis.

15 Q. And at pages four and five of your testimony  
16 you give us several examples of recent areas of activity  
17 which you have undertaken; is that correct?

18 A. Yes.

19 Q. Now, on page four you list two studies that you  
20 prepared on the economic impacts of the Shoreham plant for  
21 Suffolk County; is that correct?

22 A. Which are you referring to? We prepared more  
23 than two studies. Which are you referring to?

24 Q. I guess I'm referring to the second paragraph of  
25 your answer on page four, where you begin, "For the County

1 of Suffolk, New York."

2 A. Yes.

3 Q. And then the next following paragraph, "studies  
4 on the effect of the Shoreham rate increase."

5 A. Yes. We prepared a number of studies for local  
6 and state government.

7 Q. Now, based in part on those studies am I correct  
8 that you prepared testimony in the matter of Long Island  
9 Lighting Company, a proceeding to investigate the cost of  
10 the Shoreham Nuclear Generating Facility, Phase 2, before  
11 the New York State Public Service Commission, Case No.  
12 27563?

13 A. As a result of these studies I prepared testimony  
14 in a number of hearings: two Public Service Commission  
15 hearings, legislative hearings and Gubernatorial Special  
16 Committee hearings; and that was one of the hearings in which  
17 I prepared testimony from these studies.

18 Q. Am I correct that your testimony was stricken  
19 in that case from the record?

20 A. No, you are incorrect. It was moved over from  
21 the -- the commission had split the discussion of the  
22 Shoreham nuclear plant into a number of cases. In that  
23 instance I provided testimony as to the economic impact of  
24 charging the Shoreham nuclear plant to ratepayers, that is,  
25 similar to Dr. Shinnar's testimony in these proceedings. The

1 commission decided to move my testimony from the engineering  
2 review of imprudence over to the ratemaking principle  
3 segment of the case.

4 So you could say that it was struck from the  
5 imprudence section and adopted into the ratemaking -- so-  
6 called ratemaking principle segment of the hearings.

7 Q. Fine.

8 Would you agree with me as a general proposition  
9 that the County Suffolk has generally been an opponent to  
10 the Shoreham Plant?

11 A. No, I would not. At the time my testimony was  
12 submitted the county executives were proponents of the  
13 plant. It changed back and forth. My position stayed the  
14 same.

15 Q. At the bottom of page four of your testimony  
16 you state that you presented testimony and studies on behalf  
17 of a group of business leaders in New Hampshire; is that  
18 correct?

19 A. That's correct.

20 Q. Does this group have a name?

21 A. There were two groups. One group was named  
22 Campaign for Ratepayers' Rights and the other group was  
23 something -- I can't remember the name, something like  
24 Business Leaders for Fair Rates or something along that  
25 line.

1 Q. Am I correct that your testimony in that  
2 proceeding recommended rejection of the utility's  
3 Newbrook financing plan until the utility conducted a full  
4 analysis demonstrating that bankruptcy would be more  
5 costly than the Newbrook financing plan?

6 A. That's correct.

7 Q. And did you also express a preliminary view  
8 in your testimony that bankruptcy would be a less costly  
9 alternative to ratepayers?

10 A. No, I did not. What I expressed was that other  
11 than -- in the absence of a full analysis then we would have  
12 to say that at first glance the risks of Chapter 11 were  
13 less than the risks of the Newbrook financing. The  
14 commission did reject the Newbrook financing.

15 Q. Am I correct that you stated in your testimony,  
16 and I quote, "A preliminary review suggests that a reorganiz-  
17 ation could succeed in keeping rates lower than than under  
18 the Newbrook plan"?

19 A. That is correct, and my recommendation was to  
20 study whether that was true.

21 Q. You also reference testimony in a recent  
22 Kansas Gas & Electric rate proceeding; is that correct?  
23

24 A. Yes, sir.

25 Q. Am I correct that this testimony was presented  
on behalf of the Alliance for Liveable Electric Rates?

1 A. Yes, a group of mid-sized manufacturers in  
2 Kansas.

3 Q. Am I correct in that proceeding that you  
4 recommended that the Kansas commission deny a rate increase  
5 associated with the prudent portion of the utility's  
6 investment in the Wolf Creek plant until the utility agreed  
7 to end all dividend payments on common and preferred stock?

8 A. I recommended that the commission adopt language  
9 similar to the Michigan order, that is, a conditional rate  
10 increase.

11 Q. Conditioned upon the ending of all common and  
12 preferred stock dividend payments?

13 A. That the company institute a cash conservation  
14 program to reduce rates, which would include elimination of  
15 the dividends voluntarily, as was done this week by  
16 Public Service of Indiana.

17 Q. On page 15 of your testimony, Mr. Palast,  
18 beginning at line three, you state, "The utility's witnesses  
19 admit that they did not seriously consider any other plan  
20 than the three-year phase-in plan they have proposed," is  
21 that correct?

22 A. That is correct. There was no other plan  
23 seriously considered by all of the evidence, by the questions  
24 we asked both in discovery and as I heard myself under cross-  
25 examination.

1 Q Now, you cite as partial support for that  
2 position PECO's response to DR-RCW4 GEC, 12/13/85; is that  
3 correct?

4 A Yes.

5 Q I would like to show you a copy of that response  
6 and could you tell me what, if anything, it has to do with  
7 rate phase-in plans?

8 (Document handed to witness.)

9 A I may have misreferenced that one. There is  
10 nothing in particular which indicates this. We specifically  
11 asked the company to provide any papers whatsoever indicating  
12 that they considered another -- any other -- period and  
13 the answer was that there were no such papers. And Mr.  
14 Paquette under cross-examination stated that other a general  
15 discussion of a possible four year period that no calculations  
16 were done as to anything other than the three year phase-out  
17 plan.

18 Q Was that Mr. Paquette or Mr. Williams?

19 A Excuse me. Mr. Williams.

20 Q Now, in reaching your conclusion did you review  
21 the company's response to DR-JFPI GEC, 12/20/85?

22 A I can't recognize that by number.

23 Q I'll show you a copy of it.

24 (Document handed to witness.)

25 A This was submitted, I would note -- or the

question was asked of the company on December 20, 1985.  
So I don't know when this -- this would have been almost  
certainly received after the preparation of testimony.

Q. After January 14, 1986? Is that your  
testimony?

A. It could have been.

Q. You don't know?

A. Excuse me. I still have no -- what we have  
here is a two year phase-in/two year phase-out. The  
company did not consider a longer phase-in period, or I  
have no evidence that they did.

Q. What else is on that document other than a  
two year in/two year out plan? Is not also a sinking fund  
depreciation plan over a ten year period discussed?

A. No, I haven't seen this. I'm surprised it  
wasn't given to me in response to the question I asked  
for these documents.

JUDGE MATUSCHAK: Keep your voice up, Mr. Palast.

THE WITNESS: I'm sorry.

BY MR. MacGREGOR:

Q. So you did not review this document in reaching  
your conclusion?

A. No.

Q. Mr. Palast, beginning at page 24 of your testimony  
you discuss certain phase-in plans in other states; is that

1 correct?

2 A. Yes, sir.

3 Q. And you provide a discussion of phase-in plans  
4 from three other jurisdictions?

5 A. Yes.

6 Q. Those being Mississippi, Kansas and New Mexico?

7 A. Yes.

8 Q. And am I correct that you concluded based upon  
9 this comparison that PECO's plan compared unfavorably to  
10 these plans because it is of a much shorter duration?

11 A. That would be stretching my methodology for  
12 reaching my conclusion. I reviewed a number of plans. Here  
13 is a discussion of some. And I have stated that in light of  
14 the fact that other utilities have accepted much longer plans  
15 or have been given much longer plans that it is unreasonable  
16 to believe that we should stick with PECO's shorter period.

17 Q. And you believe the three plans you have  
18 discussed here represent utilities in similar situations to  
19 Philadelphia Electric Company, or that the facts of the cases  
20 are similar to the facts that we are dealing with here in  
21 this case?

22 A. I took three utilities to give a view of the  
23 range of possibilities. This is not intended to be necessarily  
24 comparable, although I believe that Kansas -- that there is  
25 a certain comparability to Kansas. I would say in terms of

1 comparison, Kansas and Mississippi are utilities with  
2 much more stringent financial problems than PECO. Public  
3 Service of New Mexico is probably in better shape than  
4 PECO if you want a comparison analysis.

5 Q Well, looking at the Mississippi plan for a  
6 moment, would you agree with me that this plan had three  
7 major components to it and that they were related to  
8 Mississippi Power & Light Company's 33 percent share of the  
9 Grand Gulf nuclear plant?

10 A They were specifically aimed at disposition  
11 of the 33 percent share of Grand Gulf.

12 Q Would you agree with me that there is an ongoing  
13 serious dispute between the Mississippi Power & Light  
14 Company and Mississippi Commission on the one hand and the  
15 Federal Energy Regulatory Commission on the other hand as to  
16 Mississippi Power & Light Company's appropriate share of that  
17 plant?

18 A Well, there is a disagreement. The settlement  
19 reached here is based upon the acceptance of the 33 percent  
20 allocation. If the allocation -- the dispute has been  
21 separated from this settlement.

22 Q Well, specifically, Mississippi Power & Light's  
23 share, according to the FERC, is 33 percent?

24 A Yes.

25 Q And the Mississippi Commission and the utility

1 believe that the utility's share should be no more than  
2 14.5 percent; is that correct?

3 A. That is correct, and the order is predicated  
4 upon the 33 percent share. If there is a change in the  
5 allocation due to a different resolution of this dispute  
6 then this order will have to be changed.

7 Q. Now, under the plan, as I understand it -- it's  
8 a little complicated -- one-third of the utility's share in  
9 the plant, or approximately 11 percent, was inventoried for  
10 ten years; is that correct?

11 A. For ten years -- in the simplest terms, the  
12 phase-in of a third of the plant doesn't begin until the  
13 tenth year of the plant.

14 Q. That's correct. And for approximately 7.5  
15 percent of the plant, which is the remainder of the  
16 difference between 33 and 14.5, that was deferred for a  
17 three year period; is that correct?

18 A. Approximately one-fifth of the allocation  
19 does not enter the rates for three years.

20 Q. So with respect to the 14.5 percent of the  
21 allocation, which both the commission in Mississippi and  
22 the utility agree is what they believe should be the  
23 utility's allocation of the Grand Gulf plant, this portion  
24 of the plant, then, was placed in rates as part of a ten  
25 year phase-in plan; is that correct?

1           A. First of all, I'm not sure that Mississippi  
2 absolutely agrees that it even deserves 14 percent. So I  
3 don't want to misstate their position. I believe their  
4 main position is that they should pay for none of this plant.

5           As to the basis for the 14.5 percent that will be  
6 phased-in in ten years, it is a little less than half of the  
7 amount of the sum that will be placed into rates, will be  
8 phased-in over ten years. The remaining majority will be  
9 phased-in over a much longer period.

10          Q. Now, I'm talking about just the 14.5 percent.

11          A. The 14.5 percent --

12          Q. It will be phased-in over four years and the  
13 deferral recovered over six years; is that correct?

14          A. Yes. That is approximately a little less than  
15 half the allocation. That is correct.

16          Q. Would you agree with me that the first year  
17 increase granted by the Mississippi commission was 14.07  
18 percent?

19          A. I would have to -- I don't have the order in  
20 front of me, but that sounds correct.

21          Q. Would you also agree with me that the  
22 Mississippi commission, in entering this order, in addition  
23 to granting a 14 percent increase in year one, granted eight  
24 to ten percent increases in years two and three and seven to  
25 nine percent increases in years three and four?

1 A. I would have to look back at that. You're  
2 talking about total base rates or are you talking about  
3 allocation of the plant?

4 Q. I'm talking about increases in rates.

5 A. I don't recollect. I haven't read the order in  
6 about a month so I don't recollect.

7 Q. If I could show you a copy of the order and  
8 particularly reference you to page 19, if you could review  
9 this paragraph would you agree with me that the numbers I've  
10 stated are correct?

11 (Document handed to witness.)

12 A. It states that the commission estimates -- it  
13 is an estimate rather than a granting --

14 Q. Fine.

15 A. There is simply an estimation of what the total  
16 rates -- how much the total rates will rise in Mississippi.

17 Q. And if that estimate is correct the rates will  
18 rise over that period approximately 45 to 50 percent?

19 A. Forty-five to 50 percent beginning from a fairly  
20 lower point in Mississippi.

21 Q. Thank you, Mr. Palast.

22 A. You're welcome.

23 Q. Perhaps I should have left the order with you.  
24 Would you also agree that with respect to this phase-in  
25 plan that the commission granted the recovery of carrying

1 charges on all of the deferred amounts?

2 A. It granted -- in an odd manner it granted  
3 recovery -- it's a very complex order. It granted recovery  
4 of -- there is an interest provision in the order.

5 Q. Right, and it states as follows: "The company  
6 shall be permitted to recover on a current basis the  
7 incremental cost of financing the inventory shares as shown  
8 in Table 1 and 2 above, that phase-in of the portion of the  
9 current recovery schedule described in paragraph three,  
10 and the deferral of rehearing amounts described in paragraph  
11 four."

12 MR. RAINEY: Excuse me. May we take a look at that?

13 MR. MacGREGOR: Sure.

14 (Document handed to Counsel Rainey and witness.)

15 MR. RAINEY: Your Honor, could the court reporter  
16 read back what Mr. MacGregor just stated?

17 MR. MacGREGOR: I simply quoted from that.

18 (Witness perusing document.)

19 MR. RAINEY: Could we just have that read back,  
20 please?

21 (Whereupon, the reporter read from the record as  
22 requested.)

23  
24 A. This is correct. The reason I said there is a  
25 complication is that there is a right of the company to sell  
power from the excess capacity and if they earn an excess

1 return thereby it would reduce these carrying costs.

2 BY MR. MacGREGOR:

3 Q But with that clarification, at least as the  
4 order stands now, until a sale is made the carrying charges  
5 were granted?

6 A That's correct.

7 Q Now, you also reference a Kansas Gas & Electric  
8 Company case in your testimony.

9 A Yes, sir.

10 Q Would you agree that the gross rate increase  
11 requested by the utility in that proceeding was approximately  
12 101 percent?

13 A I would agree with that, yes.

14 Q Would you agree with me that the increase approved  
15 by the commission in that proceeding on a gross basis was  
16 approximately 46 percent?

17 A Over a period of time, yes.

18 Q To be spread over a period of time?

19 A Yes.

20 Q And am I also correct that with respect to the  
21 phase-in plan that was adopted in that proceeding that the  
22 commission granted the recovery of carrying charges on the  
23 deferred balance?

24 A Yes, it did.

25 Q Mr. Palast, in preparing your testimony and

1 in reviewing plans from other jurisdictions, did you become  
2 aware of the fact that the Illinois Commerce Commission  
3 approved a four year phase-in plan with respect to Union  
4 Electric's requested 45.6 percent increase to reflect its  
5 share of the Callaway plant?

6 A. Yes.

7 Q. And did you become aware of the fact that the  
8 Missouri commission approved a six year phase-in plan with  
9 respect to the 46 percent increase requested by Union  
10 Electric for its share of the Callaway plant?

11 A. I reviewed as many plans as I could obtain,  
12 including Missouri, Louisiana -- which is a much longer  
13 period -- California's proposed methods, a longer period;  
14 some are shorter and some are longer.

15 Q. Did you become aware of the fact that Idaho  
16 Power Company has proposed a three year phase-in related to  
17 a 27 percent increase associated with its Valmy 2 coal plant?

18 A. The utility's proposal?

19 Q. Yes.

20 A. I haven't seen the utility's proposal yet. I  
21 usually wait for the order.

22 Q. Are you aware of the fact that New Orleans  
23 Public Service Company has proposed a four year phase-in  
24 associated with its 35 percent requested increase for its  
25 share of the Grand Gulf plant?

1 A. New Orleans has proposed.-- New Orleans'  
2 proposal is at this moment before the City Council of  
3 New Orleans.

4 Q. That's correct.

5 A. That's the proposal of the utility. Whether it  
6 will be adopted or not, I cannot say.

7 Q. But that is their proposal, as you understand it?

8 A. That is their proposal as I understand it. But  
9 I also understand that they may modify their proposal.

10 Q. Now, at page 28 of your testimony you discuss  
11 the topic of recovery of deferred revenues. Am I correct  
12 that you believe that the company's proposed three year  
13 recovery of revenue deferrals is too short?

14 A. I believe that a three year recovery is very  
15 short.

16 Q. And you propose a ten year period, is that  
17 correct, in your testimony?

18 A. I have suggested a minimum of ten years.

19 Q. Now, the company has not requested to recover  
20 carrying charges on the deferred revenue under its phase-in  
21 plan, has it?

22 A. That's correct; and I agree with the company's  
23 position.

24 Q. In each of the Kansas plan, the Mississippi plan  
25 and the New Mexico plan that you discuss in your testimony

1 in addition to the ones that I have just discussed with  
2 you, am I correct in each of those cases included was the  
3 recovery of carrying charges on the deferred balances?

4 A. While they included recovery of -- you have to  
5 look at the entire context --

6 Q. I'm asking a very specific question. Did the  
7 plans include the recovery of carrying charges on the  
8 deferred balances?

9 A. It didn't include carrying charge on the  
10 majority of the plant which was deducted from rate base.

11 Q. Well, I'm speaking with respect to the phase-in  
12 plan if adopted.

13 A. Let's split that into two cases: Kansas and  
14 Mississippi. In the case of Mississippi the deferral plan  
15 is based on what's called an inventorying method.

16 Q. And carrying charges were allowed?

17 A. And carrying charges were permitted on the amount  
18 inventoried, so that, for example, while some of the plant is  
19 not added and will not be added to the rates until the tenth  
20 year carrying charges will be allowed in the meantime.

21 In the Kansas case --

22 Q. Let's stay with Mississippi for a minute. I  
23 believe we agreed before that the commission granted carrying  
24 charges not only on the inventoried amount but the deferral  
25 amount and the phase-in amount as well; is that correct?

1 A. Well, the terminology used throughout is  
2 inventorying of varying groups, if I may. We will  
3 deferral or inventory parts.

4 Q. Fine.

5 A. On whatever parts that have been deferred or  
6 inventoried there is a carrying charge.

7 In Kansas there was a deduction -- I would have to  
8 look back -- somewhere of a billion dollars for excess  
9 capacity and imprudence, and that was removed from the rate  
10 base. In other words, there is no carrying charge on that  
11 sum at all.

12 For the remaining portion, and for the short period  
13 of time, which is very small, a carrying charge was permitted.

14 Q. It was a 46 percent rate increase granted in  
15 that case; is that correct?

16 A. The company received well less than half of what  
17 they asked for, and on what they received they were given  
18 carrying charges.

19 Q. On what they received?

20 A. That's right.

21 I should correct that. Remember that they did  
22 receive some portion of the plant which they may depreciate  
23 but not include in the rate base.

24 Q. Now, on page 36 of your testimony you begin your  
25 discussion of the Financial Accounting Standard Board's

1 Standard No. 71; is that correct?

2 A. Yes, I do.

3 Q. You state on page 36 of your testimony generally  
4 accepted accounting principles and particularly FASB 71  
5 are not binding on this commission with respect to rate-  
6 making; is that correct?

7 A. That is correct.

8 Q. You would agree with me, however, and I think  
9 you state in your testimony, that there are certain  
10 consequences that may occur if a utility does not comply  
11 with generally accepted accounting principles, including  
12 FASB 71?

13 A. Well, I would say no for the most part.

14 Q. There are no consequences?

15 A. I didn't say that there are no consequences.

16 It's a complicated answer. There are some consequences but  
17 they are minor. I would say that if this Commission goes  
18 forward with an order that it considers just and reasonable  
19 the major consequence would be that the final draft of  
20 FASB 71 will reflect the reality of this order rather than  
21 the other way around.

22 In addition, the reporting of income, probably  
23 because I'm a student of Milton Freidman and the Chicago  
24 School, we do believe in efficient markets and we believe  
25 that you can't fool the public very easily or investors

1 very easily. If you report sums as income or you report  
2 them as deferred, the investor knows very well what is  
3 deferred and what is not, what they can expect to receive  
4 and what they cannot expect to receive. The method of  
5 reporting, per se, should not have a significant long-term  
6 effect on the investors' perception of a company.

7 Q. I'm speaking more in terms of accounting  
8 principles here, Mr. Palast. Now, in the absence of 71,  
9 FASB 71, generally accepted accounting principles for a  
10 non-regulated utility would apply and the revenues would be  
11 recorded on the income statement in the year received and  
12 expenses would be recorded on the income statement in the  
13 year incurred; is that correct?

14 A. If it's a cash basis company. I mean there are  
15 accruals. There are sums due and owing or capitalized  
16 sums.

17 Q. But with respect to the phase-in, if we did not  
18 have a FASB 71 the company could not currently record on its  
19 income statement the deferred revenue under the phase-in  
20 plan? Do you know the answer to that question?

21 A. I think that it could not.

22 Q. So under the company's plan if there were no  
23 FASB 71 the company would only be able to report on its  
24 income statement one-third of the increase requested in this  
25 case if the full increase were granted by the Commission in

1 the first year?

2 A. If we are talking about an unregulated company  
3 there would be no such thing as deferred revenue because in  
4 an unregulated firm you either sell your product or you don't.  
5 It has a value or it doesn't. Only in regulated industries  
6 can you charge a price for an item which is above its  
7 market value, which is what the company is seeking to do here,  
8 to somehow impose a price above a free market value for  
9 electricity. And you can't do that in an unregulated  
10 environment or record it in an unregulated environment because  
11 it would never be recovered, deferred or otherwise.

12 Q. If there were no FASB 71 and the Commission entered  
13 an order in this case approving the company's phase-in plan  
14 as filed, the company's income statement would only reflect  
15 the revenue that it billed during the first year rate are in  
16 effect, which under the company's plan is one-third of the  
17 amount requested in that case; is that correct?

18 A. Let me see if I have your question correctly.  
19 You're setting up a hypothetical. You are saying that FASB --  
20 no FASB 71, even the one that exists today? That does not  
21 exist?

22 Q. That's correct -- or for whatever reason the  
23 company doesn't comply with its requirements or cannot  
24 utilize it.

25 A. Let us say that FASB 71 does not exist, that

1 there are no special rules to regulate the industry.

2 Q. That's correct.

3 A. In which case we have a world in which the  
4 company could sell its products only at the market value of  
5 that product.

6 Q. We have rates established by the Commission that  
7 allowed them to charge certain rates.

8 A. We would have regulation but no accounting rules?

9 Q. That's correct.

10 A. I'm kind of stumped by the hypothetical but I  
11 will do my best.

12 In that case I would assume that in this world in  
13 which there is regulation but no rules for regulation if I  
14 were an auditor I might say that this sum is -- if I feel  
15 that there is a likelihood of collecting this sum I would  
16 say that it could be booked.

17 Q. That's permitted in the absence of 71, in your  
18 view, under generally accepted accounting principles?  
19 Is that your testimony in this proceeding?

20 A. Again, we are setting up a hypothetical --

21 Q. Is that your testimony, Mr. Palast?

22 A. Under the strict terms of your hypothetical it's  
23 conceivable that an auditor could take that view, or it's  
24 conceivable that an auditor could take the view that these  
25 sums are not due and owing and will never be received.

1 Without guidance from FASB an auditor would have to use  
2 their judgement as to the probability of collection.

3 Q. And they would have to apply generally  
4 accepted accounting principles in reaching that conclusion?

5 A. That is correct.

6 Q. And you believe under generally accepted  
7 accounting principles, in the absence of FASB 71, that the  
8 company would be permitted to defer the revenue which it  
9 will not receive until subsequent years?

10 A. I'm not sure whether they would be permitted or  
11 not. The auditor would have to determine whether he believes  
12 that is probably -- whether there is a high probability of  
13 collection.

14 Q. And you believe the auditor has that discretion  
15 in the absence of FASB 71? Is that your testimony?

16 A. Well, again, we are talking about --

17 Q. Is that your testimony?

18 A. Again, we are talking about a world -- again, we  
19 are talking about a world which cannot and will not exist,  
20 in which we have a regulated industry but there is no accounting  
21 standard for measure the cash flows of regulated industries.

22 Q. Well, let's talk about a hypothetical that may  
23 exist, Mr. Palast.

24 A. Okay.

25 Q. That is, the exposure draft currently issued by

1 the Financial Accounting Standards Board to revise Statement  
2 No. 71 is adopted.

3 A. Yes?

4 Q. Now, you state at the bottom of page 31 of  
5 your testimony that no exposure draft has been issued as of  
6 this writing of your testimony; is that correct?

7 A. As of this writing, as I stated, beginning.  
8 Since then an exposure draft has been issued and I have  
9 reviewed it and my basic conclusion is the same.

10 Q. When was your testimony submitted in this  
11 proceeding, Mr. Palast? Am I correct that it was January  
12 14, 1986?

13 A. January 14, 1986.

14 Q. Am I also not correct that the exposure draft  
15 of FASB 71 was issued on December 19, 1985, almost a month  
16 before your testimony was filed in this case?

17 A. That is the date of issuance, and Mr. Farling  
18 in response -- PECO claimed that they would send me  
19 immediately upon issuance of that 71 exposure draft a copy  
20 of it, which I never received from the company at any time.  
21 However, I did receive it from other sources in other  
22 cases on which I was working.

23 Q. And when you filed this testimony on January  
24 14th you were not aware that an exposure draft had been  
25 issued?

1 A. I had just received word that an exposure draft  
2 had been issued.

3 Q. On January 14th you were not aware of that  
4 fact?

5 A. I was aware just about January 14th that an  
6 exposure draft had been issued.

7 Q. Well, you state in your testimony that at the  
8 time you filed your testimony there was no exposure draft.

9 A. Is that what I state?

10 Q. Yes.

11 A. And where did you see that?

12 Q. The bottom of 39: "It has not approached the  
13 proposal stage, that is, as of this writing, no exposure  
14 draft has been issued for comment."

15 A. "As of this writing." It's on the date of the  
16 writing. I had not received the response of the company that  
17 they would send me the exposure draft when it was issued.  
18 So I expected the company to respond, they didn't, and that  
19 put me a couple weeks behind in finding this document.

20 Q. You wouldn't otherwise have been independently  
21 aware of this in your work?

22 A. Yes, I would. I just wouldn't have rushed out  
23 and got it the day after it was issued.

24 I did receive it. I received copies from three  
25 different sources, none of them the company.

1 Q. And none before January 14th?

2 A. That's right.

3 Q. Do you have a copy of the exposure draft with  
4 you today?

5 A. Yes.

6 Q. Could we look at it for a moment?

7 A. Yes.

8 Q. Looking at paragraph four of the draft, would you  
9 agree with me that it states as follows: "All current  
10 operating" --

11 MR. RAINEY: Just a moment, please, while he gets  
12 to the page. Thank you.

13 (Witness perusing document.)

14 MR. RAINEY: Proceed.

15 BY MR. MacGREGOR:

16 Q. It states, "All current operating costs that are  
17 deferred for future recovery by a regulator pursuant to a  
18 phase-in plan shall be capitalized as a separate asset (a  
19 deferred charge) if all of the following criteria are met.  
20 If any of those criteria is not met none of the costs that  
21 are deferred for future recovery under the plan shall be  
22 capitalized for financial accounting purposes."

23 And paragraph four goes on to state three criteria,  
24 the first being that, "The costs in question are deferred  
25 pursuant to a formal plan that has been agreed to by the

1 regulator," second, "The plan specifies the timing of  
2 recovery of all costs that will be deferred under the plan,"  
3 and third, "All costs deferred under the plan are scheduled  
4 for recovery within ten years of the date when deferral  
5 began," is that correct?

6 A. That's what it says, yes.

7 Q. Would you agree with me that your plan, which  
8 does not allow for recovery of all costs deferred under the  
9 plan until 17 years would not apply, at least to this  
10 exposure draft of FASB 71?

11 A. It would apply. It would be accounted for  
12 differently. The company would have much lower income in  
13 the early years and much higher income in the higher years.  
14 In the very, very unlikely event that this is adopted  
15 there would be a major change in how the income statement  
16 is recorded.

17 Q. Have you examined what you refer to as a major  
18 impact might be on the company in 1987, '88, '89?

19 A. Well, we would have -- well, definitely there  
20 would be a stream decline in reported income and a big fat  
21 footnote at the bottom saying that we have this revenue  
22 deferred and due and owing. I have looked at this not only  
23 for PECO but for other utilities which would be affected by  
24 this sudden ten year cliff edge and because I believe it  
25 would have such a major effect -- it would have a very major

1 effect on reported income and certain indicators. That is  
2 why I believe it won't be adopted.

3 Q. So it wouldn't surprise you to find that if  
4 this occurs the company's earnings would be insufficient to  
5 cover its current dividend in 1987, 1988 and 1989?

6 A. You mean its current reported income. Remember  
7 that the FASB's reporting -- or the FASB's requirement --  
8 now I'm using the wrong terminology. This draft proposal's  
9 requirement, which is not the current rule of accounting,  
10 if this draft exposure is adopted --

11 Q. That's correct. My questions assume that.

12 A. If this draft exposure is adopted there would be  
13 no change in the amount of cash received by the company.  
14 It is not in the least affected. Its ability to cover or  
15 not cover its dividends, its ability to meet its cash needs,  
16 is not directly affected by the change in how its cash flow  
17 is reported.

18 Q. But recorded earnings on an accrual basis and  
19 coverages on an accrual basis would be affected?

20 A. Recorded earnings would be affected and coverages  
21 despite -- it's interesting that the FASB believes that  
22 there wouldn't be -- you should note on the back of this that  
23 they believe there really is no serious problem with the  
24 coverages, but I believe that there may be for certain  
25 companies.

1 Q. Only if your longer than ten year phase-in  
2 plan is adopted?

3 A. If a longer plan, a reasonable plan --

4 Q. Longer than ten years.

5 A. A reasonable plan longer than ten years is  
6 adopted.

7 Q. Do you think the possibility that the exposure  
8 draft will be adopted is a risk worth considering by the  
9 Commission in entering an order in this proceeding?

10 A. I will give you a complete answer to that.  
11 One, the Commission should never ignore evidence of any  
12 activity which may bear on the consequences of its actions.  
13 However, if the Commission slavishly adheres to a draft of  
14 the Financial Accounting Standards Board, which has taken  
15 in no notice or consideration from regulators and has so  
16 stated, which has heard from no utilities which would be  
17 affected by this order and it's so stated, which voted four  
18 to three to issue this exposure draft, hardly a resounding  
19 recommendation, we would be in trouble. I think if the  
20 Commission attempts to guess, harms the economy of this city  
21 by attempting to guess what this group in Stamford,  
22 Connecticut may or may not do -- PECO's Mr. Farling suggested  
23 adjusting the rates according to what he thought the draft  
24 would be based on the AICPA issues paper and I would note  
25 that the exposure draft agrees on almost no points at all

1 with the AICPA issues paper, and therefore, given the  
2 tremendous difference between draft one and draft two we  
3 might find that the final draft, or draft three, may be  
4 further still from either of those propositions.

5 Therefore, to write an order trying to out-guess  
6 the FASB on what it may do I think would be very irrespon-  
7 sible.

8 Q It shouldn't be considered at all?

9 A Again, I didn't say --

10 Q It should be considered, but not --

11 A As even the Illinois commission said, the  
12 FASB does not set rates in Illinois but we don't ignore  
13 the information that's provided by these discussions.

14 Q Did the Illinois commission you referred to also  
15 state in its order as follows: "The time period for the  
16 phase-in should be relatively short. This means at least  
17 that full recovery of the deferred revenues cannot be  
18 postponed for the full life of the plant, and even more,  
19 that at least the deferral period and probably also the  
20 recovery period must take no more than ten years"?

21 A Well, the Illinois commission is the only  
22 commission far that has made any adjustments in an attempt  
23 to out-guess the FASB, even though it admitted it is doing  
24 so very reluctantly. I think that they have made a mistake  
25 by doing so.

1 Q. Did the Illinois commission also state that,  
2 "Full capitalization should be allowed on deferred revenues,  
3 that is, any deferred revenues should themselves earn a  
4 return, including both the equity and debt components of  
5 that return"?

6 A. That is my understanding. I've read the order.

7 Q. Now, at page 47 of your testimony you state  
8 that the effect of extending the phase-in from three to  
9 seven years will be negligible; is that correct?

10 A. If you could site my statement -- okay.

11 Yes. I believe that in the overall ability of the  
12 company to obtain financed capital it needs for reasonable  
13 projects that the effect will be negligible.

14 Q. And as an example you state that a seven year  
15 phase-in plan will require the company to capitalize only  
16 \$32 million more during the year for deferred revenue than  
17 it would under its own three year plan; is that correct?

18 A. There is a word left out and if it's creating  
19 problems let me correct it. As shown in Exhibit GP-7, a  
20 seven year phase-in will require the company to capitalize  
21 only \$32 million more during the -- and the word "first"  
22 is left off of the sentence -- during the first year for  
23 deferred revenue (annualized) than it would under its own  
24 three year plan.

25 Q. So the material shown in Exhibit GP-7 and your

1 statement on page 47 of your testimony deals only with  
2 the first year rates are in effect; is that correct?

3 A. Yes.

4 Q. Now, if we extended that analysis, Mr. Palast,  
5 and looked over the first seven or so years the plan was in  
6 effect am I correct that that \$32 million figure would  
7 increase to \$1.1 billion?

8 A. The total capitalization of deferrals?

9 Q. Yes.

10 A. Yes, about \$1.02 billion, net of tax, yes.

11 Q. A significantly different number than \$32 million?

12 A. That is correct. Over time it increases. At  
13 the end of the period, just as at the end of the phase-in  
14 period of the company, the company will have to capitalize  
15 two-thirds of a billion; our plan requires approximately  
16 three times that sum.

17 Q. But you elected only to show the \$32 million  
18 figure in your testimony?

19 A. I elected. I reviewed all the others too.

20 Q. But you did not present them in your testimony?

21 A. No, I did not.

22 Q. On page 51 of your testimony, Mr. Palast, you  
23 discuss the impact of the various phase-in programs on  
24 internal cash flow; is that correct?

25 A. Yes, I do, sir.

1  
2 Q And in the middle paragraph on page 51 you  
3 state that, "The company's internal cash flow under its  
4 three-year phase-in plan will equal about 58.7 percent of  
5 construction spending," for the first year of the phase-in  
6 plan; is that correct?

7 A Yes.

8 Q And you compare that number to the 47.2 percent  
9 figure which would be produced under your seven year phase-  
10 in plan; is that correct?

11 A Yes, adjusted from '86 pro forma.

12 Q Correct.

13 And once again, you have not presented any figures  
14 for any years after 1986 in your analysis for your seven  
15 year phase-in plan?

16 A Actually due to the fact that after the filing  
17 date of the testimony we received an updated extended -- we  
18 had asked the company for projections. These were not  
19 provided to us until after the filing date of the testimony.

20 Since receiving Mr. Paquette's extension of his  
21 exhibits from the '86 pro forma through 1989, I have done  
22 some basic calculations showing that for the most part this  
23 condition still exists.

24 Again, obviously, a slower phase-in means less  
25 internal capital for the company but not so much that it  
reverses the great improvement that occurs because they

1 have completed the Limerick nuclear plant.

2 So since the writing of this testimony, after I  
3 received Mr. Paquette's exhibits, I did review the following  
4 years, as I had done before by estimates but now I had some  
5 better figures.

6 Q Mr. Palast, I'm going to provide you with  
7 certain figures that the company has calculated and you can  
8 accept them subject to check and you can tell us whether  
9 you believe they are wrong. For discussion purposes, the  
10 company has calculated the effect on internal cash flow of  
11 your seven year phase-in plan and has determined that internal  
12 sources of funds as a percentage of construction excluding  
13 AFUDC, which is the similar figure you present on Exhibit  
14 GP-11, will fall to nine percent in 1987, eight percent in  
15 1988 and 6.4 percent in 1989.

16 A Nine percent in '87?

17 Q Right. And 8.0 percent in '88.

18 A Okay.

19 Q And 6.4 percent in '89.

20 And in addition we have determined, or calculated,  
21 that net cash flow as a percentage of total capital --

22 A Could you give me the indicator that you're  
23 discussing again?

24 Q Internal sources of funds as a percentage of  
25 construction excluding AFUDC.

1 We have also calculated net cash flow as a  
2 percentage of total capitalization under your plan and  
3 determined that in 1987 the figure would be .6 percent,  
4 in 1988 the figure would be .5 percent and in 1989 the  
5 figure would be .3 percent, as compared to the 3.0 percent  
6 figure employed by Standard & Poor's for maintenance of a  
7 BBB bond rating.

8 A. And this is the net cash flow --

9 Q. As a percentage of total capitalization.

10 A. Let me ask you a question. Does this assume  
11 the completion of Limerick 2?

12 Q. Yes.

13 A. Let me take a look at something now.

14 (Witness perusing documents.)

15 A. You show eight percent from the updated version  
16 I received after the filing of my testimony, and I show that  
17 in 1988 internal sources as a percentage of construction  
18 excluding AFUDC is approximately 20 percent. So we have  
19 some type of disagreement.

20 Q. When you calculated that number did you consider  
21 the impact of reduced investment tax credits and deferred  
22 taxes that the company would incur as a result of not  
23 paying taxes on the deferred revenue currently?

24 A. So you're loading in the fact -- in other words,  
25 you're loading in your figures an inability to call on tax

1 credits that you would otherwise have available?

2 Q. Correct. Under both our plan and your plan  
3 there will be no tax paid on the deferred revenue, so  
4 the company will incur less tax expense and have less  
5 investment tax credits and also it will affect deferred taxes  
6 as well; is that not correct?

7 A. But you will have, then, an investment tax  
8 credit left over for another day.

9 Q. Absolutely.

10 A. I would be happy to review your figures against  
11 mine when we have the opportunity.

12 Q. Thank you.

13 One point on page 48, just for my clarification.

14 A. Which page, sir?

15 Q. Forty-eight.

16 A. Yes, sir.

17 Q. Beginning about in the middle of the first big  
18 paragraph, the sentence that begins in the middle of the  
19 line, "Because the AFUDC was previously reported as income,  
20 the cash collection of the sum does not appear as an addition  
21 to income during the phase-in period."

22 A. Yes.

23 Q. And then the last sentence, "In Peco's case  
24 cash earnings will be higher than reported due to the  
25 reversal of AFUDC on Limerick 1."

1 Is that correct? Is that your understanding of  
2 AFUDC?

3 A. Let me see if I can explain the sense of this  
4 paragraph. I was reading it yesterday and noted that it  
5 may have been confusing the way I phrased it.

6 Q It was somewhat confusing to us. I would  
7 appreciate a clarification.

8 A I'm glad for the opportunity to clarify it.

9 We often hear from the utility rate of return  
10 witnesses and executives of rating agencies that a utility's  
11 quality of earnings is insufficient because the AFUDC is  
12 an inordinate percentage of the income. However, what is  
13 not shown when these calculations on the quality of earnings  
14 appear is that at a certain point this effect reverses and  
15 the quality of earnings -- the best way to put it is that  
16 the quality of earnings rises. The AFUDC, before there was  
17 a non-cash component of earnings.

18 In effect, when Limerick 1 enters the rates, phased-  
19 in or not, this process reverses and AFUDC cash is being  
20 collected by depreciation charges on the plant. But there  
21 is no income being shown while this cash is collected. In  
22 other words, this is not being reported as income because it  
23 was reported before.

24 So what you have is you have an addition to cash, you  
25 have an addition, a bolstering of the quality of earnings.

1 It's very simple.

2 Q Let me ask you this: the AFC is capitalized  
3 as part of the cost of the plant; is that correct?

4 A The AFC is --

5 Q Becomes part of the cost of the plant that is  
6 depreciated in rates.

7 A Well, we use the terminology, becomes part of  
8 the cost of the plant. It's a sum which is capitalized and  
9 then amortized over the life of the plant as part of the  
10 depreciation charge.

11 Q Well, the company's rate base claim for Limerick  
12 1 in this case includes the AFUDC accrued during the course  
13 of construction.

14 A That is correct.

15 Q And that will be recovered as depreciation  
16 expense --

17 A Not as income.

18 Q -- And as return on investment; and that will  
19 flow through the income statement and show on the bottom  
20 line earnings and income of the company.

21 A Excuse me. When the AFUDC -- let's take a  
22 billion dollars of AFUDC if we may just to have a working  
23 figure, depreciated over 30 years. That's \$30 million a  
24 year. If that is charged to consumers, that depreciation  
25 of the AFUDC amount -- let's forget the rate basing aspect

1 of it. That \$30 million does not show up as an addition  
2 to income of \$30 million per year, it's shown as a charge  
3 to income. It's shown as depreciation.

4 Q. And there is revenue to cover it.

5 A. Yes, there is. And that's the entire point, that  
6 there's cash -- before quality of earnings for PECO and other  
7 nuclear constructing utilities during the construction phase  
8 is low because they are reporting income but not getting the  
9 cash. Post-construction the story reverses -- and the company  
10 did not mention this in its rate of return testimony -- the  
11 story reverses and they are receiving cash but not recording  
12 it as income.

13 I'm not saying it's improper, but I'm trying to  
14 show what happens to a company, why its finances improve  
15 as you go from pre-construction to post-construction.

16 Q. You're getting at why the finances improve.  
17 There is nothing wrong with the reporting process in the  
18 company's financial statements.

19 A. I'm not saying that you should begin reporting  
20 AFUDC depreciation as other than depreciation.

21 Q. And technically there is no reversal in an  
22 accounting sense of the former AFUDC charges. There is  
23 no reversal of the accounting entry on the books of the  
24 company. I'm just trying to get a sense of --

25 A. There is -- that term is actually proper. There

1 is a reversal since it's not eliminated. You're taking  
2 an item off the balance sheet. You're amortizing it. So  
3 that the process is reversed. So you're charging a charge.  
4 You're getting cash but you're not reporting income. So  
5 the quality of earnings improves thereby.

6 Q. All items are reported on the financial statement?

7 A. All items are reported but it's not reported  
8 as income. It's reported as depreciation charge.

9 Q. Now, on page 57 of your testimony you discuss the  
10 topic of security ratings; is that correct?

11 A. Yes, I do, sir.

12 Q. On page 58 specifically you discuss Central  
13 Maine Power Company, and in the first paragraph of your  
14 answer on that page you summarize a settlement of a rate  
15 proceeding in which Central Maine agreed to write off  
16 certain portions of its investment in Seabrook 1 and  
17 Seabrook 2; is that correct?

18 A. That's correct.

19 Q. Would you agree with me that you have been  
20 somewhat incomplete in describing that order, that a  
21 number of other things took place in that proceeding?  
22 For example, there were three other cancelled plants at  
23 issue in that proceeding which the Maine commission allowed  
24 recovery of investment over ten years with a return on the  
25 unamortized balance, and with respect to Seabrook 1 the

1 70 percent not written off was allowed to be recovered over  
2 30 years with a return on the unamortized portion of the  
3 investment, and that there were also provisions of recovery  
4 of certain portions of the costs not written off on Seabrook  
5 2.

6 A. A couple of things. I think that while you now  
7 have added a few extra points to the order, it may be  
8 worthwhile putting in the entire order by stipulation from  
9 that case into this record.

10 Q. I'm just trying to say that there are other  
11 things going on here than just the write-off.

12 A. But in addition to those other things, though,  
13 I would also note that when you say that they were permitted  
14 70 percent, or in one case only 60 percent, they were  
15 disallowed at least 30 percent of Seabrook 1, they were  
16 disallowed 40 percent of Seabrook 4 --

17 Q. Up to a certain date.

18 A. -- But the additional amount also has -- the  
19 amount that can be recovered -- has a cap on it and that  
20 cap, just so you're aware and this Commission is aware,  
21 has already been exceeded. The company has already made  
22 provisions for the fact that it's going to incur a  
23 continuing loss unless it can sell its Seabrook share.

24 Q. You refer to the fact that Duff and Phelps  
25 upgraded Central Maine Power Company shortly after this

1 order was entered; is that correct?

2 A. That's correct.

3 Q. And then on a previous page you refer to the  
4 fact that Standard & Poor's also upgraded Kansas Gas &  
5 Electric after its rate order; is that correct?

6 A. That's correct.

7 Q. Am I correct that you have neglected to point  
8 out that Duff and Phelps, the agency to whom you referred  
9 on Central Maine Power Company, downgraded Kansas Gas &  
10 Electric after the entry of the Kansas rate order?

11 A. I wouldn't call it neglect, but I didn't include  
12 that. I didn't give a complete rendering of all the  
13 discussion of the ratings.

14 Q. But you referred to Duff and Phelps with respect  
15 to Central Mainer but then switched to Standard & Poor's  
16 for the Kansas Gas & Electric?

17 A. I referred to Duff and Phelps because PECO has  
18 proffered -- I'm writing rebuttal testimony -- proffered  
19 the testimony of Mr. Abrams of Duff and Phelps, who has  
20 made a claim that less than complete treatment of PECO's  
21 Limerick 1 costs could cause tremendous financial problems  
22 for the company. And I wish to note that it was the same  
23 Mr. Abrams that made the same statement in the Central  
24 Maine Power case and then when Central Maine Power was  
25 stuck with a 30 to 40 percent write-off and other

1 restrictions that immediately thereafter Mr. Abrams'  
2 firm upgraded the company.

3 The implication that neglect was involved is  
4 improper.

5 Q Well, you would agree with me, though, that  
6 you apparently consider Mr. Abrams important and  
7 Duff and Phelps important and you did not mention in your  
8 testimony that they downgraded Kansas Gas & Electric.

9 A I don't consider Mr. Abrams important or Duff  
10 and Phelps important. I think that Mr. Abrams makes  
11 statements in rate cases about what will happen to utilities  
12 and he has been proven wrong.

13 Q Duff and Phelps did downgrade Kansas Gas &  
14 Electric?

15 A I believe so.

16 Q Finally, Mr. Palast, again on page 66 of your  
17 testimony, you discuss the company's unrecovered revenue  
18 collection rider; is that correct?

19 A Yes, sir.

20 Q And as I understand your testimony you are  
21 generally fairly satisfied with the rider, with the one  
22 major exception which you discuss at the bottom of page  
23 67 of your testimony; is that correct? The mechanics of  
24 the rider don't seem to trouble you?

25 A Actually I have two objections to the rider.

1 One, however, I believe is best addressed by Dr. Shinnar  
2 because it's economic.

3 Just so we can be clear which objection we are  
4 talking about, I would not endorse necessarily the  
5 concept that the Limerick revenues should be allocated and  
6 owed by class.

7 Q. Okay.

8 A. I think that is best left to Dr. Shinnar to  
9 discuss.

10 Q. Fine. I will leave that aside for the moment.

11 A. Thank you.

12 Q. At the bottom of page 67 you describe the  
13 company's plan and you say, "To this extent, PECO's plan  
14 is similar to other phase-in plans." And you go on to  
15 say, "PECO's plan deviates in one major respect: if,  
16 during the next three years," which I take it you mean  
17 the first three years of the phase-in program, "the  
18 company's total revenues fall short of its predictions,"  
19 and then you continue in bold face type, "the entire sum  
20 of the revenue shortfall will be added to the accumulated  
21 deferred revenue account and added to rates over three or  
22 more years."

23 Is that correct?

24 A. Yes. That is my understanding of the revenue  
25 rider.

1 Q And you continue further down on page 68, the  
2 second line of the next answer, "If PECO has underestimated  
3 its test year revenues for 1986, PECO should not in 1989  
4 reach back and recover 100 percent of the shortfall of 1987."

5 Is that correct?

6 A That's correct.

7 Q I believe you stated before that you were present  
8 for the cross-examination of Mr. Williams in this case on  
9 December 13th?

10 A I was present for a substantial portion of it.

11 Q I would like to show you a portion of his  
12 cross-examination by Ms. Chestnut of the Trial Staff.

13 A Excuse me. What date was this?

14 Q December 13, 1985.

15 MR. RAINEY: May we have a moment to look at this?

16 A I'm sorry, sir. I was there during the cross-  
17 examination of Mr. Paquette, not Mr. Williams.

18 BY MR. MacGREGOR:

19 Q Just to clarify this point I would like to show  
20 you some portions of Mr. Williams' cross-examination and  
21 ask that you review them.

22 I think you can begin at the bottom, the question  
23 that begins at the bottom of transcript page 622.

24 (Witness perusing documents.)

25 A I have now reviewed this document.

1 Q Would you agree with me that, in fact, at least  
2 according to Mr. Williams' cross-examination in this  
3 proceeding that it's not the company's position that any  
4 shortfall between what's deferred and the \$670 million will  
5 be collected through the surcharge during the three year  
6 recovery period?

7 A Well, my understanding is that it will. If  
8 the company is saying that it's changing it's proposal --

9 Q The company has not changed its proposal.

10 A Then let me go back to the file, because I'm  
11 always happy if there is -- if the consumers are getting  
12 a better deal than I thought. Let me just look here.

13 (Witness perusing documents.)

14 A Now, it's my understanding of the company's  
15 proposal -- and I would be very pleased to find out that  
16 I'm wrong because it's a very unique proposal not adopted in  
17 any other state so it took me a while to try to figure it  
18 out.

19 My understanding is that the rate will be set at  
20 and -- as you say Mr. Williams says in his cross-examination --  
21 billed at the rate in which revenues are increased by  
22 \$671 million per year.

23 Q Designed to collect that amount?

24 A Designed to collect that amount on a test year  
25 basis. However, the amount which will be paid, charged as

1 currently due and owing by consumers, will be one-third  
2 additional of that amount, which is something like \$224  
3 million.

4 Now, the difference -- let us take the first year  
5 difference, which is something like \$448 million -- or  
6 \$446 million -- which is deferred. That's year one.

7 Q. And I guess my question goes to this: is it your  
8 understanding that the company will defer \$446 million  
9 regardless of what sales produce during that period that the  
10 rates were in effect?

11 A. That the company will defer the difference as  
12 billed. My objection -- let's see if we can agree. Maybe  
13 my objection has been taken care of. My objection goes to  
14 the following concept: let's say that the revenues received  
15 are exact, that billed is \$671 million, actually deducted  
16 is \$224 million, leaving a sum of \$447 million for collection  
17 during the revenue surcharge period. And in each of the  
18 three years of the surcharge or phase-out period, whatever  
19 you call it, \$149 million will be charged back to ratepayers  
20 in each of those years.

21 However, if due to curtailment in usage -- and  
22 remember that there is at this moment a charge and some  
23 doing by class -- let's take manufacturers -- if a  
24 number of manufacturers leave the area due to higher rates  
25 the remaining manufacturers will be responsible for paying

1 that \$149 million shortfall even if they were not the ones  
2 to whom the bill was sent.

3 Q. Let's look at page 67 of your testimony, at the  
4 bottom. You said if during the next three years. You're  
5 not talking about the recovery period there. You said in  
6 the next three years, which I assume is the first three  
7 years that rates will be in effect. If, during that  
8 period the company's total revenues fall short of its  
9 prediction -- I take it that means that if sales are less  
10 than the company anticipates, so the amount deferred is not  
11 \$446 million, the amount collected under the deferral is  
12 not \$446 million but something less than that because sales  
13 fell.

14 A. Okay.

15 Q. The company is proposed to make up that  
16 difference in the surcharge; is that your understanding?

17 A. Yes. In fact, let's split my objection into  
18 three parts.

19 Q. Let's look at the first part.

20 A. Okay. As to the question, the way it is worded,  
21 it appears that if there is a shortfall that sums will be  
22 accumulated in a deferred account and therefore if the amount  
23 of revenue declines, is less than received, then the company  
24 will seek to obtain the shortfall. That is, if it does not  
25 receive \$224 million in the first year but instead due to

1 curtailment receives \$200 million, that the \$24 million will  
2 be added into the accumulated deferral.

3 If that is not so, then I'm happy to hear that.

4 Q Well, I am happy to tell you that that's the  
5 case, and I take it that would take care of at least that  
6 objection to the unrecovered revenue rider.

7 A I'm glad we are all happy. But that is one  
8 objection, yes.

9 MR. MacGREGOR: Thank you, Mr. Palast.

10 Your Honor, that concludes my cross-examination.

11 JUDGE MATUSCHAK: Let's take a ten minute recess.

12 (Recess.)

13 JUDGE MATUSCHAK: We can proceed whenever the parties  
14 are ready.

15 Who wants to proceed next? Staff?

16 MS. CHESTNUT: I will, Your Honor. Thank you.

17 CROSS-EXAMINATION

18 BY MS. CHESTNUT:

19 Q Good morning, Mr. Palast.

20 A Good morning.

21 Q Mr. Palast, my name is Marcie Chestnut and I'm a  
22 member of the Commission's Trial Staff.

23 Mr. Palast, you were asked some questions by Mr.  
24 MacGregor this morning with respect to the deferred surcharge  
25 proposed by the company; is that correct?

1 A. Yes.

2 Q. And Mr. Palast, would you agree that the  
3 amount of the deferred revenue will vary with the revenues  
4 generated by the actual sales during this period?

5 A. Yes, they will.

6 Q. And isn't it correct, Mr. Palast, that whatever  
7 that deferred revenue amount is, it is guaranteed to be  
8 recovered under the company's proposal?

9 A. By the company's proposal there is a unique and  
10 unprecedented guarantee.

11 MS. CHESTNUT: Thank you, Mr. Palast.

12 That's all the questions I have, Your Honor.

13 JUDGE MATUSCHAK: Consumer Advocate.

14 MR. WERSAN: No questions, Your Honor. Thank you.

15 JUDGE MATUSCHAK: Mr. Kleppinger.

16 CROSS-EXAMINATION

17 BY MR. KLEPPINGER:

18 Q. Good morning, Mr. Palast. My name is David  
19 Kleppinger. I represent the Philadelphia Area Industrial  
20 Energy Users Group. I just have a few brief questions.

21 A. Yes, sir.

22 Q. Are you generally familiar with the concept of  
23 sinking fund depreciation?

24 A. Yes.

25 Q. Now, under your understanding of the current

1 version of FASB 71 would it be your position that FASB  
2 71 in its current form would tolerate and permit qualified  
3 opinions to be rendered by the CPAs under a sinking fund  
4 depreciation program for Limerick Unit 1?

5 MR. MacGREGOR: Objection, Your Honor; beyond the  
6 scope of Mr. Palast's testimony.

7 JUDGE MATUSCHAK: Well, it's not beyond his  
8 testimony because he included that in his testimony.

9 MR. MacGREGOR: There's no reference to sinking  
10 fund depreciation in his testimony, Your Honor.

11 MR. KLEPPINGER: That's correct, Your Honor, but  
12 there is reference to FASB 71 and as all the parties here  
13 today know there are several proposals on the table  
14 regarding phase-ins, modifications of phase-ins and  
15 whether or not they qualify under FASB 71. During Mr.  
16 MacGregor's cross-examination he raised some questions as  
17 to whether Mr. Palast's plan would --

18 JUDGE MATUSCHAK: We are going to overrule the  
19 objection. You may proceed.

20 MR. KLEPPINGER: Thank you, Your Honor.

21 A. If I may, let me just correct one term of art.  
22 I believe you mean, if I may, that under current FASB 71,  
23 Statement 71, an auditor can give an unqualified opinion  
24 under a sinking depreciation method or under the method that  
25 I have proposed. Either way it would permit an unqualified,

1 that is, acceptable, opinion of the company's books.

2 Q. I apologize for my accounting terminology.

3 Similarly, Mr. Palast, under the proposed draft  
4 exposure of FASB 71 would it be your position that a sinking  
5 fund depreciation approach to a modified phase-in plan, if  
6 you will, it would also be permissible for an accountant to  
7 render an unqualified opinion for that?

8 A. Let me split the answer in two parts if I may.  
9 Yes, there could be an unqualified opinion assuming the  
10 deferred revenues are booked as current revenues. Any plan  
11 can receive -- any base plan -- can receive an unqualified  
12 opinion. It just matters how the current and deferred  
13 revenues are recorded to the income sheet.

14 MR. KLEPPINGER: Thank you, Mr. Palast.

15 That's all I have, Your Honor.

16 JUDGE MATUSCHAK: Is there any other cross-examination  
17 of this witness?

18 MR. CLARK: Yes, Your Honor.

19 CROSS-EXAMINATION

20 BY MR. CLARK:

21 Q. Mr. Palast, I'm Roger Clark of the Governor's  
22 Energy Council.

23 On page 22 of your testimony you state that your  
24 recommended seven year phase-in and ten year recovery period  
25 will still mean that the Philadelphia economy will be burdened

1 because you will allow for increases in rates beyond those  
2 projected as safe for the economy by Dr. Shinnar. Do you  
3 know how much above those safe levels of Dr. Shinnar your  
4 seven year and ten year program is?

5 A. I can give you some guidance as to that. I  
6 would like to defer to Dr. Shinnar for any exact calculations.  
7 One of the great difficulties is that we don't have a  
8 secure projection of base rate and fuel charge increases  
9 during the interim period.

10 In other words, the proposal I have still permits  
11 the company to increase its base rates and fuel charges on  
12 a normal rate setting basis during that period.

13 We simply are trying to, in my judgement, to create  
14 some type of balance between the serious needs of the  
15 Philadelphia economy from my own readings and Dr. Shinnar's  
16 study and the financial needs of the company which we don't  
17 want to unduly impair.

18 Q. And Dr. Shinnar is the one to ask about the  
19 details and specifics of those levels?

20 A. That is correct.

21 Q. On page 34 and 35 you state several conditions  
22 behind your ten year recommended recovery period, and the  
23 final one you mention is that you assume there will be some  
24 write-off of Limerick 1 as a result of this proceeding.

25 How little of a write-off can there be and still have

1 your recommendation be a ten year period? What is the  
2 critical write-off amount, in other words?

3 A. I must admit I'm very reluctant to give some  
4 type of cutoff point. If one reads the Shinnar study and  
5 reads some of my own studies in the area of rate setting and  
6 economic impact, a basic rule of thumb is to attempt to keep  
7 the overall rate within two parameters: first and foremost,  
8 that it does not exceed the overall rate of inflation, and  
9 secondly, that the rates do not get out of line with the  
10 rates charged in competitor cities to industrial and  
11 commercial customers.

12 So basically, the overall -- in other words there's  
13 a number of conditions laid out here and you can come up  
14 with any number of combinations. But the idea to protect  
15 the economy is to stay within those parameters.

16 Q. What was the size of the write-off that you're  
17 assuming in staying with the ten year recovery period?

18 A. To me the ten year recovery is a minimum and  
19 I would say that -- let's put it this way: I'm not going to  
20 make a recommendation as to imprudence. I think I stutter  
21 every time I say imprudence because it's such a difficult  
22 subject to handle. I have not studied nor testified on the  
23 imprudence subject. I understand and I would assume that  
24 there would be major deductions. There have already been  
25 some preliminary rulings in this proceeding as to that matter.

1 I would not change my recommendation if the size  
2 of the deduction were equal to the Kansas deduction, in  
3 which somewhat more than half of the revenues requested by  
4 the company were rejected.

5 Q I was trying to get that number.

6 My final question, sir, has to do with your  
7 recommendation about energy savings, a guarantee of the  
8 energy savings, and also a requirement of a operating  
9 capacity factor of 65 percent. You discuss this on page  
10 64 of your testimony.

11 A Yes, I do.

12 Q Will you tell me, please, why you choose that  
13 65 percent number as a capacity factor target?

14 A I was relying on the opinion and order in  
15 Limerick Unit 2 as a benchmark.

16 Q And you simply take the same number as the  
17 Limerick 2 order?

18 A Yes. I look at that as a policy target.

19 MR. CLARK: Thank you, Your Honor.

20 JUDGE MATUSCHAK: Is there any other cross-examina-  
21 tion of this witness?

22 MS. BUSH: Yes, Your Honor.

23 CROSS-EXAMINATION

24 BY MS. BUSH:

25 Q Mr. Palast, I'm representing a local coalition

1 of ratepayers and I have a few questions for you. I think  
2 your responses to Mr. Clark answered some of my questions.

3 I wanted to focus on page 19 of your testimony,  
4 the first full answer there. You state there, "Generally,  
5 commissions consider rates too low which prevent a  
6 utility from raising capital. That is the lower limit below  
7 which rates are unreasonable."

8 I take it in making that statement you're not  
9 offering a legal opinion but your policy experience;  
10 is that correct?

11 A. I'm talking about my experience in regulation  
12 and my understanding of the matter regulatory policy.  
13 It's not a legal rendering and that statement should not  
14 be taken to mean to raise capital for any scheme, idea  
15 or plan that the utility can scheme up or dream of.

16 Q. And in making that statement you would not be  
17 considering what the financial consequences of a rate  
18 decision that had to do with measuring the used and useful  
19 nature of the plant that would be included in rates are?

20 A. No. If there is a finding that plant is neither  
21 used nor useful and this results in very severe negative  
22 financial consequences for the utility, as we had in the  
23 New Hampshire situation, then this basic standard would not  
24 apply. You would end up in a crisis financial situation.

25 MS. BUSH: That's all the questions I have. Thank you.

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

JUDGE MATUSCHAK: Any other cross-examination of this witness?

MR. MacGREGOR: Yes, Your Honor. I have just one or two follow-up questions from Mr. Clark's cross-examination.

JUDGE MATUSCHAK: Let's see if anybody else has cross-examination for the witness first. Is there anybody else?

(No audible response.)

JUDGE MATUSCHAK: Okay.

FURTHER CROSS-EXAMINATION

BY MR. MacGREGOR:

Q. Mr. Palast, you were asked certain questions by Mr. Clark of the Governor's Energy Council concerning a Limerick 1 write-off and also your proposal that the company guarantee the Limerick 1 energy savings; is that correct?

A. Yes.

Q. Would you agree with me that neither of those subjects are reflected in the financial data that you provided for us in your exhibits? The financial data in your exhibits assumes no Limerick 1 write-off and does not reflect the impact of an energy savings guarantee?

A. It reflects the impact of the fuel savings which the company says will exist. I take the company at its word that in fact that fuel savings will exist.

1 Q. But it does not reflect the application of a  
2 guarantee of those fuel savings?

3 A. Let me see if I understand your question. You're  
4 saying if the company has --

5 Q. If the company were required to guarantee fuel  
6 savings under your proposal and the Limerick Unit for  
7 whatever reason operated at less than 65 percent capacity  
8 factor during a particular year, for example because it was  
9 on a scheduled refueling outage, then that would affect the  
10 company's earnings if it were required to guarantee a 65  
11 percent capacity factor; and that possibility is not  
12 reflected in your financial exhibits?

13 A. Well, let's make this even more clear so that  
14 we will know exactly what is reflected and what isn't.  
15 For example, I discuss Exhibit GP-7 and I talk about the  
16 additional financing needs of the company. I am relying on a  
17 statement by Mr. Paquette that there will be \$211 million  
18 in fuel savings. If Mr. Paquette is incorrect or he believes  
19 that the company cannot actually produce that fuel savings  
20 then that number is wrong and my number would have to be  
21 changed accordingly.

22 Q. My question is this: it's not a question of being  
23 correct or incorrect. That number is an estimate, is it not,  
24 Mr. Palast?

25 A. Mr. Paquette's number is an estimate, I agree.

1 Q. And it could be high or low for any number of  
2 reasons in the future, reasons within and without the  
3 company's control?

4 A. It could be -- I'll accept the first part of  
5 the sentence, that it could be higher or lower.

6 Q. It could be higher or lower for a variety of  
7 reasons?

8 A. Yes.

9 Q. And if we apply your guarantee of energy savings  
10 proposal and if fuel savings are more or less than what is  
11 projected then the numbers in these financial statements  
12 would change because of the guarantee?

13 A. If the company is wrong and if the plant does  
14 not produce the fuel savings that it should produce --

15 Q. That it's estimated to produce.

16 A. Well, in my opinion should produce in order to  
17 be entered into the rates. If it does not provide that  
18 benefit then of course there will be some deterioration in  
19 the company's financial indicators, which usually happens  
20 in a commercial operation when you make a mistake.

21 Q. Based upon your extensive nuclear experience,  
22 Mr. Palast, would you agree with me that a nuclear unit  
23 normally achieves a 65 percent capacity factor during a year  
24 in which it has a scheduled refueling outage? Or do you know?

25 A. It may have a lower capacity factor whether it's

1 scheduled or not.

2 Q Is that answer to my question yes or no? Or  
3 do you know the answer?

4 A Yes. The answer is yes.

5 Q And the other part of my previous question to  
6 you was whether the financial figures set forth in your  
7 exhibits reflect any Limerick 1 write-off or disallowance  
8 for imprudency or excess capacity.

9 A They do not. That doesn't necessarily mean that  
10 they would all have to be adjusted thereby. Some cash flow  
11 would increase, some would decrease. There would be tax  
12 benefits from a write-off, there would be losses due to a  
13 write-off.

14 Q Is the answer to my question yes?

15 A The answer is yes.

16 MR. MacGREGOR: Thank you. That's all I have.

17 JUDGE MATUSCHAK: Mr. Rainey.

18 MR. RAINEY: Your Honor, may I have a minute?

19 (Pause.)

20 MR. RAINEY: Your Honor, I have just one question on  
21 redirect.

22 JUDGE MATUSCHAK: Very well.

23 REDIRECT EXAMINATION

24 BY MR. RAINEY:

25 Q Mr. Palast, earlier in his cross-examination

2033

1 Mr. MacGregor asked you about whether or not FASB 71's...  
2 exposure draft should be given any weight or whether it  
3 should be ignored. Would you tell us your opinion with  
4 respect to what weight the Commission should give to  
5 the exposure draft of FASB 71?

6 A. I would be pleased to.

7 The Commission should never ignore any type of  
8 document, pronouncement, by any other agency which might have  
9 an affect upon its renderings whether it's the Congress of  
10 the United States and potential changes in the tax law, which  
11 have not been discussed here, whether it is the NRC or this  
12 Financial Accounting Standards Board.

13 I'm very, very concerned, however, that such a  
14 weighty issue as the one we have before us in which the  
15 company's future hangs in the balance and the city's future  
16 hangs in the balance is determined by speculation about what  
17 a group of people untutored on this subject may decide in  
18 1987 about financial accounting and the reporting of what  
19 this Commission may do. I'm very concerned about an order  
20 based on such speculation.

21 We had the testimony of the company's auditor, Mr.  
22 Farling, who suggested that the order in effect be based on  
23 an early draft of a change in the statement, the AICPA issues  
24 paper. If we had followed that reasoning and the exposure  
25 draft had not been issued this Commission would have made some

1 very, very serious mistakes because the exposure draft is  
2 completely different from the issues paper.

3 I believe that the final decision of FASB may be  
4 far different from the exposure draft for many of the  
5 reasons I've stated, such as it was a four-to-three decision;  
6 these people are not expert in regulation, per se; they  
7 state that they have not received any comments from  
8 utilities that they would be substantially harmed by these  
9 changes -- and I can name a half a dozen states right off  
10 the bat that would have serious problems: Ohio, New Mexico,  
11 California, Arkansas, Louisiana, New York, Maine and possibly  
12 some other states. So I believe that they will hear from  
13 these utilities and that there will be some adjustments  
14 made.

15 In addition, I'm very, very concerned that this  
16 Commission does not defer to the accounting profession's --  
17 when I say "accounting profession's", the reporting accounting  
18 profession's ruling body as if it were a supreme court of  
19 regulation. It is not.

20 Rates still should be set in a reasonable manner  
21 which balances the interests of consumers and investors. I  
22 believe that if this Commission puts forward a reasonable  
23 statement and does in effect commit to paying the company  
24 out over a reasonable period of time then in fact the  
25 auditors can in good conscience book the deferred income

1 as current because it is a commitment from this Commission  
2 to in effect collect the sum.

3 It is this new idea that there is a cliff which the  
4 company falls off after ten years, very novel, which does  
5 not exist anywhere else in the accounting profession and it  
6 hasn't existed in previous drafts of the issue papers and I  
7 don't think it will survive the final wording. But ..  
8 ultimately this Commission must decide on its own what is  
9 the reasonable course of action in rate setting and not  
10 ignore what may be the ultimate statement but maintain a  
11 reasonable point of view, and I believe that they will find  
12 that the accountants for reporting purposes will then be  
13 able to make there determinations once they see that the  
14 Commission has acted reasonably.

15 Just one more comment on this question. Though I'm  
16 not necessarily in favor of writing an order in this manner  
17 other commissions -- for example, we had some lengthy  
18 discussion of the Mississippi order today. The Arkansas  
19 commission recently issued an order in which they said  
20 here is our order, we intend not to speculate about what  
21 FASB 71 may ultimately turn out to be in the future. We are  
22 going to do the correct thing by our ratepayers and have a  
23 phase-in period which goes far beyond ten years or any other  
24 limit. However, we will make note that this rule is in flux  
25 and in our order we are saying that we will reconsider our

1 order -- not change it to meet the new rule -- but we will  
2 reopen and reconsider our order if the rules is changed and  
3 if this creates a problem for the utility or any of the other  
4 parties in the case.

5 So this Commission has that option to say rather  
6 than anticipating what FASB will do to say that we recognize  
7 that the rule is in flux and that if need be we may adjust  
8 our ruling at a later date and reopen the hearings.

9 MR. RAINEY: No further questions, Your Honor.

10 JUDGE MATUSCHAK: That is a point that I was going  
11 to interrogate the witness on. I think that pretty well  
12 clarified it to my satisfaction.

13 Anything further?

14 MR. MacGREGOR: Yes, Your Honor.

15 RE-CROSS-EXAMINATION

16 BY MR. MacGREGOR:

17 Q. Mr. Palast, would you agree with me that FASB 71  
18 of course is not the only issue that should be considered in  
19 approving a phase-in plan? As you discuss in your testimony  
20 the financial impact of that plan over the course of the  
21 plan period is something that certainly should be considered  
22 as well?

23 A. Yes.

24 Q. And I believe you stated that the Financial  
25 Accounting Standards Board was untutored on this subject.

1 Can you please state for me the current members of the  
2 Financial Accounting Standards Board?

3 A. I can't name them off-hand. I looked at the  
4 listing.

5 Q. And have you studied their background,  
6 credentials and experience as a basis for your conclusion  
7 that they are untutored on this subject?

8 A. When I say untutored I mean that in a very  
9 specific and not in a perjorative sense. These are people  
10 who are specialists in reporting earnings. They should not  
11 be seen as a super regulatory body. They are not meant to  
12 be experts in the field of regulation.

13 They claim within the statement, within the notes  
14 attached to the exposure draft, that they spoke to repre-  
15 sentatives of a number of utilities who said that they would  
16 not be affected by these rule changes. They spoke at great  
17 length to the Edison Electric Institute. There is no  
18 indication that they spoke to this Commission or other  
19 regulators dealing with these problems, that they heard from  
20 consumer agencies or others who might be affected by the  
21 indirect effect of these reporting requirements, nor have  
22 they heard, apparently, from utilities that would have very  
23 serious problems if these rules were changed and applied  
24 retroactively.

25 With the possible exception of Dayton Power & Light,

1     though it's not recognized in the FASB 71 notes, I do note  
2     that they are very upset that it may overturn the compromise  
3     reached in Ohio.

4             But what I mean by untutored is that these are people  
5     who are expert in the field of financial reporting and they  
6     are well known experts in that field. But they are not  
7     experts -- they are seeking expertise from sources in the  
8     area of regulation.

9             I hope that this Commission participates in the  
10    hearings that they have. And first and foremost this  
11    Commission should take a look at its own requirements to set  
12    rates in a reasonable manner.

13            Q.    So your conclusion as to their background is not  
14    based on any examination of their credentials or backgrounds  
15    or former experience, I take it, since you can't tell me who  
16    is on the board?

17            A.    It's based on their statements of how they went  
18    about -- when I say "they", the members of the board. They  
19    have a statement that's included with the exposure draft  
20    explaining --

21            Q.    I'm asking you whether you examined their  
22    credentials.

23            A.    Okay. That's what I looked at, their credentials  
24    for examining a regulatory matter.

25            Q.    Did you examine the credentials of the members of

2041

1 the Financial Accounting Standards Board, specifically,  
2 each individual member on the board, and can you tell me  
3 what their backgrounds are, where they worked outside of  
4 the board --

5 A. I haven't read their resumes, no.

6 Q. You have not even examined their resumes at all?

7 A. No, sir.

8 MR. MacGREGOR: Thank you. That's all I have.

9 JUDGE MATUSCHAK: What is the nature of the  
10 exposure draft? Is that in the nature of a preliminary  
11 draft subject to comments or input from other people before  
12 a final draft.

13 THE WITNESS: This is an extra copy of the exposure  
14 draft. They intend to hold hearings on June 4 through 6  
15 at Stamford, Connecticut, a period of public commentary.  
16 The Wall Street Journal has talked to people who have said  
17 they don't expect a ruling until '87. There is a great deal  
18 of consternation about the rule. I don't know how it will come out.

19 In other words, it's a draft of a change of a rule.  
20 What has been discussed earlier by Mr. Farling and myself  
21 is a previous draft which was known as the AICPA issues  
22 paper.

23 JUDGE MATUSCHAK: Ms. Chestnut.

24 MS. CHESTNUT: Your Honor, I think Mr. Palast has  
25 pretty much answered my question, but I just want to really

1 nail it down for sure here.

2 RE-CROSS-EXAMINATION

3 BY MS. CHESTNUT:

4 Q Mr. Palast, in your opinion is it likely that  
5 a final version of FASB 71 will be made effective prior to  
6 or on June 27, 1986?

7 A Given that public hearings will just be held on  
8 June 4 and that this is a very controversial change, in order  
9 for them to issue a ruling they would have to do so virtually  
10 immediately upon conclusion of these hearings. I assume that  
11 that would be impossible.

12 MS. CHESTNUT: Thank you.

13 JUDGE MATUSCHAK: Any final draft that they make is  
14 not necessarily binding on this Commission in what they do  
15 and on the manner in which they set their rates?

16 THE WITNESS: No. I appreciate you're asking me  
17 that because in all of our discussions we forget the most  
18 important thing: that body has no authority over what this  
19 Commission does. This Commission may do whatever it believes  
20 it must do in setting reasonable rates.

21 The only thing that body does is to tell the auditors  
22 how they will report it. And as I said before, there is an  
23 efficient market. Investors are not foolish. They know  
24 what revenues are current. They know what revenues are  
25 deferred. They will know what the deferral period is. If

1 you call all the revenue current they will certainly know  
2 that it's not all current no matter how it's reported. If  
3 you call none of the deferred revenue current they are not  
4 going to believe that that money will never come. They  
5 have a commitment from this Commission and they will  
6 evaluate it accordingly.

7 So from the investors' point of view it's simply  
8 whether the Commission's deferred revenue granted is in  
9 the income statement or the footnotes to the income state-  
10 ment; and that is what this issue is about and it has no  
11 binding effect on what the Commission itself determines  
12 what is proper and reasonable and should order PECO to do.

13 JUDGE MATUSCHAK: I think that in one of the other  
14 rates cases that we participated in it was suggested that  
15 some deviation be made in the reporting thing or that the  
16 reporting be done in a certain way but that there be a  
17 footnote explaining the actual effect.

18 THE WITNESS: They would have to explain. I'm sure  
19 that there will be a footnote either way. So it's a question  
20 of whether the deferred revenue goes up into the line that  
21 says current revenue for the year or goes into the footnote,  
22 or the proportion of the deferred revenue is in the footnote  
23 or is in the statement itself. That is really the discussion  
24 as to the reporting.

25 It's all going to be reported. Investors will know

1 exactly what's happening one way or the other. And this  
2 Commission is not bound in its decision anyway.

3 JUDGE MATUSCHAK: However, this Commission should  
4 take cognizance of the matter and consider that and whatever  
5 effect it may have on the company's financial reporting  
6 system and financial ability to effect a credit rating and  
7 so forth.

8 THE WITNESS: Also, it should be understood that  
9 credit agencies, as we have heard from the company's own  
10 witnesses from the rating agencies, these are not foolish  
11 people. They are not slaves to numbers. And, for example,  
12 this company has for many years had a higher rating than  
13 its financial indicators deserved. Now it has ratings which  
14 are below what some of its indicators say it deserves. That's  
15 because the agencies understand and take a general look at a  
16 company and they aren't simply slaves to a particular ratio  
17 or number. If there is an accounting change which happens  
18 to affect an indicator they are aware of what that means.  
19 If the company has cash flow promised in the future and  
20 they feel secure about it -- a commitment from this Commission  
21 is good security in my opinion and makes it a probability --  
22 the rating agencies will certainly take that into account  
23 and they will simply not dismiss revenue, say that revenue  
24 has suddenly gone out the window just because this year they  
25 can't report it due to a new technical change in financing.

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

People know what this company will make. The cash flow is coming in as promised and the reporting is really secondary to how the investment community will rate this company.

JUDGE MATUSCHAK: Do you have anything further?

MR. RAINEY: Nothing further, Your Honor.

JUDGE MATUSCHAK: Any further cross-examination of this witness?

MR. MacGREGOR: No, Your Honor.

JUDGE MATUSCHAK: Thank you.

(Witness excused.)

JUDGE MATUSCHAK: I imagine that this is an appropriate time to take a recess for lunch.

MR. CALVERT: Your Honor, if I might suggest, Mr. Rainey and I want to have a sidebar conference concerning Dr. Shinnar's testimony and some problems we are having in scheduling with Dr. Shinnar. Would it be possible perhaps for us to take a very brief recess now and let Mr. Rainey and I have a chance to talk -- because of the witness he wasn't able to -- and then perhaps report back to Your Honor to see if we have to argue the point or if we can indicate some sort of agreement?

It would prevent me -- I'm not going to have to be here this afternoon. It would prevent me from having to come back this afternoon. I'm happy to do it at Your Honor's

1 convenience.

2 MR. RAINEY: Your Honor, if I might, I really don't  
3 think there is much to argue at this particular point. I've  
4 submitted to the parties present and Your Honor a letter  
5 stating what our position on the availability of Dr.  
6 Shinnar is and to the extent that there is a significant  
7 deviation from that then we would have to argue that.

8 JUDGE MATUSCHAK: Well, we will take a short recess  
9 so Counsel does not have to come back. For any of the others  
10 who do not wish to remain, we won't come in before 1:30.  
11 We will hold this session in abeyance until we formally  
12 adjourn. Parties not interested in this phase, if they wish,  
13 may leave. We will not reconvene before 1:30.

14 (Recess.)  
15  
16  
17  
18  
19  
20  
21  
22  
23  
24  
25

1 JUDGE MATUSCHAK: Back on the record.

2 MR. CALVERT: Your Honor, we have been having some  
3 continuing discussions with the City's lawyers with respect  
4 to the scheduling of both obtaining information from and  
5 the cross-examination of and rebuttal testimony in relation-  
6 ship to Dr. Schinnar's testimony in this case.

7 You will recall that last Wednesday, a week ago this  
8 past Wednesday, we appeared before Your Honor and we  
9 attempted to work out something of an agreement.

10 Some additional problems have arisen, and I won't  
11 at this point argue the case to Your Honor; I am hoping to  
12 avoid that.

13 What I believe we have agreed to at this stage is  
14 that the company's experts on modeling and relating to  
15 Dr. Schinnar's model are going to meet with Dr. Schinnar  
16 at the University of Pennsylvania on Monday, the 10th of  
17 February, and on Tuesday, the 11th of February, to the  
18 extent that a continued meeting is necessary, and take  
19 whatever time is necessary on those days to work with  
20 Dr. Schinnar and find out the substance of his model, the  
21 underlying data, the code, the parameters of the model,  
22 the various pieces of information that a technical expert  
23 would need to both understand the model, to validate the  
24 model and hopefully to test the model and to test variances  
25 to see how sensitive the model is to various different

1 parameters and different data inputs.

2 In order to do that, I think that the lawyers don't  
3 have to be involved with those sessions, and I believe that  
4 Ms. Foa will speak to this. But I think we have agreed that  
5 we won't be there. We will let the technical people talk.

6 Our experts tell us that it may be important for  
7 them to have a user number and have access to themselves to  
8 be able to use the model.

9 Unlike many of the models, analyses, that have been  
10 utilized by the various parties in this case, the company  
11 included, this is not on a floppy disk; I believe it is on  
12 tape, and a lot of the information is contained in the  
13 University's main frame or main computer, so that one has  
14 to have access to that. It is not a matter of going out  
15 and rebuilding this model on your own system, as most of the  
16 experts have been able to do, and then playing around with  
17 the data. We need access to that computer and that  
18 facility.

19 I believe Ms. Foa has agreed that we can do that,  
20 but it may require some additional time even beyond Tues-  
21 day for us to, in essence, test the model.

22 Dr. Schinnar may very well not have to be there at  
23 that point. Once we learn how to use the model, then it is  
24 just a matter of testing.

25 My concern is that he is presently scheduled to be

1 cross-examined on Thursday, the 13th of February, and re-  
2 buttal testimony on all of the Limerick issues, of which  
3 Dr. Schinnar would fall within, is due on February 19, which  
4 I believe is the next Wednesday.

5 We are going to try, through the system I have just  
6 described, to see if we can gather enough information and  
7 enough understanding of the model, to proceed on that  
8 schedule.

9 I think it is important, however, to alert Your  
10 Honor to the fact that we may have to come back on Wednesday,  
11 the 12th of February, and say that either there are techni-  
12 cal problems or there are factual problems and we simply  
13 don't have the information needed to go forward on that  
14 schedule with Dr. Schinnar.

15 I am not making that request at this time, but I  
16 don't want to come in at the last minute and have Your  
17 Honor say, "Well, gee, this is a last minute thing," be-  
18 cause I am trying to keep the Court advised as we progress  
19 with the progress we're making.

20 MS. FOA: Your Honor, if I may; Pamela Foa. I am a  
21 Divisional Deputy City Solicitor for the City of  
22 Philadelphia.

23 The company has requested that certain underlying  
24 data, underlying the technical report and underlying the  
25 testimony and model be generated. That process has begun

j4

1 and will be completed on Monday, and they will have that  
2 data available.

3 They have also asked that they be permitted to test  
4 the model. I am told by Jerry that this involves user  
5 numbers and the like. I don't know what this involves, but  
6 there should be no problem; they will be permitted to test  
7 the model.

8 I am also told that this is a model which is easily  
9 run, and the learning process will take a very short time,  
10 and so we will expect that Monday and, if necessary, Tues-  
11 day, will be more than sufficient for their experts to  
12 gain the familiarity they wish or to run the test they wish  
13 with the model.

14 We now anticipate that there should be no problem  
15 with going ahead with the examination as it is presently  
16 scheduled.

17 My understanding is that we have an agreement to  
18 meet on Monday and, if necessary, on Tuesday; and really,  
19 all that Mr. Calvert is doing here is preserving a right  
20 we all understand he has to come back at any point and  
21 raise new problems or questions about the schedule.

22 JUDGE MATUSCHAK: What does it look like for  
23 Dr. Schinnar to be cross-examined on Thursday? Will you be  
24 prepared in any event to cross-examine Dr. Schinnar on  
25 Thursday?

j5

1 MR. CALVERT: No, Your Honor. Without having the  
2 information that we hope to obtain on Monday and Tuesday,  
3 the answer is no, we won't be prepared.

4 In order to cross-examine him about his model, we  
5 have to know the model and understand it and so on.

6 But assuming we obtain the information, assuming  
7 there aren't any glitches in the system that we have just  
8 described to Your Honor, yes, I should be prepared. I  
9 anticipate being prepared on Thursday. That is why at  
10 this point we are not asking for --

11 JUDGE MATUSCHAK: Very well.

12 MS. FOA: May I just raise one other question? I  
13 understand that you don't wish to attend. I don't think  
14 the City has made a final decision about whether or not it  
15 would like its lawyers present. We would be there just to  
16 generally oversee and to help with any problems that arose.

17 But I take it you are not filing any objection to  
18 our being there?

19 MR. CALVERT: No, I'm not filing any objection.  
20 Again, time is extremely compressed, extremely short. I  
21 happen to know that the more lawyers that are involved, the  
22 less that seems to get done, particularly where experts are  
23 involved, who, with all the other parties, have done a very  
24 good job of talking back and forth.

25 If you're going to have lawyers there, unfortunately,

1 I'll have to have somebody there, and it tends to escalate.

2 I would like to have the lawyers out of it and let  
3 the experts talk and then report back to us.

4 JUDGE MATUSCHAK: If she is going to be there, or  
5 some representative from the City, then I suggest that you  
6 have someone there so there can't be any misunderstandings.

7 MR. RAINEY: Your Honor, if I may add something.  
8 It is also my understanding that we will be putting  
9 together a protective order to protect any information  
10 which Dr. Schinnar feels is proprietary from being taken  
11 out of the University of Pennsylvania.

12 We will prepare that and have that signed and sub-  
13 mit that to Your Honor and to all parties of record in  
14 this particular case.

15 JUDGE MATUSCHAK: Very well.

16 MR. CALVERT: Your Honor, we have no problem with  
17 that. There is a standard protective order which all the  
18 parties have signed, which I suspect will cover this situa-  
19 tion, too. But we are, obviously, willing to sign whatever  
20 protective order is appropriate.

21 MR. RAINEY: Your Honor, if I might also add that  
22 we have presently -- Dr. Schinnar has presently answered  
23 five sets of interrogatories. There are Set 6 interroga-  
24 tories which are currently outstanding.

25 In order to meet the company's needs of making

j7°

1 Dr. Schinnar available, we may not be able to complete those  
 2 interrogatories by Tuesday when they are due. We would  
 3 like that to be taken into consideration.

4 We would hope that all concerns with regard to those  
 5 interrogatories might be resolved at the meeting itself;  
 6 and so we would want that understanding as well, so that  
 7 the company doesn't come back to you on Wednesday and say,  
 8 "Well, we met with Dr. Schinnar, but because he hasn't  
 9 provided the answer to Set 6 interrogatories, we are not  
 10 prepared."

11 They do have, as I said, the five sets of interroga-  
 12 tories that have been responded to, so that they can form  
 13 some bases now for cross-examination of Dr. Schinnar.

14 JUDGE MATUSCHAK: If there are some loose ends, we  
 15 can pick those up.

16 MR. RAINEY: Thank you very much, Your Honor.

17 JUDGE MATUSCHAK: Very well. We expect counsel to  
 18 cooperate with each other to the end so that everybody has  
 19 an opportunity to present their positions adequately in  
 20 this matter.

21 MR. CALVERT: Thank you, Your Honor.

22 JUDGE MATUSCHAK: We will now recess until 1:45.

23 (Whereupon, at 12:45 p.m., the hearing was adjourned,  
 24 to be reconvened at 1:45 p.m., this same day.)

25

j8

AFTERNOON SESSION

(1:45 p.m.)

1 JUDGE MATUSCHAK: On the record.

2 Mr. Wersan.

3 MR. WERSAN: Thank you, Your Honor.

4 At this time I would like to mark for identifica-  
5 tion and move into evidence OCA Statement No. 7, which is  
6 the direct testimony of Thomas E. Knudsen on behalf of the  
7 Office of Consumer Advocate.

8 It is my understanding that there is no cross-  
9 examination for Mr. Knudsen, and the company is willing to  
10 stipulate that OCA Statement No. 7 is a true and accurate  
11 document, and that there are no changes.

12 MR. HALL: Your Honor, I think I would phrase it a  
13 little differently.

14 MR. WERSAN: I'm sorry. I didn't mean to misrepre-  
15 sent your position, Mr. Hall.

16 MR. HALL: Your Honor, the company has reviewed  
17 Mr. Knudsen's statement and in its opinion that statement  
18 generally reflects adjustments and proposals made in other  
19 Consumer Advocate testimony.

20 The company will be cross-examining those technical  
21 witnesses extensively and, therefore, sees no reason to  
22 cross-examine Mr. Knudsen.

23 We do stipulate that the document is prepared by  
24  
25

j9

1 Mr. Knudsen and that in his judgment it contains true and  
2 accurate information.

3 JUDGE MATUSCHAK: Is he here?

4 MR. WERSAN: He is here, Your Honor.

5 JUDGE MATUSCHAK: First offer your statement, iden-  
6 tify your statement, and then we will put him on temporarily  
7 to have him identify it.

8 Whereupon,

9 THOMAS E. KNUDSEN

10 having been duly sworn, testified as follows:

11 DIRECT EXAMINATION

12 BY MR. WERSAN:

13 Q Will you please state your name?

14 A Thomas E. Knudsen.

15 MR. WERSAN: Your Honor, I would like to identify  
16 for the record, as OCA Statement No. 7, the direct testi-  
17 mony of Thomas E. Knudsen.

18 JUDGE MATUSCHAK: Very well.

19 (Whereupon, the document was marked  
20 as OCA Statement No. 7 for  
identification.)

21 BY MR. WERSAN:

22 Q Mr. Knudsen, do you have this document before  
23 you?

24 A I do.

25 Q Was this document prepared by you or under your

j10

1 supervision?

2 A. It was.

3 Q. Do you have any changes or corrections at this  
4 time?

5 A. There are no changes.

6 Q. If I were to ask you the questions contained in  
7 OCA Statement No. 7, would your answers be the same as  
8 they are?

9 A. Yes.

10 Q. Would those answers be true and accurate to the  
11 best of your knowledge, information and belief?

12 A. Yes.

13 MR. WERSAN: Your Honor, I would like to move into  
14 evidence OCA Statement No. 7.

15 JUDGE MATUSCHAK: Statement No. 7 is admitted into  
16 evidence, subject to any timely objections or exceptions  
17 that may be filed.

18 (Whereupon, the document marked as  
19 OCA Statement No. 7 was received  
in evidence.)

20 MR. WERSAN: Your Honor, the only other thing I  
21 would like to say is that Mr. Knudsen's testimony presents  
22 the OCA's rationale in the adjustments that we are making.

23 The technical witnesses present the basis for those  
24 adjustments in terms of the quantification, et cetera.

25 I would not want it to be reviewed as if

jll

1 Mr. Knudsen simply adds those up; he provides the rationale  
2 on behalf of the Consumer Advocate's Office.

3 MR. HALL: Your Honor, as I indicated, the company  
4 does not feel the need to cross-examine Mr. Knudsen. We  
5 believe the statement rests on other Consumer Advocate  
6 witness statements that we will be cross-examining fully,  
7 and that rebuttal evidence will be sufficient to address  
8 the matters which Mr. Knudsen discusses.

9 JUDGE MATUSCHAK: Does any other party wish to  
10 cross-examine Mr. Knudsen?

11 (No response.)

12 JUDGE MATUSCHAK: Very well; the witness is excused.

13 (Witness excused.)

14 JUDGE MATUSCHAK: Ms. Chestnut.

15 MS. CHESTNUT: Thank you, Your Honor.

16 Staff would like to call as its next witness,  
17 Mr. Dennis P. Dougherty.

18 Whereupon,

19 DENNIS P. DOUGHERTY

20 having been duly sworn, testified as follows:

21 DIRECT EXAMINATION

22 BY MS. CHESTNUT:

23 Q. Good afternoon, Mr. Dougherty.

24 A. Good afternoon.

25 Q. Mr. Dougherty, would you please state your name

j12

1 and business address for the record?

2 A. Dennis P. Dougherty. My business address is  
3 P.O. Box 3265, Harrisburg, Pennsylvania, 17120.

4 Q. By whom are you employed, and in what capacity?

5 A. I am employed as an Audit Supervisor by the  
6 Pennsylvania Public Utility Commission, Bureau of Audits.

7 Q. Mr. Dougherty, have you prepared direct testi-  
8 mony for use in this proceeding?

9 A. Yes, I have.

10 MS. CHESTNUT: Your Honor, I have distributed  
11 copies of Mr. Dougherty's prepared direct testimony to  
12 Your Honor, to the parties and to the court reporter.

13 I request that the statement be marked for identifi-  
14 cation as Staff Statement DPD-1.

15 JUDGE MATUSCHAK: It will be so marked.

16 MS. CHESTNUT: I would like to note also for the  
17 record that Staff Statement DPD-1 also contains Exhibits  
18 DPD-1 through 30.

19 JUDGE MATUSCHAK: Very well.

20 (Whereupon, the documents were  
21 marked as Staff Statement No. DPD-1  
22 and Staff Exhibits Nos. DPD-1  
through DPD-30 for identification.)

23 BY MS. CHESTNUT:

24 Q. Mr. Dougherty, do you have before you what has  
25 been marked for identification as Staff Statement DPD-1?

1 A. Yes, I do.

2 Q. Does this document represent your direct  
3 testimony?

4 A. Yes, it does.

5 Q. Do you have any additions, changes or corrections  
6 to make to this document at this time?

7 A. Yes. There is a correction that I would like  
8 to make. It is in reference to a Commission Order.

9 The first reference to such Order is on page 2,  
10 line 4. The docket number indicated in the direct testi-  
11 mony is "I-8010034." The correct docket number is "I-80100341."

12 That same correction has to be made also on page 3,  
13 lines 18 and 24, and page 4, line number 3.

14 Q. Mr. Dougherty, with the correction you have  
15 noted, is the information contained in Staff Statement No.  
16 DPD-1 true and correct to the best of your knowledge,  
17 information and belief?

18 A. Yes, it is.

19 Q. If I were to ask you today the questions con-  
20 tained in Staff Statement No. DPD-1, would your answers be  
21 the same as they are therein?

22 A. Yes, they would.

23 MS. CHESTNUT: Your Honor, I request the admission  
24 into evidence, subject to any timely motions to strike or  
25 other objections, of Staff Statement No. DPD-1.

1 JUDGE MATUSCHAK: Under those conditions, the motion  
2 is granted.

3 (Whereupon, the documents marked as  
4 Staff Statement No. DPD-1 and Staff  
5 Exhibits Nos. DPD-1 through DPD-30  
6 were received in evidence.)

7 MS. CHESTNUT: Your Honor, Mr. Dougherty is avail-  
8 able for cross-examination.

9 JUDGE MATUSCHAK: PECO.

10 MR. HALL: Thank you, Your Honor.

11 Your Honor, I have a brief exhibit that I will be  
12 using during my cross-examination of Mr. Dougherty.

13 I would ask that Mr. McGrail distribute the exhibit  
14 at this time.

15 CROSS-EXAMINATION

16 BY MR. HALL:

17 Q Good afternoon, Mr. Dougherty.

18 A Good afternoon, Mr. Hall.

19 Q Mr. Dougherty, turning your attention to what  
20 I have identified on its cover as PECO Exhibit No. 4, would  
21 you agree with me that this exhibit contains several  
22 interrogatory answers which you provided in response to  
23 our interrogatory requests?

24 A I would like to take a moment, please, to look  
25 at that Exhibit No. 4.

(Pause.)

A Yes; that is correct.

j15

1 Q Mr. Dougherty, is the data provided in this  
2 exhibit true and correct to the best of your knowledge  
3 and belief?

4 A Yes, it is.

5 MR. HALL: Your Honor, I would ask that PECO  
6 Exhibit 4 be identified for the record as PECO Exhibit 4,  
7 and be admitted into the record for purposes of use in  
8 cross-examination, and also for general purposes in the  
9 proceeding.

10 JUDGE MATUSCHAK: It can be so identified. Do you  
11 want to offer it now also?

12 MR. HALL: I believe I might as well, Your Honor.

13 JUDGE MATUSCHAK: Any objections?

14 MS. CHESTNUT: I will not raise an objection at  
15 this point, Your Honor, subject to if I later deem its  
16 use inappropriate in Mr. Hall's cross.

17 JUDGE MATUSCHAK: Well, it is Staff's product.

18 MS. CHESTNUT: I have no objection to our inter-  
19 rogatory being made part of the record, Your Honor. I just  
20 don't know what purpose Mr. Hall intends to use it for,  
21 and that would be the reason why I would hesitate to agree  
22 to let it in.

23 JUDGE MATUSCHAK: Very well. PECO Exhibit 4 is  
24 admitted into evidence, subject to any objections. We will  
25 take care of the objections if you have them later on.

1 (Whereupon, the document was marked  
2 as PECO Exhibit No. 4 for identi-  
3 fication, and was received in  
4 evidence.)

5 BY MR. HALL:

6 Q Mr. Dougherty, before getting into the substance  
7 of your testimony, I would like to take a minute to look at  
8 your educational and work experience background.

9 Referring you to Appendix A to your testimony, is  
10 it in fact true that your educational background has been  
11 in accounting where you have a Bachelor of Science Degree  
12 from York College of Pennsylvania?

13 A That is true, Mr. Hall.

14 Q Is it also true that your work experience has  
15 been entirely with the Pennsylvania Public Utility  
16 Commission in the Audit Bureau of that Commission?

17 A That is also true.

18 Q Would I be correct, looking at the bottom of  
19 Appendix A, that the major cases and activities upon which  
20 you have worked while at the Commission are referenced in  
21 the ten items set forth therein?

22 A That is true.

23 Q In your prior experience working with the  
24 Commission, Mr. Dougherty, have you ever had occasion to  
25 work on a matter involving a nuclear power plant construc-  
tion project?

j17

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

A. Yes, I have.

Q. When and where was that?

A. That was approximately three years ago, Mr. Hall, out at Duquesne Light's Beaver Valley Nuclear Power Plant.

Q. What did you do at that time?

A. It was in conjunction with a CPR or a continuing property record audit. We were reviewing certain plant additions located at that facility.

Q. Was this in connection with Beaver Valley Unit 1?

A. I believe most of the plant additions that we were reviewing were applicable to the common facilities.

Q. Common facilities between Beaver Valley 1 and 2?

A. That's correct.

Q. Is it not correct that those units are separated by a substantial period in terms of their completion dates?

A. Beaver Valley Unit No. 1 is on line now; Unit 2 has not come on line yet.

Q. And it was on line, was it not, in 1976?

A. Beaver Valley Unit 1?

Q. Yes.

A. I believe it was 1976.

Q. What were the nature of the common facilities that you reviewed during that audit?

A. It was primarily the emergency response facility.

Q. Limited to that one facility?

j18

1 A. Yes.

2 Q. Was the purpose of your audit to determine the  
3 total costs as shown on the utility's records for that  
4 facility?

5 A. The purpose of our review was to verify the  
6 accuracy of the costs recorded on the company's books.

7 Q. And that particular project, I take it, did not  
8 result in any testimony in any proceeding before the  
9 Commission?

10 A. No, it did not.

11 Q. And at no other time have you had experience,  
12 while working with the Commission or in any other capacity,  
13 in reviewing costs for construction of a nuclear power  
14 plant facility; is that correct?

15 A. That is correct. I believe I indicated in my  
16 pre-filed direct testimony that I do not believe such prior  
17 experience is necessary to perform the quantifications  
18 associated with Limerick Unit No. 1 not meeting the April  
19 1981 in-service date.

20 Q. I take it, just to continue this one step fur-  
21 ther, Mr. Dougherty, that you have no experience as an  
22 engineer or a construction manager or supervisor or  
23 scheduler relating to the construction of nuclear or other  
24 power plant facilities?

25 A. That is correct, Mr. Hall.

j19

1 Q Now, turning to the substance of your testimony,  
2 Mr. Dougherty, am I correct that your purpose in conducting  
3 the analysis that you conducted was to attempt to assign  
4 a dollar cost to the fact that Limerick 1 and common plant  
5 was not completed in April 1981, but rather was completed  
6 in February 1986?

7 A The quantification of the costs associated with  
8 Limerick Unit No. 1 not meeting the April 1981 in-service  
9 date consisted of comparing the project-to-date costs as of  
10 April 1981 with those costs as of October 1984.

11 Q Mr. Dougherty, my question, I think, was a little  
12 more limited than your answer.

13 My question is: the sole purpose, the entire pur-  
14 pose of your analysis here, as I think you clearly state  
15 in your testimony, is to develop a cost quantification for  
16 the event that I described?

17 A Yes. The purpose of the testimony is to assign  
18 a cost associated with the unit and the common facility not  
19 meeting the April 1981 in-service date.

20 Q You have made, in the testimony, no evaluation  
21 of whether or not the unit in fact could have met that  
22 April 1981 date; is that not correct?

23 A That's correct, Mr. Hall. I am of the opinion  
24 that the Commission already made that determination -- I'm  
25 sorry; that is correct.

1 Q Is it not true, Mr. Dougherty, that at page 3  
2 of your testimony you explicitly eschew any purpose of  
3 making such an analysis or determination and state that you  
4 are not qualified to do so?

5 A That's correct.

6 Q Now, Mr. Dougherty, would I be correct that you  
7 did not participate in any capacity in the first Limerick  
8 investigation at Docket No. I-80100341?

9 A That's correct.

10 Q Is your statement with respect to the meaning  
11 of the Commission's Order at that docket, with regard to  
12 its conclusions respecting the company's 1976 and 1978  
13 deferral announcements, merely a recitation by you of the  
14 position of Trial Staff as developed by counsel for Trial  
15 Staff in this proceeding?

16 MS. CHESTNUT: Objection, Your Honor. I think that  
17 is an improper question.

18 MR. HALL: I think it is a fair question, Your Honor.  
19 If he is simply relying upon his counsel's --

20 JUDGE MATUSCHAK: This is cross-examination. We  
21 will overrule the objection.

22 THE WITNESS: Could you repeat that question,  
23 Mr. Hall?

24 MR. HALL: Could I ask the reporter to read it back?  
25

1 (Whereupon, the reporter read from the record, as  
2 requested.)

3 THE WITNESS: No, it is definitely not. I think  
4 the Order speaks for itself.

5 BY MR. HALL:

6 Q So, in essence, Mr. Dougherty, you are relying  
7 on the statements you make in your testimony with respect  
8 to that Order upon solely your own reading of that Order?

9 A Yes; and, as I said, I think the Order speaks  
10 for itself and is quite clear.

11 Q Mr. Dougherty, as we have discussed, you are  
12 an accountant and auditor for the Commission; is that not  
13 correct?

14 A That is correct.

15 Q Would you agree with me, sir, that those back-  
16 ground credentials do not provide you with any greater  
17 knowledge or expertise respecting the interpretation of  
18 Commission Orders than others; for example, lawyers or  
19 others in this room?

20 A That's correct.

21 Q And would I be correct, Mr. Dougherty, that you  
22 were not, at the time of the Docket No. I-80100341 pro-  
23 ceeding or at the time of the development and issuance of  
24 the Commission's Order in that proceeding, a member of any  
25 Commissioner's Staff or a participant in the drafting of

1 that Order?

2 A. Since 1976, I have been an employee of the  
3 Bureau of Audits.

4 Q The answer to my question, I take it, is yes,  
5 you were not -- or no, as the case may be; I forget how I  
6 phrased it. You were not a member of --

7 A. That's correct, Mr. Hall.

8 Q Referring to the Commission's Order,  
9 Mr. Dougherty, is it not true that the Commission dis-  
10 cusses the 1976 and 1978 deferral announcements made by  
11 the company at pages 13 to 17 of its Docket No. I-80100341  
12 Order?

13 A. I have a copy of that Order, if you will bear  
14 with me for a moment, please.

15 Pages 13 to 17, Mr. Hall?

16 Q Yes.

17 (Pause.)

18 A. Yes; page 17 of the Order specifically states  
19 that "The Commission is of the opinion that PECO management  
20 did not exercise judgment sufficient to meet a reasonable  
21 man's standard in delaying construction at Limerick in  
22 1976 and 1978."

23 Q I take it, Mr. Dougherty, from your quotation  
24 of that passage, that it is during this section of the  
25 Order, i.e., pages 13 to 17, and particularly the

that you rely upon as being the alleged  
commission upon which you base your

with page 11, I believe it is,

without those delays, the in-service

which indicates that  
date would have been April 1981.

Well, now, Mr. Dougherty, referring back to  
pages 13 to 17, you will agree with me, sir, will you not,  
at no place in those pages does the Commission men-  
tion an April 1981 completion date for the Limerick  
facility?

A. I just indicated, Mr. Hall, --

Q. Mr. Dougherty, I asked the question, and the  
question asked very clearly, pages 13 to 17. We will get  
to page 11 in a minute.

A. You are correct, Mr. Hall.

Q. At page 11, which you have referenced,  
Mr. Dougherty, I take it you are referring to a paragraph  
in the middle of that page which merely states that, "In  
1976, to match growth in capacity additions with a lower  
spring 1976 load forecast, PECO further delayed construc-  
tion and revised the in-service dates for the Limerick  
Units Nos. 1 and 2 from April '81, April '82 to April '83,  
April '85, respectively," is that correct?

A. That's correct.

1 Q And that is the only reference, I take it, in the  
2 Commission's Order upon which you rely as to where in  
3 April 1981, the possible completion date for Limerick is  
4 mentioned?

5 A That's correct.

6 Q Mr. Dougherty, would you agree with me that at  
7 page 11, and also throughout pages 10, 11 and 12, in  
8 discussing the construction deferral announcements made by  
9 the company, the Commission is merely setting forth factual  
10 statements and discussing the testimony that is provided  
11 by the company, the Consumer Advocate or the Staff? It is  
12 simply a factual recitation, is it not?

13 A As opposed to what, Mr. Hall?

14 Q As opposed to a statement of what are perceived  
15 to be the Commission's conclusions, a statement of  
16 conclusions.

17 A No, I would not agree with that. I think it is  
18 clear on page 17 that the Commission is expressing an  
19 opinion.

20 Q I'm not referring to page 17; I am referring to  
21 pages 9 through 12, and over to the top of page 13. And my  
22 contention is that those pages merely state the positions  
23 of the parties and the witnesses before the Commission and  
24 recite background factual detail respecting the case; is  
25 that not correct?

j25

1 A. Yes; that appears to be correct.

2 Q. Is it not correct that the Commission states its  
3 conclusions and its opinions at pages 13 to 17?

4 A. It appears like page 13 starts with the  
5 Commission's conclusions or opinions. It also appears  
6 like they continue past page 17.

7 Q. But I am only asking with regard to the 1976  
8 and 1978 deferral announcement issue. That is the part of  
9 the Order, is it not, the only part of the Order, at which  
10 the Commission states conclusions and opinions?

11 A. That is correct.

12 Q. As we have previously established, there is no  
13 statement in that section, is there, with respect to an  
14 April 1981 completion date for Limerick 1?

15 A. That is correct. The April 1981 date, as I  
16 understand it, was obtained through Forecast No. 1.

17 Q. Mr. Dougherty, if you know, is it not correct  
18 that no nuclear power plant which received its construc-  
19 tion permit and began construction in 1974 achieved a  
20 commercial operation date by April 1981?

21 MS. CHESTNUT: Objection, Your Honor; outside the  
22 scope of his testimony.

23 MR. HALL: I think it challenges his testimony and  
24 his credibility; it is very relevant.

25 MS. CHESTNUT: Your Honor, he specifically made no

1 determination as to when the plant should have been  
2 completed.

3 JUDGE MATUSCHAK: We will overrule the objection.

4 THE WITNESS: Could you repeat the question, please,  
5 Mr. Hall?

6 MR. HALL: Could the reporter read it back, please?

7 (Whereupon, the reporter read from the record, as  
8 requested.)

9 THE WITNESS: I don't know, Mr. Hall, nor do I  
10 think it is relevant or important that I needed to know in  
11 order to form the quantification of the construction  
12 delays.

13 BY MR. HALL:

14 Q I take it you would also not know,  
15 Mr. Dougherty, when the first BWR nuclear power plant to  
16 be completed, which had been begun at the same time as  
17 Limerick was -- you would not know that fact either?

18 MS. CHESTNUT: The same objection, Your Honor. It  
19 is clearly outside the scope of Mr. Dougherty's testimony.

20 JUDGE MATUSCHAK: Overruled.

21 THE WITNESS: Again, no, I don't, nor do I think it  
22 was important.

23 BY MR. HALL:

24 Q Mr. Dougherty, turning to the quantification  
25 methodology which you used in your testimony, at page 3

1 you state that your analysis to quantify the additional  
2 costs due to Limerick 1 and common non-completion in  
3 April 1981, assumed that the plant was both completed in a  
4 construction sense and became commercial, went into  
5 commercial operation, in April 1981; is that not correct?

6 A. That's correct.

7 Q. Could you define for me, Mr. Dougherty, how you  
8 define "construction completion"? What constitutes con-  
9 struction completion?

10 A. To my mind, Mr. Hall, that is when the nuts and  
11 the bolts, if you will, have all been put in place.

12 Q. So, in essence, your assumption is that on  
13 April 30, 1981, the company tightens up the last nuts and  
14 bolts and, at the same time, declares the unit to be  
15 commercial and providing commercial service for ratepayers;  
16 is that correct?

17 A. In the quantification of the delays, that is  
18 the assumption that we made; yes.

19 Q. If you know, Mr. Dougherty, is it not correct  
20 that there is a substantial testing period which is re-  
21 quired by the Nuclear Regulatory Commission following a  
22 nuclear power plant's construction completion, which must  
23 be completed prior to putting it into commercial operation?

24 MS. CHESTNUT: Objection, Your Honor.

25 Mr. Dougherty is not presented as a witness to discuss

j28

1 NRC matters. He is an auditor, and he is here to discuss  
2 solely the quantification analysis he performed.

3 JUDGE MATUSCHAK: Objection overruled.

4 THE WITNESS: Could you repeat the question,  
5 please?

6 MR. HALL: Would the reporter read back the  
7 question?

8 (Whereupon, the reporter read from the record, as  
9 requested.)

10 THE WITNESS: Yes, I believe there is such a testing  
11 period.

12 BY MR. HALL:

13 Q. Would it not be correct, Mr. Dougherty, that  
14 that testing period can go on for several years and, on  
15 average, it runs about a full year at this point?

16 A. I don't know.

17 Q. Would you accept that subject to check, or as a  
18 hypothetical? Let's take it as a hypothetical.

19 MS. CHESTNUT: Then I object to it as a hypothetical,  
20 Your Honor. There is no basis on the record for that  
21 statement.

22 MR. HALL: If Your Honor please, I can rephrase the  
23 question to avoid the objection.

24 JUDGE MATUSCHAK: You can't have him assume it  
25 subject to check; you can't force him to testify on it.

j29

1 That is part of your case. You can testify to that.

2 He indicated there was a time that was needed to  
3 authorize commercial in-service production of the plant.

4 The difficulty we find was he assumed that the  
5 completion of construction and the in-service date was  
6 simultaneous, and the witness obviously has changed that  
7 testimony by his later statement.

8 BY MR. HALL:

9 Q Mr. Dougherty, to avoid the difficulty, the  
10 testing period that we're speaking of here, is it not  
11 correct, is the period between fuel load at a nuclear  
12 power plant and the period at which or the point at which  
13 that plant is granted a full operating license by the  
14 Nuclear Regulatory Commission?

15 A That is my understanding.

16 Q Would it not be correct, or do you know, that  
17 that period at the Limerick facility required approximately  
18 14 months?

19 JUDGE MATUSCHAK: How many months?

20 MR. HALL: Fourteen months, Your Honor.

21 THE WITNESS: Yes, I would agree with that, Mr. Hall.

22 BY MR. HALL:

23 Q And, indeed, that is the period roughly from  
24 October 1984 through to late-1985, I believe it was?

25 A I would agree with that.

1 Q Is it not correct, Mr. Dougherty, that under the  
2 accounting rules of this Commission, that AFUDC continues  
3 to accumulate as a project cost on the entire completed  
4 construction cost of the unit during this period?

5 A That's correct.

6 Q And is it not also correct that utilities  
7 experience additional direct costs during this period?

8 A That's correct.

9 Q And I believe, in fact, you reference the  
10 magnitude of those direct costs at page 4 of your testimony  
11 as being some 8.6 percent of the total costs being claimed  
12 in this proceeding?

13 A Where are you at, please, Mr. Hall?

14 Q Lines 15 to 18.

15 A Lines 15 and 16 indicate that as of October 30,  
16 1984, the direct expenditures were approximately \$2.155  
17 billion.

18 Q And then don't you continue, Mr. Dougherty, by  
19 stating, "...or 91.4 percent of the \$2.358 billion  
20 Limerick Unit 1 and common direct costs contained in the  
21 instant proceeding"?

22 A That's correct.

23 Q And is it not correct, Mr. Dougherty, that the  
24 additional costs of some \$203 million, which constitutes  
25 the other 8.6 percent of costs, were incurred by the

1 company after October 1984 during this testing period we  
2 have been discussing?

3 A. That's correct.

4 Q. Mr. Dougherty, is it not correct that your  
5 quantification method as presented here today ignores these  
6 cost effects of this testing period?

7 A. Because we work with all actual data, Mr. Hall,  
8 we were required to work with the actual expenditures up  
9 through October 1984. So to that extent, the \$203 million  
10 is not included in the direct cost quantification.

11 Q. And you would agree then, I take it, that that  
12 direct cost quantification is understated to the extent  
13 of its failure to include that \$203 million?

14 A. I would agree with that. If I might, I have a  
15 rough or preliminary calculation of the effect of that, if  
16 you will bear with me a moment.

17 (Pause.)

18 Q. Mr. Dougherty, if you would like, you can  
19 supply that to me in writing. I think it would be easier  
20 than for me to try to deal with it here today. We will  
21 get through quicker.

22 MS. CHESTNUT: Your Honor, I think Mr. Dougherty  
23 should be allowed to explain his answer here. He has the  
24 calculation with him.

25 JUDGE MATUSCHAK: Is it in one of your exhibits,

1 Mr. Dougherty?

2 THE WITNESS: Pardon me?

3 JUDGE MATUSCHAK: Is it in one of your exhibits?

4 THE WITNESS: No, it is not, Your Honor. It is a  
5 handwritten note to myself.

6 JUDGE MATUSCHAK: I see. Will you supply that?  
7 Do you agree to supply that?

8 MS. CHESTNUT: Certainly, Your Honor.

9 JUDGE MATUSCHAK: Very well.

10 BY MR. HALL:

11 Q. Mr. Dougherty, in addition -- we have been dis-  
12 cussing the direct cost effect of this testing period. I  
13 believe you also agreed that there is an AFUDC cost effect  
14 associated with that period; is that not correct?

15 A. I am aware that the company continued to accrue,  
16 I believe it was in the neighborhood of \$400 million,  
17 during the testing period.

18 Q. In fact, that was approximately \$428 million,  
19 was it not, Mr. Dougherty?

20 A. It was in that neighborhood, yes.

21 Q. And your analysis does not, I take it, credit  
22 the company with those specific costs; your quantification  
23 ignores those costs experienced by the company?

24 A. Yes, it does. However, there is an offset to  
25 that due to the non-recognition of the post-October 1984

j33

1 direct cost expenditures in the quantification.

2 Q First, let me establish, Mr. Dougherty, it is  
3 correct that you have stated that your quantification of  
4 the costs of Limerick at a 4/81 in-service date is under-  
5 stated because of your failure to give the company credit  
6 for this additional AFUDC cost? That is correct, is it  
7 not? And then we'll talk about the offset.

8 A That's correct.

9 Q Now, the offset that you're citing is the fact  
10 that you have also failed to credit the company with the  
11 additional \$200 million of direct costs that were  
12 experienced during this testing period; is that not  
13 correct?

14 A Would you mind repeating that, please?

15 Q If I understood you correctly, Mr. Dougherty --  
16 and perhaps I did not -- it seemed to me that your answer  
17 was suggesting that there was an offset against this  
18 failure to credit AFUDC because you also failed to credit  
19 the company with the additional \$200 million of direct  
20 costs which the company experienced to complete the  
21 facility and bring it on line during this testing period.  
22 Is that what you meant to say?

23 A I think, Mr. Hall, the use of project-to-date  
24 data up through October 1984 results in two things. First  
25 of all, the direct cost quantifications are understated;

j34

1 the AFUDC quantified amount is overstated.

2 Q That is the point, Mr. Dougherty, that I am  
3 having difficulty understanding, because I think we have  
4 just agreed, have we not, that as the result of cutting  
5 off your analysis in October 1984, you failed to credit  
6 the company with some \$428 million of AFUDC experienced  
7 and needed to complete the Limerick facility.

8 Now, how is that an offset to a similar failure to  
9 credit the company with some \$200 million of direct costs?

10 A I think, Mr. Hall, if I could go through my  
11 preliminary or rough calculation, it might help explain  
12 the situation.

13 Q Why don't we do that? I agree with you.

14 A As we both agree, there was approximately \$203  
15 million worth of direct costs incurred post-October 1984.

16 Had I had the opportunity to work with those  
17 amounts in the quantification process, I calculated that  
18 approximately \$18 million of those costs would have been  
19 included in the cost quantification. I got that merely  
20 by dividing the total directs associated with not meeting  
21 the April '81 in-service date -- and that amount is  
22 \$192,735,190 -- I divided that by the total October 1984  
23 project-to-date direct expenditures of approximately  
24 \$2.2 billion. The resulting amount, or 8.94 percent, I  
25 then extended times the \$203 million, to arrive at the

1 \$18 million.

2 To include the impact of the additional AFUDC on  
3 that amount, I determined that approximately \$30 million  
4 additional AFUDC would have to be accrued on that amount.

5 I'm sorry; I know that wasn't very clear.

6 Q I was going to say, it didn't really help me.

7 Mr. Dougherty, let me see if I do have the numbers  
8 correct.

9 What you're saying is that you took the direct  
10 cost number of \$203 million that we have discussed. I  
11 take it using the same system that you present in your  
12 Exhibit DPD-1, you sought to deflate that, and gave me a  
13 lower number than that?

14 A No. I didn't use that same system, Mr. Hall.  
15 I didn't have the time necessary to use that system.

16 I took the -- if I can refer you to Exhibit DPD-4 --

17 Q Yes; I have it.

18 A The direct cost, the right-hand column,  
19 associated with not meeting the April 1981 in-service date  
20 is approximately \$193 million.

21 I divided that amount by the total October 1984  
22 project-to-date directs, merely to develop a ratio of the  
23 cost associated with not meeting the delays with the total  
24 project-to-date expenditures.

25 Q And then you applied that percentage --

j36

1           A. I applied that to the \$203 million to approxi-  
2           mate the additional direct cost that we would have quanti-  
3           fied had we had the opportunity to work with the more  
4           current data, if you will.

5           Q. And what was the final number you obtained  
6           from that?

7           A. \$18 million.

8

9

10

11

12

13

14

15

16

17

18

19

20

21

22

23

24

25

1 Q And that \$18 million is the addition, I take it,  
2 to your adjustment?

3 A That would be the de-escalated post-October 1984  
4 dollars.

5 Q And that would leave, by your calculations,  
6 \$185 million by which your quantification of Limerick's  
7 appropriate 1981 completion costs would be; you would  
8 agree that you would have to adjust --

9 A You would have to accrue AFUDC on the additional  
10 \$185 million.

11 Q And you would have to add \$185 million, or  
12 conversely deduct \$185 million from your proposed adjust-  
13 ment?

14 A (No response.)

15 Q Trying to restate that to make it a little  
16 simpler, your adjustment as proposed in your testimony,  
17 you would agree, is overstated by \$185 million because it  
18 fails to reflect \$203 million of additional direct costs  
19 that you and I have been discussing?

20 A I don't know, Mr. Hall, if that is correct or  
21 not.

22 Q What would you need in order to pass judgment  
23 on that?

24 A (No response.)

25 Q Let's see if we can't recap it, Mr. Dougherty.

1 We have agreed, have we not, that there was spent by the  
2 company during a testing period not reflected in your  
3 analysis \$203 million of additional direct costs; is that  
4 not correct?

5 A That's correct.

6 Q And by additional direct costs we are speaking  
7 of expenditures for men, for nuts, for bolts; it is not  
8 AFUDC and it is not overheads?

9 A That is correct.

10 Q That \$203 million, you would agree with me, is  
11 not reflected at all in the cost that you develop as  
12 being the complete cost of Limerick at April, 1981?

13 A That's correct.

14 Q However, you agree with me that that cost should  
15 be reflected there and the company should be credited,  
16 under your quantification system, with that cost; is that  
17 not also correct?

18 A That's correct.

19 Q So is it not clear then, having deflated that  
20 \$203 million down to the \$185 million by the calculation  
21 that you have provided me, that even in your own view,  
22 which I don't necessarily agree with, but in your own view  
23 your calculation of Limerick's cost must be increased by  
24 \$185 million, or conversely your adjustment must be  
25 reduced?

1 A No, I don't agree with that, Mr. Hall.

2 Q Why not?

3 A I view it as our quantification is overstated  
4 approximately \$30 million rather than the \$185 million.

5 Q Isn't it correct though that that \$30 million  
6 is simply the AFUDC that the company would be entitled to  
7 on the \$185 million; is that not right?

8 Isn't that the way you calculated the \$30 million  
9 figure?

10 A That's correct, and I misstated. I believe our  
11 adjustment is overstated approximately \$12 million, which  
12 is the net of the \$30 million additional AFUDC accrual and  
13 the \$18 million additional direct cost quantification.

14 Q The \$18 million, as I understand it, is simply  
15 the devaluation of the \$203 million; is that not correct,  
16 moving from 1984 --

17 A That is correct.

18 Q -- to 1981 dollars?

19 A That is correct.

20 Q That's the part of the dollars spent, direct  
21 dollars, in 1984 that under your quantification method  
22 you wouldn't give the company; is that right?

23 A That's correct.

24 Q However, you would have to give them the \$185  
25 million, would you not?

1           You don't question the need for the company to  
2 test its reactor, do you?

3           A    You are correct, Mr. Hall.

4           Q    So then your adjustment is understated by  
5 \$185 million direct costs, plus the effects of AFUDC on  
6 that; is that not right?

7           A    That's correct.

8           Q    And the effects of the AFUDC, as you have  
9 calculated them, are \$30 million?

10          A    That was a rough approximation, yes.

11          Q    And that's for a total of \$215 million; is  
12 that not correct?

13          A    That's correct.

14          Q    Is it not also correct that there is a third  
15 component here that we discussed previously but we have not  
16 discussed in terms of numbers, and that is the \$428 million  
17 of additional AFUDC experienced by the company on its  
18 previously expended direct costs during the testing period?

19          A    I recognize the existence of that amount.

20          Q    And your analysis does not credit the company  
21 with those dollars; you have agreed to that previously.

22          A    Yes.

23          Q    And we have not as yet -- then would you not  
24 agree that your proposed adjustment is further overstated  
25 by approximately \$428 million, with the necessity of

1 deflating it if your system is accepted by the Commission?

2 A I don't agree with that, Mr. Hall.

3 Q Why not?

4 A I don't know.

5 MR. HALL: If Your Honor please, would it be  
6 appropriate to take a short break?

7 JUDGE MATUSCHAK: All right; let's take a ten-  
8 minute recess.

9 (Recess.)

10 JUDGE MATUSCHAK: When you are ready.

11 BY MR. HALL:

12 Q Mr. Dougherty, I would like to refer you for a  
13 brief moment to PECO Exhibit No. 4, the interrogatory  
14 responses that you prepared. Is it not correct that  
15 Interrogatory Response III-1 and III-2 provide the  
16 citations to the Commission's Order at the 1980 docket  
17 number, reflecting your views with respect to where that  
18 order refers to an April 1981 in-service date?

19 A That's correct, Mr. Hall.

20 Q And referring to Interrogatory Answer III-5,  
21 that answer refers, does it not, to the fact that your  
22 analysis employed only data as of the end of October, 1984  
23 and that Staff does not intend to revise or update the  
24 calculations in this proceeding to employ a later date?

25 A That is correct.

1 Q And would that statement in essence be a state-  
2 ment that Staff did not intend to adjust its proposed  
3 Limerick imprudency adjustment to reflect the additional  
4 costs which you and I have just stated, despite your  
5 recognition that that adjustment was overstated?

6 A That's correct.

7 Q Mr. Dougherty, I want to speak to you for a  
8 moment about some of the more detailed methods that you  
9 employed in your testimony and attached exhibits to attempt  
10 to, shall we say, quantify or deflate the company's actual  
11 construction costs for Limerick back to an April 1981  
12 completion date.

13 Do you have before you Exhibit DPD-1?

14 A Yes, I do.

15 Q Now, Mr. Dougherty, is it not correct that the  
16 general method that you followed in seeking to perform  
17 your quantification analysis was to first determine total  
18 costs as shown by the company's books and records at the  
19 project of construction at October 1984 and April 1981,  
20 and then to determine the difference between those two  
21 values? That was the first step in your analysis?

22 A That is correct. Labor was restated to a  
23 dollar per hour basis, and material was quantified or  
24 the post 4-81 costs were assigned associated with the delay  
25 based in changes in the producer price indices.

1 Q And those calculations are shown on DPD-1, with  
2 labor at the top and materials at the bottom; is that correct?

3 A That is correct.

4 Q And as a second step of your analysis, is it not  
5 correct that what you were doing -- or are doing is taking  
6 the dollars spent on construction of Limerick after April,  
7 1981 and seeking to spread those dollars into construction  
8 periods prior to April, 1981 as if those dollars had been  
9 spent then?

10 That's the theory of your approach, isn't it?

11 A Yes, I think the theory, Mr. Hall, is that, for  
12 instance, the \$16.9 million applicable to the first half  
13 of the exhibit would represent an approximation of the cost  
14 that would have been incurred had the project been  
15 completed by April, 1981.

16 Q Now, in point of fact, your analysis contains  
17 some simplifying assumptions, does it not, which I believe  
18 you describe at page 18, I think, in your testimony; at the  
19 top of page 18, lines 1 through 10.

20 A That is correct.

21 Q And those simplifying assumptions, in essence,  
22 are that all dollars expended after April, 1981 were in  
23 fact expended in October, 1984, and that in fact those  
24 dollars are moved only to April, 1981, and not to an earlier  
25 date?

1 A That is correct.

2 Q And I take it you would agree with me that that  
3 assumption, particularly the assumption that all the dollars  
4 were spent in October of 1984 is inaccurate, would you not?

5 A Inaccurate?

6 Q Inaccurate. It is not a truly correct view of  
7 what happened?

8 A No, it isn't, but then again neither is the  
9 assumption that all of them should have been made in April,  
10 1981.

11 Q Indeed, if one was to complete the plant it is  
12 true that one would have had to spend that money before  
13 April, 1981, would one not?

14 A That's correct, Mr. Hall -- or up through April,  
15 1981.

16 Q What kind of an analysis have you made, Mr.  
17 Dougherty, to attempt to determine whether or not those  
18 offsetting inaccuracies fully offset each other or not?

19 A I have made no such analysis.

20 Q Now, Mr. Dougherty, looking at the last column  
21 of the labor, Account 50, Piping Adjustment, you there show  
22 dollars per hour. Do you have those figures before you,  
23 the 20.5881 and the 16.1466?

24 A Yes, I do.

25 Q Let me ask you a couple of questions about how

1 those figures were derived. I take it the 20.5881 is simply  
2 the division of the dollars in the second column by the hours  
3 in the first column for October 1984.

4 A That's correct.

5 Q And is the hours stated for October, 1984 the  
6 total hours for the project on this particular activity?

7 A For that particular account, yes.

8 Q And just to step back one further step, this  
9 calculation that you are presenting here for labor is a  
10 sample, and you did numerous other calculations throughout  
11 your analysis exactly the same way?

12 A Yes, we did, for all of what we call the nine  
13 major accounts we accumulated the data by.

14 Q And how much of the total cost of labor did  
15 those nine labor accounts constitute?

16 A I don't know if I can answer that without  
17 looking at our work papers, Mr. Hall?

18 Q Was it a very substantial percentage, 90 percent  
19 or something of that nature?

20 A Again, I don't know off the top of my head with-  
21 out reviewing the work papers.

22 Q Returning to the 20.5881 and the 16.1466, you  
23 determine that there is a difference between those cost  
24 per manhour figures of \$4.4415 cents, do you not?

25 A Yes, we have.

1 Q And you do that simply by subtraction, as shown  
2 there?

3 A That is correct.

4 Q Would I be correct that the central principle  
5 of that is an assumption on your part that costs had  
6 increased in the post April, 1981 period for construction  
7 manhours due to increases in wage rates of construction  
8 people?

9 A I don't think that is a result of any assumption  
10 on my part. I think it is reflected -- the numbers were  
11 obtained directly from the company's -- or rather Bechtel's  
12 LD-160 ledger. I think it reflects actual changes in the  
13 labor wage rate.

14 Q I agree with that, Mr. Dougherty, but what I'm  
15 trying to get at is the theory of why this Commission  
16 should disallow \$4.44 of construction manhour labor, which  
17 was experienced in the April, 1981 to October, 1984 period;  
18 would you express that for us? Why do you propose that  
19 this Commission disallow those costs?

20 A Well, based on the Commission's Order at  
21 I-80100341, the Commission decided that the plant should  
22 have been completed by 1981. Based on that fact, it is  
23 my opinion that the labor costs should have been on a  
24 project-to-date basis of \$16 an hour rather than the \$21  
25 an hour figure.

1 Q Why is that, Mr. Dougherty; why is the \$4.45  
2 difference for dollars expended after April, 1981 -- why  
3 is that not appropriately reflected in the pre-1981 cost  
4 of the plant, in your judgment?

5 A Because the actual wage rate pre-1981 was \$16  
6 and approximately 15 cents, based on the costs obtained  
7 from the LD-160 ledger, and associated hours.

8 Q Let's examine what are the possible reasons  
9 that the cost rate could have gone up from \$16 to \$20  
10 during this period. Would you agree with me, Mr.  
11 Dougherty, that one of those reasons may be that the  
12 company was employing a different and more expensive mix  
13 of craftsmen after April, 1981 to do the type of work that  
14 was involved after April, 1981, as compared to the prior  
15 period; is that correct?

16 A I have no way of knowing whether that is correct  
17 or not, Mr. Hall.

18 Q From your point of view though, it is a  
19 possibility, I take it?

20 A Certainly it is possible.

21 Q Now, would you agree with me that -- and again  
22 assuming that that work had to be done with the more  
23 expensive mix of craftsmen, should not the cost of that  
24 more expensive work be reflected in a cost allowance for  
25 an April 1981 completion date?

1 A That's a possibility.

2 Q Now, in addition, Mr. Dougherty, would it be  
3 correct that it is possible that the higher cost of labor  
4 on average for the October, 1984 period could reflect the  
5 greater use of overtime by the company in order to get the  
6 Limerick plant completed?

7 MS. CHESTNUT: Your Honor, I think I am going to have  
8 to interpose an objection here. Mr. Hall's questions are  
9 getting increasingly divorced from reality. If he could  
10 show us some kind of basis in the record for these  
11 assumptions, that's fine; otherwise I think it is going to  
12 have to be clear on the record that these are simply --

13 JUDGE MATUSCHAK: I think Mr. Hall is trying to  
14 prove his case through cross-examination. I do not think  
15 that is proper. I sustain the objection.

16 MR. HALL: Your Honor, I'm glad Ms. Chestnut asked.  
17 I do have a reference in the record to precisely this  
18 point, and I do believe that we can ask the witness to look  
19 at that.

20 BY MR. HALL:

21 Q Mr. Dougherty, have you seen the testimony  
22 presented by the Theodore Barry individuals with respect  
23 to construction management in construction of the  
24 Limerick Plant, and particularly Schedule 32 of that  
25 testimony?

1 A No, I haven't.

2 Q Mr. Dougherty, let me take a moment to show you  
3 that.

4 (Document handed to witness.)

5 JUDGE MATUSCHAK: You may proceed.

6 BY MR. HALL:

7 Q Have you had a chance to review that, Mr.  
8 Dougherty?

9 A I have looked at it, Mr. Hall.

10 Q Is it not correct, Mr. Dougherty, that this  
11 schedule shows that the percentage of manhours spent in  
12 an overtime mode at Limerick increased significantly --  
13 and by that I mean by a factor of up to four to five -- in  
14 the post-1981 period as compared to the pre-1981 period?

15 MS. CHESTNUT: Objection, Your Honor. While this  
16 schedule does purport to show the percentage of overtime,  
17 its credibility has not yet been ruled on in this proceed-  
18 ing, and as such it has simply been offered to support the  
19 company's position. I think there has been no showing that  
20 this is indeed accurate.

21 MR. HALL: Your Honor, it does constitute a basis  
22 in the record upon which one can assert that overtime has  
23 increased.

24 JUDGE MATUSCHAK: Wasn't that testimony admitted  
25 into evidence?

1 MR. HALL: Yes, it was. There was no motion to  
2 strike filed on this testimony.

3 JUDGE MATUSCHAK: Objection overruled.

4 THE WITNESS: The schedule reflects an increase in  
5 overtime post-1981.

6 BY MR. HALL:

7 Q And you would agree with me, would you not, Mr.  
8 Dougherty, that that increase would be reflected in the  
9 higher average hourly cost for labor in the post April,  
10 1981 period?

11 A I would agree that is a possibility, Mr. Hall.

12 Q If you know, Mr. Dougherty, is it not correct  
13 that the plants with shorter construction schedules have  
14 had to use extensive amounts of overtime to obtain those  
15 schedules?

16 A I don't know, Mr. Hall.

17 Q Mr. Dougherty, again referring you to Exhibit  
18 DPD-1 and the calculation related to materials prices,  
19 would I be correct that in the adjustment methodology that  
20 you have made looking at producer price indices you have  
21 made no attempt to determine whether -- or what the causes  
22 of additional costs in the post April, 1981 period for  
23 materials were?

24 Is that question clear?

25 A If you don't mind, would you please repeat it?

1 Q I don't mind at all.

2 Similar to the questions that I asked you with  
3 respect to the labor calculations, would I be correct in  
4 understanding that you have made no effort to determine  
5 whether the total increased costs that you show for materials  
6 of approximately \$14.865 million for the post April, 1981  
7 construction period for Limerick -- you have made no  
8 effort to determine what the causes of those increases  
9 might be, whether inflation or expensive equipment or what-  
10 have-you?

11 A That's correct.

12 Q Mr. Dougherty, does your analysis include -- or  
13 is it based upon a quantification related to the totality  
14 of Limerick common plant or only 50 percent of common  
15 plant?

16 A It reflects 100 percent of common plant.

17 Q Is there somewhere in Staff's presentation where  
18 an adjustment is made to reduce the magnitude of the Limerick  
19 adjustment associated with the '76 and '78 deferrals to  
20 reflect only 50 percent of common plant?

21 A No, there isn't.

22 MS. CHESTNUT: Excuse me, Your Honor. For the record  
23 I should state that Staff Witness Gruber did make such an  
24 adjustment.

25 JUDGE MATUSCHAK: Is it broken down 50 percent and

1 100 percent? Is it broken down?

2 MS. CHESTNUT: Yes, Your Honor.

3 MR. HALL: Can Gruber explain how the adjustment was  
4 made?

5 MS. CHESTNUT: Or Mr. Rosenthal will be able to  
6 discuss it also, as can Mr Gruber.

7 MR. HALL: Thank you.

8 BY MR. HALL:

9 Q Mr. Dougherty, on Schedule DPD-3 and also let  
10 me refer you to Schedule DPD 21A, you there state a  
11 percentage figure identified as the ratio of Bechtel  
12 non-manual costs of delay to total post-1981 Bechtel non-  
13 manual costs.

14 You state that figure, but the figures differ. I  
15 am a little confused as to why. Would you explain to us why  
16 they differ?

17 A That's a good question, Mr. Hall. I can't  
18 respond to that now. I will have to check and provide you  
19 with an answer.

20 Q On pages 22 and 23 of your testimony, Mr.  
21 Dougherty, you have again noted several approximations that  
22 you have made in your study which you believe to be off-  
23 setting. These approximations deal with the calculation  
24 of AFUDC. Have you made any analysis to determine whether  
25 those approximations are in fact fully offsetting?

1           A    Could you refer me to the specific line you are  
2   referencing, Mr. Hall?

3           MS. CHESTNUT:  Excuse me, Mr. Hall.  Could you refer  
4   me to the page you are referencing too?

5           MR. HALL:  Pages 22 and 23, lines 24 to 27 on page  
6   22  and lines 1 to 10 on page 23.

7           THE WITNESS:  Would you mind rereading the question  
8   please?

9           (Whereupon, the reporter read from the record as  
10  requested.)

11          THE WITNESS:  No, I haven't.

12          BY MR. HALL:

13          Q    Finally, Mr. Dougherty, have you done any  
14  analysis respecting the manpower that would be required by  
15  the company to construct Limerick to the schedule that you  
16  have proposed, or whether that manpower would be available  
17  if the company had sought to obtain it?

18          A    I don't believe I have proposed any schedule.  
19  I have quantified what I believe to be the costs associated  
20  with not meeting the appropriate time period -- the time  
21  period deemed appropriate by the Commission.  To answer  
22  your question, I have not made any type of analysis to  
23  determine the availability of manpower.

24          MR. HALL:  That's all the questions I have, Your  
25  Honor.

1 JUDGE MATUSCHAK: Is there any other cross-  
2 examination of this witness?

3 (No response.)

4 JUDGE MATUSCHAK: Any redirect?

5 MS. CHESTNUT: Your Honor, may we have five or ten  
6 minutes?

7 JUDGE MATUSCHAK: Very well. We will have a short  
8 recess.

9 (Recess.)  
10  
11  
12  
13  
14  
15  
16  
17  
18  
19  
20  
21  
22  
23  
24  
25

1 JUDGE MATUSCHAK: Back on the record.

2 MS. CHESTNUT: Your Honor, I have a few questions for  
3 Mr. Dougherty on redirect examination.

4 JUDGE MATUSCHAK: Very well.

5 REDIRECT EXAMINATION

6 BY MS. CHESTNUT:

7 Q Mr. Dougherty, there was considerable discussion  
8 on the record concerning the post-October 1984 direct costs  
9 and AFUDC, and I think the record is a little confused as  
10 to how those costs were related to Staff's adjustment.

11 Could you please explain how those costs were taken  
12 into account in Staff's position in this case?

13 A I will certainly try. The post-October 1984 costs  
14 of approximately \$203 million are not reflected in the  
15 Staff's quantification of the costs associated with not  
16 meeting the April 1981 in-service date.

17 The \$1.1 billion figure is an amount that Staff has  
18 calculated which represents the costs associated with the  
19 delays. It is not an amount that reflects a completed cost  
20 of the plant.

21 Q So is Staff recommending that those post-October  
22 1984 costs be reflected in the allowable costs of Limerick  
23 Unit 1?

24 A They are included in the company's claim for  
25 Limerick Unit 1 and common.

2702  
2 Q. And what your quantification does, Mr. Dougherty,  
3 if I could continue, is you quantified the cost at a certain  
4 date and Staff is recommending that that quantification be  
5 deducted from the company's claim in this case?

6 A. That is correct.

7 Q. It is not your testimony, Mr. Dougherty, that --  
8 you are not testifying, Mr. Dougherty, to what you think  
9 the completed cost of the plant should be?

10 A. That is correct.

11 Q. Now, Mr. Dougherty, with respect to the company's  
12 April 1981 in-service date, which was the date in place  
13 prior to the company's announcement of the 1976 delay, do  
14 you know if that date incorporates a pre-operational testing  
15 period?

16 A. Yes, I would imagine that it does.

17 Q. Mr. Dougherty, with respect to the labor accounts  
18 maintained by Bechtel, do they reflect any breakdown of the  
19 different types of laborers or craftsmen?

20 A. Our quantification -- and I would like to refer  
21 Your Honor to page 9 of the pre-filed direct testimony --  
22 I'm sorry; the bottom of page 8 and then page 9. The labor  
23 cost quantification began with the accumulation of the labor  
24 hours and associated costs by the nine accounts reflected on  
25 page 9. So that there was some recognition given to the  
variance or the different composition of the labor

1 craftsmen in the quantified amount.

2 Q And is this true also for the different types  
3 of materials, Mr. Dougherty?

4 A Yes, that is correct.

5 Q Mr. Dougherty, was the company able to provide  
6 in the course of your study the accumulative manual and non-  
7 manual overtime for Unit 1 and common?

8 A No, they weren't. We requested that information,  
9 but the company responded that such information was not  
10 available.

11 Q Finally, Mr. Dougherty, is it Staff's position in  
12 this proceeding that Limerick Unit 1 could physically have  
13 been completed by April 1981?

14 A No, it is not.

15 MS. CHESTNUT: Thank you, Your Honor. I have no  
16 further redirect.

17 JUDGE MATUSCHAK: Anything further, Mr. Hall?

18 MR. HALL: Yes, Your Honor.

19 RE-CROSS-EXAMINATION

20 BY MR. HALL:

21 Q Mr. Dougherty, referring to the AFUDC value  
22 associated with the post-1984 testing period for Limerick,  
23 the \$428 million figure that we discussed, would you explain  
24 to me how Staff's proposal permits the company to recover for  
25 those costs? I'm afraid I still do not understand that.

1           A. Staff's quantification, Mr. Hall, the AFUDC portion  
2 of that -- let me refer to the exhibit, if I might, please.  
3 It is Exhibit DPD-4. The \$927 million of quantified AFUDC  
4 was developed by first of all quantifying the direct costs  
5 associated with the delays, giving the company additional  
6 AFUDC on the incremental post-4-81 costs, and subtracting  
7 that amount from the amount of AFUDC claimed in the instant  
8 proceeding.

9           Q. Let me think about that for a minute, Mr.  
10 Dougherty.

11           (Pause.)

12           Q. Could you point to me where in your exhibit,  
13 Mr. Dougherty, that calculation appears?

14           A. I believe it is on Exhibit 28, Mr. Hall.

15           Q. And where specifically on Exhibit 28?

16           MS. CHESTNUT: Your Honor, present in this room are  
17 the auditors who worked with Mr. Dougherty on the study, and  
18 they have the work papers that we used. Mr. Dougherty would  
19 like to take a minute and confer with them.

20           JUDGE MATUSCHAK: If you want to go off the record  
21 and see if we can clear some of this stuff up. I'm having  
22 some problems here, too.

23           Before you do that, though, on the record here,  
24 Mr. Dougherty, I notice some of your exhibits show costs  
25 associated with not meeting an in-service date of April 1981.

1           Is it your understanding that the completion of  
2 construction and the in-service dates coincide, are the  
3 same?

4           Was the original estimate of the company of April '81,  
5 was that supposed to be the conclusion of construction or  
6 was that supposed to be commercial in-service date?

7           THE WITNESS: Your Honor, the order entered August  
8 27, 1982 indicated that the April 1981 date was applicable  
9 to the plant being in service.

10          JUDGE MATUSCHAK: I see. Now, you have assumed that  
11 any delays in the in-service date of Limerick 1 and ~~common~~  
12 was due to delays caused by the company?

13          THE WITNESS: I did not make that assumption, Your  
14 Honor. I believe the Commission had --

15          JUDGE MATUSCHAK: In your figures you made that  
16 assumption, though?

17          THE WITNESS: That's correct.

18          JUDGE MATUSCHAK: And you state that you did not  
19 and were unable to determine whether there were other factors  
20 which would cause the company to be unable to complete,  
21 for reasons not of their own, other than their own, not  
22 complete the construction of Limerick 1 by April '81? You  
23 made no survey of that? You made no consideration of that?

24          THE WITNESS: That's correct.

25          JUDGE MATUSCHAK: If the company were to present

1 evidence that some of the time of delay was for causes other  
2 than their own, how would we go about adjusting your figures  
3 to eliminate that non-accountable delay? Could we do it  
4 by a mathematical manner in any way, or how would you  
5 suggest?

6 MS. CHESTNUT: Excuse me, Your Honor. Mr. Rosenthal  
7 is the witness who should be answering that question. It  
8 is certainly a legitimate question, but Mr. Rosenthal is  
9 the Staff witness who is testifying to Staff's recommenda-  
10 tion here. Mr. Dougherty is only testifying to the method  
11 used to quantify this delay.

12 JUDGE MATUSCHAK: Very well.

13 MS. CHESTNUT: I'm sure Mr. Rosenthal will be glad  
14 to answer that question.

15 JUDGE MATUSCHAK: Very well. Proceed.

16 BY MR. HALL:

17 Q Mr. Dougherty, I'm afraid I must disagree with  
18 you with respect to the AFUDC component we talked about  
19 previously.

20 Looking at your Exhibit DPD-28A, is it not correct  
21 that what you have done is you have taken the total AFUDC  
22 claimed by PECO, which includes the \$428 million of AFUDC  
23 claimed for the period post-October 1984, and you have  
24 deducted from that the AFUDC that you allow as described at  
25 page 7 of your testimony, that AFUDC being the AFUDC

1 accumulated up to April of 1981, and the recalculated AFUDC  
2 on the direct expenditures that you spread prior to April 1981;  
3 is that not correct?

4 A. That is correct, Mr. Hall?

5 Q. And is it not true that that has the effect of  
6 disallowing the \$428 million of AFUDC that we previously  
7 discussed?

8 A. Well, had the plant been completed in April 1981,  
9 that additional \$428 million of AFUDC would not have been  
10 accrued.

11 Q. But you agree that that is based on the assumption  
12 that there would be no testing program, as you've indicated  
13 and agreed the NRC requires, since you have assumed the  
14 construction completion and in-service will be the same  
15 date?

16 (Pause.)

17 MS. CHESTNUT: Mr. Dougherty, perhaps you could take  
18 a moment and consult with your associates.

19 Could you go off the record for a second?

20 JUDGE MATUSCHAK: Off the record.

21 (Discussion off the record.)

22 JUDGE MATUSCHAK: Are you ready to proceed?

23 THE WITNESS: Yes, Your Honor.

24 BY MR. HALL:

25 Q. Are you ready to answer the question?

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

A. Could it please be repeated?

MR. HALL: May we have that read back?

(Whereupon, the reporter read from the record, as requested.)

THE WITNESS: We have assumed that the completed construction and the in-service are as of April 1981. The testing period, however, Mr. Hall, I'm of the opinion should have occurred prior to that time.

BY MR. HALL:

Q. Would that not change the AFUDC calculation that you've made very drastically?

A. Our AFUDC calculation in my mind reflects the amount of AFUDC that would have been accrued had the in-service date been April 1981. That amount is then subtracted from the company's rate claim.

Q. But isn't it correct, Mr. Dougherty, that, in fact the AFUDC calculation you have used in fact assumes that the April 30, 1981 date is the company's fuel load date, October 1984? Isn't that clearly stated in your testimony?

A. It is stated as being the in-service date.

Q. But is it not correct that what you've done in your calculation is you have taken the costs which the company experienced from April 1981 through October 1984, and you have spread those costs over the period ended April 30, 1981 and the prior 42 months? Is that not correct?

1 A. That is correct.

2 Q. And you have ignored in that spreading and  
3 analysis all costs experienced by the company during the  
4 testing program that was after October 1984; is that  
5 not correct?

6 A. All direct costs.

7 Q. All direct costs, yes. Is that not correct?

8 A. Yes.

9 Q. So in point of fact, if your position now is  
10 as you've said that the testing program should have  
11 preceded April 1981, is it not correct that your AFUDC  
12 calculation is inconsistent with that present position?

13 A. No, I don't believe it is.

14 Q. Is it not true, Mr. Dougherty, that you agreed  
15 with me that there is a testing period that is required  
16 for nuclear power plants of some 14 months? Is that not  
17 right?

18 A. Yes, I did.

19 Q. And that period, in fact, follows the construction  
20 completion of the plant; is that not correct?

21 A. That is correct.

22 Q. And at that time, is it not correct that the  
23 plant sits there for the entire 14 months having had the  
24 dollars spent on it, the great majority, for construction  
25 completion and accrues AFUDC? I believe you agreed to that

1 as well.

2 A. Yes, I have.

3 Q. And is it finally not correct that your calculation  
4 does not contain any period of that nature prior to April  
5 1981?

6 A. That is correct.

7 MR. HALL: That's all the questions I have, Your  
8 Honor.

9 JUDGE MATUSCHAK: Anything further of this witness?

10 (No response.)

11 JUDGE MATUSCHAK: Is it your testimony now that you  
12 have considered that the plant would be completed and in  
13 commercial service April 30, 1981? Is that the basis on  
14 which you provided your figures? All of the testing, all of  
15 the loading, and all of that would have been done by  
16 April 30, 1981; is that your position?

17 THE WITNESS: That the in-service date would have  
18 been April 30, 1981.

19 JUDGE MATUSCHAK: Just answer my question. It is  
20 your position that by April 30, 1981, the loading, the  
21 testing and the availability of plant for commercial operation  
22 would have been completed by that date?

23 THE WITNESS: That's correct, Your Honor.

24 JUDGE MATUSCHAK: Do you know whether or not that  
25 is the date the company in their original estimate estimated

1 the in-service date or the conclusion of construction? Do  
2 you know what the estimate was? Do you know what the  
3 Commission considered in their order, whether April the 30th  
4 was the in-service date after all testing or whether that  
5 was supposed to be the completion of construction?

6 THE WITNESS: The Commission order indicated that  
7 that date was the in-service date.

8 JUDGE MATUSCHAK: Is there anything in the order  
9 which says that?

10 THE WITNESS: Yes, there is, Your Honor. It is  
11 page 11, Section C.

12 JUDGE MATUSCHAK: What does it say? Do you have  
13 that section there?

14 THE WITNESS: I have the order, Your Honor, if you  
15 bear with me a moment.

16 (Pause.)

17 THE WITNESS: Page 11, Section C: "In 1976, to match  
18 growth in capacity additions with a lower Spring, 1976  
19 load forecast, PECO further delayed construction and revised  
20 the in-service dates for the Limerick Units Nos. 1 and 2  
21 from April 1981/April 1982 to April 1983/April 1985,  
22 respectively."

23 JUDGE MATUSCHAK: Very well.

24 Anything further?

25 MR. HALL: No, Your Honor.

1 JUDGE MATUSCHAK: Anything further?

2 MS. CHESTNUT: No, Your Honor.

3 (Witness excused.)

4 JUDGE MATUSCHAK: As I understand it, you only have  
5 one witness tomorrow?

6 MR. WERSAN: That's right, Your Honor. We have  
7 Dr. Hanauer on NRC regulations and on the Mark II issue.

8 I would like to note at this time, Your Honor, that  
9 next Tuesday the OCA will be presenting Mr. James J. O'Brien  
10 on a Limerick issue relating to the quantification of when  
11 the plant could have been done.

12 I would like to note for the record that the OCA  
13 has indicated to the company that some of the quantifications  
14 attached to his testimony were actually done by Mr. John  
15 Plunkett from Komanoff Energy Associates. He is an associate  
16 of Mr. Charles Komanoff, who will be on the stand on Monday.  
17 We will make Mr. Plunkett available for cross-examination  
18 on the calculations which he did if the company so desires.

19 JUDGE MATUSCHAK: Very well.

20 MR. HALL: Your Honor, I understand there is also  
21 an oral argument tomorrow with regard to the Staff's Motion  
22 to Strike on the 80/20 testimony. The company will be  
23 prepared to argue that first thing in the morning and would  
24 prefer to do that before --

25 JUDGE MATUSCHAK: Do I understand the Commission Staff

1 wants the oral argument?

2 MS. CHESTNUT: Yes, Your Honor. I don't care whether  
3 it is before or after Dr. Hanauer's testimony, though.

4 JUDGE MATUSCHAK: Very well. We will have that first  
5 thing in the morning.

6 MR. HALL: In addition, Your Honor, I understand  
7 that we may be requesting or will be requesting oral argument  
8 with respect to the motion to strike portions of  
9 Dr. Hanauer's testimony.

10 I have spoken to the Consumer Advocate and we are  
11 tentatively thinking of holding that on Tuesday, subject  
12 to Your Honor's approval.

13 JUDGE MATUSCHAK: Very well.

14 MR. WERSAN: On the oral argument, it would be my  
15 preference to do it after the cross-examination of the  
16 witnesses.

17 MS. CHESTNUT: Perhaps we could start earlier that  
18 day.

19 JUDGE MATUSCHAK: Our position in this matter is  
20 to at least permit the introduction of the testimony into  
21 the record and if we strike it, to strike afterwards. So  
22 in the event we are in error, the record will be there and  
23 we will not have to have a remand for that testimony. The  
24 testimony will be there and the Commission can do what they  
25 want with it if we are in error. So at least it will be on

sl4

1 the record.

2 And the same thing goes with the cross-examination.  
3 The cross-examination will be completed. So if we are in  
4 error in the matter, the Commission can itself strike or  
5 reinstate any testimony that we may strike or any cross-  
6 examination we may strike.

7 What we are trying to avoid here is to complete  
8 this rate case so it doesn't have to be remanded for further  
9 testimony.

10 Very well. We will adjourn at this time until  
11 tomorrow morning at 10:00.

12 (Whereupon, at 4:10 p.m., the hearing was adjourned,  
13 to be reconvened at 10:00 a.m., Friday, February 7, 1986,  
14 in Philadelphia, Pennsylvania.)

15

16

17

18

19

20

21

22

23

24

25

C E R T I F I C A T E

1  
2 We hereby certify, as the stenographic reporters,  
3 that the foregoing proceedings were taken stenographically  
4 by us, and thereafter reduced to typewriting by us or under  
5 our direction; and that this transcript is a true and  
6 accurate record to the best of our ability.  
7

8 COMMONWEALTH REPORTING COMPANY, INC.

9  
10 By: Robert J. Stonaker  
Robert J. Stonaker

11  
12 By: Sandra Milus-Brown  
13 Sandra Milus-Brown  
14

15  
16  
17 \*\*\*  
18  
19  
20  
21  
22  
23  
24  
25