COUNCIL OF THE CITY OF PHILADELPHIA

PUBLIC HEARING

COMMITTEE ON FINANCE

and

COMMITTEE ON TRANSPORTATION AND

PUBLIC UTILITIES

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Room 696, City Hall
Philadelphia, Pennsylvania
Wednesday, March 24, 2004
2:10 p.m.

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BILL 040153 - An Ordinance approving the Fiscal Year 2004 Capital Budget providing for expenditures for the capital purposes of the Philadelphia Gas Works...

RESOLUTION 040149 - Resolution authorizing City Council's Committee on Transportation and Public Utilities to hold public hearings to investigate the proposed gas cost rate increase to be effective September 1, 2004...

RESOLUTION 040216 - Resolution authorizing City Council's Committee on Transportation and Public Utilities to investigate and hold hearings on the Petition of the Philadelphia Gas Works to the Pennsylvania Public Utilities Commission...

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COUNCILMAN DARRELL CLARKE
COUNCILMAN DAVID COHEN
COUNCILMAN W. WILSON GOODE
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COUNCILMAN BRIAN O'NEILL
COUNCILMAN JUAN RAMOS
COUNCILMAN FRANK RIZZO
COUNCILWOMAN MARIAN B. TASCO
COUNCIL PRESIDENT VERNA

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I N D E X

03/24/04 - FINANCE - BILL 040142

COUNCILWOMAN BLACKWELL: Good afternoon. Thank you for your patience. We would now like to begin our Finance Committee with regard to PGW. We have a quorum present. To my left is Councilman W. Wilson Goode; to his left, Councilman Brian O'Neill; to his left, Councilwoman Marian Tasco; to my right, Councilman Rick Mariano; also a member of our Committee Councilman Frank DiCicco is standing on the side. So we have a quorum. We will begin our testimony.

Before I call on the Clerk to read the title of the bill, I would like you to note that in addition to PGW's Capital Budget, this Committee is also scheduled to hear testimony on Resolution No. 040229 sponsored by Councilman Brian O'Neill which deals with the senior citizen discount. Soon after we finish taking testimony, the Committee will recess to allow testimony to be taken on the two resolutions listed before the Committee on Transportation and Public Utilities. Once that is finished, the Committee on Finance will reconvene for the purpose of reporting out the bill.

We will now call on the Clerk to read the title of Bill No. 040153 concerning the Philadelphia Gas Works Capital Program.

THE CLERK: Bill No. 040153, an ordinance approving the Fiscal Year 2004 Capital Budget providing for expenditures for the capital purposes of the Philadelphia Gas Works, including the supplying of funds to be obtained in connection therewith, and acknowledging receipt of the Forecast of the Capital Budget for Fiscal Years 2005 through 2009.

COUNCILWOMAN BLACKWELL: Thank you very much.

We would ask those representing Philadelphia Gas Works to come forward and begin their testimony. We understand that we have prepared testimony from Craig White, acting CEO and Senior Vice President of Philadelphia Gas Works.

The Clerk will also read the title of the resolution before you begin since we will hearing them consecutively.

THE CLERK: Resolution 040229, a resolution calling upon the Committee on Finance to conduct hearings on the audit of the Senior Citizens Discount Program offered by the Philadelphia Gas Works.

COUNCILWOMAN BLACKWELL: Thank you very much.

Thank you. Good evening, Gentlemen. Mr. White, Mr. Knudsen, we ask you to identify yourselves for the record and begin your testimony.

MR. WHITE: Good morning, Madam Chairwoman. My name is Craig white. I'm the acting Chief Operating Officer for Philadelphia Gas Works.

MR. KNUDSEN: Good afternoon. My name is Tom Knudsen. I'm Chief Executive Officer of the Philadelphia Gas Works.

COUNCILWOMAN BLACKWELL: Thank you.

MR. WHITE: Madam Chairwoman, I'd first like to begin by thanking you for this opportunity to come before you today. I'd also like to take a moment and indicate that the Capital Budget which I'm here to discuss was worked -- it's worked its way through the procedure, and I want to personally thank Chairwoman of the Philadelphia Gas Commission Tasco and the Gas Commission, along with the Gas Commission staff, which includes the Executive Director, Ms. Parrish and Hearing Examiner Tarlton Williams (ph). I have, as you know, submitted testimony for the record and I certainly am prepared to read it, summarize it, or if you prefer not do either and just accept questions at this point. I'm at your discretion.

COUNCILWOMAN BLACKWELL: Would the Members of the Committee like the testimony read or would you like -- perhaps a summary would be great and then we'll start with questions.

MR. WHITE: Very good. Thank you.

As I indicated, I'm here in reference to the Capital Budget. PGW's Capital Budget is at a level of $65 million. That $65 million is primarily almost exclusively made up of costs that deal with supporting the core business. By the core business, I mean our distribution function, our field services, and our gas processing.

As you know, we have an extensive system of mains and services in the streets of Philadelphia. Much of that is cast iron which we have to replace under our Prudent Main Replacement Program.

Secondarily, we have two gas plants, and the two gas plants have liquefaction facilities that are necessary to enable us to meet our requirements in both normal and in worst-case winter situations.

The remaining 10 percent of the budget deals with smaller items in the areas of transportation, information technology, and some of the smaller areas of the company.

But in summary, the majority of this budget, as I had indicated, reflects continued effort to support the core business. And in recognition, obviously, of our financial condition, we have looked for every opportunity to reduce costs and, of course, we worked hand-in-hand with the Gas Commission -- when I say hand-in-hand, the Gas Commission oversaw the process. And we're here before you today post that process.

COUNCILWOMAN BLACKWELL: Thank you very much.

Mr. Knudsen, would you like to make remarks or are you prepared to just take questions?

MR. KNUDSEN: If you would, Madam Chairwoman, I'll just read it. It's a very brief piece of testimony, just so that the record is clear.

With regard to the Senior Citizen Discount Audit, PGW recently sent letters to customers participating in the Senior Citizen Discount Program because an audit that we had conducted indicated that those customers were no longer alive or with us and were not the appropriate customers of record. It is important for a host of reasons that our records be correct. The letters we sent serve two purposes. Actually, we have sent some, and we have more to send.

First, it is to inform the surviving household members who might be eligible for the senior citizen discount that they could remain on the program if they only provided PGW with proper documentation for eligibility.

The second purpose of the letter, obviously, was to ensure that those who are no longer eligible or who are not eligible in that household, that they can no longer continue with the discount. In other words, they didn't meet the criteria of being 65 years of age or older.

After the initial mailing of 4,000 accounts, which raised concerns amongst some of our senior citizens, we are now sending out only a thousand of these per week. Of the total 60,000 customers who qualify or had qualified for the senior citizen discount, we determined that 13,000 of them fit within this category of concern. We have set up a special procedure at the district offices to minimize the confusion going forward for those who are now and will be receiving the balances of these notices.

We have proposed, as you know, that the -- there was an agreement amongst parties that was presented to the Public Utility Commission and is now awaiting their decision to continue the Senior Citizen Program but under new eligibility requirements, effective September 1, 2003. For the current participants of that date, there is no change. If the senior citizen discount is applied for after September 1st, eligibility would begin from that date of application --

COUNCILWOMAN BLACKWELL: Would you pull your microphone a little closer? It's hard to hear you.

MR. KNUDSEN: I'm sorry.

COUNCILWOMAN BLACKWELL: Thank you.

MR. KNUDSEN: And most importantly, all new applicants must be 65 years of age, reside at the address receiving the discount, be responsible for the PGW bill, and have household income less than the 250 percent of the federal poverty standard for a two-person household, which is currently about $30,000.

As I said, these changes now await the PUC approval.

I am available for whatever

questions you might have, particularly on the question of the audit.

COUNCILWOMAN BLACKWELL: Thank you very much.

With regard to the Capital Program, I have a few questions.

Number 1, regarding the gas processing department, what is the status of the previously approved project to replace PGW's aging LNG plant?

And with that question, there are a couple other questions.

When will the new plant be operational?

And will the delays result in higher cost for consumers?

And finally, on the LNG plant, should we expect to see additional capital funding for this project?

MR. WHITE: Madam Chairwoman, I would like to answer that question. As far as the new LNG plant, we certainly expected it to be online before this point in time. The manufacturer of the facility Air Products, ran into some design problems. They've made modifications. We're in the testing phase again as we speak. And at the present time, the plant has not been able to be run at the contractual performance specifications. We do not anticipate any additional requests for spending pertaining to that plant. The arrangements that we have made with the contractor require the contractor to pick up all the costs to complete the project and make it operational.

We are optimistic that this plant will be operational in the very near future, but I must say with complete candor that we have been working for about six months now on completing the project with the manufacturer, and they are having difficulties. So I cannot give you any absolute assurances as to when the plant will be complete. What I can assure you of is that we are not spending the dollars and the ratepayers of Philadelphia Gas Works aren't contributing anymore dollars.

COUNCILWOMAN BLACKWELL: Thank you.

Last year, PGW installed automatic

meter reading devices throughout the City. Have there been complaints from customers resulting from the new meters.

MR. WHITE: I would say to the contrary. We're better than 99 percent saturated as far as automatic meter reading devices are concerned. We only have 1800 homes that do not have a automatic meter reading device, and we have a program to complete that by September. So that answers the first part of the question.

The second part of the question is whether we're getting complaints. Certainly, the facts that customers aren't getting estimated readings as they were prior to the automatic meter reader devices -- and just to give you an idea, better than 50 percent of all of our reads were estimated. Now, better than 99 percent are actual. So we're about to go into the phase of replacing units that wear out and replacing batteries in units as they expire over time.

COUNCILWOMAN BLACKWELL: Thank you. Before I ask my next question, the Chair notes

Vice Chair of the Committee, Councilwoman Blondell Reynolds Brown is here and also Frank Rizzo. We thank them. Councilman Michael Nutter is likewise here and will Chair the Transportation and Public Utilities hearing when we recess this one.

My next question is, with respect to limited line item transfer authority, do we have your assurances that PGW will not use this line item transfer authority to fund new projects which should be presented as proposed amendments to the Capital Budget?

MR. WHITE: You must certainly do. In no instance will we overrun the budget. We are just talking about line item transfers within a category such as our distribution department. We may move dollars from four-inch main replacement to eight-inch main replacement. But all in all, the cost will stay within budget.

COUNCILWOMAN BLACKWELL: Great.

What is the status of the weather normalization adjustment?

How does this impact seniors and

people who are on a fixed income?

MR. WHITE: The current status of the weather normalization adjustment for this year, it's pretty much been a normal winter, so in a normal winter the customers are not going to be billed incrementally or they're not going to be receiving a credit. I think at the present time, we are probably at about $1.5 million worth of warmer than normal credits, but, of course, there's a band around that weather normalization that we only collect above and below a 2 percent band. So the winter is not yet over, but the numbers are very close this year. It's not like a few years ago when we had a winter that was 35 percent warmer than normal. We're actually experiencing a winter that's a little bit warmer than normal, but not much. So it will not have a significant impact, in my opinion, this year.

COUNCILWOMAN BLACKWELL: Thank you.

When do you, or do you anticipate repaying the loan City Council made?

MR. KNUDSEN: We're in the process

of -- and that will be discussion before the Transportation Utilities Committee -- of attempting to finance the company's operations. At the present time, it is not clear to me precisely when we'll be able to pay that. We are anticipating and budgeting, and if the appropriate actions are taken both at the PUC and on the part of our customers, most importantly on the part of our customers, if they pay their bills and particularly this summer as we go into fall, then we would be on schedule to pay the 40 million back in 2006, as anticipated. Obviously, we have some uncertainties about that right now, but that is the plan, is to pay it back in 2006.

COUNCILWOMAN BLACKWELL: Thank you.

Can you let us know if it's PGW's plan to acquire land as part of its Capital Program?

MR. WHITE: The only land that we have interest in is the section of our Richmond plant facility in the Tioga section that was formerly the Franklin Smelting facility. The piece of the Franklin Smelting property that actually encroaches on our fence line is an area that we would like to acquire, and we have had discussions with PIDC in reference to that piece of property.

COUNCILWOMAN BLACKWELL: So that's still ongoing in discussion?

MR. WHITE: Yes, ma'am.

COUNCILWOMAN BLACKWELL: In light of the financial straights, is there still talk of, quote/unquote, selling PGW that you're aware of?

MR. KNUDSEN: Councilwoman, there's no active conversation about selling PGW at this time.

COUNCILWOMAN BLACKWELL: Thank you very much.

COUNCILWOMAN BROWN: I have a follow-up question.

COUNCILWOMAN BLACKWELL: Follow-up question, Councilwoman Brown.

COUNCILWOMAN BROWN: Thank you, Madam Chair.

Good afternoon, gentlemen.

In response to Chairwoman

Blackwell's question regarding the City payment back to the City, your response was, "If appropriate action is taken by both the PUC and the customers."

What is the desired appropriate action of the PUC?

MR. KNUDSEN: That is the subject for the Transportation and Utilities Committee. I have proposed a type of regulatory treatment that in the event that we're not able -- and I don't take this position, by the way. I think we do have the ability and the opportunity to have our customers pay for their bills this summer. In the event that they were not able to pay the amount of money that we need to continue to operate the company, then the request to the PUC is for a flexible clause that would give us just that amount of money that we need to keep operating, and that is the action that I want the PUC to take.

It may very well be -- and I'll emphasize this in the next proceeding as well -- that if we collect from our customers in the manner that I think we can and that they must pay, then we will not exercise this clause, this flexible clause this year. But if they don't pay the way we need them to pay, then I had very little option but to propose such a mechanism.

COUNCILWOMAN BROWN: Has PGW been down this road before of wanting to consider the option of what you call a flexible clause?

MR. KNUDSEN: We haven't up 'til now. In each of the two prior proceedings where we've sought rate relief from the PUC, we sought a permanent increase in rates. For a whole host of reasons, I don't think that's the appropriate response, and I would be prepared to talk about specifically why I think a more flexible approach is more merited here.

COUNCILWOMAN BROWN: Very well. I'll wait until the next hearing. Thank you.

COUNCILWOMAN BLACKWELL: Thank you.

The Chair also notes that Councilman Ramos is here who is also a member of this Committee.

03/24/04 - FINANCE - BILL 040142

Councilwoman Tasco.

COUNCILWOMAN TASCO: Good afternoon, Mr. White, and good afternoon, Mr. Knudsen.

As you stated earlier, the Gas Commission did and does sit to hear the testimony relative to the Capital Budget as well as the Operating Budget. And certainly, there are many discussions that take place at that time that the Council does not have access to that information. So a number of the questions I will be asking will be questions, yes, we have asked, but I want this record to be clear here which will give us some idea about what the financial condition of PGW is, because we do all have some responsibility to try and figure out how we rectify the problems at PGW. So it's very important for the Councilmembers to have some knowledge of what you and the company encounters and what we've heard during our course of the deliberations with you before the Commission.

We understand that maintaining the safety and reliability of the gas distribution system is of paramount importance. At the same time, PGW's capital spending must fit within its present financial constraints.

PGW contends to be completely dependent on long-term debt to fund capital improvements. There have been no internally-generated funds for many years, and PGW's financial forecast show there will be no internally-generated funds anytime soon. PGW contends to be burdened with $1 billion in long-term debt. PGW's debt service cost continue to be its third highest rating cost, second only to the cost of gas supply and labor expense. Rather than moving towards significant debt reduction, PGW is in a hole which is getting deeper every year.

In June 2001, PGW issued $120 million of debt for its capital needs.

In December 2002, PGW issued another $125 million in revenue bonds.

In the Fiscal Year 2004 operating forecast, PGW projected it would issue another 125 million in December 2004 and then another 125 million in December 2006.

Now PGW is indicating that the December 2004 issue will have to be moved up to the late summer or early fall of the year.

The question is, at this rate, is there any end in sight?

And how will PGW ever make headway towards achieving its stated financial goals when it is taking on this much additional debt every year and a half or so?

MR. KNUDSEN: Councilwoman Tasco, if I might, I'll respond to that.

Within the last 12 to 15 months, gas prices have gone up substantially, in fact, markedly. Some of our customers have seen a 50 percent increase in their bills. That being said, prior to the run-up last year or the beginning of the run-up in the prices last year, PGW was on target with its workout program to continue its obligations, both to meet the $45 million repayment in August of 2006 and to start paying down some of the outstanding long-term debt. It is only as a result of the buildup in gas costs over the last 12 or so months that are beyond the control of the company, that are the function of market conditions, national market conditions that we find ourselves in the circumstance we are right now.

It is my position that regardless of what has happened to the markets, people must pay their bills. So my response to you is that I think there has to be a requirement on the part of the Administration and maybe this Body, certainly some of the social service agencies, to require people to pay the money that is owed. Short of that, there is no answer to this problem. We want to be as responsible as we need to be in dealing with people as equitably and fairly in as even-handed a manner as we can. But they must pay their bills. Otherwise, no company can survive.

COUNCILWOMAN TASCO: Could you tell me what is PGW doing to ensure that the most risk-prone iron cast mains are being replaced first? And what steps is PGW taking to ensure that its current practices are effective and up to date?

MR. WHITE: Councilwoman, I'd like to answer that.

As I had indicated in my written testimony, there are a number of things we look at in determining what is the riskiest or the riskier mains in the streets of Philadelphia. We have approximately 1700 miles out of our 3,000 miles of mains that are cast iron. We look at a number of things, not the least of which is the break rate of mains in a particular block and, of course, we fix a break after it occurs. But once a block has a certain number of breaks in it, one reaches the conclusion that that is a riskier situation and that, of course, rises to the top. We use a model, a projection model or a model that evaluates the risk profile. And what we have done is we've established a 18-mile program, which is a little more than 1 percent or about 1 percent a year of the cast iron, and we remove that. And that's the largest expenditure in our current Capital Budget. There's approximately 20-plus million dollars associated with the prudent main replacement program, and then, of course, there's other utility work that we have to account for when our facilities are undermined. But certainly to be specific in reference to your question, we look for the riskiest blocks. We have a number of both historical and projection tools to ensure that we target the right blocks and we move forward with a capital program targeting those blocks.

COUNCILWOMAN TASCO: One final question. Just give us an update on your fleet reduction. I know we've asked you over and over again in terms of reducing the PGW fleet. What are you doing to reduce its vehicle fleet cost and the size?

MR. WHITE: In the very recent past, we reduced the number of sedans in an agreement with the Philadelphia Gas Commission. We further have frozen the level of field service van requirements. In light of our financial condition, instead of requesting an $8 million Capital Budget for the replacement of vehicles that are beyond the point where you, using best practices, would replace them, we've opted to continue to utilize those vehicles and continue to maintain them, and hence our budget has been reduced materially.

As time has gone by, we have been able to come up with new strategies. At the request of the Commission to reduce the fleet, we are attempting and we are being successful at using vehicles on cross-functional or on a cross-departmental basis where collections may be working and field services are not at the same level of staffing at a particular time in a day, we will shift vehicles from one area to another. So we're looking for opportunities to keep the fleet at the size that it's at right now, which is much smaller than it was. And then, of course, we're looking for ways to maintain these vehicles in a more efficient way to keep the cost down.

COUNCILWOMAN TASCO: Thank you.

Thank you, Madam Chair.

COUNCILWOMAN BLACKWELL: Councilman O'Neill and then Councilman Nutter.

COUNCILMAN O'NEILL: Gentlemen, your

'03 Capital Budget, how much was that?

This is '04, right, that we're doing today?

MR. WHITE: Yes. The '03 Capital Budget, I believe, after amendments, was in the same neighborhood as this Capital Budget.

COUNCILMAN O'NEILL: And have you spent part of it, all of it? How much is remaining?

MR. WHITE: Well, in the course of a fiscal year, we spend very close to what we budget. But in many cases, it is budget dollars from the prior year that actually gets spent in the current year. So you've always got this stepping forward where some programs start and then for a variety of reasons -- I'll give you one example, Councilman. If we do a large project where multiple utilities have to get in and do the work, for instance, the Water Company has to get in and then we have to come back in at a later date, that may cross fiscal years so the actual spending that was approved in one year may occur in the next year. But certainly, we keep our overall spending within the budget limits that are approved by City Council.

COUNCILMAN O'NEILL: And your line item changes are brought back to the Finance Committee to the Capital Budget?

MR. WHITE: The line item authorization that we're talking about here is just line item transfers within a particular department within the company. And at this point, the line item authorization is pursuant to some discussion and agreement with the Philadelphia Gas Commission.

COUNCILMAN O'NEILL: So you don't have to bring any line item changes back to City Council once the budget is passed?

MR. WHITE: It's not my understanding that we have to bring in --

COUNCILMAN O'NEILL: In other words, we approve A, and you do B or C or some other item; you need the Commission approval but not City Council's?

MR. WHITE: I guess the way I would answer that, Councilman, is we're only transferring within the category. So we're not starting a new program. It's not as if the Council authorizes PGW and their gas processing plant to purchasing a new natural gas heater to heat the gas, we're not going to take that money and then buy a boil-off compressor. We have to use the money for what it's intended for.

The primary reason was for our distribution department where we can't anticipate exactly how we're going to spend money within that department. We don't know when we have a cast iron main break or even a break somewhere in the City, we're not sure that's going to be a six-inch, an eight-inch, a larger diameter. We have certain budgeted amounts in those categories, but invariably the amount that we budget may differ from the amount we actually replace. So we asked for the authority to move within those line items, and that was really the intent.

COUNCILMAN O'NEILL: That authority is in the Gas Commission to give you?

MR. WHITE: Yes. As I understand it, the City Council has provided that to the

Gas Commission.

COUNCILMAN O'NEILL: This is the end of March '04. Council is getting ready to deliberate the City's Capital Budget for '05, which is our normal time frame. We'll have to pass it by the end of May, '05, starting July 1, '04. How come we are behind -- and this is not the first time. We're behind on the PGW Capital Budget by almost a year in terms of that fiscal year process that we do with the City.

MR. WHITE: I would say that it's a phenomena that's occurred over the last couple of years, and we have to return to a March 1st filing with the Gas Commission. We intend to do that next year. We went through a period of time where we did a consolidated budget where we tried to consolidated both the Operating and Capital Budgets. And the company was unable to meet certain targeted filing dates due to the fact that we're in the middle of the operating season and the complexities of the budget process. But we believe with the flexibility that we have with the line item transfer capability and we believe that with the recognition that we enter the fiscal year with an approved budget, that we will be filing the '05 budget March 1st of next year, and we intend to submit this year -- I'm sorry. The upcoming budget, we intend to submit to the Gas Commission by May 1st.

COUNCILMAN O'NEILL: May 1st of this year?

MR. WHITE: Yes.

COUNCILMAN O'NEILL: So the '06 you'll submit in March of '05.

MR. WHITE: That's correct.

COUNCILMAN O'NEILL: Okay, that's fine. Thank you.

COUNCILWOMAN BLACKWELL: The Chair notes that Councilman Cohen is here. Thank you.

Councilman Nutter.

COUNCILMAN NUTTER: Thank you, Madam Chair.

Mr. Knudsen, I wanted to ask you a couple questions, and then you made a statement which I'll acknowledge I was talking while you were talking, but I heard something in that legislator's third ear that caught my attention. I wrote it down, I need to come back to it.

Councilwoman Tasco went through a list of recent borrowings. What is the total outstanding debt of PGW at this point?

MR. KNUDSEN: It's about a billion one.

COUNCILMAN NUTTER: A billion one?

MR. KNUDSEN: With the short-term debt included, yes.

COUNCILMAN NUTTER: What's the breakdown of the billion one between short-term and long-term?

MR. KNUDSEN: It's about 965 million long-term and about 125 or so million short-term.

COUNCILMAN NUTTER: So about 90 percent of your debt is long-term debt?

MR. KNUDSEN: Yes.

COUNCILMAN NUTTER: From time to time, the issue arises with regard to asset sales. That's been a topic of conversation from time to time with regard to the company, and it's been a recent topic of discussion -- not the general term "asset sales," I have not heard PGW say that in recent times.

Have you had any discussion or -- for instance, the 21st Century Review Forum on behalf of the Mayor did a significant amount of work in a variety of places. Have you had any discussions with anyone in recent times about possible asset sale involving PGW?

MR. KNUDSEN: I've had no discussions in the last 18, 24 months about the sale of PGW.

COUNCILMAN NUTTER: When was the last time you did have a discussion?

MR. KNUDSEN: When it was a current topic about two years ago at the time that the feasibility study was still underway and so forth.

COUNCILMAN NUTTER: And did you get a copy of the feasibility study?

MR. KNUDSEN: No, I did not.

COUNCILMAN NUTTER: You never

received a copy of the feasibility study?

MR. KNUDSEN: No, I did not.

COUNCILMAN NUTTER: The study was about PGW, right?

MR. KNUDSEN: It was conducted for and by the Finance Department. We were interviewed, but there was no real reason for me to see the study. No action was taken on it.

COUNCILMAN NUTTER: Okay. You mentioned the $45 million, again, I think the outstanding loan in the context of one of your responses to Councilwoman Tasco. When was that initial forwarding of funds or technically filing of funds?

MR. KNUDSEN: January of 2001. If you recall, in the winter of 2000-2001, we had a substantial spike in the cost of gas. And because of the condition that the company was in at the time, we had no working capital, much as we are right now. And in that period the 45 million was advanced to us, it was then negotiated over a period of time for repayment in August of 2006.

COUNCILMAN NUTTER: So it's still the original $45 million still that's outstanding?

Have you made any --

MR. KNUDSEN: Well, understand it's in a fund where we make -- essentially, the money is segregated. And as we develop any kind of working capital, we pay down the note. The balance may go down to 20 or 25 or $30 million. We use it as a revolving credit kind of facility. But the nominal amount of the loan we can borrow up to at any one time is $45 million.

COUNCILMAN NUTTER: Do you ever actually anticipate repaying that loan?

MR. KNUDSEN: Well, as I said in my earlier comment, until last spring or last summer, I fully anticipated paying it. We had a full workout plan and we were on that plan. When the gas cost escalated last spring and summer and have continued since then, it's put that whole program at risk. My issue with the circumstance right now is that I think our customers need to pay. There's a lot of people who can pay, if not all of the bill, most of the bill; if not all of the bill, some of the bill. But we need to get the cash in the door. If we are able to obtain the funding that we need to operate from our customers in return for the services that we provide, we can stay on course. We've lost a year, year and a half, but we can stay on course.

COUNCILMAN NUTTER: In response to one of the questions, I believe again, from Councilwoman Tasco -- and I don't know what the question was and I also don't know what the beginning of the answer was, but what I took down was -- maybe you'll recall -- "there was no answer to this problem."

What question was that in response to?

MR. KNUDSEN: What I said was that if people don't pay their bill -- Councilwoman Tasco was asking about the financial workout, how were we going to not incur all of this debt going forward. If people don't pay their bills, we've got a very basic problem; we don't have a business. At some point we have to make sure that people who are responsible and incur these obligations pay for them. So that was when I made that statement. It was in the event that our customers absolutely would not pay or did not pay that there was no real answer to this problem other than bankruptcy.

COUNCILMAN NUTTER: What happens in that scenario?

MR. KNUDSEN: Well, I don't know that it can get to that position. Somewhere along the line we will have to shrink the company substantially and provide core services to the point where people pay enough that we can keep this system alive. But we're talking serious stuff here because I don't know where the funds will come for PGW. We are -- we provide a substantial service to this community in providing gas to a whole host of people who cannot afford it on some level.

COUNCILMAN NUTTER: Okay, we can pick that back up in the Transportation and

Public Utilities.

Let me ask you about a replacement question. I don't know whether it was yourself or Mr. White. You said you have a 1 percent per year replacement program?

MR. WHITE: Yes. Our Capital Program pertaining to our cast iron main replacement, we do it in accordance with best practices, and best practices calls for companies with the sizable inventory that we have of cast iron to replace it at a minimum of at least 1 percent. And of course, you want to establish that 1 percent at a point in time so that the timing which you remove cast iron isn't infinite. So right now we're at around 1700 miles and we're replacing 18 miles a year. So we're a little over 1 percent being replaced a year.

COUNCILMAN NUTTER: What's the average -- what's the current average life of the system?

MR. WHITE: Well, some of this pipe is well beyond it's accounting useful life. But if it's undisturbed, cast iron will last --

COUNCILMAN NUTTER: How about its operating useful life?

MR. WHITE: It's operating useful life if left undisturbed can go for many, many years. What we're doing, as we're targeting those sections of the pipe --

COUNCILMAN NUTTER: Can you modify a little bit beyond many, many?

MR. WHITE: Some of the cast iron has probably been in the ground since 1850.

COUNCILMAN NUTTER: Still today?

MR. WHITE: Yes, still today. Some of it is that old.

COUNCILMAN NUTTER: How much of the system is that old?

MR. WHITE: I wouldn't be able to answer that. I'd have to get back to you on that. I certainly can tell you that the pipe that is typically the older pipe that we would not have remove that we don't have as much of a problem with would be your larger diameter cast iron. There's less risk with large diameter because it can bear the weight of pipe if it gets undermined. The smaller diameter pipe, of course, if it's undermined in any way, certainly, that's where you run into problems.

COUNCILMAN NUTTER: Okay. I'll come back. Thank you.

COUNCILWOMAN BLACKWELL: The Chair notes that -- Councilman Rizzo wants a follow question. And we also thank Councilman Kenney for being here.

Councilman Rizzo.

COUNCILMAN RIZZO: Thank you, Madam Chair. Mr. White, you indicated that when I believe it was Councilwoman Blackwell asked about land acquisition that you're looking to purchase a piece of land from the Franklin Smelting property?

THE WITNESS: Yes, sir.

COUNCILMAN RIZZO: Are you aware that the slag pile at that site is a Superfund location?

MR. WHITE: Yes, sir. But that piece of land where the slag pile is, that's on the other side of -- I believe it's Venango

Street. We're talking about just the small piece of the Franklin Smelting property that encroaches in the area of the Philadelphia Gas Works.

COUNCILMAN RIZZO: So PGW is not going to buy a Superfund site?

MR. WHITE: No. But certainly that particular facility had significant issues over the course of time, but clean-up has occurred.

COUNCILMAN RIZZO: Well, I'd be interested because the Franklin Company's telling the federal government that they don't have the wherewithal to clean that site up, so I'd like to know who you're negotiating with because they're suggesting that these folks aren't even around to be responsible for that clean-up. So I would really like to find out because I would love to go after some of that money the minute that they're selling something. So could you help me with that?

MR. WHITE: Yes. My understanding is that Franklin Smelting isn't in the picture here at all. It's the PIDC, Philadelphia

Industrial Development Corporation, that owns the property. And the Philadelphia Industrial Development Corporation has an obligation to sell the property, as I understand it, at the best fair market price. And we are in the process of negotiating what we believe is an appropriate fair market price for a piece of property in the condition that that's in.

COUNCILMAN RIZZO: And it's not contiguous with the location where the present slag pile is tarped and fenced?

MR. WHITE: That's correct.

COUNCILMAN RIZZO: Thank you.

Thank you, Madam Chair. I appreciate that.

Is it an appropriate time to ask a quick question about the collection policy? Could I do that right now?

Mr. Knudsen, could you explain the process that PGW follows? I believe the process that you follow, and correct me if I'm wrong, is different than other gas utility companies. How I understood, as an example, PECO Energy -- and I'm doing this from memory now. That if a person doesn't pay their bill, that April 1 comes around, the service is terminated. The service is not restored even when winter approaches if they don't pay their bill.

I understand that PGW will reestablish the service like I just described if the customer doesn't pay their bill when winter comes. Are you following the same policies that other gas utility companies, or do we do something different here?

MR. KNUDSEN: Councilman, we follow the same policies that are provided for all utilities in Pennsylvania. It's known as Chapter 56 and it's the Rules of the Pennsylvania Public Utility Commission.

COUNCILMAN RIZZO: So if a person right now is turned off when the moratorium is over -- April 1, is it?

MR. KNUDSEN: April 1.

COUNCILMAN RIZZO: The whole summer goes by, they're off, their service is off. They haven't paid a dime. You put them back on?

MR. KNUDSEN: No. The regulations or the process calls for our never turning them on if they do not approach the company for a payment arrangement, some way of paying down whatever the accrued bill is and maintain themselves currently going forward. Then we're in a position to turn them on according with the regulations. If they never make a payment, if they never approach us, they stay off for the entire winter.

COUNCILMAN RIZZO: Well, what I understand is maybe we do something a little different than you just described. I've been led to believe that there are customers that are shut off in April, that somehow without paying one dime are restored when the winter heating season is upon us. Are you telling me that if a person doesn't make any arrangement and isn't paying that they are not put back on?

MR. KNUDSEN: That is the policy. They have to make some arrangement with the company for some kind of payment on some sort of going-forward basis or they don't get turned off.

COUNCILMAN RIZZO: What if between April 1, October, November, they've made an arrangement but they haven't kept the arrangement?

MR. KNUDSEN: There is the circumstance that people who may make an arrangement and break the arrangement in such a way that the process -- there are six steps to termination. They take a number of weeks. If they make an agreement and break the payment in a time frame that they can get to December 1st before we can turn them off, according to the rules and regulations, then they are on the system until the end of March. Yes, that circumstance can evolve.

COUNCILMAN RIZZO: I'll be honest. Many people that I've talked to from other utilities blame our policies like you just described as part of you digging yourself in deeper and deeper and deeper every year.

You as an executive of this company, top executive, you don't think you could fix this by working on these policies that you just described, the loopholes and the way people manipulate the system? Because when people know that the minute winter comes that they're going to be reinstated, you don't give them much of an incentive to pay their bill.

MR. KNUDSEN: Councilman, we are more sensitive to the issue here. Let me say two things, the winter moratorium being the most troublesome of all of this. It is not a Pennsylvania-alone policy. Winter moratoriums apply basically in most cold weather states. So we're not alone in this. And I think the theory that gave rise to a moratorium was a good one. I mean, it basically said there were certain people who are going to get strapped financially or by circumstance and we need to make it that they can keep warm in their homes until they can get themselves back on their feet, presumably by the end of the winter. The difficulty is that those theories were first presented some decades ago.

To answer your question about me as an executive, I am very instrumental in the Energy Association of Pennsylvania. We are trying very hard to get some of these policies through the Association because no one utility really can effect this by themselves to bring to the attention of the powers that be that some of these processes and policies don't work anymore or they work to the detriment of the utility as an enterprise and to the detriment to many of the customers who pay their bills.

COUNCILMAN RIZZO: Am I hearing you say that these policies that allow people -- the scenario that I would like to hear -- and again, the people that you can't truly pay is one issue and people that play the system is another issue. What I would like to hear eventually happen is when a person is shut off on April 1st, that they better start thinking about paying the bill, proving the fact that they can't pay or prepare to move in with a friend or family member and the service not be restored.

I also heard that there are situations where people bypass meters and get themselves back on with very little -- with the automatic meter now -- very little observation by the utility and it's rare you even know when a person is stealing gas because you're not making many premise visits, et cetera, to identify that. So I don't know how much that contributes. I don't think that many people are stupid enough or sophisticated enough to bypass a meter because it's very dangerous to do. But it just amazes me that we have a policy that people have learned to play the game and we haven't been able to counter with something to prevent what we've been talking about for the last few minutes here. It just seems to me like there is a way to fix it if somebody truly wants to.

MR. KNUDSEN: If I may, I'll respond on three points. The first is that we are poised to send out termination notices -- are you ready for this -- 130,000 customers starting April 1st over a number of weeks moving forward. In the last two years combined, we ended up shutting off, literally terminating service for close to 60,000 customers. In that two-year period, we've also come to a point where 6,000 never went back on the system. So we're taking the necessary action, but there's a real issue, there's a humanitarian issue at some point as to how far we continue with this. But we are being very aggressive this year. We were aggressive last year, but even more so for a whole host of reasons, including the financial problems we're in, to redeploy forces within the company to collect the money; and if we can't collect the money, to shut people off; and if we can't get in their homes, to dig them up and do it from the street. We are very, very serious about saving this company. And the only way we can do that is to make it important to our customers who historically haven't paid to come forward and pay their bills.

COUNCILMAN RIZZO: Thank you, Madam Chair. I'll go further our next hearing. Thank you, Madam Chair.

COUNCILWOMAN BLACKWELL: Thank you.

The Chair notes the presence of Darrell Clarke and of our Council President

Anna Verna.

Let me ask you, Mr. Knudsen, when does the moratorium start? Is it December?

MR. KNUDSEN: December 1st.

COUNCILWOMAN BLACKWELL: And I've been around long enough to know that I believe moratoriums some years ago was October. Now we're all the way to December.

And let me say that the only solution for these kinds of problems is more employment. You have a minority of people in anything who try to, quote/unquote, hustle the system. But for the most part, as you know, people can't afford to pay. Anytime 50 percent of people are under some payment agreement are not paying, then it means that we have employment issues and people can't afford to pay. So I say that for the record so that the record will reflect not everybody is about trying to get money from people who don't have it. I don't want to hear about us having problems that we don't hear anymore, about people on fires or using kerosine heaters or otherwise having maladies that occur or loss of life because people don't have gas. So I know this is a big issue. All of us certainly want to save PGW. But at the same token, we have to understand that it takes money to pay bills. And, as you admitted, our gas bills have gone up 50 percent. If my bill is high and I earn money, I know what it is for the next person who doesn't. So we have to be mindful of that as well.

The Chair recognizes Councilman Goode and then Councilman Mariano.

COUNCILMAN GOODE: Thank you, Madam Chair.

Good afternoon, Mr. Knudsen.

MR. KNUDSEN: Good afternoon, sir.

COUNCILMAN GOODE: At this hearing or at the next hearing, do you expect PFMC to testify? Or is anyone here present from PFMC?

MR. KNUDSEN: I don't expect anyone to testify, and we have board member here, yes.

COUNCILMAN GOODE: Would you say the Number 1 challenge for PGW in terms of turning it around or coming on better financial footing is collection efforts?

MR. KNUDSEN: No question. It is our Number 1 priority.

COUNCILMAN GOODE: Do you think you're at all hindered by your structure in terms of those collections efforts, in other words, the fact that you are a quasi-governmental non-profit?

MR. KNUDSEN: No.

COUNCILMAN GOODE: How many of your counterparts around the nation are structured similarly?

MR. KNUDSEN: Well, there are about 600 municipal utilities of various sizes of which we're the largest. We're the only sizable utility in the State of Pennsylvania that's under the Pennsylvania Public Utility Commission.

COUNCILMAN GOODE: How many are municipally owned?

MR. KNUDSEN: Within the State of Pennsylvania?

Well, there's really only two of any

size.

Oh, I'm sorry. In the nation? No, there's 650. I can confirm about that number, but it's about that.

COUNCILMAN GOODE: Within the top 10 cities, there are two?

MR. KNUDSEN: No, of the top 10 cities there are -- there are two in Pennsylvania. Probably 8 or 10 that are reasonably sizable; Memphis, San Antonio, us, a few others.

COUNCILMAN GOODE: Within the top 10, just Philadelphia and San Antonio?

MR. KNUDSEN: I'm sorry?

COUNCILMAN GOODE: Within the top 10, just Philadelphia and San Antonio?

MR. KNUDSEN: No. I'm saying that the top 10 of the nation would include Memphis, Philadelphia, San Antonio, Colorado Springs. There are a number of larger cities that have municipal systems.

COUNCILMAN GOODE: When was the last time PGW or its predecessors were in this type of financial operational crisis?

MR. KNUDSEN: Well, the last time -- the most parallel time was in the fall and moving into the winter of 2000-2001.

COUNCILMAN GOODE: I'm really speaking before that period. In the history of PGW, I'm really looping all of that within the four or five years as the same crisis.

MR. KNUDSEN: Well, I don't think PGW -- well, there's two answers to this. One was that the rates for PGW were incredibly stable from about 1987 through 2003 or 2002. They averaged about $900 a family. The issue was that at certain points in the late 1990s when the company should have requested a rate increase, it didn't happen. And --

COUNCILMAN GOODE: My question really is before that period.

MR. KNUDSEN: I don't know.

COUNCILMAN GOODE: My research tells me that it was 1897.

MR. KNUDSEN: That may be.

COUNCILMAN GOODE: And that in 1897 is when the City decided to move into its arrangements with UGI.

Do you think at this point it was talked about selling PGW?

The issue was raised years ago. The issue is being raised again and will continually be raised. At that point in 1897, the same issue was raised and there were no buyers. But what did happen was it was placed under a private, I believe, for-profit management contract.

Do you believe there's any benefit whatsoever of having a for-profit management contract, not necessarily a sale, but having for-profit managers in place?

MR. KNUDSEN: I don't mean this to be self-serving. I don't think that that kind of arrangement would be particularly beneficial in the sense that the rules that we all live under, unless those are changed, any successor management would have to live with the customer service rules that exist. I think we're doing a very credible job of working with those.

COUNCILMAN GOODE: I didn't raise it as a critique of your management capacity.

More so the fact that there is more incentive for a for-profit company if the Number 1 issue is actually collection efforts.

MR. KNUDSEN: Councilman, the issue is a social issue. I don't know that private management of PGW could solve what is essentially a social problem. As the Chairwoman just said, most of our customers or a great many of them don't have adequate incomes to support the rates.

COUNCILMAN GOODE: So you're suggesting that your collection efforts are not going to dramatically improve anytime soon?

MR. KNUDSEN: No, I'm suggesting that our collection efforts will improve and I'm hoping to the point where we are back to a point of stability.

COUNCILMAN GOODE: What will you do differently to improve your collection efforts?

If you're suggesting that creating a for-profit incentive would not do it, what will you do differently?

MR. KNUDSEN: Well, for example, when this problem surfaced for us last summer, I did what I would have done if I were a private manager. I sought out the advice of some of the best people who could advise us in collection practices. So we have for the last five months been revamping our entire operation to benchmark against the best that the industry has, align ourselves with best practices, and essentially gear ourselves so that when the moratorium comes off next week, we're ready to go. The folks that I have retained to advise us would have given the same advice whether I was a private manager or the fact that I'm public manager.

COUNCILMAN GOODE: Short of a for-profit management contract, do you have for-profit collection efforts underway?

MR. KNUDSEN: Yes. We are in the process right now of very actively writing off the accounts that we're not able to collect and placing them with collection agencies who are for-profit. And then to the extent they can't collect, we're in the position of selling the receivable.

COUNCILMAN GOODE: What percentage of your collection is for-profit?

MR. KNUDSEN: Well, it's hard to frame it because what's out with these agencies right now is really older paper. I think we have -- let me just check a second. We presently have about $200 million with private interests trying to get the money either from the customers -- basically trying to get it from the customers.

COUNCILMAN GOODE: What percentage does that represent of your total collections.

MR. KNUDSEN: Well, that represents maybe -- I'm trying to think about our gross receivable. It's probably about three months of operation. It's about a third of our receivable.

COUNCILMAN GOODE: And so do you see any benefit to creating further profit incentive in terms of expanding your collection efforts?

MR. KNUDSEN: Could I outsource more and do something --

COUNCILMAN GOODE: Could you outsource more and get more back if you create a for-profit incentive?

MR. KNUDSEN: We're looking at that right now. It's a complicated question for us. But, yes, we're looking at some additional outsourcing.

The difficulty is that we have done a very good job of training our folks to the point where they're doing as good in terms of contacting customers, making the phone calls productivity levels as some of the private companies that we're looking at, so it's not a simple answer. But we are looking at any time that we can find a higher level of productivity at a cheaper price, we're going for it.

COUNCILMAN GOODE: But I can tell you, that was the response of a public manager rather than a private manager. I don't think a private manager is concerned about developing in-house capacity unless somehow it deals with profit motive. And right now what we're talking about is enhancing collection efforts. And either you can enhance collection efforts by employing a for-profit incentive or you can't. And if those efforts are better served that way, then more of those efforts should be directed toward a for-profit incentive.

MR. KNUDSEN: Let me answer this way. Right now, we are looking at every opportunity, not only in collections but in other areas of the company as well, we are gauging what we can do best in-house. And there are certain things that we do better than the industry, than you could outsource or you could have others do. But we're looking across the company right now at every opportunity we can to potential effect greater economies.

COUNCILMAN GOODE: I am really focused on collections, though.

MR. KNUDSEN: All right. Fine.

COUNCILMAN GOODE: Are you satisfied that more should not be outsourced with a for-profit incentive?

MR. KNUDSEN: I'm not satisfied with

that, and we are looking at additional opportunities, yes. I'm just simply saying it's not a simple process for us.

COUNCILMAN GOODE: Thank you, Madam Chair.

COUNCILWOMAN BLACKWELL: You're welcome.

Councilman Mariano.

After Councilman Mariano, Councilman Clarke and then Councilman Cohen.

COUNCILMAN MARIANO: Thank you, Madam Chair.

Mr. Knudsen, a little bit on what Councilman Rizzo asked you and a little bit with Councilwoman Blackwell. Despite the economic problems, more like a public safety, if I understand the way you answered Councilman Rizzo, if someone gets their gas turned off and they never apply again, they don't come in and try to make some kind of payment program, it just stays off?

MR. KNUDSEN: Yes.

COUNCILMAN MARIANO: Does anybody for safety-wise ever go around that house like maybe December or January figuring, if there's people in this house and it's obvious because the electric meter's probably turning so there's other utilities and the water bills, does anybody go around and say, "Well, how are they heating this house now? Are they doing it with coal all of a sudden? Are they doing it with fire?" Do we follow-up ever anymore? Or does it become a catch 22 where you've got to hire more people to do that?

MR. WHITE: Councilman, we don't follow-up to see whether there's an alternate use. We do do a winter survey as required by the PUC of all people that are off. And we try to see during that winter survey what other forms of energy they may be using. But, of course, during the year, if we've turned someone off, we have the automatic meter reading trucks that are still circling the City or running through the City identifying whether there's been self-turn-ons or things of that nature. So there's different ways to handle that as well.

COUNCILMAN MARIANO: Does the

automatic meter reading truck, that can tell if somebody --

MR. WHITE: Sure. If the meter index changes, we can determine that the actual gas --

COUNCILMAN MARIANO: If you come in a house and you do a turn-off inside, not out at the curb, you don't take the meter reader out?

MR. WHITE: No, sir.

COUNCILMAN MARIANO: So if I side step that and put a flexible pipe like any plumber knows how to do --

MR. WHITE: Well, if you illegally put a bypass on, I will not know that from outside the house.

COUNCILMAN MARIANO: Then there's a public safety issue, which is what I'm getting at. Do we try to find out? Like, "Hey, wait a second. You're going in that house; how are you heating it?"

It may be labor intensive, but it's public safety. If there's 50 percent of the people who aren't paying their bills -- I'm not going to take the economic part because that's been taken care of here for now. But public safety-wise, is there some reason or don't we have some kind of ethical responsibility to find out are these people dying in the houses, are they freezing? That's a concern. And the other concern is, are they going to blow the rest of the block up because some, for lack of a better word, half-ass plumber does the hook-up?

MR. WHITE: I'll answer the first part of that. I'd submit to you that people who have an illegal bypass, the chances of them letting us in the property willingly is probably nonexistent. Now, there are occasions where other things happen within the property that create access. Once we get access, of course, if we spot an illegal bypass, we shut the gas off.

COUNCILMAN MARIANO: If I call you and say, "This address, I have a strong suspicion that they have an illegal hook-up," do you follow up, coming from a City Councilman's office.

MR. WHITE: We have a meter investigation unit and we follow up on all tips.

COUNCILMAN MARIANO: Even if it's a unanimous tip on the line?

MR. WHITE: My understanding is we follow up on all tips.

COUNCILMAN MARIANO: Could you explain follow-up?

MR. WHITE: We will make a visit to the property.

COUNCILMAN MARIANO: I don't answer the door because I'm a scammer anyhow and I know how the little hook-ups are. I pretend -- whoever's at the door, it's not for me. What process do we go through? Do we check that off and go somewhere else?

MR. WHITE: Well, if I cannot get in the property and I have no indication that gas is being used in the property, at that point I have no recourse.

COUNCILMAN MARIANO: Do we go back and look at the records? Possibly it's a rental property and someone else owns it and we call that someone to say, "You know, we really need to get in your property, Mr. Mariano, because we suspect one of your tenants hasn't been using any gas for three years and we want to know how it's heated. And since you do own the property and if it explodes and burns down the whole block, you may be liable."

I suspect that landlord -- I'm not trying to jackpot you here. This is public safety-wise. I understand your job is sort of like being the captain of the Titanic. You're captain, but it's still the Titanic. So I don't play the jackpot thing.

MR. WHITE: I understand what you're saying. Certainly, if we can get access, we will. There are people that will game us, and we know that.

COUNCILMAN MARIANO: But where do we stop? We can go back for 10 minutes here, but if there's a strong suspicion that one of us tells you, there should be no stopping. If you have to stand outside at night and run in the door when somebody comes in, for lack of better words, to see if there's gas being operated, that could save a lot of lives.

MR. WHITE: I would submit that our people are very experienced and very creative and they will look at any evidence that they can come up with through records, whether it be, in your example, a landlord. And in those circumstances, with a landlord, if the landlord gives us access to the property, certainly we'll get in there and we'll take care of that situation.

COUNCILMAN RIZZO: Point of information.

Mr. White, when you have a customer, a residential customer that's been off for a year or two years, don't you think it's to the best interest of the utility to dig it up and shut it off so you know it can't be tampered with. I mean, there's the answer. Once you know that a customer's been off two, four, six, eight, ten months, I think you should invest in actually cutting off the service to the property to assure that a person -- if they haven't had gas for a year, it's unlikely that they're going to ask you to put it back in 13, 14 months. So to ensure that there's no theft of service or tampering with facilities, why don't you just cut the service?

MR. WHITE: Well, Councilman, that in point of fact is a Public Utility Commission requirement, and where resources limit us, obviously we have to prioritize safety first. But certainly, we get into situations where we are able to shut the service off at the curb. Certain situations do arise where a house where -- just to give you an example, last year we had a house that are very experienced personnel indicated that it was not inhabited, and in point of fact there was an individual in that house. And the gas was turned on by that individual and being used. So in turning the gas off, we actually put -- you know, there was an individual in the home that was actually without heat at that point. Albeit, they should not have had the gas on, but nevertheless we turned the gas off.

COUNCILMAN RIZZO: You'd be less in debt today if you shut it off at the curb.

MR. WHITE: We certainly would be. And in point of fact, we do have a requirement to terminate gas in vacant properties. And there are safety requirements and you are accurately pointing that out.

COUNCILMAN RIZZO: Well, there's Councilman Mariano's point.

Thank you for that point of order.

COUNCILMAN MARIANO: Thank you. That's all.

COUNCILWOMAN BLACKWELL: Thank you.

Councilman Clarke, would you wait a moment for Councilman DiCicco and then we'll call you? Thank you.

COUNCILMAN DICICCO: Thank you, Councilman Clark.

Good afternoon, gentlemen. I stepped out of the room for a few minutes, so hopefully the question I'm about to ask has not already been asked. And if it has been, I'll wait to read the record.

Concerning the collections, I

understand about 50 percent of the customers of PGW pay their bills, the other 50 percent are not paying.

MR. KNUDSEN: It's not fair to characterize it that way. What we've said is that half of our customers have difficulty paying. They don't necessarily pay regularly, they don't necessarily pay faithfully.

COUNCILMAN DICICCO: But 50 percent are paying regularly?

MR. KNUDSEN: That's correct.

COUNCILMAN DICICCO: What do other cities and municipalities -- what do they do that may be different than what we're doing?

I'm certain other municipalities, especially large cities, places that have a large population of poor people are faced with similar problems. Are they doing something any different than we are? And what is it that makes it different and why can't we be doing the same thing? I think they're just in the same situation that we're in.

MR. KNUDSEN: I think there's two answers to that question. The first is that

Philadelphia is somewhat unique -- Philadelphia Gas Works is somewhat unique in that we are both the City and the County and we do not have a large industrial base, a large commercial base, nor do we have any opportunity to grow the system beyond sort of the physical restraints that we're under such as other utilities do. Baltimore has the, not only the City of Philadelphia, but the environs. New York, much the same. Boston much the same. We're one of the few utilities that is really land locked in a sense.

Where these utilities have both the opportunity for growth as well as having larger customers, this burden is shared with these other customers. It is allowed regulatory process to do that. We can't do that. And with a loss of industry, with a loss of large load with our inability to grow the system -- and I'll get a plug in here. I think PGW doesn't get a fair shake at bidding on some of the larger projects in town. We want to be at that table early. But be that as it may, PGW has a unique set of issues in that regard. That's Point 1

Point 2 is, some of the cities and some of the states have supplementary programs that -- and I'll have to get you a list of those. For example, Pennsylvania and Massachusetts are the only cold weather states that don't contribute to the LIHEAP funding of some sort. Some of the cities have mechanisms to provide supplemental income for these purposes, to the customers who aren't paying. But I can get you better -- I'll provide you with a listing of some of these alternatives.

But that's generally what's going on. I mean, most utilities are able to share the burden of their uncollectible.

Now that being said, there is a rising concern, certainly in Pennsylvania right now, with the other local distribution companies, the other gas companies, that their percentages of uncollectible are rising. Now, they're nothing like our 8 or 10 or 12 percent. But where they were maybe a half percent or a percent, 10, 15 years ago, they're inching up to 2, 3 percent. Some of them have gone to 5 percent in the Pittsburgh area. So this is not necessarily a Philadelphia-only problem. And that's a theme that I'll come back to in the next hearing. This is a growing issue across the country and certainly across Pennsylvania right now.

COUNCILMAN DICICCO: My final question. When you compare the payments that are made for the utility of PGW for gas, compared to the other utilities that your customer base is entitled to and has access to, electric bills, cable TV, whatever, where do you fit in on that list in terms of who gets paid first?

MR. KNUDSEN: We're at the bottom. Well, I think generally our sense of this is that it goes maybe phone, electric, cable, water, gas.

And the difficulty, Councilman, is -- and we've had a lot of discussion about this inside the company -- that there's a culture that goes back not a few years but many, many, many years that somehow gas is a free good to some people in this town. And we're in that position of now meeting that problem head-on because the bills have gotten so high that it can no longer be tolerated. It was tolerated for many, many years. It was clear that that was the problem. But now it's not tolerable.

COUNCILMAN DICICCO: Maybe you should somehow figure out how to become a subsidiary of Comcast and then the billing would be combined.

(Laughter.)

COUNCILMAN DICICCO: Very interesting. So you're at the bottom of the list when it comes to payment, generally speaking?

MR. KNUDSEN: That's our sense of what -- that's what we get anecdotally when we're trying to determine what some of these priorities are in some of our survey work. That's the kind of sense that we're getting. This isn't a scientific determination, but we're not far off.

COUNCILMAN DICICCO: Thank you.

Thank you, Madam Chair, and thank

you, Councilman Clark.

COUNCILWOMAN BLACKWELL: You're welcome.

Councilman Clarke.

COUNCILMAN CLARKE: Thank you, Madam Chair.

Good afternoon, gentlemen.

MR. KNUDSEN: Good afternoon, sir.

COUNCILMAN CLARKE: Let me ask a couple of questions. I think I was walking in the room when you were talking national policy so I don't know to what degree you discussed the issue.

MR. KNUDSEN: We haven't discussed it. We were sort of saving it for the second session.

COUNCILMAN CLARKE: The second session today?

MR. KNUDSEN: I think so, yes.

COUNCILWOMAN BLACKWELL: Yes, we're still on the Capital Project and the senior discount. As soon as this testimony is completed, we'll recess for Councilman Nutter's Transportation and Public Utilities

Committee.

COUNCILMAN CLARKE: I'm going to have to leave City Hall shortly. I can't ask those questions now, Madam Chair?

COUNCILWOMAN BLACKWELL: Certainly, Councilman.

COUNCILMAN CLARKE: Thank you.

First of all, I just want to get some clarity. While I've heard you discuss various issues in terms of what needed to be done to make this a more healthier company, not even suggesting that in any way, shape or form it can be a profitable company. You talked about increasing collections. And the conversations the other day with you, you talked about conservation efforts. But at the end of day -- and I believe to some degree we're essentially playing a shell game. We're moving money around, we're moving priorities around. But at the end of the day, I just think that the affordability of gas is to the point where people just simply can't pay. Are there deadbeats; absolutely. Do people have their priorities skewed; absolutely. But at the end of the day, there are truly people out there who just cannot afford to pay. I don't believe that you have 130,000 shut-off notices and at least half of those people, probably more, just can't pay regardless of their priorities. Would you agree with that?

MR. KNUDSEN: I would agree with that.

COUNCILMAN CLARKE: And I think if you look at the correlation on a national level and international level, an increased cost of gas versus the increase in shut-off notices, you'll see a direct link, I would assume.

MR. KNUDSEN: There is a correlation, yes.

COUNCILMAN CLARKE: In our conversation yesterday, we talked about -- excuse me for getting a little frustrated with the whole issue in the meeting yesterday, because at some point you just get tired of hearing the same old thing year after year, and understanding that on a national level there probably needs to be some readjustment on our policies. And you talked about the fact that a number of caches of natural gas are drying up as we speak. As a result of that, people are essentially getting as much out of the public as they can while they still have that natural commodity left.

One of the things that I want to get on the record today is from an Administration's perspective and policy and understanding that the City's position as it relates to our ability to regulate rates and have some jurisdiction over the company has been diminished with the takeover to PUC. I guess what I want to know is what are we doing, first of all, you or us, as a company to, first of all, educate people?

Because I think we agree -- we talked about that yesterday, that the average citizen believes that when the gas bill goes up, their perception is it's just simply the government and PGW gouging people and they don't really view it from a national perspective that there's a policy that obviously needs to be changed.

What we're doing today and prior to today and probably subsequent to today, we're going to be talking about moving pieces of the pie. But at the end of the day, this commodity is going off the roof and something needs to be done.

What is the company going to do, what should the government do to effect national policy?

I just don't believe we can continue along this path.

What are we doing? I mean, I know we hire lobbyists for casino gaming, we hire lobbyists for other issues related to our ability to get some relief on a state and federal level. What are we doing on this issue?

MR. KNUDSEN: I think there's a couple of things that are more local. The Energy Association of Pennsylvania, it represents gas companies and electrics, has taken the position that there ought to be more in-state drilling for natural gas. There are relatively substantial reserves of gas still in Pennsylvania. And the question is how you do that and so forth. So that has been a proposal of the Energy Association, or bringing that to public attention that this is an option.

COUNCILMAN CLARKE: Walk me through this process. I'm assuming that the federal level, they set national policy.

MR. KNUDSEN: Yes.

COUNCILMAN CLARKE: Do they regulate the State's ability or the utility's ability within the state to get natural resources, to drill for gas? Or is that done on a federal level?

If the State of Pennsylvania decided, all the municipalities decided that it would be to our best interest --

MR. KNUDSEN: There would be no restriction on anybody drilling for gas in Pennsylvania. It's really a question of state regulation or priorities. For example, some of it is state land and will you drill on state land, so that has to be a change of public policy, allow drilling to occur in certain areas that are off bounds right now. But there would be no restraint on drilling that I know of in the state once the state authorities were to allow that to happen. And that's a conversation that the Energy Association is trying to encourage right now.

At the federal level, there are clearly policies that are articulated and formulated that affect us.

And what Councilman Clarke and I are discussing is a conversation we had in his office yesterday.

There are two contravening public policies or counter-indicated public policies. One is a policy that is constraining the supply of gas, the drilling for gas, the increasing the amount of gas available for customers. And on the other side, there's a policy that says, "We want to use natural gas for all new electric generation." Every generating plant, electric plant that's come on line since, I think, 1998 has been natural gas driven. Well, that has created an enormous difficulty for us. And what it does is it's raised the price of gas across the board. So without supply and with more demand, the price of gas has gone up. And that's why we're living right now with the situation as it is. Now, will this go on for a couple years? Yes. Will it adjust down? We hope so.

COUNCILMAN CLARKE: So is our ability to impact on the national policy solely this particular -- what was the name of the state organization?

MR. KNUDSEN: The Energy Association. No. There are other groups that are very actively involved in this. The American Gas Association, and in capacity as CEO, I was invited to join that Board, are very active in attempting to bring these problems to the attention of federal legislators, both the House and Senate, and have been relatively successful at it.

I think the great tragedy right now is that the energy bill, which has been under development for several years, looks like it will not go forward and therefore some of

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issues have been set back for a while.

COUNCILMAN CLARKE: Are you coordinating your efforts with the citizens of the state and the nation? Are you guys just kind of going along or are you educating the public to get them on board?

I mean, at the end of day, this is a presidential year. We're talking about a federal policy. And my concern that the average citizen is not educated enough to understand the implications of the federal policy as it relates to our ability locally to provide affordable energy to people. And if we don't have our people engaged in the process, I think it will be much more difficult to make an impact on those decisions.

MR. KNUDSEN: To answer your question specifically, both the major national organizations that are involved with this question, the American Gas Association and the American Public Gas Association, both of which we have roles in and have exerted whatever influence we had to make these things happen, both of them are actively engaged in both the education process and the lobbying process. Within the state, the Energy Association of Pennsylvania has been very responsive to this set of problems, as has the Public Utility Commission. They understand the problem that supply shortage has created for many of the utilities, and PGW in the extreme.

Our problems are not different from other utilities. We just have more of them, more of the same issues.

COUNCILMAN CLARKE: Can you do me a favor? Can you provide, through the Chair, the pertinent agencies or groups that are engaged in this lobbying effort? I'd like to get involved and at least have some of my constituents involved in the process.

MR. KNUDSEN: I can certainly do that.

COUNCILMAN CLARKE: Thank you.

Madam Chair, thank you. Thank you for accommodating my need to ask those questions now.

COUNCILWOMAN BLACKWELL: Thank you

very much.

Councilman O'Neill and then Councilman Cohen. And Councilman Kenney you have a question too?

COUNCILMAN KENNEY: Yes.

COUNCILWOMAN BLACKWELL: Councilman O'Neill.

COUNCILMAN O'NEILL: Mr. Knudsen, you mentioned at the briefing that just a few years ago you had 20 distributors or so that you used to buy gas from?

MR. KNUDSEN: I think it was like 28 suppliers.

COUNCILMAN O'NEILL: And you're now down two or three or four.

MR. KNUDSEN: Mr. white can answer that better.

MR. WHITE: Actually during the course of a year, we may buy from over 40 or 50 different suppliers. We look for a significant amount of our supply for the winter operating season, which is typically December through March where you have your cold temperatures and heating demand. We had a significant drop-off in the number of suppliers that were interested in serving markets like PGW's. You know, there's a variety of reasons for that. But certainly, we're doing everything we can to stimulate additional interest in dealing with PGW. To date, we believe it has impacted us in a negative way, but it could very easily impact us if the number of suppliers were to drop to a smaller level. Right now there's still plenty of competition.

COUNCILMAN O'NEILL: Is that because nobody's buying gas any cheaper than you?

MR. WHITE: I'm not sure I understand the question.

COUNCILMAN O'NEILL: Is anybody selling gas any cheaper than your more limited number of suppliers?

To me, it would seem that a lot of people are avoiding you, it's almost red lining because they think we have financial problems or something like that.

MR. WHITE: Well, obviously, there are risk assessments of PGW and people have limitations on how much they will sell to PGW, and it's usually a dollar amount. The problem we have run into is not PGW, per se. It's the fact that when the price went from $2.50 to $6, the amount of volume you could buy under, say, a $10 million risk level had now been reduced by more than 50 percent. So the amount of suppliers that were willing to sell you the same volume of supply aren't out there. They have a limited level of risk. And this also was exacerbated by post-Enron. So you've got a couple of things impacting here. You've got the post-Enron debacle, then you've got the increase in price which reduces the amount of volume you can buy for a particular level of risk.

A company, for instance, may have a $25 million risk profile with PGW. They would sell us $25 million at any one time --

COUNCILMAN O'NEILL: What's a risk profile? Could you explain that to us?

MR. WHITE: Sure. Just as many large companies have risk departments, they will assess what the assurance of payment and return on their investment would be. With PGW and other large utilities like Keyspan, PSE&G, South Jersey, there's a certain level that each individual supplier, a Hess, a Shell, a Texaco, may indicate as being a prudent purchasing level. Now, obviously, they look at PGW's financial condition when they set that. Certainly, with the combination of PGW's financial condition, the combination of prices going up, they're going to be able to sell less volume at a prescribed level of risk. For us, it may be 10 million; for PSE&G, it may be 50 million. Obviously, PSE&G can buy a lot more volume with that 50 million of access to that particular company. That doesn't necessarily mean that we'll buy from that company. They still have to provide it at the cheapest price. And we're doing lease cost purchasing, so we're buying the gas as cheaply as we can.

COUNCILMAN O'NEILL: Right, but not necessarily with the same market availability as maybe some of the ones you just mentioned, some of the other companies.

MR. WHITE: That's correct. But that, Councilman, has always been there. PSE&G has 1.5 million customers. We have 500,000 customers. There's an economy of scale there and so forth.

COUNCILMAN O'NEILL: But their debt might not be as serious as ours and some other things like you mentioned today, the collection factor isn't as serious.

MR. WHITE: That's correct.

COUNCILMAN O'NEILL: And I'm not beating on you, I'm just stating a fact I think that part of the reason gas is as expensive for us may be because we're PGW and you have all those other things going on.

Councilman Goode referred to the private factor; you, to the social responsibility and the like.

MR. WHITE: Councilman, I would point out that we file our gas cost recovery rate annually and on a quarterly basis, and we've historically been in the top 50 percent of the state. Right now, when we filed our last quarterly update, other than one of the very small companies in the state which is always considered an outlier, we were the third lowest priced, from the gas supply standpoint, in the state. Now, obviously, that changes from quarterly filing to quarterly filing, but we have not historically been below the 50 percent rate. We have been historically a good company from a purchasing standpoint even with some of these challenges that we have.

COUNCILMAN O'NEILL: I understand.

LIHEAP, a couple years ago when you were in here particularly with the loan in 2001, we were hitting on these issues, it became clear through your testimony that you were frustrated that a lot of people who were LIHEAP eligible weren't applying for it and there hadn't up to then been a policy of requiring or forcing or somehow getting people, however you did it, who are in the problem category, unable to pay, difficulty paying but clearly LIHEAP eligible, there were people who fit the LIHEAP profile were having other people pay for their gas because of the gas billing works at PGW and yet could have been having the federal government pay for their gas instead.

Are you still having -- I know you said in your testimony that you're a national model. But are you still having trouble getting LIHEAP eligible people to comply who fit into that other half? Could you explain?

MR. KNUDSEN: We do a good job of getting subscribers to LIHEAP. The problem that we run into is not that we have enough subscribers, it's the problem that there's only so much money. And this is a whole other argument and problem for us right now. I'll be very candid. We feel we don't -- how should I say this?

COUNCILMAN O'NEILL: Could you answer the first question now? Do you get everyone within that 50 percent category that's eligible for LIHEAP to apply for it?

MR. KNUDSEN: We don't get everybody, but we get enough.

COUNCILMAN O'NEILL: What's enough?

MR. KNUDSEN: I think we have 60,000

subscribers.

COUNCILMAN O'NEILL: 60,000 subscribe to LIHEAP?

MR. KNUDSEN: Yes.

COUNCILMAN O'NEILL: Out of how many? That's all I'm looking for. Out of how many that are eligible? That's what I'm trying to get.

MR. KNUDSEN: We think there's about 90,000 who could qualify for LIHEAP.

COUNCILMAN O'NEILL: So you get about two-thirds of those who qualify?

MR. KNUDSEN: Two-thirds would be about right.

I'm sorry, I didn't understand the question.

COUNCILMAN O'NEILL: Fine.

Councilman Goode mentioned along a line of questioning about UGI comparison and private companies in general.

Is it true that we have only begun very recently reporting people's credit who don't pay their bills to us?

You wouldn't believe how many people

assume that's an automatic like other bills you don't pay. Could you explain that?

MR. KNUDSEN: The issue for us was that once the computer system went bad in 1999-2000, we didn't have sufficiently accurate information that we could report the information to a credit agency. We are beyond that now, and we are in the process of reporting people to credit agencies now.

COUNCILMAN O'NEILL: Prior to 1999, you did?

MR. KNUDSEN: Yes.

COUNCILMAN O'NEILL: The last thing on the private company. You have 200 million or roughly one-third of your collectibles out with private companies, you said?

MR. KNUDSEN: That's right.

COUNCILMAN O'NEILL: Do private companies have an advantage in that, whether it's socially responsible or not, an advantage that they place liens on the real estate where possible? There's no liens placed?

MR. KNUDSEN: We do the liening.

COUNCILMAN O'NEILL: You do place

liens on properties?

MR. KNUDSEN: Oh, absolutely. We're very active with that. We're 250, 300 a week of liening. We're very active with that

COUNCILMAN O'NEILL: That's all I have.

COUNCILWOMAN BLACKWELL: Thank you.

Councilman Cohen.

COUNCILMAN COHEN: Thank you, Madam Chair.

COUNCILWOMAN BLACKWELL: You're welcome.

COUNCILMAN COHEN: Tell me, how much does LIHEAP help pay in terms of dollars?

MR. KNUDSEN: Councilman, in terms of the program, it depends on what the federal government and the state government allocate toward us. Over the last five years, for example, the amount of LIHEAP has varied from maybe 15 million to 22 million normally. And that really big year in 2001, we got 33 million. But by and large, it's about 15 to $20 million. In that event, people get about $300 per family of LIHEAP relief.

COUNCILMAN COHEN: Do you have any statistics with respect to what it is you actually get?

MR. KNUDSEN: Yes. I can provide those to you.

COUNCILMAN COHEN: And you think your $300 on the average is a fair estimate of LIHEAP receipts?

MR. KNUDSEN: Yes, I think that's a fair estimate for what the individual family receives, that's correct.

COUNCILMAN COHEN: And what would that be arithmetically if you multiply that by 50,000 families?

You indicated you thought there were about 50,000 families.

THE WITNESS: That's about $15 million, that's right, a little bit more than that.

COUNCILMAN COHEN: What is the total revenue of PGW?

MR. KNUDSEN: $800 million.

COUNCILMAN COHEN: So it would be a relatively small sum?

MR. KNUDSEN: That's correct.

COUNCILMAN COHEN: Let me go to another area. I happen to live in the area that was affected sharply by the fire at Ogontz and Olney. At some point, we learn bits and pieces as to what was happening when the flames sort of got out of control and they quieted down and we felt good and then they got out of control again. And we were told that the fire is being fed by gas. And we said in our naivety we said, "Well, why doesn't somebody turn the gas off?" And we were told, well, at the time this was installed, there was no way of turning it off and it's just a constant flow of gas into this area which was feeding the fire because it's such an old item. And ultimately it took a number of hours, and then they said, well, they did find a way to shut off the gas; otherwise, there was no way of controlling the fire.

Was that true, the report we had that we have such old equipment in which gas flows to a main center or some kind of center from which various houses get their gas and that the center receiving the gas from another source just gets it constantly and can't be turned off? Is that an accurate description of some equipment? Can you tell me, if it is so, about how old is that equipment and what's the problem throughout the City on that? Because that's a kind of frightening thing because we knew the fireman were fighting against the flames very hard for a number of hours and there was no progress.

MR. WHITE: Well, actually, Councilman, if I may, that was not an accurate statement. First of all, the pipe that was ruptured was a 20-inch cast iron main. That is the type of piping that we are most concerned about. It was hit by a backhoe operator. The valves that were able to turn that gas off were quite a distance away. So what you actually saw was the fact that you have a 20-inch diameter pipe was performing as a reservoir, and the gas that was coming out of the points from the two points where it was shut down was actually burning for quite some time.

I was in constant contact with Fire Commissioner Hairston. And at no time -- while the flames were burning, that was probably the safest position that we could be in. And then as we extinguished the fire, we extinguished it once we had reduced the pressure in the line down to a point where there was no risk to the public. So the reason it lasted as long as it did primarily was the fact that you had a lot of gas from the point where it was shut off at both ends and it was still burning that gas off.

COUNCILMAN COHEN: Do you think there's a risk throughout the rest of the City because of their use of the same kind of piping arrangement?

MR. WHITE: Well, we have 1700 miles of cast iron. And we have what we call a high pressure and a low pressure system. That pipe that was hit was part of our high pressure system. There aren't typically customers on high pressure lines. The high pressure lines actually feed the lower pressure customer lines. And in this case, that's why you didn't lose service in your home. We were able to continue to feed the low pressure lines by the fact that we have an integrated network of piping. So we were able to cordon off, so to speak, that one particular area of piping to ensure public safety and to ensure that we didn't lose gas service to you in your home.

COUNCILMAN COHEN: To make sure I understand you, could you give me a conclusion? Are you saying that that kind of piping is safe and people ought not to be concerned?

MR. WHITE: I would say people are not to be concerned because PGW is managing the system and removing the pipe that has the greatest risk. And we remove 18 miles a year of pipe. When you assume there's about 500 feet in a block, we're removing about 80 blocks a year of the riskiest main in the City of Philadelphia and replacing that with new main that has very little chance of any type of accident.

COUNCILMAN COHEN: All right, good. I may have to come back to you to make sure I understand it. I'm not absolutely clear. But you say that the problem was the accumulation of gas, not because there was no way of shutting it off, but it was safer to let it be used up by burning?

MR. WHITE: There were other reasons why we let it burn as long as we did. We had to make sure that the electric company didn't have facilities. We didn't want to put the firemen at risk. And Commissioner Hairston and I were in constant contact with the electric company. So there was some other things going on that precipitated the term of the fire or the length of time that the fire burned. But certainly, it was a safe situation.

COUNCILMAN COHEN: We were very impressed by how all the city agencies acted, and to the extent the Gas Works was involved in it, it did a good job. That gives me a good opportunity to then give you the other side.

Seems to me over the last few years I've gotten more complaints about lack of interest, coldness of replies to people calling in for service, whether they had a contract or didn't have a contract didn't matter. They'd be told kind of sharply that nobody can come out for two or three days. I know one weekend I couldn't believe it. I called in, I couldn't get a soul at the gas company who knew anything about anything. And I don't know, it's probably several years since Mr. Knudsen and I ever talked because I can never get through to him no matter what. I leave a message; I don't get a response. Or if I call him, I don't get a response. I had always had gotten responses before. And that seems to be very close to the kind of cold, detached way many members of your staff seem to be responding. There was a time when the Gas Works was thought of more kindly by people. It could be maybe the money they owe. I don't know. But the feeling between users of PGW and PGW is not good. So I'm just wondering if some of that coolness can change and if you can do something about helping to educate your workers to be more sympathetic, to understand that if it's an older couple in their 70s or 80s to be told on a Tuesday that nobody can come out until Friday to check the fact that the light has gone out and people don't know what to do with it and it's cold out, that would be very helpful.

You can respond to that if you want because I'm going to go on. That's all I'm going to deal with on that subject.

MR. KNUDSEN: With regard to the issue of courtesy, there's a standing order that people will be courteous on our phones.

COUNCILMAN COHEN: Could I urge you to repeat that to your people because we get so many complaints about that, as if the people there are just so insensitive and unsympathetic. I don't know what group they are that get called, they're working on the phones. But people, when they're calling you, they're looking to your company to help them.

And since I mentioned company, isn't it a fact that PGW is kind of an artificially contrived company? Aren't you really in fact a collection of buildings and somewhat different from other agencies?

MR. KNUDSEN: That's correct.

COUNCILMAN COHEN: And in that connection, do you know how your rate of collection compare with, say, with the Water Department?

MR. KNUDSEN: Our rate of collections?

COUNCILMAN COHEN: Does the Water Department have, say, 50 percent of people who don't pay regularly? Don't they bill us monthly? I'm pretty sure before my wife took over the responsibilities for payment, I think we get a monthly bill.

MR. KNUDSEN: Yes.

COUNCILMAN COHEN: Do you know what their problem is? Do they have the same kind of problem?

MR. KNUDSEN: They have a problem similar to ours, but it's not as extreme. Their bills are much smaller than ours.

COUNCILMAN COHEN: They are much

smaller.

MR. KNUDSEN: Their bills are more affordable in terms of the size of the utility.

COUNCILMAN COHEN: Well, take the City of Philadelphia. There was some statement I think Mayor Street made recently, maybe it was in his budget address, that historically the rate of collection in Philadelphia by the government, by the City government, had been running at 92 percent but that during the recent period it had dropped to something like 87 and a half or 88 and a half. And I wondered whether if you were not considered a separate company, could that be a part of the problem why your rates are lower? Because if the City has the rate of collection and their bills can be as high as yours, real estate taxes can be very high and there's been a lot of unhappiness about the real estate rates, there's been a lot of dissatisfaction. I'm wondering why the difference in the collection rate of PGW from that of the City and maybe it would be better if we dispense with the formality of bond -- maybe that can be worked out in other ways so the City can take over the bond responsibility of the Gas Works. Maybe if the payments were going to Philadelphia, they would be better off. Because I don't understand why there would be that difference in the collection figure. You're 50 percent would be matched -- I don't know, it's not quite the same as what the Mayor said. He didn't define whether there are late payers or not, but he said the rate of collection was 88 and a half percent. Would it be possible for you work out an analogy to what your figure would be if you used the same standards that the City of Philadelphia used in its real estate or tax collection generally? Because I think you're right that those amounts would be much more appropriate than the Water Department because the City bills can be very high, even higher than the Gas Works.

MR. WHITE: Councilman, there's a piece of confusion here that I'd like to clear up. We have 50 percent of our customers that have trouble paying their bill. But we historically collect about 92 percent, similar to the City. And we have dropped as low as 87 percent or 87 cents on the dollar as a result of this climb up in gas costs. So some of the same numbers that you're repeating with respect to the City mirror very closely Philadelphia Gas Works' situation. At 92 percent, we have our nose just out of the water and we're surviving. At 87 percent, we're losing considerably. We lose about $8 million for every percent below 92. So if you're at 87 percent, we're $40 million below where we need to be.

COUNCILMAN COHEN: Well, that's very encouraging if you're at the same level. I thought that maybe that was one of the problems and maybe we could straighten it out by having everybody know that it's really City of Philadelphia. But you're saying it's not and you lose about 8 million for each percentage below 92?

MR. WHITE: Yes, sir, we lose about $8 million for every percentage point.

COUNCILMAN COHEN: I'd like to compare that and get the City's reaction.

Now, you're not going to pay the $18 million this year, right, to the City?

MR. KNUDSEN: That's right.

COUNCILMAN COHEN: At least, the present thinking is you're not going to.

MR. KNUDSEN: The present thinking is that the 18 million stay with PGW.

COUNCILMAN COHEN: Well, let me commend you for that. I always thought that was an improper payment made. I thought the City was exercising its power to compel the Gas Works. I don't know of any other agency that has to pay that amount. I know the Mayor feels very strongly about it, but at least this year he's accepted the notion, I think, that he's not going to get it. Maybe that's for budget purposes only. We may see a different Mayor Street on that issue than what he announced.

All right. Thank you very much. I'm hoping that after I talk to the City I'll agree with you that you've cleared up the mystery as to why your rates seem to be low when in fact it's not low, the rate of collection. Thank you very much.

COUNCILWOMAN BLACKWELL: Thank you.

Councilman Kenney. Thanks for your patience.

COUNCILMAN KENNEY: Thank you, Madam Chairperson.

Gentlemen, the first thing I want to say before I start the questions, I think you're both doing the best job you possibly can under the constraints that you are put under, both from the PUC and state regulations and customers and other things in the City. I think you're honest people. I think you've changed that attitude or perception over there from the last crew that we had, and I just want to commend you on doing your best. Although I don't think necessarily your best is going to be enough.

I want to just move for a moment to the LNG plant, the liquid natural gas plant. Is there somewhere in the Capital Budget here, it's not delineated, that would indicate the amount of money you're intending to invest in the LNG plant in 2004 and going forward?

MR. WHITE: It is delineated in here under the gas processing area.

COUNCILMAN KENNEY: What's the total?

MR. WHITE: About $6 million, $6.6 million.

COUNCILMAN KENNEY: Without being too technical, what does that include?

MR. WHITE: Well, primarily we have a very old 30-plus-year-old plant that we utilize to take gas off of the pipelines which is in a gas state, gaseous state like air, and we turn it into liquid. Well, that plant requires a certain amount of maintenance and ongoing repair. Most of this is to, in fact, keep that older plant up and running while at the current time we're testing a new plant that we're trying to bring up to replace the old plant.

COUNCILMAN KENNEY: That is in process now or that's in planning?

MR. WHITE: The new plant has been

built. It was never intended and it was actually contracted for under prior management. I don't want to say we're dealing with the hand we're dealt here, but we are. And we're trying to get that plant online, and then there will also be some supplemental requirements above and beyond that to replace the old plant.

COUNCILMAN KENNEY: What's the total capital need for either the upgrade or replacement of the old plant, of the old LNG plant? If it was Christmas and you were getting a gift, what would be the number you would need to get that thing fully operational?

MR. WHITE: First of all, we're taking the old plant out of service because it's just too old and too risky to have it in service.

COUNCILMAN KENNEY: So we need to build a new one?

MR. WHITE: The new one that we built was a $20 million plant. That's what we call the Phase I plant. It replaces approximately 50 to 70 percent of the existing plant that we have today. To make up the difference, you're probably looking at another $15 million plant. So all tolled we're talking about somewhere in the neighborhood of 35, maybe upwards of 35 to as much as $40 million. Twenty million has already been spent, sir.

COUNCILMAN KENNEY: What we're doing now is planning on investigating about 6 million to keep it online?

MR. WHITE: We have to run this plant in concert with the other plant until we build the third replacement.

COUNCILMAN KENNEY: Explain the benefit to a fully operational, a full capacity LNG plant to this utility. What does it do and what does it save? It gives us the ability, I assume, to store gas in a liquid form while pricing issues are being --

MR. WHITE: The pricing issue is one thing. The most important thing is we do not have to reserve very expensive pipeline capacity on either Texas Eastern Pipeline or

Transcontinental Pipeline. They're the two pipelines that service us from the Louisiana Texas Basin. Most of your supply comes from on and offshore Texas and Louisiana. That pipe to replace that LNG plant, we spend another $70 million a year in what we call pipeline demand charges. They're the fixed charges that they charge you. Unlike how we charge our customers, we charge our customers for the gas they use on a volumometric basis or when it goes through the meter. The pipelines charge us a fixed cost.

COUNCILMAN KENNEY: Hypothetically, what would be the savings or benefits financially to this company if we had a modern or fully operational, not tied together with baling wire and duct tape, my favorite tool? If we had one of those plants, what would that be as a result of savings or benefit to the company financially?

MR. WHITE: If I may, there's two parts to that answer. The first part is the existing 30-year-old plant has been saving us 60, $70 million a year. The new plant that we're building is a much more efficient plant and will operate with less, what we call, fuel requirements. There are large engines that have to be run with the old plant that aren't necessary in the new plant. So there would be a savings, an ongoing operating savings of a few million dollars a year, probably 4 to 5 million. So you're going to continue to the 70 million a year and an incremental savings 4 to $5 million a year.

COUNCILMAN KENNEY: The company is paying for that capital expenditure? We have the money to do this?

MR. WHITE: Yes. As a matter of fact, we've already spent that money and that plant is in, hopefully, the final stages of testing. But as I indicated earlier -- I don't know whether you were here, Councilman -- Air Products, the designer and builder of that facility is having a little difficulty getting that facility tested at contractual levels. So we're working with them to accomplish that.

COUNCILMAN KENNEY: And what are the

reasons for that?

MR. WHITE: It appears that there were some design difficulties, design problems. They re-piped certain -- or certain components of it had been changed, and we're still not operating where we believe we have to be. And there are specific strict contractual requirements that they must meet. And we will not take ownership of that plant or we won't convert that plant into our operating plant until such time that it is completed.

COUNCILMAN KENNEY: Every time a discussion of a potential sale is raised, the issue of the company's debt is a primary obstacle, I would assume, to any kind of discussion. Do you in any way from your experience see a way to either restructure to get some type of legislative relief or some type of rating agency cooperation to take the dead issue off the table? Not off the table as far as owing it, but as far as being able to potentially transfer the company or to sell the company?

MR. KNUDSEN: It's a good question. The debt is a part of the problem. PGW has been looked at by several folk. And there are three issues. One is the debt. How do you defease a billion one of total debt? How do you restructure that?

There's a second problem which is the fact that the demographics and economics of the City are what they are and we have 250,000 customers struggling to make regular payments. Nobody wants to buy that problem.

COUNCILMAN KENNEY: Not to interrupt you, but aren't they the same customer base?

MR. KNUDSEN: Many of them are, that's correct. As we were talking earlier, we're at the bottom of the stack in terms of who gets paid. But also Craig is reminding that PECO has a much larger service territory. Their write-off -- and I was talking with the president of PECO recently -- it's about a percent and a half. Ours is 10 or 12. So that's their ability to spread their costs around.

The third issue is as difficult and

that is that there are certain post-retirement benefits, healthcare benefits that have been promised to employees in the past that anybody looking to buy the company must address. Either the City would have to take that obligation back on themselves or there would have to be some accommodation for somebody buying.

COUNCILMAN KENNEY: I guess we're talking about the indemnity coverage?

MR. KNUDSEN: No, no. Well, it's a complicated situation. People who retired and they had been promised an indemnity program, they are still on the indemnity and we're working to move them on to a cheaper program.

COUNCILMAN KENNEY: How many are those, just ballpark?

MR. KNUDSEN: I think I'll have to get you that. It's not a big number. Most of the retirees are on Blue Cross Plus programs, one sort or another, or on HMOs. But that benefit has never been funded, unlike the pension where we have been funding it all the way along. This post-retirement benefit has not been, so that represents a major liability that would have to be addressed in any sale. So it's those combination of factors that makes us a very difficult --

COUNCILMAN KENNEY: While it is difficult and complicated, would you in your estimation think that it was impossible?

MR. KNUDSEN: I don't know that anything is impossible. It would be a very creative solution. I don't know of anybody out there -- and I'm pretty familiar with the utility industry -- who wants to take on this set of factors.

COUNCILMAN KENNEY: Let me go to the other side of the scenario, and that is -- and I was very clear in your testimony -- relative to PGW's inability to expand outside of the City limits. That's probably not going to change. Our customer base is probably going to get older and poorer. And if we don't pursue this very difficult process of trying to sell the company, which I don't think ultimately benefits the City other than that the Gas Works would be a stable company with a much larger amount of resources, both capital and other economic resources, that the customer of the City of Philadelphia in the end would be better served and probably served at a relatively competitive price. I guess the question is, if you can't expand and grow and your bills keep getting more uncollectible even though you're going to make your best effort to do it, there's nothing else to face but bankruptcy. I don't see any other option other than, again, the City taking on more responsibility. The City's facing a $225 million hole in its budget and more going forward. At some point in time, the money runs out, the customer base isn't paying or can't pay, and you can't expand your customer base outside the City, I don't see a scenario that is a positive scenario other than trying to limp this along until it eventually dies.

MR. KNUDSEN: Well --

COUNCILMAN KENNEY: And it's not your fault. I think you're doing the best you can.

MR. KNUDSEN: But I think there are

several answers. One is that the economics of the City change such that you do have growth, you do have income that's being created and people can pay these bills. Putting that aside for the time being --

COUNCILMAN KENNEY: Is that happening?

MR. KNUDSEN: Well, no. I'm saying that would be one resolution is that real incomes would rise.

One of the pieces of the testimony that is in the second session talks about the fact that if gas costs drop, our experience is that people do pay because it's more affordable. Their real incomes are very different.

To answer your question, I think the answer lies -- there's a two-part answer. One is I think economic growth has to be part of the solution. And I also think there probably should be a public policy discussion as to exactly what the social requirements on the paying customers of PGW should appropriately be. And that's really what the discussion is about.

COUNCILMAN KENNEY: And that's my last question because I know we're going into the next hearing. And I'm not trying to put you on the spot, but you've made the suggestion and that's why I have to ask you. What in God's name do I as an elected official say to people who pay their bills faithfully, would rather go without than to not pay their gas bill -- I mean, I had grandparents who would send me around the check cashing agency with the exact amount of money and the money for the money order to pay that bill first before they went to the movies or went to dinner or did anything else or bought new clothes. What do I say to that group of people who you've got to charge $90 now because they paid their bills on time to take care or supplement people who either can't or won't? When people say this to me -- and you have to understand, the level of anger out there about this proposal, even though it's $90, which is for some people substantial, I don't know how to respond to them because -- I just don't know what to say to them.

COUNCIL PRESIDENT VERNA: Most people are saying, "I won't pay the surcharge."

COUNCILMAN KENNEY: I understand people are now talking about just refusing to pay the surcharge. And it really is frustrating. And I know it's frustrating for you, I know you're doing your best, but what do you tell that middle class family who says, "You know what, maybe it's time to just really seriously look at getting out of here."

And I'm telling you, they're doing it, they're talking about it. They've been thinking about it for awhile, but things like this push them over the edge.

MR. KNUDSEN: There's no question -- and let me address this very specifically. Our proposal doesn't necessarily lock in $90 a customer. This is a flexible rate. And if to the extent that we collect money from our customers, we don't exercise flexible clause. I think part of the answer is that we don't know exactly what the proportions are between those who can pay and don't, and those who can't pay. We don't know precisely what that is. But certainly in the short term I think an answer is that the public policy of Philadelphia, and that's the Administration and this Body and the administrative agencies, make it very clear that there is no tolerance for not paying this bill, that you stand to jeopardize the entire City in this instance. So that's a different conversation, though. And I know it's not an easy conversation, but it's the one that has to occur. And that's what this anger is about. And we're fully cognizant and, believe me, I was the last one to want to propose anything in this regard. But I have a fiduciary responsibility that says come this summer and we have to make payments, where is the cash going to come from? So this was my solution.

COUNCILMAN KENNEY: I had raised this issue once with you before relative to being on a budget, requiring a mandatory budget. Because I understand some of our problems have to do with the issue of cash flow at certain times of the year. And I know it's much easier for someone to pay $50 a month on a monthly basis steady than to get hit with a $400 -- is it required?

(Inaudible.)

COUNCILMAN KENNEY: Okay, I'm sorry. I waited. I used to be over there, but now I'm over here and I'm waiting and I just want to get it all in if I can.

Councilwoman Tasco, I will let you go to the next hearing. Thank you.

COUNCIL PRESIDENT VERNA: May I ask a question?

COUNCILWOMAN BLACKWELL: Certainly, Madam President.

COUNCIL PRESIDENT VERNA: Mr. Knudsen, if the requested capital budget of $65 million is approved, when do you anticipate that you will have to enter the capital markets?

MR. KNUDSEN: We have to enter the capital markets late this summer.

COUNCIL PRESIDENT VERNA: What is the rating agency's take on PGW's fiscal health?

MR. KNUDSEN: They're not happy, to say the least.

COUNCIL PRESIDENT VERNA: And what happens if they're not happy?

MR. KNUDSEN: Well, several things happen. One is that this clause that I am proposing they view favorably. I mean, they are not interested in the politics or the social theory of this, they want to know where the money is going to come from to service the debt. So that part of it they would view favorably. The --

COUNCIL PRESIDENT VERNA: But then again there's also an "if" attached to that; if the PUC approves that.

If they don't approve, where are we.

MR. KNUDSEN: Well, if the PUC doesn't approve this clause, and it's very controversial because although there are other states that have done this, Pennsylvania doesn't have one of these. If they don't, then we will look to file for a base rate increase. The money has to be generated to keep this utility alive and the gas flowing.

But coming back to the S & P or the rating agency response, I think the other aspect of this is that we have to demonstrate this summer that we are running an absolute first rate collection function and that we are getting money into this utility. And that's why I'm appealing to this Body and the Administration to support as a matter of public policy that people must pay these bills. But that's what they're going to be looking for between now and August or we're going to pay a very hefty premium for this debt.

COUNCIL PRESIDENT VERNA: Of the 130,000 shut-offs that you indicated earlier, do we have any indication at all as to how many of those customers would be eligible for LIHEAP?

MR. KNUDSEN: Let me just inquire a minute.

We don't know specifically how many of them would be eligible. We don't, as a matter of course, collect income information.

It's not something that we've done in the past, although we're going to have to do more of that.

COUNCIL PRESIDENT VERNA: I think that's something that should be done. If people aren't paying and if there are avenues that we could help them to pay --

MR. KNUDSEN: Well, let me be clear though --

COUNCIL PRESIDENT VERNA: But isn't there more than one program that can help many of these people, like Crisis?

MR. KNUDSEN: Well, LIHEAP and Crisis go together, and we have enrolled as many people as there is money.

COUNCIL PRESIDENT VERNA: So that would be what $300, did you say?

MR. KNUDSEN: Three hundred dollars per family.

COUNCIL PRESIDENT VERNA: And how much would Crisis be?

MR. KNUDSEN: No, that's combined. The money combined is 350 to $400, something in that range. It varies by year depending upon how much the federal government appropriates, but that's about what LIHEAP/Crisis contributes to our money.

COUNCIL PRESIDENT VERNA: I still think of the 130,000 shut-offs, there would have to be people in that group that would certainly be eligible for LIHEAP or some assistance. And if we know now, then we would be in a much better position next year to know that these people at least could apply and get the $300.

MR. KNUDSEN: The issue for us is that there's only so much money. We have a program --

COUNCIL PRESIDENT VERNA: But if I recall, when you were here last, you were pleading with us to let many of our constituents know that they could apply for LIHEAP because you said that we did not have that many customers applying.

MR. KNUDSEN: No --

COUNCIL PRESIDENT VERNA: That's what you said. As a matter of fact, -- am I correct in my understanding?

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COUNCILWOMAN BLACKWELL: Yes, Madam President. I agree with what you're saying, because now Mr. Knudsen is saying that the issue is how much money we receive to go into these programs. It was those applicants. He said today that two-thirds of those so far that they know qualify have been contacted. So that leaves us in no man's land. I said yesterday to them that I don't agree with telling people you're paying for the person who doesn't pay if in fact two-thirds we are reaching and if in fact there's no money there any way. So I don't think it's fair to make people -- I mean, most people would give a dollar for a senior. People don't mind paying for people who can't. But to start a fight -- and the gas company says they don't do it, but I don't agree with those who say I'm not paying for somebody or if a person wants to get a cell phone or go to the movies -- I mean, this is 2004. People have needs and I don't think it's fair to try to make people fight one another when we're all, quote/unquote, in the same boat. I don't agree with that. I agree with what you're saying. This time last year, we were looking for applicants for LIHEAP and Crisis. Now this year we've reached the ceiling about the monies we get in. But even in spite of all that, I don't think it's fair for those individuals outside of this room who decide to make people fight one another about who pays and who doesn't and what they're allowed to do or buy with their dollars. I mean, I think that's a bit absurd.

MR. KNUDSEN: May I just respond a little bit on this question of LIHEAP?

One of the initiatives at the energy association state-wide that we executives are trying to get going is an appeal to the legislature to put some money behind LIHEAP for Pennsylvania, that they make some contribution to this effort as a state body. As I indicated earlier, there's only two states who do not participate across the northern tier of cold states and that is Massachusetts and Pennsylvania. So that's something that we're actively pushing in

Harrisburg right now, is to get some funding in this regard, to essentially make the pie larger.

Councilwoman, I'm doing everything we can to get the money in.

COUNCIL PRESIDENT VERNA: I understand, but I do recall last year you were almost pleading with us to try to get people to apply for LIHEAP.

MR. KNUDSEN: We were successful. We have enough subscribers; now we don't have enough money.

COUNCIL PRESIDENT VERNA: And we certainly tried our best to accommodate.

MR. KNUDSEN: Thank you.

COUNCIL PRESIDENT VERNA: I just want to ask one other question before we go into the next hearing.

Did the PUC ever make a determination regarding the senior citizens' discount, those that would be effective as this past September.

MR. KNUDSEN: It was on the agenda last Thursday, and for whatever reason they were never told. They withdrew it for reconsideration at the next meeting. We just don't know.

COUNCIL PRESIDENT VERNA: After the winter is over.

So in all likelihood, do you think they'll make some determination before next winter?

MR. KNUDSEN: I think it will be either in this session coming up or the one after. I don't think they want to delay it. There was just some considerations that hadn't been resolved on their part.

COUNCIL PRESIDENT VERNA: Thank you.

COUNCILWOMAN BLACKWELL: Thank you, Madam President.

Councilman Ramos, then Councilman Rizzo, and then we'll recess.

Councilman Ramos is going to defer to the next hearing.

Councilman Rizzo, would you like to wait until the next hearing or --

COUNCILMAN RIZZO: No, this is relevant to this hearing.

I'd like to switch gears for a minute, and I apologize if you've addressed this issue, but I would like to talk about some quick arithmetic that I've done and I want to talk about other than residential customers.

It appears to me that there's almost $14 million in debt from businesses. The big industrial customers tend to pay their bills, but I'd like to know do we have any customers that owe us close to $14 million here? And if I'm wrong on my arithmetic, please correct me. But I understand it's about 13.7 in money that's out there from small businesses, middle sized businesses that have not been paid.

Why would we even tolerate for 30 seconds a business not paying their gas utility bill?

MR. KNUDSEN: We have about 20,000 smaller commercial customers who are in this category that you're talking about. About 25 percent of them are delinquent at any time. I'll be candid with you. Until a year or two ago -- about a year ago, we gave some real consideration to being hard on these people because they may be new businesses getting started. They employed people. So basically, we attempted to collect the money, we were at some times more lenient than we might have been. We're not that way anymore and we haven't been for about a year. We're cutting people off as their bills go into the appropriate arrearage.

COUNCILMAN RIZZO: Again, we started this hearing talking about policies, policies that allow a business to go and buy -- and I understand that you don't want to be responsible for a business going under, but you're going under. They'll be around --

MR. KNUDSEN: No. That's the problem, they aren't.

COUNCILMAN RIZZO: They may be around.

MR. KNUDSEN: They may be around.

COUNCILMAN RIZZO: And you may not be.

MR. KNUDSEN: That's correct.

COUNCILMAN RIZZO: And obviously,

your policies, you have to start thinking why we're in the situation we're in. And if you're telling me that we have almost $14 million of debt that small businesses haven't paid and you're not being really aggressive, if I were a small business person and I knew that you weren't going to come after me, guess what, I'd probably buy more inventory, I'd probably paint the store, or I'd do something different with your money to make me more money.

MR. KNUDSEN: We are doing that and have been doing that for about a year.

COUNCILMAN RIZZO: Well then how come the number is where it is?

MR. KNUDSEN: If you look at some of the numbers, a large percentage of it is in the under 30-day. It's current and then you have 30 to 60 and -- a lot of it is not that old of money and we have a very aggressive program to make sure that these people try to stay current with their bills. This is not easy. And a lot of these are tenant/landlord situations. These are small residential buildings that have a whole other set of problems associated with and relative to the PUC and what we can and cannot do with these people.

COUNCILMAN RIZZO: I'm not talking about residential.

MR. KNUDSEN: I'm saying these are commercial accounts but are three apartments, two apartments, whatever. And they go into arrears and then we have certain responsibilities because there are families in these residences that we can't just turn off because that's our desire.

COUNCILMAN RIZZO: I understand and appreciate the compassion, but I think the days of compassion have passed.

MR. KNUDSEN: Thank you.

COUNCILWOMAN BLACKWELL: Thank you very much. I never think the days of compassion will pass. I'm sorry, but I can never morally forget our obligation to people in need and quality of life in our City.

COUNCILMAN RIZZO: I'm talking businesses.

COUNCILWOMAN BLACKWELL: Having said that, due to the hour, we're going recess our finance hearing until Tuesday the 30th, at 2:00 p.m.

Having said that, we will ask you if you will look at the senior citizen discount. There are some concerns, especially by the sponsor of one location being listed in each neighborhood in the City and about four or five locations and the fact that in a 30-day period with it being so far, some people by the time some seniors are able to act, they have to make arrangements to get there and so we're asking if you would consider during this time some process to extend this 30-day period for the senior citizen discount applications.

MR. KNUDSEN: We will.

COUNCILWOMAN BLACKWELL: Thank you.

We will assume that for the purposes of our hearing that we will on Tuesday begin with the senior citizen discount. We will assume that the rest of the discussion with regard to the Capital Program has been completed, so everybody's clear where we are.

And we are happy to now defer to my colleague and chair of the Committee on Transportation and Public Utilities. Thank you very much.

(Hearing adjourned at 4:25 p.m.)

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COUNCIL OF THE CITY OF PHILADELPHIA

PUBLIC HEARING

COMMITTEE ON TRANSPORTATION

AND PUBLIC UTILITIES

- - - -

Room 696, City Hall
Philadelphia, Pennsylvania
Wednesday, March 24, 2004
4:30 p.m.

- - - -

RESOLUTION 040149 - Resolution authorizing City Council's Committee on Transportation and Public Utilities to hold public hearings to investigate the proposed gas cost rate increase to be effective September 1, 2004...

RESOLUTION 040216 - Resolution authorizing City Council's Committee on Transportation and Public Utilities to investigate and hold hearings on the Petition of the Philadelphia Gas Works to the Pennsylvania Public Utilities Commission...

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I N D E X

COUNCILMAN NUTTER: Thank you, Madam Chair.

As the Chair has laid out, the Finance Committee, with the sponsor's agreement, if we don't finish the testimony today on these two resolutions, do we want to carry on onto the same day, or do you want a different day? What was that date?

COUNCILWOMAN BLACKWELL: Tuesday, the 30th, at 2:00.

COUNCILMAN NUTTER: For the Committee on Transportation and Public Utilities, anything that's not completed today will again be combined with Committee on Finance on Tuesday the 30th at 2 o'clock.

There are two resolutions. Resolution No. 040216 and Resolution No. 040149.

Resolution No. 040149 is authorizing City Council's Committee on Transportation and Public Utilities to hold public hearings to investigate the proposed gas cost rate increase to be effective September 1, 2004, requested by the Philadelphia Gas Works (PGW) with the Public Utility Commission, and in furtherance of such investigation authorizing the issuance of subpoenas to compel the attendance of witnesses and the production of documents to the full extent authorized under Section 2-401 of the Home Rule Charter.

Resolution No. 040216, authorizing the City Council's Committee on Transportation and Public Utilities to investigate and hold hearings on the Petition of the Philadelphia Gas Works (PGW) to the Pennsylvania Public Utilities Commission to establish a cash receipts reconciliation clause (CRRC), in order to reconcile PGW's projected and actual cash receipts with billed revenues on an ongoing basis; the causes and necessity for a CRRC; and further authorizing the Committee to issue subpoenas and such other process as may be appropriate to compel the attendance of witnesses and the production of documents in furtherance of the investigation to the full extent authorized by Section 2-401 of the Philadelphia Home Rule Charter.

We'll take a five-minute short

recess stenographer break.

(Brief recess.)

COUNCILMAN NUTTER: Ladies and gentlemen, we're back.

Can the witnesses come back to the table, please?

Mr. Knudsen, can you proceed with your testimony? Do you have separate testimonies for these two items?

MR. KNUDSEN: Sir, I provided -- I'm not quite understanding what the process is going to be. I provide a comprehensive testimony for all three of the resolutions and then split one off for the senior citizens and gave that separately. It is included here, but the testimony that reads, "My testimony for regarding the three resolutions," is the appropriate testimony for this part of the hearing.

Do you have that? It should have some colored graphs in it.

COUNCILMAN NUTTER: Yes, I see it.

Why don't you go through your testimony. Members may have questions on any one of these items. I understand that there was some spirited discussion already about some of these, so why don't you proceed?

MR. KNUDSEN: If it's your pleasure, I won't read the testimony, I'll really just summarize it.

COUNCILMAN NUTTER: That would be nice.

MR. KNUDSEN: The first question that's posed here is, what is this cash receipts reconciliation clause?

The problem that confronts the company is, as we have stated earlier, historically, we've collected about 92 cents on the billed dollar. This last year, we collected 87 cents on the billed dollar.

COUNCILMAN NUTTER: Why?

MR. KNUDSEN: Because the numbers of people who we would normally have expected to pay didn't and largely because, in our view, their bills went from $900 per family per year, which it had been for almost 15 years from the late '80s though 2003, it escalated to $1300 a family last year and escalating to

$1460 this year. It is this escalation that we think the elasticities kicked in and people just weren't able to afford as much and they didn't pay their bill.

The difficulty that we have is that for every cent on the dollar that we didn't collect, it's worth 8 million bucks. We lost $40 million of liquidity in this exercise. And what happened was that this shortfall occurred very suddenly last summer when we would normally have expected to receive a large part of our receivables come in in the May through August period. It collapsed on us.

So coming into this year, there were several considerations. One is I felt we needed to upgrade our collections effort, and I brought in a very good consulting firm to do so and we have made major progress in the effectiveness of our collection efforts even in light of the winter moratorium. Understand that come December 1st a lot of our efforts are frustrated because we can't turn anybody off and the motive to pay is heavily reduced by that portion of our paying public who find it to their advantage not to pay.

Now, as we came into our summer or as we're coming into this spring and summer, it is essential that PGW be viable financially. We must raise some debt.

COUNCILMAN NUTTER: You must raise some --

MR. KNUDSEN: We must sell some bonds this summer, late this summer. We have to keep our construction program going. We must be viable in terms of providing safety and reality in terms of our system.

With the shortfall in our liquidity and our cash availability with the need to be in the financial markets, I was confronted with only really two options. One was to file for a base rate increase. The other one was to take my lead from some of the other states who have put in flexible clauses that essentially are designed to address a specific set of circumstance and go away if necessary. And rather than create a permanent burden on our customers, because PGW already has the highest rates in the state, we opted for this lesser approach.

COUNCILMAN NUTTER: Let me ask you a couple quick questions.

First, where did this idea come from?

MR. KNUDSEN: The CRRC?

COUNCILMAN NUTTER: Yes.

MR. KNUDSEN: It was my idea.

COUNCILMAN NUTTER: It was your idea?

MR. KNUDSEN: Yes.

COUNCILMAN NUTTER: Has PFMC -- PFMC is your governing Board, is that correct, Philadelphia Facilities Management Corporation?

MR. KNUDSEN: That's correct.

COUNCILMAN NUTTER: And have they approved this proposal?

MR. KNUDSEN: They have.

COUNCILMAN NUTTER: Was there a resolution of the Board?

MR. KNUDSEN: There was.

COUNCILMAN NUTTER: And was it

unanimous?

MR. KNUDSEN: Yes.

COUNCILMAN NUTTER: Where else is a proposal or program like this in place either in the Commonwealth of Pennsylvania or anywhere in the United States of America?

MR. KNUDSEN: There is no program in the Commonwealth of Pennsylvania. That's one of the reasons that it's controversial. There is a very similar program in Ohio available to all utilities, and it's basically designed for utilities to collect on their uncollectible charges. It's very parallel to where we are right now. There is a similar type of mechanism in Georgia. There's a similar type of mechanism in Memphis.

COUNCILMAN NUTTER: How much of the average ratepayer's bill now is covering non-payment or inability to pay by other customers?

MR. KNUDSEN: Well, you have to define the terms, but I will tell you in our bill right now there's something called the universal service charge which captures all of these programs and it's about --

COUNCILMAN NUTTER: How many programs do we have?

MR. KNUDSEN: Well, you have the senior citizens discount, you've got the CAP Program, you have conservation, and there's a small piece in for our restructuring expense. As we came into being under the purview of the PUC, we had certain charges that we had to incur. That's about $1.15 out of our $14.65. So that's about 1/14 of the total. Now, that's part of the problem. That's about 7, 8 percent.

We also write off or provide for non-collection of an equal amount of money.

COUNCILMAN NUTTER: Of what?

MR. KNUDSEN: Of about an equal percentage. So it's about 14 to 15 percent of our total revenues can be captured as paying for those who can't pay.

COUNCILMAN NUTTER: So then is it correct to say that about 15 percent of the average ratepayer's bill is paying for in essence non-paying or inability-to-pay customers?

MR. KNUDSEN: That's correct.

COUNCILMAN NUTTER: You're now proposing to tack on some other amount of money. I don't know what the percentage is, but in the plainest of English, what incentive would there be for anyone to pay their bill?

They now know that the cost is going to be passed on to -- it's like going through the grocery line. I mean, if you can load up your cart with whatever you want and pretty much be assured that the person behind you is going to pay the tab, I mean --

MR. KNUDSEN: Why pay?

COUNCILMAN NUTTER: Right.

MR. KNUDSEN: First of all, our rates aren't that much higher than the rest of the state. So right now we're relatively competitive. That's Point 1.

Point 2 is --

COUNCILMAN NUTTER: But many of the people in Philadelphia are a lot poorer than other parts of the state.

MR. KNUDSEN: Well, that's exactly

what our problem is.

COUNCILMAN NUTTER: You can finish. Or members may have questions.

My last thing will be, you're asking the PUC for a two-year program or in two years the PUC would determine whether or not to allow the program to continue, they could, I guess, theoretically do nothing and the program would just stay in place.

MR. KNUDSEN: Or go away.

COUNCILMAN NUTTER: If you were to get this approval from the PUC, who would decide when to implement the CRRC; PGW?

MR. KNUDSEN: Let me be very clear what it is, all right? If we collect 92 cents on the dollar this year, this clause will not go into effect. And that's why I wanted a flexible clause so that it wasn't automatic that rates went up. But we had to have some provision that we would get money into the company to support our fiduciary responsibilities of both keeping the place operating and paying for the bonds. If we get to 92 percent in this collection effort, then the mechanism is in place and we don't use it. But it is there in the event that if rates keep going up that we have some way of assuring the bondholders and the stakeholders that PGW can sustain itself going forward.

COUNCILMAN NUTTER: Well, I understand that, but let me just at least posit this and then I'll relinquish the microphone. Not that you would do this at least consciously. But there is at least the more than likely scenario that even if rates didn't go up but if somehow some way collections fell off and you went below the 92 percent threshold that you want to attain and if -- and I don't know how aggressive the collections process is, but if for some reason there was some shortfall in that particular area, haven't you, in fact, created a readymade pool of dollars through this program such that you will either get people to pay their bills or costs will go up, as you've laid out these other situations so even if people want to pay but the costs are going too high, they can't; or costs could stay level, collections for some other reason drop and you'd institute the CRRC anyway, correct?

MR. KNUDSEN: Yes. We have to have sufficient liquidity to run this company.

COUNCILMAN NUTTER: I understand that, but the only point I'm arguing at the moment now is what keeps the pressure on the company to make sure that you're collecting everything that you can and should?

MR. KNUDSEN: Because 92 percent, I'm right here (indicating), I'm barely above water. And there's no way that this company can survive indefinitely that way. The incentive for us is to cut costs and to create an environment where we are collecting money from our customers in excess of 92 percent. We need 94, 95 percent.

COUNCILMAN NUTTER: I understand that. I'm not going to be able to stay, which ultimately may be a benefit to just about everyone in the room. I can't keep doing this.

MR. KNUDSEN: I agree.

COUNCILMAN NUTTER: As a public

official, as a ratepayer -- maybe my house is not the most energy efficient home in the City, but the bills are pretty hefty and obviously I pay my bills. But we can't keep doing this. It's going on and on and on, and you're stretching your brain, scouring the country, finding other ways and mechanisms to try to do this. It's bandage after bandage. There is no plan whatsoever that I've heard about or seen -- and we had a report that apparently most people haven't seen, including you, and it was about your company. Somebody's got to lay a plan out on the table to change the dynamic here and change the function. You can't keep limping along this way. The company is bleeding, the patient dying, and we just keep coming up with different ways, as you indicated, to keep your nose above water. You can't run a company like this.

So it seems to me that while you're trying to run the place, either internally, through the Gas Commission, hire a consultant. Someone needs to come in here with a true turnaround plan of how this company is going to function and operate under the current circumstances of the population that we have, unless another million relatively well-off people want to come into Philadelphia anytime soon. But given the 1.5 million people that we have today, somebody's got to walk in here and tell us what to do with this thing. I cannot do this anymore. I'm not going to spend all this kind of time going through this over the course of the next three or four years. It is the absolute definition of insanity. We continue to do the same thing over and over and over again getting the same result and expecting something different. I think you need to come back to us with a plan.

MR. KNUDSEN: Fair enough.

COUNCILMAN NUTTER: Councilman Ramos, Councilman Cohen.

COUNCILMAN RAMOS: Mr. Knudsen, I agree with my colleague Councilman Nutter's poignant analysis of the situation, and I also agree with his recommendation that a plan needs to -- I think some of that might call for us to get more involved in a way to design or to present a plan to the people of Philadelphia.

I had a question concerning the debt collection. You said you have now contracted a company that you feel satisfied with their debt collection. Give me some indications of your satisfaction.

MR. KNUDSEN: Well, the conversation earlier was in outsourcing activity, and we have outsourced the collection of about $200 million worth of what amounts to now fairly old receivable paper. The folks that are --

COUNCILMAN RAMOS: How old, Mr. Knudsen?

MR. KNUDSEN: Well, some of this could be as little as six month, some as old as a year and a half.

COUNCILMAN RAMOS: And outsourcing means?

MR. KNUDSEN: Outsourcing means we've given it to somebody outside the company and they are performing -- three are certain benchmarks for the collection industry, and they are performing about where they could expect them to perform. We get 2, 3, 4 percent back on the money we've given out. That's as good as it's going to get.

COUNCILMAN RAMOS: I came upon a person that's in the debt collections business a few months ago. And I said, "Are you doing anything with the gas company?" He said, "I don't even want to touch the gas company. I can't make any money, I can't collect."

Do you feel comfortable enough that with this company you're going to be able to recover 93, 94 percent?

MR. KNUDSEN: Let me come back to the earlier point that I made. I think there is a culture of entitlement amongst a lot of the customers of PGW, and it goes back not a decade, it goes back generations. We hear this anecdotally.

I think the Mayor and this Body and the agencies whether it's the DPW or whatever, have got to make it very clear that people must pay these bill. It's like a tax bill.

When it's in arrears and it's putting the Gas Works and it's putting the City in some kind of financial stress, people must pay these bills. And the question is distinguishing between those who can't and those who don't and can, and that's the issue.

COUNCILMAN RAMOS: I would think that even if you have the best collections agency out there now working for you, that your success is going to be very limited because you would still have a high percentage of people, whether they are just not wanting to pay or probably more as equal a number or higher people that cannot pay. So if people cannot pay, it doesn't matter how good of an agency you have, if they don't have it, they don't say you and you stay in hole that you're in.

MR. KNUDSEN: But the problem we have, Councilman, is if that's the case, then this is not a viable enterprise and we'd better acknowledge that right now and either socialize it in some way or let it go under. I don't have the answer. If people don't pay the bills, then we have a transference that has to occur to the General Fund or we appeal to for to Harrisburg for supplementary funds. If we have so many poor people to whom we provide service and they cannot participate in the process of receiving that service and paying it, the commercial contract, then we have to redefine the terms of this company. We cannot continue this way. And I absolutely agree with Councilman Nutter on that. I think there has to be a discussion about the social burden that the customers are bearing to keep people in their homes in the wintertime warm. Is that a responsibility of the other ratepayers or is that a more general responsibility of the body politic? That conversation has got to occur.

I don't have the answer for -- this year, we will do everything we can in the best -- to your point about a collections agency, I think we've created at PGW the best capability that it's had ever and I would stack it against private industry right now in its ability to reach out, make contact, do the appropriate things, state-of-the-art benchmarking, whatever you want to call it. And if that doesn't work, then we have a whole other conversation about PGW, because if bills continue to go up, then more and more people will slide from that half. That half will grow to 52 percent or 54 percent or 55 percent of our customers who can't pay regularly or don't pay regularly.

COUNCILMAN RAMOS: Thank you, Mr. Knudsen. Your response in agreement with Councilman Nutter and myself -- and I don't want to assume other colleagues probably feel the same way. We were going through this in -- we had hearings here on healthcare and the issue is broader than the closing of one hospital. It is how do we now manage to keep hospitals, how do keep utilities that people need in this City in a way that's accessible to them? And we have some very challenging times ahead of us because it's not just in utilities but in other phases of our daily lives in this City.

Thank you so much for coming before

us, and we have some very tough times again.

MR. KNUDSEN: We do indeed, Councilman. And thank you for your help.

COUNCILMAN COHEN: I think we should replace the leadership at the Gas Works because I think one of the reasons for your failure is that you have no respect for City Council, you excluded them from consideration, you thought you had full authority. Yet you're here, you were here earlier this afternoon asking for help on a Capital Budget and you're trying to indicate that you're interested in Council support. You're not; you're not the least bit interested because you took this action knowing it was against the will of City Council yet you didn't discuss it in advance, you didn't show us any respect, any interest in our position. I think by that action, you've shown that the Gas Works under its present leadership is not competent of running the show. I'm not going to decide to assist the Gas Works under its present leadership at all. And I think conversation ought to begin and you ought to acknowledge your failure as Chief Executive and you ought to remove yourself so that we can put people in who have confidence in City Council as well an executive who just doesn't ignore us but wants to participate with us. Otherwise, I think you're just operating a shell game, and that's what I think you've been doing. You decided you were going to have this all your own way, or maybe you're negotiating with other people or talking to them. You're certainly not talking to City Council. And until and unless you immediately withdraw this request from the Gas Works as an insult to the senior citizens of Philadelphia, I see no way of accepting your leadership at the Gas Works.

MR. KNUDSEN: Thank you for your comments.

COUNCILMAN COHEN: Now Councilwoman Tasco.

COUNCILWOMAN TASCO: Good afternoon, Mr. Knudsen, again. Thank you. I won't call for your resignation, but I will ask -- at least the people at PFMC knew, and the question I have is when did you figure out you were going to file this and why wasn't there any discussion, not only with City Council, but with the Gas Commission about this plan?

MR. KNUDSEN: Well --

COUNCILWOMAN TASCO: It could have saved you some grief.

MR. KNUDSEN: I think this proposal, we were faced with -- we had several options. And this particular option required action no later than the 1st of March. And as of early, sort of mid-February, we still had not formulated our thinking about this. And it evolved in a very quick time frame. We did share some thoughts with the Executive Director of the Gas Commission. But this was a very fast-evolving proposal. And the problem was to get it into the time frame at the PUC, we had to file by March 1st.

I think we have not in the past sought the approval of the Gas Commission or City Council when we have raised gas rates. We raised them quarterly. We have not made it a policy to do so. When we raised base rates the last time in the manner in which we did, we did not seek the approval of the --

COUNCILWOMAN TASCO: But this is not the traditional gas rate or the base rate; this is a different kind of program that you're triggering.

MR. KNUDSEN: But we did something similar to this back in 2000-2001.

COUNCILMAN COHEN: You knew the strong position City Council had if there was an ordinance passed by City Council in opposition to this.

MR. KNUDSEN: Not that I was aware, Councilman.

COUNCILMAN COHEN: You knew that City Council had taken a very strong position against this kind of thing for senior citizens. At least you could have had the courtesy on the problem of payments and senior rate discounts and you went ahead with that without any discussion with City Council.

MR. KNUDSEN: Well, that was a larger political discussion, Councilman. As we had that conversation, PGW itself -- this was an administration issue and management itself --

COUNCILMAN COHEN: Felt that you could find some kind of language to try to cover up the idea that it was thumbing its nose at City Council and telling City Council, "Butt out. We're competent, we're going to handle this ourselves."

Go handle it.

MR. KNUDSEN: Well --

COUNCILWOMAN TASCO: I agree with Councilman Nutter because my question earlier too is what is the incentive for PGW to engage in active collections if they know, "If we don't get the money, we can just pick it up from the ratepayers and trigger the CRRC and there's no incentive to do the collection."

MR. KNUDSEN: Well, I respect that. And one of the reasons that I proposed the structure of this clause the way that I did was that I understand after -- my experience is 30 years of appearances before the Public Utility Commission. I knew the question would be raised, "What is your incentive?" And one of the reasons that we delayed doing anything was that I knew the question would come to us, "What have you done at PGW to collect these funds?" And I needed in that juncture to demonstrate that we had this collections initiative in place and that it was starting to work, that we had the possibility of collecting the money that was out there.

Come directly to your question as to what's our incentive. We have enormous incentives to continue to collect money. Ninety-two percent does not give us any real leeway at all. We must go beyond 92 percent to 94 or 95 percent in order to start to work this company out of the hole, as someone characterized it earlier, that we're in. It is that incentive that's driving this management team. We've got to get to a position of paying down the short-term debt, we've got to get to a position of paying off the $45 million loan, and we've got to get to a position of generating funds internally to apply against our construction funds or we'll never get out of this mess.

COUNCILMAN COHEN: You're never going to get out of it until such time as you recognize the role of City Council.

COUNCILWOMAN TASCO: David, let me finish my line of questions.

COUNCILMAN COHEN: Go ahead.

COUNCILWOMAN TASCO: Let's put on your consumer hat. You sat on the side of the table as consumer advocate. Because you said earlier -- having sat through all of this since I've been on the commission, the company is getting deeper and deeper. We're not finding a way out. In 1994, I believe the Phoenix Company came in and they were supposed to turn it around; they didn't turn it around. We got new management; we didn't turn it around. And here we are worse off, in more debt than we were. Certainly, there has been some circumstances such as BCC failure. And how much was the restructuring cost?

MR. KNUDSEN: Five million dollars.

COUNCILWOMAN TASCO: The cost of restructuring the company, going to State PUC, how much did that cost?

MR. KNUDSEN: The out of pockets were about 6 or $7 million.

COUNCILWOMAN TASCO: And you had other problems too. But you talked about socializing the company. Do you see that being the final answer? Because we don't seem to have another answer to getting PGW -- because nobody's going to buy it.

What is your consumer thought about this? And what can you and your company do to engage the discussion around what is really needed? Because what's happening, we're all jumping around it. We're not really coming to the table to say the company has failed or is failing or will fail, and what do we do about it? Because this is really just Band-Aid effort. If this doesn't work, we'll have to find something else to work. There are not too many options for you to address the many problems that we have. So where is your advocacy to do something different and something that's not in keeping with the usual solution?

MR. KNUDSEN: If we can't get

customers to pay and if there is no purchaser for this utility, it would seem to me that the only conversation that you can say is some kind of a State solution, an authority provision, something that removes PGW from the governance of the City and may raise it up a notch, raise it to the State level.

COUNCILWOMAN TASCO: Where does the money come from? Are they going to put the money in it?

They can give the money without making a authority, they can just make us a line item in the budget.

MR. KNUDSEN: Well, that would be an answer then. I mean, any place where there's a willingness to put some funds, not into the operations of PGW, that's not where the money needs to go. The money needs to go to people in order to fund their bills. That's a very different proposition. We're not looking for money to run the company; we've got that. It's the money that we need to have people pay their bills. Now, if that can be addressed either in terms of the General Fund or some kind of state source, then so be it. In fact, as I said earlier testimony, we're looking for the State to put some money into LIHEAP so that there's some supplemental funds coming.

But I agree with Councilman Nutter. We don't want to be continuously at this problem forever. There's got to be some addressing of this question of how people are going to pay for gas service. There's another alternative, you discontinue gas service for X numbers of people and find some alternative, put them on electricity which, for all intents and purposes, is cheaper. Certainly cheaper for us.

COUNCILWOMAN TASCO: One of the impediments you have spoken about is the inability to shut people off in the wintertime. Even though they cut off in the summer, you have to cut them back on. And we know people get into this game. That's how PGW has gotten into the position it has gotten into. People made an agreement, kept it just at the point and then when they get to the winter, cut it off. The bill gets bigger and bigger and bigger and they play that game every time.

One of the recommendations that did come from Phoenix to the Gas Commission when we had regulatory authority was to have the ability to cut them off in the wintertime. Now, have you approached the PUC -- in spite of the fact that that may be their rule, knowing the condition of this company and the problems that we have, have you given them the approach and say, "Look this is a way we did it prior to you taking over. At least this plan was on this table."

How can you and have you talked to them about doing something like that? Because they have to see that there's some need here that may be different than other utilities in the State.

MR. KNUDSEN: Well, there's nothing like a crisis to generate a little attention. I am not well regarded at the PUC right now for the problems that are attendant to PGW. As I said, everybody's got these issues, we've got them worse than everybody else.

To answer your question, yes, there is an initiative in the State amongst the executives of the utilities to look seriously at some of these provisions.

COUNCILWOMAN TASCO: Can you move them along a little faster? Have you talked to the State -- we're meeting, just for the record, the Gas Commission and the PFMC Board set up a meeting with the State delegation to talk to them about increasing the funding for LIHEAP. And of course, as we meet with the -- a lot of these problems have come up. Certainly we ought to use our political leverage to get the state political agency to move quicker. You've got a Governor up there that's certainly friendlier to us than in the past. Could we please get his attention?

MR. KNUDSEN: Councilwoman, I'd be happy to talk with you about exactly that. I mean, we have this initiative going with the Philadelphia Delegation. We should maybe take different approaches we have to date to bring this message around to the bureaucratic agencies in a different way. And I absolutely agree with you. But understand the other initiative that's underway is through the industry and essentially presenting these problems to the Pennsylvania Public Utility Commission as very real and ones that are not given to easy solutions, but we have to change some of this.

To answer your question specifically about a winter turn-off, I think you understand that this is an age old tradition. It's been around for decades. We would like to propose that not everybody be privileged in this way, that maybe folks who have higher incomes would be subject to -- would not be subject to the moratorium and, in fact, we could turn them off if they didn't pay their bills. But then this becomes a much more complex political question at that point.

COUNCILMAN COHEN: It does. And I'd suggest to both of you that this firestorm would be nothing compared to something that would happen if there was turn-off and someone were found dead in bed of freezing.

COUNCILWOMAN TASCO: Let's talk

apartment owners who own these large companies and have these outstanding bills and there may be a couple that have several apartment buildings that owe maybe a hundred thousand dollars or more. How do we allow them to get such high bills?

MR. KNUDSEN: We don't. But to go after them, we have spent thousands of man hours and lots of money tracking these people and with some success, but with a lot of frustration because they manage to elude us in the courts and the processing of our applications against them. It isn't for lack of trying, but there is some real frustration out there of our efforts. But we're going to keep pushing.

COUNCILWOMAN TASCO: Let me ask a couple questions, then I'll be done.

The Mayor recently confirmed that the City's budget for Fiscal Year 2005 no longer assumes that PGW will make the $18 million payment due by June.

Is it your understanding that this payment is being deferred until later, or is it that the City will not be paid at all this year?

MR. KNUDSEN: My understanding is that the City will forego the payment completely this year. That's what we have been told.

COUNCILWOMAN TASCO: Then does this mean that City Council has to approve this by the ordinance, the management ordinance?

MR. KNUDSEN: As I understood the conversation with the Finance Director and the Mayor's Chief of Staff that there is an ordinance being proposed to allow this to happen, yes.

COUNCILWOMAN TASCO: Thank you. I think we'll let you go a little bit today, right, David? We're going to recess until the 30th also at 2 o'clock.

MR. KNUDSEN: Thank you very much to you and to the Committee and the opportunity to present our case to you. Thank you.

COUNCILMAN COHEN: I certainly urge that between now and the 30th you give every consideration to the withdrawal of your application, telling them that you thought you had the authority, or whatever reason you wanted to give, and you're withdrawing and will communicate with them later.

MR. KNUDSEN: Thank you for your thought.

COUNCILMAN COHEN: I'm committed to not supporting anything for PGW as long as you disregard City Council. You've done that constantly. This is not the first time, Mr. Knudsen. We've had this discussion in open meeting. But you continually choose to ignore City Council except in those instances where you need our help specifically, like on a budget. And that's all you use us for, for that purpose. And until that changes, I'm convinced the management is more at fault than anyone else because you freeze everybody from helping you by your elitist manner and refusal to recognize the proper authorities in Philadelphia.

MR. KNUDSEN: Councilman, it's our intention to work more closely with Council, and I appreciate your admonition on this and we will respond. Thank you.

COUNCILMAN COHEN: Thank you.

COUNCILWOMAN TASCO: I think what we'll do, when we have the hearing on the 30th, the witnesses will come prior to the testimony from the company. So Mr. Bertocci, if you wanted to testify, you'll be one of the first.

COUNCILMAN COHEN: Mr. Bertocci, you feel you would like to be heard today?

MR. BERTOCCI: I'm not going to be here next week so...

COUNCILMAN COHEN: Why don't you come today?

MR. BERTOCCI: I just have a few comments.

COUNCILWOMAN TASCO: Come on. We'll wait.

Good afternoon. Would you state your name for the record, please?

MR. BERTOCCI: My name is Philip Bertocci. I'm the supervising attorney of the Energy and Community Legal Services. I'm testifying here today on behalf of Community

Legal Services constituents which represent low income people in Philadelphia, up to 187.5 percent of poverty. Many of these folks do not benefit from LIHEAP and do not benefit from CRRP, the low-income programs, so they bear the full brunt of any PGW rate increases because there's nothing available to them except whatever resources they might have.

I have presented some written testimony, and I'm not going to read it. I'm just going to summarize some aspects of it or highlight some aspects of it for your attention.

I put together a chart at the end of my testimony which just summarizes what the level of rates are in Philadelphia now, what they would be as of September 1, 2004, with the GCR whip PGW has applied for, and what they would be with the GRC plus this CRRC, which everyone knows what it means now so I don't have to go through it again.

The bottom line is -- the bottom line on my chart too is if the CRRC was approved at the level which is proposed and if the GCR was approved at the level at which it is proposed, there's a potential that customers would have a total bill, a total annual bill of $1,505 annually. Now, $1500 annually is a very large amount. PGW as of last November had an annual bill of more than 10 percent than the next natural gas utility which was equitable in Pittsburgh. The annual bill was $300 more a year than PECO Energy Gas which operates in Southeastern Pennsylvania and has some very poor sections as well as having some sections which are not so poor. But, of course, we have Chestnut Hill and some fairly prosperous sections of the City also.

I think that we have to look at the CRRC proposal in the context of a utility which already has unacceptably high bills and a utility in which bills have gone up very fast in a short period of time.

I'm like Mr. Knudsen, I think that the reasons that the increases really started in November of 2000 and in November of 2000 bills were about the $850 level, 850 to $900 level, and they've gone up steadily from there. I don't believe that is totally a result of simply gas costs, as Mr. Knudsen says. In fact, about three-eighths of that increase since 2000 can be directly attributed to a base rate increase of $70 million. So there are a lot more factors going into this. This is not an increase which -- I don't think PGW's present situation can be described merely in terms of due to factors beyond PGW's control. The factors which give us a potential $1500 bill involve the total utility, all the ways in which PGW has been managed and mismanaged over the years.

Sometimes PGW wants to describe it as a culture of non-payment or a culture of entitlement. I would say more likely that what we are experiencing in part is a crisis of credibility. This is a utility which has had great trouble accurately and consistently billing its customers. It struggled since 2000 in order to get a credible collections system together, contrary to what you've heard today, although I think the foundation has been laid. I think that we have a call center which is better than what existed before. It still is not state-of-the-art. They're still not answering 80 percent of their calls in 30 seconds. PGW employees are still not consistently talking to customers and telling them exactly what their rights are and what their bill is and being able to give a credible explanation to many bills which seem to be, at least from the basis of what I have seen, bills that seem to be rightfully too high and incorrect. So that this is a much more complicated situation than the company would like us to believe.

Not to take anything away from the tremendous effort and dedication of PGW's present management. This is not intended to be any kind of personal attack on them. It's intended to say that there are policy issues here which go way beyond the immediate crisis which brings us here.

The last thing that I want to say -- because I know it's been a long day -- is that it seems to me that the CRRC is not the first thing one would suggest; it's the last thing one would suggest. Giving up the $18 million payment this year or putting a plan by which a portion of the $18 million payment was given up for a series of years could be part of a larger plan to make sure that PGW begins each fiscal year with the level of cash which it needs in order to get gas for the coming year.

There's also the possibility, which PGW has not mentioned at all today, of various kinds of gas management contracts which enable PGW to husband its cash in a way where it doesn't need so much money right at the beginning of the fiscal year.

Those are things which I know that PGW is considering but have not been brought before you, and they would be ways in which this cash problem could be dealt with.

Furthermore, we need still steady pressure in terms of improving collections. It's good that Accentia (ph) is here. We have yet to see any real results from Accentia's activities. We know that they're putting a plan together. We know that they are charting a course but, again, as you know, with any business, and this is a big business, a change takes a certain period of time. It's not going to be immediately discernable.

The other thing I want to say is that it is always a kind of a wishful thinking that goes on. But, for instance, we hear that PGW is in fact reporting people that can pay but won't to collection agencies. I think the term that was used was "a process," we're in the process of reporting them. Well, as far as I know, it's only in the process. That doesn't mean that anybody has actually been reported. People have been told if they don't pay -- this is the best knowledge that I have. People have been told if they don't pay, they may at sometime be reported to a collection agency. I would expect -- not to a collections agency, to a credit reporting agency. I would expect that if PGW put together a program of that sort just like other programs like the senior citizen program, that there needs to be groundwork laid. The public needs to be informed as to exactly what to expect. The program has to be well defined. And if all those things happen, that would create a major incentive on the part of those people who can pay but won't to move PGW up the list right next to their mortgage in terms of their payments.

I know it's been a long day. I thank you for giving me the opportunity to talk. I will be out of town next week, but I'm always available if any Councilperson has a question or their staff has a question. I can give my perspective and give you some idea which perhaps you might want to verify with PGE.

COUNCILWOMAN TASCO: Thank you very much for your testimony.

COUNCILMAN COHEN: Is there anybody else who wishes to be heard this afternoon?

If not, the hearing will be recessed until Tuesday, March 30th at 2 o'clock. The Committee stands in recess until that time.

(Council adjourned at 5:25 p.m.)

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C E R T I F I C A T I O N

I HEREBY CERTIFY that the foregoing proceedings of the Council of the City of Philadelphia of Wednesday, March 24, 2004, were reported fully and accurately by me, and that this is a correct transcript of the same.

RE: COMMITTEE ON FINANCE
COMMITTEE ON TRANSPORTATION
AND PUBLIC UTILITIES

____
Lisa C. Bradley, RPR