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IN THE COMPETITION
APPEAL TRIBUNAL

Case No. 1106/5/7/08

Victoria House,
Bloomsbury Place,
London WC1A 2EB

18 September 2009

Before:

LORD CARLILE OF BERRIEW Q.C.
(Chairman)
RICHARD PROSSER OBE
GRAHAM MATHER

Sitting as a Tribunal in England and Wales

BETWEEN:

ENRON COAL SERVICES LIMITED
(in liquidation)

Claimant

– v –

ENGLISH WELSH & SCOTTISH RAILWAY LIMITED

Defendant

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HEARING – DAY THREE

APPEARANCES

Mr. Paul Lasok Q.C., Mr. Daniel Beard and Mr. Rob Williams (instructed by Orrick, Herrington & Sutcliffe (Europe) LLP) appeared for the Claimant.

Mr. Mark Brealey Q.C. and Miss Maya Lester (instructed by Freshfields Bruckhaus Deringer LLP) appeared for the Defendant.

1 THE CHAIRMAN: Welcome to the video conferencing suite RCJ style.
2 MR. LASOK: I ought to apologise for two things. The first thing is that my learned friend and I
3 have switched round. We do not believe that the Tribunal is going to be deceived by the
4 change of position. It is simply that my learned friend wants to be closer to the witness, Mr.
5 Staley. In the afternoon, if the Tribunal is happy with that, we will switch back to where we
6 were.

7 THE CHAIRMAN: You can sit wherever you like. The only thing that has happened this
8 morning is that I cannot see Mr. Williams properly. Otherwise, we are fine. I will deprived
9 of his film star good looks! Then I forget Mr. Brealey!

10 MR. LASOK: Sir, apologies for the delay in starting.

11 THE CHAIRMAN: I understand that Mr. Staley has come from Singapore. Are you absolutely
12 sure that he is ready to start?

13 MR. LASOK: He nods.

14 THE CHAIRMAN: If he wants a break at some point -- We will have a break mid-morning
15 anyway, but if he wants a break because he is exhausted --

16 MR. LASOK: I am much obliged.

17 THE CHAIRMAN: We have had the s.58 note which we will read over the weekend, if we may.
18 I do not think we have to read it during the day today, do we?

19 Mr. STUART STALEY, Sworn

20 Examined by Mr. LASOK

21 Q Mr. Staley, you have got to your left a row of files which we are calling bundles. Could you
22 go to Bundle D, Volume 1, please.

23 THE CHAIRMAN: You must realise that the configuration of the bundles for us is not very good
24 here. It will take a little longer.

25 MR. LASOK: Could you go to the beginning? At Tab 1, could you look at that, and particularly
26 p.15, which contains a signature? Could you tell us whether or not that is your statement,
27 signed by you?

28 A It is my signature.

29 Q When was the last time you were able to read your statement?

30 A Is this my first or my second statement?

31 Q This is the first statement.

32 A Probably within the last thirty days.

1 Q If you go further on in the bundle you will come to another tab, Tab 16A at p.115.1. Could
2 you have a look at that, and in particular p.115.14, and tell us whether that is your signed
3 statement?

4 A Indeed. That is my signature.

5 Q Have you had a chance, an opportunity to read the transcript of the hearing over the last
6 couple of days?

7 A Not much. I scanned some of it on the flight.

8 Q Have we got a clean copy of the transcript? (After a pause) I would like to give you a copy
9 of the transcript of yesterday's hearing. Does the Tribunal happen to have a copy of
10 yesterday's transcript?

11 THE CHAIRMAN: I am told we have - though I was not aware of it until a moment ago.

12 MR. LASOK: Could you turn to Day 2? Mr. Staley, could you possibly look to p9, please? This
13 is the evidence given by Mr. Crosland yesterday. If you have p.9, could you read from line
14 24 to p.10, line 9? Page 9 starts, "Q. I think you deal with some of these things --" Could
15 you read from there to the end of the answer at line 9 on the next page, please? (After a
16 pause) Do you have any comment that you would like to make about the answers given by
17 Mr. Crosland which are indicated by the letter A in the margin, and in particular the answer
18 that he gave on p.10 at lines 5 to 9?

19 A Well, first, I don't think it has anything to do with mark to market accounting. So, I don't
20 understand that comment. Second, the characterisation of Enron's business as being backed
21 off against contracts I don't think is generally true. But, there were elements of our first
22 transaction with Edison Mission for which it was true.

23 Q Could you explain what is described at line 5 on p.10 as 'market to market accounting' but
24 it may be mark to market accounting? Could you explain what that is?

25 A It is an accounting convention where assets are daily or regularly valued against their then
26 current market value.

27 Q Could you now turn to p.42, please? Go to line 12. Do you have a line 12 on p.42 that
28 says, "Q. Okay. Purchasing on an *ad hoc* basis --"

29 A Yes.

30 Q Could you read from that line to line 17 on the same page? (After a pause) I think that you
31 were basically in charge of Ferrybridge and Fiddler's Ferry after AEP acquired both power
32 stations from Edison. Can you remember when that was?

1 A I joined AEP in December 2001 and from probably March 2002 I was responsible for the
2 coal supply to those stations and from September 2002 I was responsible for the entire
3 European operation for AEP.

4 Q Do you happen to know whether or not Edison had done any hedging in 2000/2001?

5 A Hedging -- The Enron arrangement that had been restructured continued at that time period,
6 and that fixed their prices and -- I think we backed it off to a dollar denominated contract, if
7 I remember correctly. So when you say 'hedging' -- There are a number of different things.
8 Hedging involves creating certainty through contractual commitments. There is a volume
9 element to that. There is a price element to that. There can be an exchange rate element to
10 that. There can be an interest rate element to it. So, I think that they certainly had some
11 elements of that covered with the ongoing supply from Enron and I believe they also had
12 ongoing commitments to receive coal at known pound Sterling denominated prices from
13 Powergen. I believe they also during that time period purchased some incremental tonnes
14 from perhaps various international suppliers, but the one that I recall is Glencore.

15 Q Do you happen to know whether or not they did any hedging or other forms of protection in
16 relation to the other supplies of imported coal or their imported coal requirements - not the
17 Enron ones, but the other stuff?

18 A Just by virtue of committing to any of those contracts, there are elements of that that could
19 be considered a hedge. So, if my memory is correct that they had purchased from others,
20 such as Glencore, even if it was just on a one-off basis, they fixed their coal price for one
21 cargo worth of coal. So, you know, that would be a very limited amount of hedging. Now,
22 if they had fixed the price and the volume for a longer period of time, they would have then
23 been making a more significant hedging commitment.

24 Q Could they have protected themselves from things like movements in the market price of
25 coal and exchange rate movements - we are talking now about imported coal - as effectively
26 themselves or would it have been better for them to have used an arrangement with Enron?

27 A I think that the larger the portfolio that someone has, the more efficiently you can manage
28 on the margin. That is precisely why, in our business model, we focused on smaller
29 generators with a limited number of plants because they could not achieve those efficiencies
30 themselves, whereas a much larger generator, such as the German utility Eon, that now
31 owns Powergen, can optimise across a much larger fleet, and therefore those efficiencies --
32 the marginal impact of one transaction, or one ship, has far less impact on the whole than a
33 smaller generator. So, it could have done some of these themselves, but my belief is that

1 anyone with a larger portfolio could have done it more effectively, and hence delivered
2 greater flexibility and less expensive pricing.

3 Q On the same page, could you go to line 20. This, you see, starts, "This is a copy --" In part,
4 this is an attempt by me to make the longest question in recorded history. Could you read
5 that down to the next page, p.43, line 27 - so that you see the question and the answer that is
6 given?

7 A The testimony or the question?

8 Q I think that might have been the second longest -- (After a pause): In the answer that is
9 given by Mr. Crosland to the question he raises two, what could be described as, objections
10 to the British Energy contract that he was looking at. The first concerns the sourcing of coal
11 because he says, if you go to lines 22 to 23,

12 "We wanted to test coals, identify specific coals that suited our power stations and
13 buy those coals".

14 Then, the second objection that he raised is in the next sentence, which is a reference to
15 there being a firm delivery tonnage of 2.3 million in the British Energy contract. He says
16 that that was 'far more than we [Edison] would have wanted to contract for'. Looking at
17 those comments made by Mr. Crosland, do you have any comments on them? Would any
18 of these elements have been negotiable with Enron, or not?

19 A They were different for almost every customer.

20 Q Then, if you go to p.44, to the bottom at line 32, could you read from line 32 to line 5 on the
21 next page, which ends with the phrase 'the horse's mouth'? (After a pause) Do you have
22 any comment on that?

23 A It's hard for me to see the benefit. I think the constraints of dealing with a single mine in
24 general - there may be one-off cases - tend to be tighter than dealing with someone who's
25 managing across a portfolio.

26 Q Then the last part of the transcript that I will ask you to look at -- At p.45 could you read
27 from line 6 down to line 11, please? (After a pause) Have you any comment on that?

28 A I disagree with that. I mean, a lot of these references seem to speak specifically to some of
29 the issues that led to the renegotiation of the first contract between Enron and Edison
30 Mission, and, again, I don't think mark to market accounting has anything to do with it. I
31 can see how it might be interpreted to have had something to do with it in the first contract
32 between Enron and Edison Mission because, as I discuss in my witness statement, they
33 made the error of contracting for entirely too much coal and then the market price declined
34 and they wanted to defer or just get out of delivery of some of those times but showed no

1 willingness to share in any of the costs associated with doing that, which obviously has a
2 link to the then current market price, which is the only connection I could make to mark to
3 market accounting. But in general our approach was what is described here as antithetical
4 to what our approach was; we did not contract specifically with third parties on down the
5 line and back to back exactly what our obligations were. In fact, the value that was created
6 by our business model was precisely from doing something other than that which was
7 maintaining the flexibility to mix and match the component parts to find the cheapest, most
8 efficient means of meeting our delivery obligations to a specific plan.

9 MR. LASOK: If you stay there Mr. Brealey will have some questions for you.

10 Cross-examined by Mr. BREALEY

11 Q Mr. Staley, could you go first to para.7 of your first statement? I apologise in advance but
12 we will be going from bundle to bundle, and document to document, but that is inevitable –
13 para.7 of your first statement. You say there that you came to the UK basically to create
14 and develop Enron’s business model in the UK. Is that correct?

15 A UK and more broadly other markets outside of the US.

16 Q So far as the UK is concerned, does that mean that the Enron-type model was rather untried
17 and untested at the time, the fact that you were coming to create it and develop it?

18 A I think that you are referring specifically to coal but I would say that it more broadly applies
19 to everything that Enron did because these markets were just deregulating at that time and
20 by definition a lot of these market activities were occurring for the first time in many
21 markets.

22 Q Is it true to say that in the UK at least there was a bit of scepticism about this E2E model
23 with the power generators in the ports, is that true?

24 A There are those that were sceptical.

25 Q If you go to para. 15 of your statement, you give a description of the Enron business model,
26 and I quote from para. 15, essentially the business model is “to manage the entire supply
27 chain of its customers’ coal requirements from origin to plant.” That is the essential
28 function of an E2E model, is it not? To manage the entire supply chain of coal
29 requirements from origin to plant, you encapsulate the function.

30 A Yes.

31 Q With that in mind, could you go to bundle D2, you will have to keep your statement open.
32 In D2 go to Mr. Crosland’s statement p.165, para. 10, in the middle of that statement says:

33 “Edison’s initial arrangements for supplying coal to those power stations took the
34 form of ‘E2E’ contracts, namely ‘end to end’ arrangements in which the power

1 station contracts with the same party for both the *supply* of coal to a port or
2 loading point, and for its *haulage* from the mine or port to the power station.”

3 - and that essentially is encapsulating again the function of your E2E model. Go to para. 7
4 of his statement, where he is talking about his core management team, which I think you are
5 aware. He says:

6 “The function of this team was to manage the process of obtaining coal from
7 initial procurement to final delivery to the power station, including by negotiating
8 favourable pricing terms and tailoring coal supply to the specific needs of the
9 power station at a particular time.”

10 Now, with these definitions in mind as to the function of the two models, I think you would
11 accept that there is a broad overlap between the two functions. You may say they operate
12 differently and the models are to a certain extent the way that you have bid portfolios, they
13 operate differently, but in broad terms, the broad function is the same, i.e. to manage the
14 process from initial procurement to final delivery?

15 A Broadly speaking they both involve supplying coal to power stations.

16 Q So you would accept from that that there is a degree of overlap between the two functions?

17 A They achieve the same end, albeit by different ways, yes.

18 Q We get a sense of this overlap, if I could ask you to bundle G2 at p.502, you may not have
19 seen these documents for a while, but it is something you were aware of at least on 17th
20 April 2000. You need to start at 503 to get a sense of what Mr. Crosland is saying to you.
21 His email to you is at 503 and your reply is at 502.

22 A. Yes.

23 Q I am particularly interested in the Weglokoks’ issue. As I understand it, Weglokoks was
24 one of the three types of coal, or coal supply in the 1999 contract?

25 A I think that’s correct, I can’t confirm that it was only three.

26 Q Can you inform the Tribunal what the issues were? Why was Mr. Crosland trying to
27 change the restrictions, and why were you pretty upset saying it was “utterly ridiculous”?

28 A I am sorry, is this all under point 3.

29 Q Yes, it is under point 3, take your time.

30 “For you to equate our discussions with Powergen/LBT to your request to contact
31 Weglokoks in an effort to change restrictions in our contract is (in my estimation)
32 utterly ridiculous.”

33 So it appears Mr. Crosland is trying to contact the supplier direct, and you are annoyed
34 because it is your contract, is that correct?

1 A Yes, it appears that that is the case.

2 Q And from that I think you would accept that whatever E2E model you are really talking
3 about there is an inherent limitation – you may say it is a good thing/ it is a bad thing – but
4 there is an inherent limitation in the Enron business model which is it precludes the
5 customer from contacting the ultimate supplier?

6 A I don't agree with that.

7 Q Well why are you saying it is utterly ridiculous?

8 A Well I think it's specific to this issue, and I don't recall for certain, but just from looking at
9 the context here, it appears that this relates to some of the disagreements that we had with
10 Mission prior to the restructuring where we felt they were trying to frustrate our ability to
11 meet our contractual obligations by delivering coal to their power stations. So I would say
12 that anything related to that ----

13 Q We will come on to the restructuring in a moment, but I would repeat the question, that
14 whatever model you are operating – and we are going to have to come on to that soon – in
15 general terms you do not like the generators contacting your counterparty?

16 A It depends on what the issue is. In fact, many times we would take our counterparties to
17 visit certain mines to help them get comfortable with either quality or security of supply
18 issues.

19 Q So if Mr. Crosland came to you and said: “Okay, I am going to make a contract on an E2E
20 basis, but I want complete freedom to contact the supplier and change the contracts that
21 you, Enron, have concluded with that supplier”, and you say “That's fine”?

22 A No. The second clause is the one I find I am disagreeing with! (Laughter)

23 Q And that is exactly what he is trying to do there, is it not? At point 3 he is upset. Can you
24 enlighten us what the restriction was – you are the author of this email?

25 A Yes.

26 Q What was Mr. Crosland trying to do?

27 A I don't recall for certain, but I think he was probably dealing with major contractual terms,
28 either volume, timing, quality, location.

29 Q Pretty important terms?

30 A Yes, and that's why I would find – back to your previous statement – the second part of the
31 second clause I wouldn't be happy with a customer contacting a supplier to adjust key
32 commercial terms in our own contracts, whereas I think what I am attempting to do in this
33 email is differentiate between operational and scheduling issues and key commercial terms.

1 THE CHAIRMAN: Forgive me, Mr. Brealey, so that, Mr. Staley, if the generator was finding
2 that Weglokoks, presumably it is in South Africa, or somewhere?
3 A It's Polish.
4 Q That the coal from that mine in Poland was producing more sulphur than they expected, to
5 give an example, would you expect that kind of issue to be dealt with through you or direct
6 with the mine in Poland?
7 A Through us.
8 Q Through you?
9 A There were restrictions in the contract for sulphur so if the sulphur content was beyond the
10 limitation in the contract the customer had the full right to reject the cargo and it became
11 our problem to dispose of it elsewhere, or alternatively negotiate an economic adjustment
12 such that they were indifferent to taking coal higher sulphur.
13 MR. BREALEY: The next question is, I think you would accept that the Enron business model
14 is largely based on supplying imported coal?
15 A No, at that time it was because of elements of the market that put a huge amount of
16 importance on low sulphur content, which typically is more commonly found outside of the
17 country than in the country and because of the cable rate, pound sterling/dollar exchange
18 rate, it was at that time really focused around international markets. But when those two
19 things changed so did our commercial focus.
20 Q And when did they change?
21 A Well, I can't remember the path of exchange rates exactly but I think they bought them
22 down at about 1.38 or so to the dollar, 1.30 the pound in 2000/2001, the pound was 2.10 last
23 year for a brief, glorious period. Then the sulphur restriction as people installed through gas
24 to sulphurisation ** their need to restrict – and I think some of that was a function of the
25 large combustion plant directive which had various time periods where it was implemented
26 and that was 2000.
27 Q In 1999/2000 do you accept that the Enron business model was largely based on supply of
28 imported coal?
29 A Yes.
30 Q It is a few years ago but could you give a percentage of imported domestic that was burned
31 in 2000?
32 A That was burned in the UK?
33 Q Yes?
34 A In 2000 my guess is that there is probably still more UK coal being burned than imports.

1 Q I think it is a given that most UK generators burn both domestic and imported coal?
2 A I can't say that definitively. There are certain plants like Energy's Tilbury plant on the
3 Thames which are much more well suited ----
4 Q The vast majority burn imported and domestic?
5 A Yes, I think so.
6 Q And from that I think you would accept that if a UK generator, for example like EME is
7 going to have an E2E contract with you, again it is inherent in that model, the Enron
8 business model, that the generator will have to conclude two haulage contracts?
9 A No.
10 Q No?
11 A We could very easily sweep the supply of indigenous coals into an end to end contract.
12 Q Are you really saying that, say, Powergen would have appointed you, one of its biggest
13 competitors, to deliver its coal to Fiddlers Ferry or Ferrybridge?
14 A I am not saying that at all. What I am saying ----
15 Q No, it is unlikely though?
16 A What I am saying is that in contracts we had, such as the contract with British Energy we
17 also supplied indigenous coals under that contract, and if they were to extend the reach of
18 that contract there is nothing that says you could not sweep all the coals that they would
19 burn in a given year under one end to end contract.
20 Q Do you accept that as far as EME is concerned in 1999/2000 Mr. Crosland would have had
21 to have concluded at least two haulage contracts?
22 A Yes, although I can't remember the specifics of the Powergen contracts. I think the
23 Powergen contracts may have been delivered at the station, in which case Mission would
24 have only – well, Mission would not have had a haulage contract for the Powergen
25 volumes, I guess is what I am saying. Does that makes sense?
26 Q Well, Edison Mission had an E2E contract with Powergen.
27 A So you are saying there were two haulage contracts in existence that applied to EME's
28 plants?
29 Q Yes?
30 A Yes.
31 Q And do you remember that Mr. Crosland found that frustrating?
32 A Yes, as did I.
33 Q You have already mentioned in answer to a question from Mr. Lasok, and it is a point that
34 you make at para. 14 of your first and 23 of your second, para. 14 if you want to go to it in

1 the first statement, where you say that essentially the focus of the E2E model was based on
2 the smaller merchants. So again, try and just ball park, excluding the large portfolio market,
3 the Powergens, what share of the market were you actually targeting?

4 A The total market or the import market?

5 Q The total market?

6 A It's been too long.

7 Q 10 per cent?

8 A I think it was more significant than that, it would have been the two Mission plants, it would
9 have been the Cottam ** that was bought by EDF, run on electricity.

10 Q It is a fact that you refer to in a complaint to the Regulator, and the Regulator decides the
11 point at para. 34 of its decision. There is a fact which says that the DIY model accounted
12 for 70 per cent of market, whereas E2E 30 per cent. Does that sound about right at that
13 time?

14 A You're talking total call consumption?

15 Q Total?

16 A Yes, that doesn't surprise me, therefore I think we were targeting more than 10 per cent of
17 the market.

18 Q When you say at para.22 that the Enron business model was highly successful supplying
19 over 50 per cent of power generators' demand from non-imported coal, just to be precise on
20 this that 50 per cent is not an E2E basis, is it? You are supplying ----

21 A I think it also included volumes that were sold CIF.

22 THE CHAIRMAN: Your voice is dropping, Mr. Staley.

23 Q I think it also included volumes that were sold CIF or delivered port rather than station.

24 MR. BREALEY: So are you able to say what percentage was being supplied on an E2E basis?

25 A No.

26 Q If you strip out the renegotiated Edison contract does that give you an idea? You say it is
27 highly successful, and you give, in support of that, that it is 50 per cent of demand for
28 imported coal, and what I am trying to work out with you is whether the two go together
29 because the 50 per cent seems to include a substantial quantity of ----

30 A E2E volumes.

31 Q Well, E2E, but also just pure CIF quantities?

32 A I don't remember the breakdown but I know we did a lot of both types of business.

33 Q Picking up on a point that Mr. Lasok referred to, if you go to para.16 of your first statement,
34 where you talk about feasibility, you say:

1 “Flexibility was the key attribute around which we built our business model.
2 Starting with the coal itself, Enron had a wide range of sources for various qualities
3 of coal.”
4 You list them. Then:
5 “The greater the number of coals that a generator was able to burn, the greater the
6 flexibility and the cheaper the price we were able to offer them.”
7 If, for whatever reason, the generator – for example, Mr. Crosland, Edison – preferred to
8 specify a limited number of different types of coal, so it wanted to limit the coal, I think you
9 would accept that it follows that a competitive disadvantage of your model is reduced?
10 A Yes.
11 Q Therefore, you are unable to get lower prices?
12 A I would say less able.
13 Q Less able – indeed, was that the case with Edison, because, as I understand it, there were
14 three types of coal in 1999, one of which was carbocol, which he did not like. Did that
15 impact on your ----
16 A Yes, I think we could have offered Mission cheaper pricing had they been more willing to
17 expand the number of coals they were willing to accept and more contractual flexibility.
18 Q Also taking the DIY model, would you accept that Mr. Crosland and his management team
19 on his DIY model, can look to a variety of potential suppliers?
20 A Yes.
21 Q An example of this, if we just go to G5, the first document, 1239 – do you see that
22 document there, “Coal Tender Assessment – June 2001”. This is a coal tender that
23 Mr. Crosland put out. I believe it was a spot contract, by looking at it – you would agree
24 with that? We see all the different companies supplying there?
25 A It supplied responses, yes.
26 Q You see half way down Enron, you must have made a tender?
27 A Yes.
28 Q Then the main paragraph, it looks as if you did not even make the second round, looking at
29 Glencore or Total. My broad point, and I think you have already accepted it, that
30 Mr. Crosland and his in-team could put a tender out and seek supply from a wide variety of
31 sources, obtaining the cheapest price?
32 A Yes, but I think you are attempting to conflate purchasing from a wide number of people
33 with optimising across suppliers from multiple origins.

1 Q It may be, but if he wants to limit his supplies to two or three types of coal it would be more
2 in his interests then to go down this road, because your business model is not as
3 competitive?

4 A I would say even for a limited number of coal – I try to make the point in both witness
5 statements that we were really engaged in two entirely different things, and our model
6 focused on trading around elements of the supply chain that DIY procurers of coal tended
7 not to trade around. So we were creating incremental value that was by definition additive
8 to the total. That incremental value would indeed be less for a smaller number of coals than
9 a larger number of coals, but it exists nonetheless.

10 MR. MATHER: Do you think, Mr. Staley, that Edison was really absolutely wedded to that DIY
11 model after Mr. Crosland had gone?

12 A I don't know. I think some of the emails that I've been asked to review indicate that we
13 always hoped not and we attempted other ways of trying to show the value that could be
14 created by an E2E supply, as opposed to a DIY supply, but I always had the impression that
15 they were always willing to consider the differences between the two. It wasn't as though
16 they categorically rejected anything other than DIY.

17 Q When he came on board in late 1999 there were confirmations – there was a December
18 confirmation of the E2E arrangement – but after that did you feel that he would really have
19 preferred to do things in a DIY way? Was there any evidence of that?

20 A It's sometimes hard to separate it from all the heat that was generated by the predicament in
21 which they found themselves with lower generation than expected, too much coal to
22 suppliers. We often – I think some of the documents I reviewed bear this out – we would
23 often offer in response to a spot tender a delivering station price.

24 MR. BREALEY: I am going to go to bundle G2 and also paras.27 and 28 of your statement. The
25 first sentence of para.27 says:
26 “The relationship between Enron and EME deteriorated in the first half of 2000.”
27 In the context of that evidence I would like to take you to certain emails. The first is at
28 p.422. Is this one of the emails that you have reviewed, do you know?

29 A Let's see, I scanned this on the plane this morning. Is there a particular part? I know the
30 nature of it.

31 Q This is to Nigel from George McClellan – George McClellan, he was the ----

32 A He was my boss.

33 Q The main man, he was in Houston?

34 A Correct.

1 Q He is referring to fairly diverging ideas, and then in the third paragraph he says:
2 “Based on Mission’s revised burn plan it is obvious that you will not require
3 quantity of imported coal already purchased from us for delivery through June
4 2001.”

5 As I understand it, and correct me if I am wrong, the original 1999 Master Coal Agreement
6 and indeed the confirmations were agreed in the US – is that right?

7 A I don’t think so.

8 Q No?

9 A There were some US personnel involved, but we certainly negotiated them over here.

10 Q Do you know why Edison over-committed itself?

11 A Their electricity models, they thought that they could create incremental value from the two
12 power plants by increasing the number of run hours. I think the capacity factor of those two
13 plants had been quite low under Powergen’s ownership. They modelled against their own
14 power price expectations and against bringing in lower sulphur imported coal. They
15 thought they would have the ability to dramatically increase the number of run hours, and
16 when they did it summarily crashed the electricity prices at certain parts of the day and
17 certain parts of the year to the point where it became uneconomic for them to run, in which
18 they contracted for far more coal under the assumption that they would be able to run many
19 more hours.

20 THE CHAIRMAN: Is this connected with the boom in the use of gas?

21 A It’s all related, but this was much more specifically related to a diversification in the number
22 of owners of coal plant. If I remember correctly, in exchange for being allowed to vertically
23 integrate and buy regional electricity companies, supply companies, the large generators,
24 Powergen, Energy, and TXU Eastern, were required to divest of some coal plant. As that
25 coal plant went from really being in an oligopoly type environment where it was controlled
26 by three people to a much more diffuse ownership, it looked a lot like the US airline
27 industry.

28 MR. BREALEY: This is dated 17th February and refers to Edison’s revised burn plan. Can you
29 remember when the revised burn plan was?

30 A Yes.

31 Q Was that the cause of the problems when they found out that they were going to take too
32 much coal?

1 A Well, I think it was patently obvious that there was too much coal even for a burn plan we
2 shared. My guess is it was rather confirmation of what everyone already knew than bolt
3 from above that shed any new evidence on the subject.

4 Q There have obviously been some proposals even at that time, and then the first sentence of
5 the fourth paragraph says:

6 "We are obviously not in a position to forgive our coal supply contracts with
7 Mission, especially as we are on mark to market accounting."

8 Mr. Lasok asked you a couple of times about mark to market accounting. What is quite
9 clear here is that you are mark on to market accounting, so what is Mr. McClellan talking
10 about here?

11 A Well, we were on mark to market accounting for liquid products that we traded, and the
12 implication of that sentence is that if were we to forgive the future obligations to Mission
13 we would have to take a significant current period loss, and that loss would not be – it
14 would be a present value loss that was taken completely in the current period, rather
15 something that was accrued over the course of the contracts.

16 Q So you value the contract on the Monday, and if you are going reduce the volumes then that
17 is going to decrease the value ----

18 A On Tuesday.

19 Q -- on Tuesday. At the bottom, again picking up something that Mr. Lasok was talking
20 about:

21 "In short we are here to work with you regarding the present difficulties, just as we
22 have in the past."

23 He is talking about a one week window ----

24 A Sorry, can I ----

25 Q Yes, of course.

26 A It's not always the case, what I've just stated. If prices have declined and we tore up the
27 contract we would mark a current period loss on the Tuesday. If prices had in fact
28 appreciated and we tore up the contract we would mark a current period gain on the next
29 day.

30 Q What about – forgetting prices – if prices remained the same, the volumes of coal that the
31 purchaser, Edison, has committed to is reduced by half?

32 A If prices were the same as on the day that signed the contract ----

33 Q If volumes are reduced?

34 A Yes, then there would be no – well, it depends.

1 Q I think what he is saying is because you value the contract at a certain quantity, because of
2 the mark to market accounting there is no way that you forego the current value of the
3 contract?

4 A Actually there is a way, and that is ultimately how that contract got restructured.

5 Q Yes, I am going to come on to that.

6 A Okay.

7 Q He talks at the bottom about:
8 "We now have a one week window of opportunity to restructure our contracts with
9 Mission, otherwise our obligations with our coal supply and transport
10 counterparties will become very cumbersome, and expensive to unwind."
11 That was one of the problems with the 1999 contract. You did have back to back contracts.
12 Edison was agreeing the purchase of a substantial volume and the only way that you could
13 guarantee Edison that volume was to have a back to back contract?

14 A I don't necessarily – those are broad statements and I don't agree with them.

15 Q You are in the loop on this, are you not?

16 A Yes.

17 Q What is he talking about here? Why are they going to be cumbersome to unwind? Why is
18 this only one window of opportunity?

19 A I don't know. That did strike me as somewhat confusing. I think it's just that the supply
20 chain in coal is not like a tap that you can turn off. There's 30 to 60 days worth of product
21 that's begun moving somewhere, and the further it gets towards its ultimate delivery the
22 more expensive it gets to deal with. So I think the reference is that the more stuff that's on
23 the water or making its way to the water that finds its way to the UK and the more coal that
24 gets piled up at the ports, the more expensive the ultimate solution is, so let's hurry up and
25 find a solution while it's still less expensive.

26 Q I think it is a little bit more than expensive because we see the reply ----

27 A Where is that, the previous page?

28 Q Yes, on 421. We have got George, and it is from Nigel, being, if I can summarise it, a bit
29 miffed that certain contracts are going to be concluded on his behalf, and the reason that
30 Mr. McClellan gives is in the very first email:
31 "We are in the final stages of entering into contracts with our various
32 counterparties in order to be in a position to fulfil our contractual requirements
33 with Mission."

1 I do suggest to you that there is a reason why they are going to be difficult to unwind,
2 because they are going to be rigid back to back contracts.

3 A Where is this?

4 Q I am sorry, it is in the top email, "Nigel, thanks for your email", and then the second
5 sentence:

6 "We are in the final stages of entering into contracts with our various
7 counterparties in order to be in a position to fulfil our contractual requirements
8 with Mission."

9 THE CHAIRMAN: I am sorry, I have not found it, which page?

10 MR. BREALEY: I beg your pardon, sir, p.421. Then the reason why they are going to have to
11 enter these back to back contracts is "in order to be in a position to fulfil our contractual
12 requirements with Mission". I suggest to you this is where there are, even under an E2E
13 contract where you are intermediary, and you are not a coal mine, and the purchaser is
14 committed to buying a large volume of coal and you have got to out to the market and in
15 order to guarantee that to the generator you have got to get a commitment, and that is what
16 the role of an intermediary is, is it not? That is inherent in your model?

17 A But how we commit is a function of how much risk we are willing to bear at any point.

18 THE CHAIRMAN: Mr. Staley, please correct me if I have got this wrong because I may well
19 have. But, it looks to me from the e-mail at pp.422/423 as though Enron were saying, "We
20 have a contract for the supply of a certain amount of coal which we are not going to vary,
21 but we are prepared to re-negotiate the phasing of deliveries". Is that what it amounts to?

22 A Yes. Then we would have also forgiven entirely the deliveries in exchange for
23 compensation for the losses that we would've won.

24 MR. BREALEY: That is essentially how the negotiations went on for the next few months - that
25 you were prepared to forego deliveries provided that Edison paid you. I take the nod as a
26 'Yes'?

27 A Confirmed. I would add a little more comment. We were certainly willing to wear some of
28 the pain to find a solution that was better for everyone - just not all of it.

29 MR. MATHER: Did you feel that Edison were, sort of, levelling with you about their
30 difficulties? Did they come to you and say, "We've got this problem"? Or, did they start
31 behaving in a tricky manner?

32 A My recollection is that it was the elephant in the room that was never openly discussed. We
33 felt that they were intentionally trying to frustrate our ability to deliver to the stations, to

1 then declare us in default of our contractual obligations. To be fair, I think that they felt that
2 we were trying to be wildly inflexible in exchange for some windfall gain.

3 Q Were you being very robust in treating this contract in accordance with dispute practice?
4 Were you taking a hard-nosed approach?

5 A We were certainly scrambling and doing everything we possibly could to meet our delivery
6 obligations. We did not want to put ourselves in a position to do anything that would be
7 cause for terminating the contract and, in the end, be even more costly for us. It was, you
8 know, probably an interaction characteristic of two American firms: "I'll race you to the
9 courthouse" ----

10 MR. BREALEY: That is certainly the impression you get from looking at ----

11 A Whoever imagined it would be me who won the race? (Laughter)

12 Q I think ultimately you both do. (After a pause) We have that as a 'Yes'. So, just to pick
13 up on a few points that were just made then -- Pages 428 to 429, again we see a flavour of
14 these e-mails where Edison is threatening (at p.429),

15 "You will not be surprised I am sure if I tell you that amongst the options that we
16 have to consider for dealing with this situation is that we proceed with a notice of
17 default on your part and formal termination of the contract ----"

18 That is consistent with both Americans trying to get to the first line. Then, on the common
19 negotiation point, if you go to p.520 -- These e-mails were essentially February. Now, we
20 have got March and most of April. What sort of negotiations -- Have a read of this first.
21 This is a letter from Edison's lawyer. So, we have got to the legal stage. He is
22 complaining that he cannot have a sensible negotiation leading to a possible restructuring
23 because you are adopting what he describes as a take-it-or-leave-it approach. You have not
24 particularised the compensation that you say that you are due if you forego volumes. Can
25 you remember whether you were taking a take-it-or-leave-it approach at that time?

26 A I wouldn't term our actions as take-it-or-leave-it. We were desperate to find a solution
27 because the costs to not finding a solution were falling largely -- exclusively -- not
28 exclusively -- I felt that the lion's share of the costs of not finding a solution were worn by
29 Enron.

30 Q If that is the case, why were you not particularising the compensation that you wanted?

31 A I don't recall this exchange of e-mails.

32 Q It appears that you are taking a hard line - you are entitled to the money and had taken a
33 legal approach.

34 A That certainly seems to be the author's opinion.

1 Q Can you recall whether you were at that time playing hard-ball? "I'll be the first one to race
2 you to the court"?

3 A No.

4 Q "Who's going to blink first?"

5 A I think that that was more February timeframe -- end of the year.

6 Q Not much has happened by the end of April 2000.

7 A Yes. Again, my recollection is that we were very motivated to find a solution, but there was
8 a substantial difference of opinion on what the costs of that solution might be.

9 Q You said you were very motivated. If you go to p.525, this is another e-mail from Mr.
10 McClellan to Nigel.

11 "It doesn't look like we've been making too much progress of late".

12 So, you say that everyone seemed to be motivated, but nothing seems to be happening. At
13 the penultimate paragraph he says,

14 "It is fairly obvious that the existing contract format is unworkable".

15 Does that conform to your recollection - that not much progress had been made in
16 restructuring this, but that the existing contract format was unworkable?

17 A Yes.

18 Q If I park the restructuring for a moment, but have a look - because it may be relevant to it -
19 at p.529 -- This is an e-mail from Mr. Kearney, saying,

20 "Given the current situation with Edison Mission, we need to start logging and
21 monitoring every single incident of perceived (or otherwise) obstruction of coal
22 delivery by Fiddler's Ferry and Ferrybridge. Every instance where Edison Mission
23 restricts the delivery of our coal through plant failure, changing loading hours,
24 pushing back trains, or other needs to be recorded".

25 Then there is a log sheet. He says that the evidence could be used in court. Was it getting to
26 a really delicate stage at this point?

27 A Yes. We felt that Edison was making it impossible for us to deliver, and then saying that we
28 weren't meeting our delivery obligations; therefore they were going to terminate the
29 contract, which, you know, for us would have been the worst possible outcome. So, this
30 looks like an effort to catalogue that activity in anticipation that that may be the route we
31 were headed.

32 Q Something seems to be happening. If you go to p.564 it seems that you have been active
33 during at least April/May because this is an e-mail from you to, as I understand it, some

1 people in your team. 'Second Mission Contract.' That must, I would have thought, refer to
2 the possible restructuring deal.

3 A I don't think so.

4 Q

5 "Don't forget that under the second deal with Mission, there is both a premium
6 and a penalty for sulphur content in the volumes delivered to LBT. We will make
7 some extra dollars on this change, so make sure we bill them for it as soon as the
8 volumes under the new contract commences."

9 I would suggest to you that you are referring there to ----

10 A When was restructuring completed? I thought it was a little bit later.

11 Q It took effect on 11th June. Sunday, 11th June. Monday morning, 12th June. This is 13th
12 May.

13 A I thought perhaps it referred to the second confirm under the Master Agreement that was
14 signed in December.

15 Q You think this is a second confirm. You do not think this is new volumes under the ----

16 A It seems to me the restructuring has yet to be completed at this point.

17 Q So, if you go then to p.575. Then, 15th May - just two days later - this is another letter from
18 Mr. McClellan. I do not think we need to go through it in any detail. Do you remember this
19 letter? Have you seen it? It was copied to you. Again, it is a, "We've got to get the
20 restructuring finalised".

21 A Okay. Which, again, seems to indicate that my e-mail of two days prior is referring to
22 something other than agreed restructuring.

23 Q Right. If you go to p.605 ----

24 A Am I supposed to take anything away from ----

25 Q I do beg your pardon. You see the paragraph,

26 "My London coal team has consistently held the belief, since reinforced in the past
27 several weeks, that the EME local operations and coal team are frustrating our
28 attempt to deliver imported coal to the power station".

29 That is consistent ----

30 THE CHAIRMAN: Mr. Brealey, the last time we looked at this document I think we had our
31 attention drawn to the penultimate paragraph on p.576. Does that paragraph, Mr. Staley,
32 really summarise the position?

33 A (After a pause) Yes. I think that certainly summarises my recollection of that time period.

1 MR. BREALEY: It seems to have had the desired effect because if you go to p.605 things seems
2 to be happening quite quickly. This is May 21st. I would be grateful for a little bit more
3 from you on the events here. Just to identify this document, this is at p.605. This is 31st
4 May. You are forwarding a term sheet. If you just identify the next pages -- You have the
5 covering e-mail. Then you have got the reply, or a note which responds to Mr. McClellan's
6 letter which we have just seen. Then, a couple of pages on we have a 'without prejudice'
7 term sheet at p.608.

8 A Okay.

9 Q The first thing I would like you to comment on -- If you look at the note at p.606, the
10 penultimate paragraph,

11 "To date every avenue we have explored to resolve the situation has led us down
12 one of two paths - either a longer term deal with hugely increased volumes which
13 creates problems with pricing and flexibility in the later years or a single year with
14 a reduction to tonnage, but with Enron demanding compensation which looks to
15 us to be unreasonable. In the latter case Enron was asked to explain the basis of
16 the calculation, as the basis for a negotiation but nothing has been forthcoming".

17 Just stopping there, does that, again, fit with your recollection?

18 A All but, again, the last sentence ----

19 Q But none has been forthcoming. (After a pause) There are no documents where we see
20 any figures for compensation. I am not sure anything turns on it, but ----

21 A Okay. Yes. I got the call, but ----

22 Q The last sentence I would like you to comment on please. It says,

23 "Indeed all alternative solutions, which removed the delivery risk from Enron and
24 leave us to manage the volume problem, are not being followed up".

25 So, there have obviously been discussions prior to this e-mail where it had at least been
26 discussed or posed that Enron give up the delivery of the coal to the power stations. Can
27 you remember those discussions?

28 A Uh-huh.

29 Q You can.

30 A Yes.

31 Q Can you give the Tribunal an idea as to how those discussions took place, with whom, what
32 they were about?

33 A I just remember the nature of those discussions. But, again, I think the issue for Enron is as
34 I've described - the value that was created by our model, derived from actively trading

1 around the components of the delivery chain, and therefore to remove that element from the
2 deal removed the bulk of the value that was created for Enron. I think it appears - and my
3 recollection is - that there were a few ways that we could make amends for that: we could
4 continue a contract for a longer period of time with greater volumes - that's a contractual
5 structure known as a 'blend and extend' which, again, allows you to recoup value in a form
6 that is, you know, hopefully palatable to the other side because they are indeed going to
7 need more deliveries and consume more coal in the future, or write a cheque. It seems that
8 really the debate was about what that number was and whether it was usurious -- I forget
9 what the adjective they used here was.

10 Q "Indeed. All alternatives which removed the delivery risk from Enron ----"

11 A "Compensation which looks unreasonable --"

12 Q Yes. But, as far as the last sentence of that paragraph is concerned, there have been
13 discussions, it seems, between you and Mr. Crosland -- or at a higher level -- between you
14 whereby that you are going to give up the delivery to ----

15 A Yes. I don't recall how much of that. I mean, indeed, in the end the restructuring had
16 Enron giving up really the port and rail components and turning it into more of a CIF deal.

17 Q We see this again, as we go to p.608, which is the term sheet --

18 "To remove Enron from any UK logistics risk Edison would accept delivery on a
19 CIF LBT basis or an FOB Colombia basis prices for this, prices for this to be
20 based on delivered to station price as above, less actual port and delivery costs".

21 So, here is the formal offer without prejudice -- the formal offer whereby you give up all
22 delivery of coal to the two power stations.

23 A Where is this?

24 Q It is right at the bottom of p.608 at (iv).

25 A (After a pause): Okay. So, it seems like the negotiation encompasses three alternatives that
26 include everything from delivery all the way to the station to delivery FOB, port of origin.

27 Q Just to try and summarise what actually happened in the restructuring deal, could you go ----

28 A Sorry. What is the date of this? Do we know?

29 Q It is under cover of an e-mail from Max to you. Go back to p.685.

30 A Here it is, 21st May.

31 Q I think it is.

32 A Or thereabouts, 19th May?

33 Q Yes. If you go to bundle D2 again where you see Mr. Crosland's statement. Paragraph 38,
34 which is at p.170 of the bundle -- a, b, c, d, e, f -- if you could just take your time and read

1 THE CHAIRMAN: You know, it is elastic.

2 MR. BREALEY: (To the witness) Just one more point on Mr. Crosland's statement. You will
3 notice at "e" there is an uplift in price?

4 A Mmm, noted.

5 Q If you go to the end of his statement at p.178?

6 A I guess I am a little bit confused, I do not recall the exact pricing mechanism, and it seems
7 to me to be a market linked price.

8 Q Can you remember there was an uplift in year three?

9 A I wouldn't characterise it as an uplift, I think the final year represented an index price,
10 which means that it would be determined by the spark market movements during that year.
11 At the point in time when the restructuring was done it would not have been clear whether
12 that was going to be a price greater than the other tonnes, or less than.

13 Q As it turned out I think it was greater.

14 A Okay.

15 Q Paragraph 57, p.178 – this is at the end of his statement?

16 A Yes.

17 Q Mr. Crosland is talking about it going into administration, this is Enron?

18 A Yes.

19 Q December 2001 AEP acquired the core business, etc. The 2000 confirmation would have
20 been half way through its second year at the time?

21 A Okay.

22 Q He says:
23 "With effect from June 2002 the 'uplift' in prices introduced to 'reward' Enron for
24 its 'flexibility' in renegotiating the coal supply arrangements with Edison would
25 have taken effect."

26 Then he says:
27 "I believe that Edison (or AEP) took the opportunity of serving Enron with notice
28 that it was terminating the 2000 Confirmation at or about the time Enron went into
29 liquidation."

30 That is his belief that the agreement was terminated. Can you remember, Mr. Crosland
31 terminating it?

32 A I don't recall, but I was asked to produce some documents, and the fact that the contract
33 between Enron and Edison Mission was listed amongst the contractual assets for sale with
34 the Coal Group to AEP leads me to believe that it had not been terminated and was still

1 active, but it was mayhem during those final days, and whether a termination notice had
2 been faxed and didn't find its way anywhere I can't confirm.

3 Q I think we can put bundle D away. We will go back to the restructuring, para. 29 of your
4 statement?

5 A Yes.

6 Q You are talking about the renegotiation, who it was with, and the last sentence: "As a
7 result, the renegotiation left both sides better off." Could we take Enron first? Why was
8 Enron better off?

9 A Well, I believe that the restructuring of the contract freed up some volumes in probably the
10 prompt year, the remaining year of the original contract that since the market price had
11 risen we were able to sell elsewhere for a price greater than we would have been paid by
12 Edison Mission under the original contract.

13 Q So on a mark to market valuation the contract became more profitable?

14 A After the restructuring?

15 Q Yes?

16 A Correct.

17 Q I imagine it was bonus time ----

18 A Sorry, the contract ----

19 Q The supply contract?

20 A Okay, the supply contract from the mine, yes, and we could sell it for a greater price.

21 Q But the overall profit to Enron was greater on 13th June than 12th June? That is why Enron
22 was better off?

23 A I do not know if I can speak specifically to those two dates, but the general trend had been
24 the major – yes, the contracts, we were able to make more money by selling that coal
25 elsewhere.

26 Q This is no criticism, but as I understand it the coal team in London got various bonuses for
27 negotiating that contract?

28 A Well, Enron had a performance bonus system, and it wasn't specific to that contract, but ----

29 Q Your bonus was greater because of the contract?

30 A Making money was a good thing, it led to larger bonuses, yes.

31 Q I say, it is no criticism, but you did get an increased bonus because Enron made more
32 money out of this contract?

33 A Difficult to draw a direct causation but I would say in general ----

34 THE CHAIRMAN: We have got the picture!

1 MR. BREALEY: Why was Edison better off?

2 A Because the original volumes for which they had contracted, that they were unable to burn
3 got spread out over a longer period of time, so that the over supply situation that they faced
4 at both of their plants was relieved.

5 Q And also they had taken in-house the delivery of the coal, which is something that they
6 wanted?

7 A Well, some of the coal, and some of the delivery.

8 Q Well they took some of the coal, but they took all of the delivery, did they not?

9 A Well there was CIF, it didn't go all the way back to the mine, if I recall correctly. It went to
10 LBT, so they took in-house the rail component.

11 Q Yes, thank you. Just going to your second witness statement, please, p.115.13, para. 32 of
12 your second witness statement, this is in response to Mr. Kearney, and after the
13 restructuring you agree that your record that the restructuring was one of the best things that
14 had happened. You nod ----

15 A Sorry, which paragraph?

16 Q 32:

17 "... I commented to our team that the restructuring of the EME agreement was one
18 of the best things that had happened to our business".

19 A Yes.

20 Q The next bit I would like you to comment on: "... because it allowed us to focus more
21 energy on customers who could recognise the value that we created for them". My question
22 to you is: why was it you believed Mr. Crosland did not value or recognise the value that
23 you say you could create for him? You were going to focus more energy on customers who
24 could recognise the value, why is it, do you think, that Mr. Crosland did not recognise the
25 value?

26 A Well, I think in part because the nature of the restructuring – as I have said at the beginning
27 the part of the business on which we were focusing, which was trading around the supply
28 chain, and creating value incremental to that which a DIY supplier typically would create
29 for themselves, I got the impression that he valued other components – direct control on
30 some of the things that he has cited in his witness statement were more important to him
31 than price and flexibility.

32 Q I do not know if you still have volume G2, could you go please, to p.558. You have
33 probably seen this document before, you have been asked to review this. Just to identify,
34 because you do not have highlighting there or anything, it is from Tom Kearney to you and

1 George McClellan, and it encloses the offer from EWS, and includes the rates which are on
2 p.559. Then the points agreed at a meeting on 16th March, can you remember anything
3 about the points that had been agreed at a meeting of 16th March?
4 A Well, I mean I can read the document. So this is on p.560? "Points Agreed ..."?
5 Q Yes.
6 A Those would have been some key commercial terms that would have been part of any
7 negotiation for rail haulage.
8 Q At 558, which is in the middle of the negotiations of restructuring and this is an offer. You
9 can see there it says, "EWS – Proposed Rate Structure after June 30 2000 First Offer".
10 A Okay.
11 Q And then Mr. Kearney is saying, "Advise we delay on contract as much as poss ..."
12 A Yes.
13 Q This is addressed to you so I would imagine that you must have agreed to delay on the
14 contract as much as possible – did you?
15 A I don't know, I don't recall. That was his advice.
16 Q It is also sent to George McClellan. So it is quite high up in the chain?
17 A Yes.
18 Q There is no communication on a new deal with EWS after this, so it appears that you did
19 delay as much as possible, but was one of the reasons that you did delay the fact that the
20 renegotiation was going off and that if you gave us delivery to Fiddler's Ferry and
21 Ferrybridge you would not need the sort of contract that was being proposed here, which
22 obviously concerned Fiddler's Ferry and Ferrybridge?
23 A Are there minimum tonnage requirements in this contract?
24 Q I think that is to be ----
25 A Because if there were no minimums I would say it wouldn't affect ----
26 Q If you are in the process of giving up Fiddler's Ferry and Ferrybridge it seems pretty bizarre
27 that you would be entering into a contract with EWS for delivery of coal to those two power
28 stations?
29 A I would say, what is the date of this?
30 Q This is 12th May, so it is ----
31 A It's before the renegotiation had been completed.
32 Q Yes, it is undoubtedly true that clearly negotiations had been going on in May.
33 A I guess my point was that if there was no minimum tonnage commitment required of us,
34 whether we were giving up the haulage to those plants would have been somewhat

1 irrelevant. You could question whether in the near term there was any point for it, but I
2 think it also probably – I haven't read it in detail, but my guess is that it might apply to
3 other plants on similar haulage routes and we were certainly pitching business to the likes of
4 British Energy's Eggborough plant and the Aire Valley, and AES's Drax plant. But without
5 a tonnage commitment there's no cost to committing, therefore no need to delay.

6 Q If you look at 560 the "Programme period/base train plan", the base train plan, would that
7 indicate a minimum tonnage?

8 A Sorry, 560?

9 Q Page 560, "Programme period" – you would agree a base train plan which would imply that
10 you are at least going to agree certain delivery schedules and for trains to be going to
11 Fiddler's Ferry and Ferrybridge, which, as you say, would be irrelevant.

12 A I think our existing contract with EWS or the terms under which we were operating with
13 them, whether there was a contract or not, probably had a base train plan of zero. These
14 rates are not specific to the plants. It says, Hunterston to the Aire Valley, Redcar to the Aire
15 Valley, Hull to the Aire Valley, that's applicable to a number of plants not just Ferrybridge.

16 Q If you look at 561, "Minimum Invoice Value, 70% of the estimated annual value of the
17 contract – paid in equal monthly payments", does that help?

18 A Okay. We don't know what the estimated annual value is – right?

19 Q Well, no, but ----

20 MR. MATHER: Does it help that on 558 at the end of Mr. Kearney's email he says "DRS is
21 looking good"? Does that provide a clue?

22 A My guess is that what was the tenor, the term of this commitment? Was this going to be
23 multi-year? My guess is that that comment indicates that what we might be able to do with
24 someone else during that time period was looking better than what EWS was offering to us.

25 THE CHAIRMAN: Mr. Brealey, I am sure it is my fault, but I am slightly losing sight of the
26 target of this sub-species of questioning.

27 MR. BREALEY: Do you want me to answer that point?

28 THE CHAIRMAN: Yes, please.

29 MR. BREALEY: It goes to causation.

30 THE CHAIRMAN: Yes, I have got that.

31 MR. BREALEY: Can I answer that question in a few minutes?

32 THE CHAIRMAN: Yes, all right.

1 MR. BREALEY: (To the witness) One of the reasons, just to pick up a point that has just been
2 made, the DRS is looking good – one of the reasons I suggest you never went back to EWS
3 is because you essentially got into bed with Freightliner?
4 A What does that have to do with DRS?
5 Q Well, DRS you were looking at, as I understand it, which would be an alternative haulier for
6 you, but then you put DRS to one side and concluded the deal with Freightliner?
7 A Yes, ultimately I guess that’s what happened.
8 Q Can you go to 644, which is in the next bundle, G3. WE have got the 12th May email from
9 Mr. Kearney with proposed terms: certain points of agreement relating to performance and
10 “Advise delay as much as possible”. On 15th June there is a final agreed term sheet where
11 key features of the Freightliner deal are summarised. Do you see that?
12 A Yes.
13 Q We have got Redcar rates, Immingham rates, there is a commitment to 1.1 million tonnes,
14 Freightliner agrees to 95 per cent performance regime.
15 A Yes.
16 Q “That contract with Freightliner delivered to Enron much of performance certainty that we
17 were seeking” – is that what you were referring to?
18 A “The performance certainty” – your question is was my reference to ----
19 Q You say in para.21 of your statement:
20 “Freightliner delivered to Enron much of the performance certainty that we were
21 seeking.”
22 A That would be the premium penalty, the discharge window, performance targets, a host of
23 terms.
24 Q Then “Bottom Line”:
25 “We will introduce real competition in the rail transport of coal for the first time
26 ever.
27 We have effectively frozen or improved our current rates until end 2001.
28 We have a bulletproof mechanism to determine/fix firm rates over a five year term
29 ...
30 We have clear two-way performance incentives and penalties
31 Next Steps – will draft contract.”
32 You say in your second witness statement, para.8, that you are the person who decides the
33 key commercial terms in each agreement?
34 A That is correct, yes.

1 Q That is pricing, volume, terms of performance. You, personally, must have thought this was
2 a good deal?

3 A The deal that we ultimately signed with Freightliner?

4 Q Yes.

5 A Yes.

6 Q We get a flavour of this – we will take this quickly because of the time – if you go to p.752.
7 This is an internal Enron email, subject “Freightliner Groundbreaking Rail Contract
8 Signed”, and from the top from Mr. McClellan:
9 “Tom – great job on the Freightliner deal
10 It’s amazing the portfolio of port and rail deals you guys are putting together.”
11 So internally within Enron this was a very attractive deal?

12 A We were quite excited about it.

13 Q Just to finish off on this, on p.872, you get some credit for it as well. At the bottom there is
14 the Enron press release:
15 “Today for the first time since rail privatisation, the UK coal transportation
16 industry has a new rail freight services supplier.
17 Freightliner Ltd will enter the market with a landmark agreement ...
18 Under the multi-year, multi-million tonne agreement, Freightliner’s ‘Heavy Haul’
19 division will start to supply Enron with rail services ...”

20 Then there is a quote by you:
21 “‘We welcome Freightliner Heavy Haul’s entry into the coal transportation
22 business’ said Stuart Staley, Vice President, Enron Coal Services Limited, ‘and we
23 strongly believe this agreement will allow Enron to provide a reliable service at
24 competitive prices to our customers over the long term.’”

25 That is a fair reflection of how you saw this agreement?

26 A Yes.

27 Q An internal email, “You are the man”.

28 A Written by someone from Enron Broadband Ventures! That’s one for the “Where are they
29 now” file!

30 Q The reason I emphasise this is because it was such a good deal that this was the reason you
31 never went back to EWS?

32 A Never went back to them?

33 Q They had a first offer on 12th May, there is a document saying “First offer”. We have got
34 the internal Enron saying, “Delay as much as possible”. As things turned out, you

1 negotiated this great deal with Freightliner and that is the reason you never went back to
2 EWS?

3 A Just from scanning it, it looks like the pricing was better, the terms were better. It appears
4 that we were – certainly the Freightliner agreement was a better fit for our business than
5 either, and I guess what DRS had on offer because we never concluded anything there, or
6 what EWS had offered.

7 Q If the prices that EWS in May had been similar to the Freightliner prices you would have
8 still gone with Freightliner because it was a better fit?

9 A Well, if EWS had agreed to the same terms, performance terms and everything, it probably
10 would have come down to other elements, perceived ability to execute and credit risk,
11 things of that nature.

12 Q What about if it was just the prices – if prices had been similar?

13 A Prices and everything, flexibility was a huge end – the ability to contract for a known level
14 of perform was hugely important to us.

15 Q That was a real incentive for Freightliner, was it?

16 A An incentive for Freightliner?

17 Q That was part of the appeal?

18 A That was part of the appeal of Freightliner, yes.

19 Q So again, if the rates had been broadly similar between Freightliner and EWS that they were
20 offering you, the Freightliner deal was a better fit, it gave you ----

21 A If the prices were similar, if Freightliner offered performance guarantees and EWS didn't,
22 no question.

23 THE CHAIRMAN: So price was important, but it is not everything?

24 A Correct.

25 MR. BREALEY: You will now need two documents. You will need the Freightliner agreement,
26 which is at 691, and I am going to have to ask you to take another bundle because I just
27 need to compare ---- I will try and take this as quickly as I can.

28 THE CHAIRMAN: Do not worry, Mr. Brealey, do not feel under pressure.

29 MR. BREALEY: Thank you. So that is the Freightliner ----

30 A The second bundle?

31 THE CHAIRMAN: You did promise a second bundle.

32 MR. BREALEY: I did, it is G4, p.942. Just to identify these two documents. If you go to 940
33 you will identify the document. It is the Coal Carriage Agreement – this is the Enron bid in
34 response to the invitation to tender.

1 A Yes.

2 Q The document in 3 at 691 is the actual Freightliner deal.

3 A Okay.

4 Q If you look at the Freightliner Agreement at p.706, as I understand it, when you bid for the
5 Enron business you were using this on the back of Freightliner?

6 A I don't know if I agree with that.

7 Q The rates that we see in the bid are based on the rates in the Freightliner Agreement?

8 A Are they?

9 Q I am asking you.

10 A I don't think so, they look different.

11 Q I did not say, "Are they same", I said, "Are they based on them"?

12 A I don't recall for certain how we priced it.

13 Q You cannot recall how you priced it?

14 A No.

15 Q Just to assist you as to whether you based the bid on the Freightliner – that is the only way
16 you were going at the time, you were not going to use anybody else, were you?

17 A We might have used EWS.

18 Q You had just negotiated this fantastic deal with Freightliner where you had got 1.1 million
19 tonnes, you had got 600,000 committed to BE and you are saying that you are going to use
20 EWS? When you used ----

21 A My recollection is that the BE contract had a lot of flexibility and if they exercised their
22 options to supply maximum tonnage we would have exceeded the capacity available under
23 the Freightliner Agreement, so we would have been forced to use EWS for anything
24 incremental to ----

25 Q I will ask the question again: when you inserted, or someone inserted, those rates on p.943,
26 can you recall whether you were using as a guide the rates that Freightliner were agreeing
27 with you?

28 A There was no question that that was a component of how we thought about pricing that
29 business, but was it exclusively that – in other words, was the plan to back to back, put the
30 two together? I don't recall. My guess is no.

31 Q If you then look at, for example, clause 4 of the Freightliner Agreement, p.694, and also
32 have a look at what you are offering Eddison at 942, I suggest to you that basically ---- The
33 covering letter is from?

1 A Stephen Pirozzi. I'm sorry. What was the page that you cited in the Edison tender
2 response?

3 Q Page 942. Compared p.694. The person who put it together was - just before we get to the
4 question - Stephen Pirozzi I understand he was quite junior in your team.

5 A He worked for Tom Kearney and the group that we had focusing on port and rail
6 agreements.

7 Q I understand that you fired him at some point; is that right?

8 A I don't recall if we fired him or if he left.

9 Q All right. The person under Tom Kearney seems to have photocopied Clause 4. So, Clause
10 4 of the Freightliner is rights and obligations of the buyer, Enron, with ----

11 A So, you are saying that performance metrics are similar between the two contracts?

12 Q Yes. Yes.

13 A Okay. No, I didn't.

14 Q I would also ask you to note that you are taking a bit of a profit on the contract because
15 whereas under the Freightliner the buyer, Enron, has one and a half hours to load and
16 discharge, you are only giving Edison one hour, fifteen minutes; is that correct? That has
17 been changed.

18 A Okay. So, they are not the same then. I thought you implied that they had photocopied
19 them.

20 Q They are the same, bar the numbers. You are just taking a bit of a profit on them. Yes?

21 A So, the performance measures are the same, but the metrics are different.

22 Q Do you not suggest that you are using the Freightliner contract to back-to-back this
23 contract?

24 A There is nothing about this that tells that we had to be using Freightliner to back the Mission
25 contract.

26 Q But it is the same wording.

27 A I think that a rail contract -- most rail contracts have similar wording in general.

28 MR. MATHER: It is not precisely the same wording. There is a difference between using
29 'reasonable endeavours' and 'guarantee' about the delivery facilities. I do not know if that
30 is material.

31 MR. BREALEY: That has been taken out, has it not?

32 A It just comes down to what risks we were willing to wear. Right? We could've promised
33 all this to Mission and supplied using EWS' service without reciprocal guarantees and worn
34 the risk of those performance deviations ourselves. Or, we could've supplied under this

1 Freightliner contract and it looks like we had even tighter tolerances with Freightliner than
2 what we were offering to Mission.

3 Q Yes. So, Edison was suffering a slight disadvantage under -- They were having to discharge
4 far more quickly than you were obligated to under the Freightliner agreement.

5 A But I would observe that performance guarantees like this would have been found -- We
6 certainly were not able to get them in the market. So, I would say that to receive those was
7 a benefit vis-à-vis the rest of the market. I mean, compared to whom -- Yes, if you look at
8 the terms in these contracts we had tighter tolerances than we were passing on.

9 Q Go to G4. If you are concerned about the 1.5 hours -- Go to p.922 of G4. Have a look at
10 4A. This is the first draft of the coal carriage agreement prepared by Mr. Pirozzi. Just to
11 identify the document: p.920. This is the junior to Tom Kearney. "Attached is the latest
12 draft --" This is dated 4th September. It has various things on the term sheet. Then, "The
13 buyer shall --" on p.922. (After a pause) That is a direct lift -- You have got the 1.5 hours
14 in the original draft. What someone has done is when the bid is actually submitted they
15 have just changed 1.5 hours to one hour, fifteen minutes, thereby giving Edison slightly less
16 time than you have. Is that correct?

17 A Yes. Agreed. I'm missing the significance of that.

18 Q I am trying to work out whether the Enron bid to Edison was based on the Freightliner
19 contract - the amazing deal that you have just signed.

20 A Yes.

21 MR. MATHER: Is it conceivable that Mr. Pirozzi used this as a helpful precedent and did not
22 necessarily commit to using Freightliner?

23 A Again, I don't recall exactly, but in a similar situation I would say that whatever we had
24 been able to negotiate with Freightliner we viewed as broadly indicative of where the
25 market ought to be able to get going forward. So, whether it's exactly the same or fifteen
26 minutes different -- I mean, I think what you're trying to ask is: were we just taking the
27 Freightliner contract, marking it up and selling the exact same thing to Mission? My
28 answer is, no, because we always supplied on a portfolio basis and at times we would use
29 other -- You know, if Freightliner was being used elsewhere we could have relied on spot
30 service from EWS.

31 MR. BREALEY: A similar point. You see at Clause 4B in the Freightliner Agreement ----

32 A Freightliner Agreement with Enron.

33 Q Yes. Sorry. 4C on p.694.

34 "The seller shall be entitled to charge an additional 5 pence per tonne".

1 Yes? That is you being able to charge Freightliner 5 pence. In the draft it is an exact copy -
2 5 pence.

3 A Wait. Is that not Freightliner being able to charge us?

4 Q “The buyer shall pay an additional charge should the buyer fail to meet the total ----“

5 A I am sorry. I am looking at C.

6 Q C. “The seller shall be entitled to --“ (After a pause) Sorry. You are absolutely -- Yes.
7 Freightliner shall be entitled to charge an additional 5 pence.

8 A Yes.

9 Q That is mirrored in C on p.922. But, someone, when it gets to p.942, takes a bit of a profit
10 and charges 10 pence. I suggest to you ----

11 THE CHAIRMAN: Mr. Brealey, I think we have got the point. The witness is saying it is a
12 template really.

13 MR. BREALEY: It is a template based on Freightliner’s agreement.

14 THE CHAIRMAN: Yes. A textual template, I think, is the witness’ evidence. We understand
15 that you are putting to him that it goes further than that.

16 MR. BREALEY: I will speed up. (To the witness): The draft. Did you put the terms which are
17 slightly disadvantageous to Edison in? Did you change them from one hour thirty to one
18 hour fifteen?

19 A I don’t recall.

20 Q Did you change the ----

21 A I would’ve approved whatever we sent out ultimately.

22 Q If you look at the draft on p.923 compared to p.943 -- Page 923. What was actually
23 submitted at p.943. The latest draft on p.923 does not have the price incentive.

24 A Which price incentive?

25 Q. You see on p.943 :

26 “Price Incentive. All trains carrying Enron coal will be subject to a minimum
27 discount of 25 pence per tonne for rail haulage”.

28 A Okay.

29 Q That is not in the latest draft which we see at p.923. Can you explain that, please?

30 A Explain it. Well, yes, we added it in for our final submission.

31 Q Was it you or was it him?

32 A I don’t recall. Again, I would’ve approved the final submission and whether I suggested
33 that we go that direction or whether someone else in the team did, I don’t know, but we
34 obviously thought it a superior total term sheet and went with that for our final submission.

1 Q There was a fairly junior person drafting this. You may have approved it. Would you not
2 agree with Mr. Kearney that this really was not much of a serious bid?

3 A No.

4 Q He says it was not a serious bid. He says this was a fairly joke bid.

5 A Yes. I disagree.

6 Q You disagree. Why do you disagree?

7 A First of all, I'm not sure what the point of a joke bid would ever be. We submit bids or
8 offers on business in an attempt to win that business. If they had come back and said,
9 "We're ready to do business", we wouldn't have said, "Just kidding".

10 Q But you would have accepted a coal haulage agreement.

11 A Well, yes. That's what we were after.

12 Q A coal haulage agreement. (After a pause) That is consistent with what you say at para. 32
13 of your statement - that you submitted a tender for rail haulage services to EME in
14 September 2000.

15 A Uh-huh.

16 Q Whatever you may say about the seriousness of the haulage bid, I suggest to you that you
17 have absolutely no chance of getting a four year E2E coal supply agreement on the back of
18 this.

19 A Okay.

20 Q Do you agree or disagree?

21 A On the back of what?

22 Q This bid.

23 A This bid was for rail haulage. We responded to that. Part of the structure of our response
24 was designed to encourage or give Edison Mission the incentive to seek something broader
25 - specifically an E2E supply of coal.

26 Q The covering letter, from Stephen Pirozzi, at p.940, in the third paragraph, says, "Should
27 you wish --" It was quite clear that Mr. Crosland did not wish to have anything to do with
28 an E2E four year coal supply agreement. Would you accept that?

29 A Where is that made clear?

30 Q As your perception of what was going to happen. Mr. Staley, as I am sure you are aware,
31 Enron has come to court to claim between £10 and £20 million for loss of profit based on
32 lost coal supplies over a four year period. You have just accepted that the bid was for
33 haulage services. I am suggesting to you that the notion of you receiving, on the back of
34 this haulage contract, a four year E2E coal supply agreement is fanciful.

1 A Okay.

2 Q Would you accept that it was a flier?

3 A I don't know how to answer your question. I guess you can see from the wording in the
4 cover letter and the term sheet that our interest was in pursuing that type of arrangement. I
5 would agree with you that what Edison Mission sent out in a tender was seeking specifically
6 rail haulage. Now, if we're talking about - as you frame the whole debate - the damages
7 caused in all of this, we were constantly seeking all types of business. Right? We would
8 obviously prioritise that, based on the expected value -- the probability of winning the
9 business and what the expected profit might be.

10 Q When you submitted this bid on 15th September in your view what chance did you have of
11 being awarded a four year E2E coal supply agreement? What chance?

12 A I don't recall, but my guess is, no, that it was ----

13 Q A small chance?

14 A I would believe strongly that we could offer superior value. Right?

15 Q Well, that becomes ----

16 THE CHAIRMAN: That is not quite the question. You were committed to E2E agreements,
17 were you not?

18 A Yes.

19 Q But, what did you expect would happen at the time of this letter of 15th September? Did
20 you think that EME would bite and come back, and say, "Let's have an E2E agreement", or
21 not?

22 A That was certainly our hope. Right? I can't -- I don't recall whether I thought it was a 10
23 percent chance or a 90 percent chance. But, if we thought it was zero we would not have
24 included the paragraph.

25 MR. BREALEY: You cannot recall whether it was 10 percent or 90 percent. Mr. Staley, the ink
26 is hardly dry on an E2E contract which you have just torn up. You have just torn up an E2E
27 contract. It is inconceivable, is it not, that Mr. Crosland is going to award you another one?

28 A Again, I viewed the issues with that contract being more specific to that
29 contract ----

30 THE CHAIRMAN: I think you can pause. I feel speeches coming on now. The point is made.

31 MR. BREALEY: The point is made, but -- Mr. Lasok, in his questions to you when you arrived,
32 went through certain types of E2E contracts that could, or could not, be offered. What I
33 suggest to you is that you never communicated any type of deal to Mr. Crosland which
34 would put him on notice that you wanted a four year E2E coal supply agreement, did you?

1 A No.

2 Q On that basis you really did not have a chance if you never actually communicated it to him.

3 A Okay.

4 Q I have no further questions.

5 Re-examined by Mr. LASOK

6 Q Obviously, given the time, I am going to be as brief as possible. It was put to you, Mr.

7 Staley, earlier today that there was an overlap between the functions of coal procurement

8 teams and the Enron model. Do you know whether or not any company with a coal

9 procurement team made an E2E arrangement or an intermediary arrangement with an

10 intermediary?

11 A I mean, as I stated in my second witness statement, everyone with whom we had an E2E

12 arrangement had a coal team of some sort. Most of them were not appreciably different

13 from the team that Edison Mission had.

14 Q Thank you. Could you go to Bundle G2, p.525? You were asked a question ----

15 A Is this an e-mail from George McClellan to Nigel Petrie?

16 Q Yes. In the middle of the page there is a sentence, at the beginning of the ante-penultimate

17 paragraph,

18 "It is fairly obvious that the existing contract format is unworkable".

19 Do you remember what you understood by 'the existing contract format is unworkable'?

20 A You know, predominantly the volumes and the timing.

21 Q Was it the E2E aspect?

22 A Well, no. I mean, I think the fundamental problem with the first contract was the volume.

23 Q If you could turn in the same bundle to p.608 -- You were asked questions about Item 4 at

24 the bottom, which starts off with the proposal that EFPL, which I think is Edison:

25 "... will use reasonable endeavours to accept tonnages at Fiddlers Ferry in

26 accordance with the Delivery Schedule",

27 and then there are alternatives which are non-E2E, or they are intermediary arrangements,

28 but they are not complete E2E. I think we know that this was in fact a proposal emanating

29 from Edison, because if we turn to p.605 we can see from the email from Max, which is in

30 the bottom half of the page, that he is sending this term sheet which has been sent to him in

31 turn by Mr. Heller. This is an Edison proposal to continue the E2E arrangement. In your

32 dealings, do you remember who was more important, Mr. Heller or Mr. Crosland?

33 A I mean I'm sure ultimately Mr. Heller was approving all decisions that were made.

34 Q Did Mr. Heller have the same views of Enron as Mr. Crosland?

1 MR. BREALEY: Well it is not for him.

2 THE CHAIRMAN: If he was told by Mr. Heller, he can answer the question, I suppose,
3 otherwise he is speculating, is he not?

4 MR. LASOK: Yes, that is right. (To the witness) Do you know?

5 MR. BREALEY: He is just repeating what he has said in the

6 A Well my recollection is based on reviewing the email from Richard Lewis in which he had
7 come from a meeting with Mr. Heller and he was quite pleased with the commercial
8 relationship between our two companies.

9 MR. LASOK: I am going to go to the discussion concerning the May 2000 offer of a
10 performance related contract from EWS and the deal that was done with Freightliner. The
11 May 2000 was an illegal abusive offer, that was how it was found by the ORR. Did you
12 enter into the Freightliner deal because of the behaviour of EWS or not?

13 A Well I guess that if high prices and poor performance qualifies behaviour, yes.

14 Q Now, I think this will be the last point, but my Junior is rapidly writing a note which will
15 almost certainly be illegible.

16 THE CHAIRMAN: I would always pay attention to Mr. Beard's notes, Mr. Lasok!

17 MR. LASOK: One finds that all these notes, the more important they are the more illegible they
18 are! (Laughter) I will continue – it may be my penultimate question – this concerns the
19 question about whether or not the bid for the coal haulage contract was intended to be
20 backed by the Freightliner contract. Now, if Freightliner had not been able to provide
21 capacity, and you had won the EME contract, what would you have done?

22 A In the short term I think we would have had no option other than to go back to EWS. In the
23 medium to longer term we would have been frantically trying to negotiate something with
24 someone else that provided better economics and better performance guarantees.

25 Q So that there was a certain element of risk ----

26 A Sure.

27 Q -- with the bid for the coal haulage contract?

28 A Absolutely.

29 Q Why were you prepared to take that risk?

30 A Because we viewed the benefits that were created for our business to be more significant
31 than the cost of that risk.

32 Q Various questions have been put to you about the Enron bid to EME and I wanted just to
33 ask you whether, if you go back to para. 35 of your first witness statement, could you just
34 read para. 35 again, please?

1 A (After a pause) Yes.

2 Q Does para. 35 express your view?

3 THE CHAIRMAN: Tough question!

4 MR. BREALEY: This is his evidence-in-chief, he has been cross-examined on it and to say:

5 does it represent his view, is neither here nor there?

6 THE CHAIRMAN: Well it is not a very difficult question to answer, it is his statement anyway,

7 but let us get on with it.

8 A Yes.

9 MR. LASOK: Thank you very much.

10 MR. MATHER: I just have two very quick factual points if I could, one is from this letter in G4

11 at p.940 from Mr. Pirozzi to Mr. Crosland. It may help if I just read it out – it is the phrase

12 we have just considered – “any combination of our haulage, freight and port throughput

13 services will help Edison Mission to streamline its import activities and minimise cost.” It

14 is not clear to me whether that sentence actually covers coal purchase or whether it is

15 confined to infrastructure and transport services?

16 A Well I think we would have considered either is the short answer. I can’t tell by reading it

17 either, but if somebody had approached us about providing freight, port and rail we would

18 have considered that just as we would have considered coal, freight, port, rail.

19 Q Thank you. The final point is again going back to the December 1999 confirm, and the

20 personnel at Edison who were around. If, before Mr. Crosland and his team appeared, who

21 would have arranged those confirms, and who would have done the September confirm?

22 Who might have been responsible for the December confirm, if you know who your

23 counterpart is?

24 A Yes, if I recall correctly the initial confirm would have been some combination of people,

25 John Pellegrini had some responsibility for that, I can’t recall for certain whether he was

26 present on the scene for the first confirm. I think by the time we did the December one, I

27 think I remember from comments earlier in these proceedings that Max Crosland had joined

28 prior to that and he probably would have been responsible for the second confirm. But the

29 first one, there were a number of people involved from Edison Mission’s London office,

30 and a number from the US headquarters office.

31 THE CHAIRMAN: Do you want to ask anything arising?

32 MR. LASOK: It was just that in relation to p.940, Mr. Mather asked a question about particular

33 words, and I wondered whether it would have been appropriate to ask the witness about the

34 next following sentence?

1 A I guess, sir – is that a question? Is it a proposed question?

2 Q Well it is Mr. Mather’s question but directed to the next following sentence.

3 MR. MATHER: Would you like to comment on the next sentence?

4 A I think it is relevant to the last exchange regarding whether Edison in fact ever asked us for
5 a four year end to end proposal. We were constantly pitching ideas to people that had not
6 been asked for and that was a big part of what we did. I don’t mean to be cute about the
7 wording because the specificity of the questions seem to conflict with the fluidity of our
8 approach to business, which was attempting to find the problems that customers faced, and
9 proposing solutions to resolve them. I think that last sentence speaks to exactly that.

10 THE CHAIRMAN: This is your iterative process, Mr. Lasok?

11 MR. LASOK: No, it is the
12 “There are many options that can be explored and would like to meet with you to
13 discuss how we can optimise your operations by fully taking advantage of the
14 Enron Portfolio.”
15 One has to read the letter as a whole.

16 THE CHAIRMAN: Mr. Staley, thank you very much for all the trouble you have taken to be
17 here, the Tribunal really does appreciate it. I hope that you will have some rest and enjoy a
18 little of the delights of London which I think you already know extremely well anyway.

19 A Thank you very much.

20 THE CHAIRMAN: We are going to adjourn until 20 to 2; it will give time to set up the
21 equipment and so on.

22 (Adjourned for a short time)

23 Mr. THOMAS KEARNEY, Affirmed

24 Examined by Mr. BREALEY

25 Q Mr. Kearney, are there various bundles? Have you got your witness statement in front of
26 you?

27 A Yes, I do.

28 Q Could you go to Bundle D3, p.838?

29 THE CHAIRMAN: Mr. Kearney, just before we continue, you can see me at the moment.

30 A I can.

31 Q Before, you could see counsel.

32 A Yes.

33 Q Just for your information, we are a Tribunal of three members. I am not sure that there is
34 anything you can do about it, but it is fair that you should know. There you are - you have a

1 wide angle shot. I am sitting with two colleagues. You will be talking to a Tribunal of
2 three. It is right that you should know that.

3 A Okay.

4 MR. BREALEY: Page 838 at the back of this bundle. Go to the back of the statement at p.853.

5 Is that your signature?

6 A Yes, it is.

7 Q Can you confirm to the Tribunal that the evidence contained in this statement is true to the
8 best of your knowledge and belief?

9 A Yes, I can.

10 Q That is all I have got to say. There is a gentleman called Mr. Lasok who is going to ask you
11 some questions in cross-examination.

12 A Mr. Brealey, I just want to make one note. My position has changed since I wrote this
13 witness statement. I am now the Chief Executive Office of Africa Commodities Group,
14 which is a joint venture between the Noble Group which is Asia's largest commodity trader.
15 I have had that position since September 1st.

16 Q Right. So, we need to amend the first sentence of para. 1.

17 A Yes. "I am currently employed --" Yes.

18 Q We will do that. Thank you, Mr. Kearney.

19 Cross-examined by Mr. LASOK

20 Q Mr. Kearney, have you got your copy of your witness statement open at the first page?

21 A Yes, I do.

22 Q You say in para. 1 that in May 1999 you joined Enron's international coal trading team
23 where you were responsible for negotiating, implementing and managing ECSL's
24 international port throughput and rail transport agreements. Have you seen Mr. Staley's
25 second witness statement?

26 A Yes, I have.

27 Q Yes. He fills out a bit more of the detail of your employment with Enron. I wondered
28 whether you could turn to it. It should be in Bundle D1.

29 A I have the second witness statement; is that correct?

30 Q Yes. Perhaps it may be easiest to read paras. 8 to 10. They are on p.115.3 to 115.4. (After
31 a pause) Do you disagree with anything which Mr. Staley says in those paragraphs?

32 A Yes, I do.

33 Q Could you tell us what?

1 A Specifically I think it's an over-statement by Mr. Staley, who I respect, that he decided the
2 key commercial terms in each agreement, such as pricing, volume, term performance,
3 guarantees and damages. If he needs to add the director of the coal group - that he had
4 alternate responsibility for reviewing and improving them, absolutely; but in terms of
5 negotiating and deciding those, together with the counterparty, I think the evidence will
6 show that I was the person that did that. In terms of the statement with regard to my bonus
7 and performance, I can only say that I was there when Mr. Staley reviewed me in February
8 2000 and the issue of the EWS contract was brought up as a key performance indicator and
9 a personal failure on my part. Lastly, I would also say that the statement about a high level
10 of management and independent deal making as far as Enron is concerned -- that was an
11 issue I certainly disputed at the time, and I still feel that it's an incorrect statement.

12 Q Is there anything in para. 10 that you disagree with?

13 A (After a pause) The issue that I think -- I was directly involved certainly with the
14 management of the railway relationship, the railway contract. In that relationship I had
15 direct contact with Edison Mission -perhaps not the decision-makers, such as Stu. I said
16 that I was not directly involved in the re-negotiation of the Edison Mission contract.
17 However, I was involved with the operational side on a daily basis, and at the time those
18 people were also informed about the state of mind of Edison Mission.

19 Q Let us move on from there. Could you turn to para. 4, please, of your statement? Could
20 you just refresh your memory by reading para. 4? That looks as though that is your
21 subjective opinion based on conclusions that you draw from the facts; is that correct?

22 A Subjective opinion. I was the person directly involved in the drafting, together with Steve
23 Pirozzi, of this rail agreement. ... agree with it, the rail tender. Since I was intimately
24 involved with the structures behind it, I think I'm in a position to comment whether or not,
25 as a company, we felt we stood a chance of winning this tender, and, more important,
26 whether we considered this a viable or commercial opportunity. At the time we didn't.

27 Q There are two things that you say there. The first is that you are expressing a personal
28 opinion on the facts. Is that correct?

29 A Inasmuch as the opinions are coming out of my mouth, yes. That is my personal opinion.

30 Q The second thing does appear to be a fact which is that Enron at the time did not believe
31 that it had a chance of getting the contract. Is that correct?

32 A Yes. I believe that is a fact.

33 Q Now, there is a problem - that is, that your view is not consistent with the view taken by the
34 Office of Rail Regulation. Have you got bundle B2 by any chance?

1 THE CHAIRMAN: I do not have Bundle B2. We have B1.

2 MR. LASOK: I think possibly we can do this from B1.

3 THE CHAIRMAN: We have had B1 brought up here, but not B2.

4 MR. LASOK: I will try and do it with B1. Could you go to p.233, para. B5 and then read (a)?

5 A (After a pause) I think I need to make a strong and clear point. I believe - and I have stated
6 this previously - up until the time that Edison Mission and Enron re-negotiated their E2E
7 contract, which I believe was June 2000, EWS performed in a discriminatory manner and
8 it's very clear in the evidence Enron incurred economic damage, and this is precisely why
9 we brought the claim to the Competition Commission. The rail tender launched by Mission
10 in August/September 2000 - we did not consider that - we mentioned it in our competition
11 case that we did not consider that a loss of business. We did not consider it a viable option
12 or even the possibility of winning that tender and we certainly did not consider it a way that
13 we could get back into supplying coal to Edison Mission. When I say in my witness
14 statement it was a joke - even George McClellan (Stuart Staley's boss) ridiculed our attempt
15 to participate in the rail tender as being 'gluttons for punishment'. I have not found - and I
16 don't recall - any evidence within Enron that stated this was a strategic move; this was a
17 way for us to get back into the business. In fact, the early drafts of that tender included
18 nothing about the provision of coal or a discount for coal. So, I think you need to view,
19 when you talk about Edison -- the renewal of business between Enron and Edison, we have
20 to talk about two distinct periods - the end of the E2E contract in June 2000 and then the rail
21 tender.

22 Q Could you look at p.249, para. B65 at the top of the page? (After a pause) Have you read
23 that?

24 A Yes, I have.

25 Q Could you turn to p.259? Could you read the first two sentences of para. B100? (After a
26 pause) Have you read that?

27 A I did, yes.

28 Q That, of course, is focusing - it may not have been obvious in the earlier paragraphs - on the
29 period May to November 2000.

30 A Yes, that would be the conclusion by the Office of Rail Regulation regarding our
31 participation in the tender. However the original complaint made only a passing reference to
32 that. I worked at Enron at the time and I in no way advocated that the loss of that tender in
33 any way was due to discrimination or in any way led to economic damage to Enron. I have
34 never said that and, to be honest with you, I have not seen a shred of evidence within the

1 Enron files which indicated we stood a chance of getting that tender, and nor that we
2 considered it seriously.

3 Q Could you look at p.281? Could you read para. B198?

4 A (After a pause) I've read it.

5 Q Now you can put that bundle away. Can you take out Bundle G5? Could you turn to
6 p.1239.2? Could you look at the bottom? This is an e-mail from Douglas Lahnborg to two
7 individuals - Paul Dawson and yourself - sent on 13th July, 2001. If you just read the first
8 few lines of the e-mail, you see that Annette -- I think Annette was an official in the ORR.

9 A Right.

10 Q "... called me and asked for some information. She would like to have a list of all bidding
11 contests that ECSL has lost (including date and name of the procurer)", that was in the
12 context of the complaint. If you go to the top of the page, we see your reply on 17th July.
13 Could you read your reply, please?

14 A Do you want me to read it out loud?

15 Q No, no, read it to yourself.

16 A (After a pause) I've read it.

17 Q So at that that stage you did regard what is described here as the "September 2000 – Edison
18 Mission Energy bid" as a contract lost as a result of EWS's behaviour?

19 A No, I didn't, I didn't. I was asked which contracts we competed against EWS against since
20 that time, I listed the rail only tenders, and I put them specifically in "rail only tenders" (in
21 quotes). When I talked about the "lost business" that refers specifically to the E2E business
22 that finished in June 2000. You are taking that out of context when I talk about "lost
23 business". I was talking specifically about the E2E, Edison's decision not to renew the
24 delivered supply deal with Enron after May 2000, we could count the EME as lost as well.
25 That relates to an E2E contract being lost in June 2000, and that is why I've maintained to
26 this day; I've always maintained that EWS discriminating against us and off loading the
27 E2E contracts with Edison Mission was a major contributing factor to that, and that we
28 suffered damage.

29 Q Why did you mention the September 2000 tender at all in response to the request?

30 A Because I was asked about all bidding contracts, that does not necessarily mean E2E
31 contracts, "all bidding contracts", that means anything that we competed against EWS on –
32 we did, we competed against EWS on two bidding contracts, rail only, I made that very
33 clear.

1 Q Because the request, if you look at the bottom of that page, dealt with the alleged
2 discriminatory pricing. The request for information made by Mr. Lahnborg was focused on
3 the allegations of discriminatory pricing?

4 A And that did not give any clear reason for why he needed info, but it related to the alleged
5 discriminatory prices. We were asked to provide information to a government agency that
6 we had contacted and submitted a complaint to. I simply responded to that information
7 because we had indeed competed against EWS. I defined them specifically as rail only
8 tenders. I did not define them as being rail only tenders that we could sneak in and get a
9 new contract with. I did however differentiate at the bottom of that email of the 17th when I
10 said the “ending of delivered supply deal in May 2000”, that was not business. That is
11 precisely what we maintained in the complaint as well.

12 Q Could you go to p.1417 in this bundle, please? (After a pause) Have you got 1417?

13 A Yes.

14 Q Is this the witness statement in the context of the ORR’s investigation?

15 A Yes.

16 Q Could you turn to p.1423, please? Could you read paras. 19 and 20?

17 A (After a pause) Yes.

18 Q Now, if you look at the end of para. 20, there is a sentence:

19 “I believe that EWS’s behaviour in charging ECSL higher prices, failing to ensure
20 adequate performance and its refusal to enter into a performance-based contract
21 with ECSL played some role in undermining ECSL’s position with regard to the
22 renewal of its supply of coal to EME’s power plants.”

23 A That specifically relates to the period up to June 2000.

24 Q Well can you just tell us when in that period the opportunity to renew supply of coal to
25 EME’s power plants arose?

26 A The coal contract with EME, which began in June 1999, was for one year and those
27 negotiations – I participated in them – it was for one year. Renewal of that contract would
28 have come during the period of Spring 2000, the period really between January and June
29 2000. It was our intention, our desire, and actually one could argue, since Edison Mission
30 was our only major coal contract, it was very much in our interest to try to renew that
31 business. So when I talk was renewal of the supply of coal to Edison Mission, I am
32 specifically talking about the renewal of the E2E contract from June 1999 to June 2000. I
33 am not talking about the rail contract.

1 Q You see it is only after that period that EME indicates to operators that it is considering its
2 future coal purchasing strategy, and that first appears in its invitation to tender addressed to
3 various train operators in June 2000. So the renewal exercise ----

4 A Actually no, I think you are reading the facts wrong. We had a contract for one year.
5 Negotiations for this contract in June 1999 it was very clear that if we performed – if we
6 performed – we would stand a chance of getting this business renewed. It was the desire of
7 Enron to enter into a two year or three year – a multi-year contract. At the time Edison
8 Mission said they only want to try it for one year and if it works – “We will see how it
9 works out, and if it works we will continue it.” Renewal of the contract relates to the June
10 1999 to June 2000 business.

11 Q In December 1999 we know that confirmations were agreed that extended coal supply to the
12 end of May 2001?

13 A Yes.

14 Q And we know that there were negotiations between Edison and Enron in the early part of
15 2000 leading to an agreement that dealt with the supply of coal which took everybody up to
16 – when, do you remember?

17 A I don’t.

18 Q Well it was to the end of December, and I think into the early part of 2001, May 2001.
19 Now, the result was that what was for consideration was the supply of coal carrying on after
20 the end of the arrangements with Enron, and that process, or the signs of that process first
21 surfaced with the invitation to tender issued by Edison originally in June, referring to the
22 review of its coal purchasing strategy?

23 A I honestly think you are drawing the wrong conclusions.

24 Q Okay, well that is your position, but the fact remains that we have a problem because the
25 ORR investigated all this and concluded, as I have indicated by showing you passages in the
26 ORR’s decision, that the behaviour of EWS imposed a competitive disadvantage on Enron’s
27 ability to renew its commercial relationship with Edison. You seem to be focusing your
28 observations on EWS’s behaviour before May. Is that correct?

29 A I’m talking about EWS’s behaviour from the period that we provided the E2E contract to
30 Edison Mission, which was effectively up until June 2000.

31 Q Well I think we will just have to differ on that. Can I ask you just this though, before we
32 depart from this, do you happen to remember whether Edison ever issued an invitation to
33 tender for the renewal of a coal supply agreement at the time that you are suggesting?

34 A I don’t recall. I don’t recall.

1 Q Because I do not think that we have any document that suggests that it ever did?

2 A The period between June 1999 and June 2000 we were Edison Mission's E2E supplier, that
3 was the agreement.

4 Q But what I am asking you is, at the time you say the renewal came up, if you remember
5 whether or not Edison issued an invitation to tender, or something similar, for the renewal
6 of the coal supply?

7 A I think we need to define what we mean by the word "renewal". There were no guarantees
8 in the first period, June 1999 to June 2000 there were no guarantees. Edison Mission had
9 told us, had told EWS and told coal suppliers, that they were going to drive this on for one
10 year – if it worked, it worked, and if it didn't work they would take other action. During
11 that time – when you talk about "renewal", renewal was a process, there was not a date by
12 which we had to renew, or even had to start renewing. The point was EWS's performance.
13 During that time period, which was appalling, EWS's behaviour towards Enron,
14 contracting with us, we felt and I believe it has been proven, was discriminatory. Did it
15 have an impact on our ability to renew that E2E contract? I believe it played a role, I
16 absolutely do and I have stated that in witness statement after witness statement, including
17 the one for this particular case. What I disagree with is that the tender in September, which
18 we respond to, has nothing to do with coal supply, it was a rail only tender. There was no
19 decision, no strategy, nothing in Enron's leadership at the time that considered that to be a
20 serious way to get back into supplying coal to Edison Mission.

21 Q Right, can we move on to para. 6, please. This is para. 6 of your witness statement. I think
22 that the bundle that you have currently you can put away. (After a pause) Have you got
23 para. 6?

24 A I do.

25 Q You say here: "The main reasons why I think the claim of loss is unsustainable is that
26 Enron's bid was not a serious one." Of course we are looking at the bid for the coal haulage
27 contract in August/September 2000. Do you follow?

28 A Yes.

29 Q I wanted to try and understand what you meant by "serious" because in (a) you suggest in
30 the second sentence that ECSL competed knowing it had no chance of winning, but then in
31 sub-paragraph (c) on the next page you say:
32 "The reasons why the bid was a non-serious one, i.e. was not likely to be attractive
33 to Edison, are clear."

1 I just wanted to know, are you using the word “serious” as meaning that Enron was not
2 serious about the bid, in other words it was a joke? Or are you saying that “non-serious”
3 means not likely to be attractive to Edison, or do you mean both?

4 A Let me just explain something. The whole idea behind the rail concept was a rail only
5 concept. We had, through a Freightliner contract, a very, very lucrative incentive scheme
6 by which we shipped coal, and continued to ship coal; we would have continual price
7 decreases with the amount of volume we shift. So if we had won and put Freightliner
8 essentially running the services for us, it would have been Edison Mission’s call, they
9 would have procured and bought coal from whoever they wanted – right? There was no
10 requirement for coal. We would benefit from it because that would count against basically
11 our contract, and the whole idea behind Enron, at least in terms of this idea, was that we
12 locked up a number of ports and Freightliner on this type of scheme, where anyone else
13 used the system we would benefit, that would make us more competitive when we did
14 compete with delivered coal contracts elsewhere in the UK. You’d have to see the rail bid
15 as a continuum of Enron’s business.

16 Q You did not actually answer my question, but I will return to it in a minute. You have
17 raised Freightliner. I think you said that winning the Edison road haulage contract would
18 enable you to count the tonnage shipped under that contract against the tonnage
19 commitments under the Freightliner contract. Is that so?

20 A You would have been able to count that.

21 Q Right. Could you turn to para. 30 of your witness statement, please? Could you read the
22 third sentence?

23 A Yes, I understand what you are saying. It wasn’t ----

24 Q Paragraph 30 ----

25 A. Listen! You look at the Freightliner contract, and you need to read that closely, you will see
26 that we have price incentives even above 1.1 million. This is not talking about taking the
27 “take or pay” element of the contract, we’ve got price incentives even above that. I wasn’t
28 talking about offsetting the “take or pay” obligation. If we had additional tonnage above the
29 “take or pay” obligation we got additional incentives. Now, you must also view this in
30 terms of some of the contracts we had at the ports. We could sell third party capacity and
31 we’d get the benefit of the rate cuts.

32 Q How close were you to the Freightliner contract? Did you know anything about it at all?

33 A I negotiated it.

34 Q So you must have known something about it?

1 A I would assume so, I negotiated it.

2 Q And how close were you to the coal purchasing agreement between Enron and British
3 Energy?

4 A I was not close to that one.

5 Q Right.

6 A Other than providing the rail information to them. I was not directly involved in negotiating
7 with British Energy, other than providing the rail inputs to it.

8 Q Right. Could you look at bundle G2? If you go to p.485.32 – do you have that?

9 A Yes.

10 Q So what you have there is the confirmation of the British Energy contract, and you see that
11 the term is 1st April 2000, to 31st March 2001. Do you have that?

12 A Yes.

13 Q Could you go to page 485.39? Do you have that?

14 A Yes.

15 Q That is the delivery schedule, and if you look in the look in the box, the last box before the
16 total, deliveries in the first quarter of 2001, that is the three months, January, February,
17 March, are supposed to be 120,000 in each month. Have you got that?

18 A Yes.

19 Q Could you put that away and bear the figures in mind. Could you go to bundle G3, please,
20 and could you go to p.691. Have you got 691?

21 A I do.

22 Q This is the Freightliner Rail Haulage Agreement dated 30th June 2000.

23 A Right.

24 Q Could you go to p.696. Have you got 696?

25 A Yes.

26 Q And could you read the first sentence of clause 6.5.

27 A (After a pause) Yes.

28 Q So you see what the problem was?

29 A What is the problem? Perhaps you could tell me?

30 Q The problem was that under the BE contract the quantities to be delivered effectively
31 exhausted the obligations of Freightliner to provide haulage?

32 A Actually, what you need to consider is how much Enron is willing to commit for hire. It
33 wasn't that Freightliner was limiting the amount that it could provide. The contract we
34 provided them with did not provoke them effectively to provide more service. Do you

1 understand? Freightliner could deliver as much service as they would like as they would
2 get coal cars on line. If we had stood up and said Freightliner provided us with 3 million
3 tonnes, they would put in a programme to do that. They didn't do that.

4 Q Cast your mind back to August and September 2000. Were you aware of the capacity
5 constraints that Freightliner was under?

6 A Was I aware – they were building new coal wagons in Poland. They were buying new D66s
7 to support a merchant's business, effectively, not built on take or pay contracts from
8 consumers like Enron and other companies.

9 Q Did you know whether or not Freightliner actually had any ability to carry additional
10 quantities for Enron, additional to the British Energy contract as from January 2000?

11 A I had personal relationships with Freightliner. Freightliner committed the amount of
12 tonnage to this contract that they felt comfortable with, given the fact that we actually made
13 no real commitment to that.

14 Q We are talking about a period from January 2001.

15 A Right.

16 Q Did you know what ability Freightliner had to move additional tonnage put to it by Enron
17 over and above the quantities agreed in the BE contract with Enron?

18 A Perhaps you could rephrase your question?

19 Q Did you know in August and September 2000 whether or not Freightliner had the capacity
20 to haul tonnage, all coal, for Enron over and above the quantities agreed in the BE/Enron
21 contract?

22 A I'm not 100 per cent sure I understand your question. I think we need to really go back to
23 the time when you're negotiating. If you look at the Freightliner contract Enron does not
24 make a huge commitment to Freightliner. Freightliner had undertaken to acquire D66s,
25 build HTAs or HAAs in Poland. It was a substantial capital commitment on their part. If
26 Enron at that time had told Freightliner, "Why should it triple your investment", and go
27 back to take or pay contracts, I believe Freightliner would have been capable of doing that.
28 We did not do that. I don't really understand the context of your question. Freightliner
29 committed as much as they were able to given the basis of our contract.

30 Q Could you go to bundle B1, please.

31 MR. BREALEY: Sir, can I just interject here. If Mr. Lasok is going to take the witness to parts
32 of the decision, from his skeleton it looks as if he is putting a certain interpretation on it. I
33 just want the witness to be aware that there is a certain interpretation, from the skeleton, on
34 Freightliner's capacity, which we disagree with. I might be able to put it in in re-

1 examination but if it is a question of interpreting the decision, it may not be a fair question
2 to the witness.

3 THE CHAIRMAN: Let us see how we go. You will bear that in mind, Mr. Lasok?

4 MR. MATHER: Could I just raise a question on the last point before we move on. On p.696 in
5 clause 6.5, the following sentence refers to extending the tonnage to 140,000 tonnes per
6 four week period, but that refers to, "subject to the availability of suitable track access parts
7 and the provision of Sunday loading and unloading facilities". Mr. Kearney, could you
8 comment on that: does that suggest that there is quite a tight constraint on Freightliner's
9 ability to deliver tonnage, and that only by really squeezing it and Sunday working could
10 they get up to that level?

11 A This is a commercial negotiation and Freightliner is committing a certain amount of
12 resource to Enron. If they were committing the maximum amount of resource that they
13 could commit on the basis of our contract, which gave a minimal take or pay and gave us a
14 huge amount of flexibility. If you deal with railways and I've negotiated with lots of
15 railways around the world, what they want in order to get into the business, they would
16 require a substantial take or pay arrangement. The negotiations at the time, Freightliner
17 said, "We are taking the decision to enter this market and taking the entire risk on
18 ourselves", which was – talking of these D66 locomotives, worth about £2.1 million. The
19 wagons themselves were several hundred thousand apiece, and their point was, "We can
20 promise as much capacity to you as you are willing to commit to us". I think it unfair to say
21 that Freightliner was constrained because of some unnatural situation, system or inability on
22 their part. If we had gone to Freightliner in August 2000 and said, "You go big, and we will
23 back you, we will put the balance sheet down, we will back you", I believe Freightliner
24 could have delivered a lot more rail service to us but at the time my hands were tied. I was
25 not allowed to commit a single tonne of finance, or a single dollar or pound to this
26 operation, all I could commit was effectively Enron's existing business.

27 Q Thank you.

28 A But if we said at the time that if we could go big, Freightliner would be able to match that, I
29 believe.

30 Q Did that figure in the contract at all and, if not, why not? Was it not customary to put that
31 sort of extension possibility in the contract?

32 A Well, if you look, there is an extension for us to extend the contract on the same price terms
33 and conditions, but, no, at the time, Enron's view was, "We don't know how long we're
34 going to have coal business in the UK". We have existing contracts with BE that we felt

1 that we would be able to continue. We took a view. We were not going to risk very much
2 in order to give Freightliner the business. If Freightliner had turned round and said, “You
3 need to do 100 per cent take or pay contract, or we’re not getting into the business”, like
4 they did the year before when we met with them, nothing would have happened.

5 Freightliner took a commercial view that they were going to get into the business and we
6 took a commercial view to take minimal risks, which I believe we put on the RAC, about
7 £500,000. For a company with a balance sheet and a turnover in the billions, a £500,000
8 risk is not much. Freightliner however took tens of millions of pounds of risk, and they
9 were not willing to commit to a maximum amount of investment without a solid contract in
10 place.

11 Q Just to conclude this, they could have walked away beyond that. If the climate had changed
12 Freightliner could have disappeared as a player?

13 A Freightliner’s view was, “We’re taking a view on the market, the market changes, there are
14 new people who are coming in, power stations are being sold, and EWS is consistently
15 under-performing”. Enron is very vocal about it. We, personally, had been very vocal
16 about EWS’s performance. I had to try, not just with Freightliner but with other third party
17 providers, to bring them into the business. I didn’t have success with PRS. I did, however,
18 have success with Freightliner, but it was really Freightliner who came to us and said, “We
19 are ready to consider this business now, how much are you willing to commit?” The
20 Enron/Freightliner contract committed a little bit, not a lot, and gave us a lot of optionality,
21 it gave us a lot of benefit if we continued doing it with them, but it didn’t commit us to
22 anything, and Freightliner invested accordingly. Actually they over-invested because they
23 actually went and did get take or pay agreements with other power companies.

24 Q Thank you very much.

25 MR. LASOK: Mr. Kearney, have you got bundle B1. Could you look at p.129, please. You
26 should have something here that in a box has got in bold “Edison Mission Energy” – can
27 you see that?

28 A I believe I have the wrong bundle, is it volume 2?

29 Q It is B1.

30 A Okay, what page again?

31 Q Page 129.

32 MR. BREALEY: I am really sorry to interrupt, but if Mr. Kearney is going to be asked to read
33 this he has got to go to p.128 right at the bottom, because it is important, if I can foreshadow

1 what Mr. Lasok's question is going to be – right at the bottom – “In any case ability” and
2 the important “net of existing contractual” ----

3 THE CHAIRMAN: All right, Mr. Kearney, start reading on p.128, seven lines from the bottom,
4 the sentence starting “In any case”, and read on until – what, the end of box?

5 MR. LASOK: I would suggest not the end of the box. It is just the last full paragraph on p.129,
6 and the paragraph following that leading to the top of p.130.

7 THE CHAIRMAN: All right, have you got that, Mr. Kearney?

8 A Yes.

9 Q (After a pause) Have you read it?

10 A Yes.

11 MR. LASOK: What you see here is that the ORR has looked at the minimum obligations under
12 the Freightliner contract, the additional contract that Freightliner had with Drax and then
13 has concluded that Freightliner could not have hauled all the tonnage under the EME
14 contract as from January 2001. It would have had to have geared up for that and it would
15 not be in a position to haul all those volumes until about ten months after the inception of
16 the contract.

17 A If you assume that the Enron contract was the base starting point, had we committed more
18 to Freightliner? Had we committed more I believe Freightliner could have easily entered
19 the market quicker with more ...

20 Q The problem is that even on the basis of that optimistic view, the finding made by the ORR
21 indicates that some lead time of some sort would have to be allowed for before Freightliner
22 could gear up to service even a part of the requirements under the EME contract?

23 A If you assume – I'm not sure I understand what your point is. If we had committed a lot
24 more to Freightliner, Freightliner would have been able to come into the market much
25 quicker and would have done – would have put a lot more wagons – the only constraint was
26 wagons, they ordered the locos. Wagons were a constraint. They didn't have the ability to
27 deliver the coal. If at the time – and I remember having discussions with them, they said,
28 “If you want more wagons, we can order them, we can put them online. We didn't commit
29 to that.

30 Q I will put that on one side for the moment and go back to the question that you did not
31 answer, and that is what is the meaning of “serious” in para.6, second line, and 6(c) of your
32 witness statement?

33 A “Serious” means whether we thought we had a serious chance of winning.

34 Q Right.

1 A Whether we thought that the rail business as a stand-only business would get us back into
2 Edison Mission supplying coal to them.

3 Q Can I draw you back to what you actually say in para.6(a) of your witness statement. Do
4 you have it in front of you?

5 A Yes.

6 Q If you have 6(a) and you look at the second line, you say:
7 “... ECSL competed for a lot of business which we knew that we had no chance of
8 winning, but through the very act of competing for the business, we would gain
9 useful intelligence about the marketplace and our own customers’ needs. The
10 Edison coal haulage tender was one of these tenders.”

11 The meaning that you gave to “serious” just a moment ago was rather different from that,
12 because you said “serious” meant whether or not Enron thought it had a “serious chance of
13 winning”.

14 A I believe I said, which we knew we had no chance of winning. You just said that, but
15 through the very act of ----

16 Q Who is “we”?

17 A “We” being Enron.

18 Q No, who is “we”?

19 A Pardon?

20 Q Who is “we”?

21 A Enron Coal Services Limited.

22 Q That is a legal person, it has no mind. Who is “we”?

23 A “We” being the collective members of the Enron Coal team.

24 THE CHAIRMAN: Who were the eyes and ears of Enron for this purpose, you and who else?

25 A In terms of the railway? With Edison Mission? With who?

26 MR. LASOK: In terms of the ‘we’ that is referred to in the third line ----

27 A ‘We’ being the coal team.

28 Q ‘We’ being the coal team. Now, could you run down a few lines? You get to the phrase
29 ‘Some on the team believed’. So, who were the ‘some’?

30 A You know, there were some on the team believed that the rail-only business would be a
31 successful business?

32 Q Yes. Who were the ‘some’? Can you give us their names?

33 A Steve Pirozzi - one. Steve Pirozzi. The person -- a junior to me, who worked with me,
34 believed that the rail-only business could be a successful business model.

1 Q Right. Who else? Anybody higher than you?

2 A I believe Riaz Rizvi bought the concept.

3 Q Right. Anybody else?

4 A Actually I would like you to refer to any item of evidence within Enron that suggested that

5 this was a serious attempt for us to get back into this whole scenario. I don't recall any

6 evidence of that fact and I don't believe anything in these piles of evidence could suggest

7 that.

8 Q Could you turn to the next page of that witness statement, p.841 of the bundle? Could you

9 go to -- It is still para. 6(a).

10 "Since I have personally negotiated the Freightliner transaction I was not in favour

11 of this rail-only tender because if we won I did not want to have to go back to

12 Freightliner and re-trade our already signed transaction".

13 Does that mean that you were out-voted?

14 A No. I mean, the bottom line is that it is not necessarily the way -- the team didn't work on

15 voting or non-voting.

16 Q Well, how did it work?

17 A Pardon?

18 Q How did it work?

19 A It worked in many ways. Some things people agreed with. Some things people didn't. I

20 personally thought the rail-only business, as thought by Steve Pirozzi, and pushed by Riaz,

21 was a silly thing. I thought it didn't make any sense. Actually, Steve Pirozzi went out to the

22 market with Riaz and tried to sell the rail-only business to other people in the market. And

23 guess what? He wasn't very successful. In his performance review of February 2001 he

24 was told that the rail-only business was a silly idea and he left the team thereafter.

25 Q In para. 8 of your witness statement -- Would you just read para. 8? (After a pause) You

26 effectively say there that the only business rationale for the tender was as a means of getting

27 a coal supply contract.

28 A Actually I'm not saying that. I'm not saying that because I was there at the time we had the

29 discussions putting this rail tender together. To be honest with you, when we had the last

30 version of the term sheet we were at the desk and I remember - distinctly remember -

31 saying, "Why aren't we selling coal? Why aren't we selling coal in this contract? Why are

32 we selling rail?" The double argument came out that, "Yeah, this is rail. We have

33 Freightliner now". He said, "Why don't we just offer them 25 cents if we haul their own

34 coal?" I remember. That was put in at the last minute. To talk about this being an

1 opportunity for us to get back into a coal contract I think is stretching the truth. I actually --
2 I don't remember a single discussion saying that if we won this business we'd be back in
3 the business of selling coal to Enron -- to EME. I don't remember a single management
4 decision or a single e-mail between George McClellan and us saying this would be the case.
5 All George said is, "You must be gluttons for punishment, having to go back and deal with
6 EME".

7 Q I think you have seen Mr. Staley's second witness statement.

8 A I have.

9 Q Could you go back to that second witness statement in Bundle D1 at p.115.12? Would you
10 read para. 29? (After a pause) It seems that Mr. Staley takes a different view from you.

11 A I explained that as, "Would you like fries with that?" approach. I stick by my
12 characterisation. That was the way we did business. Now, I don't recall long hours
13 strategising over the use of this rail contract being a way to get back into the EME business.
14 What I do recall is that some in the group felt this would be legitimate stand-only business.
15 Enron had created an Enron freight business in the United States, which is where you get
16 involved in this, and, to be honest with you, I think these guys thought there was a
17 possibility of doing that in the United Kingdom. If we had won the rail tender, it would
18 have given us information as traders which would have been useful. We would know what
19 coals Edison was shifting; who was buying; what coals other people were burning. We had
20 a series of contracts with ports and with Freightliner which we would benefit by if other
21 people used our third party network.

22 Q You see, the problem is that Mr. Staley was superior to you. He takes a different view.
23 There is simply no contemporaneous, or other, documentary evidence to support your
24 account ----

25 A Actually there is. There is a draft of the rail proposal on September 4th from which the 25
26 pence per tonne proposal is missing. (After a pause) I would further add that in the
27 original complaint we did not identify the loss of the rail tender as having any effect. We
28 mentioned it in the complaint, but we mentioned it on a timeline. We did not issue it as
29 causing any economic harm to Enron.

30 Q What I wanted to do was to go to Bundle G3 at p.880. This is an e-mail from Riaz Rizvi.
31 Do I remember correctly from an earlier answer that he was one of the proponents of the
32 rail-only contract?

33 A He was the proponent of the, "Would you like fries with that?" strategy.

34 Q So, he was not a proponent of the rail-only contract idea.

1 A Have you met Riaz?

2 Q No. That is not the answer to my question.

3 A Riaz took a view that this would be a useful strategy to try and get to get know the
4 counterparties. We used rail. We would also offer fuel oil. We could sell port services.
5 These were all part of our bundle of services we could provide.

6 Q Right. Can you read his e-mail, please?

7 A Actually, could you hold up for a second? I might have the wrong bundle.

8 Q Bundle G3, p.880. Could you read the e-mail, please? (After a pause) This is an internal
9 Enron e-mail.

10 A Right.

11 Q Can you tell me where in that e-mail we see something along the following lines: "We have
12 no chance of winning this, but through the very act of competing for this business we would
13 gain useful intelligence about the marketplace and our own customers' needs"?

14 A There is also nothing in this saying that, "This is an incredibly strategic opportunity and we
15 will be able to leg into Edison Mission and supply them with coal for eternity". It simply
16 says, "We have a basket of services that we can sell. We can sell them rail and we can sell
17 them into the stockpile".

18 Q Where in this e-mail does it also say that the team believe - or, indeed, some of the team
19 believe - that we should offer rail services as a stand-alone business by essentially re-selling
20 Freightliner services to third parties and this business should not be, or is not going to be,
21 linked to coal sales.

22 A You know, it doesn't say that, but since I was there and participated in many of these
23 conversations, and, to be honest with you, there are lots of other documents that are not
24 included in this that talked about the sale of rail services -- I'm not sure I really understand
25 your point. If all you're betting on is this document -- I believe actually George
26 McClellan's statement that, "You must be a glutton for punishment" was the response to
27 this e-mail.

28 Q But that is not suggesting that you are not going to get the contract. That suggests that you
29 may get the contract. You are a glutton for punishment because you want to have another
30 deal with EME. There was a bit of a dispute with EME over the year.

31 A I knew George McClellan. Okay? I worked with George McClellan. What George
32 McClellan meant by that e-mail is, "Are you crazy dealing with Edison Mission again? Are
33 you crazy?"

34 Q So, he thought that that was a real possibility, was it?

1 A I would be wasting time. That was his indication. (After a pause) I worked with the man.

2 Q Right. Could you put that document away and go to Bundle G4?

3 THE CHAIRMAN: I presume, Mr. Lasok, you would rather sit through because of the cost of all
4 this equipment?

5 MR. LASOK: I am in the hands of the Tribunal or, indeed, Mr. Kearney because it is late at
6 night.

7 THE CHAIRMAN: What time is it, Mr. Kearney?

8 A It's five of ten here in Singapore.

9 (Short break)

10 MR. LASOK: Could we go to Bundle G4, please? Could you go to p.940?

11 A Excuse me. My notebook just exploded.

12 Q Page 940. This should be a document dated 15th September, 2000. It is the tender that
13 Enron put in in response to the Edison invitation to tender. This is a covering letter. If you
14 look at the second sentence of the first paragraph it refers to the fact that they (Enron) have
15 tried to meet Edison's need for flexibility and sourcing its fuel from multiple locations as
16 well as its desire to drive down costs in all parts of the value chain. Then, if you miss out
17 the next paragraph, there are two more paragraphs. Could you just read those? (After a
18 pause) Can you just explain to me why we have these comments in the letter if you say that
19 the purpose of responding to this tender was just to get coal haulage?

20 A I always found this letter to be a bit of an anomaly because Steve Pirozzi was a very junior
21 member of the Enron team. He worked for me. I always found this one strange because if
22 this was such a serious response from Enron, I would've thought Stu or George McClellan
23 would've handled this. If this was really a coal tender -- because Stu handled all the coal
24 tenders with Riaz. He was really driving the coal tender and the coal response and
25 especially the Edison Mission relationship. I always found this to be a little odd - that a
26 junior member of the Enron coal team was allowed to submit this tender - because Stu
27 really had the relationship with all the generators, and Stu had other relationships with
28 Edison Mission -----

29 THE CHAIRMAN: I am not sure where this is getting us because it is plainly a tender, is it not?

30 A It is a tender, yeah, but I was surprised that Stu did not respond to it.

31 Q Next question, Mr. Lasok?

32 MR. LASOK: Presumably he did not respond because he agreed with it.

33 THE CHAIRMAN: Let us move on.

1 MR. LASOK: You can put away this document. Could you go back to your witness statement?

2 Could you go to p.841? If you look at the third to fourth lines from the top, you have got
3 your repeated belief that there was no real prospect of winning the tender. But, then you
4 say,

5 "I recall that we told Edison to send us an invitation to participate and that in
6 doing so Edison was simply obliging our request".

7 Who was the 'we'?

8 A 'We' being the Enron coal team.

9 Q So you all gathered round a 'phone.

10 A I'm using a colloquial expression 'we', meaning Enron. Enron was the initiator of the
11 request. Enron was the initiator.

12 Q Who rang Edison?

13 A I believe -- If I remember correctly, Riaz spoke with Max and said -- They were talking --
14 They met, and then he said, you know, "We have this new rail relationship with
15 Freightliner. Perhaps there's something we can do here. Why don't you include it in your
16 tender and I can take a look at them". That is my recollection of it.

17 Q Right. There is a difference between Riaz or anybody else talking to Edison in the form of
18 Max Crosland, or something like that, and speaking in glowing terms about the Freightliner
19 deal -- There is a difference between that and a conversation in which the same things may
20 be said, but Riaz, or whoever it is, goes on and apparently tells Mr. Crosland, or somebody
21 else to send an invitation to participate. Now, I am wondering whether your recollection of
22 this event is accurate. Now can you cast your mind back to the time we are talking about,
23 which is August 2000? I know it is very difficult, but can you do that?

24 A Yes, I can.

25 Q So, what is your best recollection of what happened?

26 A My recollection is that there were members of the Enron team that had some
27 communication with Edison. This is after the Freightliner deal had been announced --
28 Basically it was well-known in the market even before it was announced. Why don't
29 we try to basically sell Freightliner services to Edison Mission? That's my recollection.

30 Q Right. You do not know how many people this information passed to you from the original
31 person who had this meeting?

32 A I believe -- Like I said, I believe it was Riaz and Max Crosland. I believe that was who the
33 conversation was between.

34 Q The problem, of course, is that Mr. Crosland does not remember anything like this.

1 A Okay.

2 Q Right. If we pass on to para. (b) we have got the, “McDonald’s. Do you want fries with
3 that order?”

4 A Uh-huh.

5 Q Do you have much experience of McDonald’s?

6 A I’m an American citizen. I’m required to. (Laughter)

7 THE CHAIRMAN: Do you, Mr. Lasok? You do not have to answer that question.

8 MR. LASOK: I have some vicarious experience but I have some direct experience. (To the
9 witness): Surely the position is this: Edison wanted to rail haulage because it was going to
10 buy coal. Was that not the case?

11 A I believe that is why a power company would be purchasing rail haulage, yes.

12 Q Okay. So, is the analogy with somebody who goes into McDonald’s and says, “I would like
13 a hamburger meal. What is the price of your fries?”, and where the response is, “Our fries
14 are X, but if you buy the whole meal the price is Y”? Would you accept that that is a better
15 analogy?

16 A No, I wouldn’t because what you have to understand about what Enron was offering -- You
17 have to understand Enron as a company. We were an energy company. An energy
18 company. Not just a coal-selling company. Not just an E2E company. Even if the Enron
19 E2E business was only one facet of the Enron coal business -- We sold coal on an FOB
20 basis. We sold coal into the stockpile. We bought coal from mines and delivered to ports.
21 The E2E model, so to speak, suited some of our customers who did all kinds of things. The
22 coal desk talked constantly to the electricity desk because the two are intertwined. Only rail
23 services into a power station would have value for Enron. So, the idea of participating in a
24 tender theoretically makes sense.

25 Q So, it did make sense.

26 A Pardon?

27 Q It did make sense.

28 A It did make sense. Why wouldn’t we? We had the contract with Freightliner. We had the
29 ability to re-sell. In fact, there was a discussion between Freightliner and Enron shortly
30 before the contract was signed in May where Freightliner wanted to explicitly put in the
31 contract that we would not be allowed to sell rail services only. In other words, any
32 contract we had with Freightliner would require effectively us to shift coal, but we would
33 not be able to sell their rail services. There was a huge point of contention between us and
34 Freightliner on this issue. This is why George McClellan intervened. In fact, there’s an e-

1 mail exchange somewhere in the evidence which points to that, where George is saying,
2 “We have to have the right to re-sell on a rail-only basis. We have to have that right” -
3 because if we acquired the rail-only business we’d have information. We were traders. We
4 weren’t just in the E2E coal business. Enron were traders and if they had access to the rail
5 information we could have access to the ports. We could know what coal was coming in;
6 who was buying coal; who was selling coal. This is information we could trade on. I’m not
7 saying there wasn’t a rationale for selling the rail-only business. I was against it. I thought
8 it was a convoluted rationale, but there is a rationale for selling on a rail-only basis, but to
9 say, “Rail-only business -- If you’re selling rail, you’re automatically getting coal --“ I
10 think it was a false conclusion.

11 Q Right. I want you to go to a little passage that appears in the same sentence, but just above
12 the, “Would you like fries?” phrase at the end of para. 6(b). Four lines from the bottom you
13 say this,

14 “Seeing that we were not expecting to shift any additional coal to Edison at the
15 time ----“

16 A Which is true. Which is true.

17 Q Okay. Who is the ‘we’?

18 A Enron Coal Services was not shipping coal to Edison Mission at the time.

19 Q That is untrue though, is it not?

20 A Actually it is. If you look at the volumes they stock, they stopped effectively when?
21 September 2000.

22 Q To begin with they were shipping coal and, furthermore, they were receiving invitations to
23 tender for coal supply from Edison at that time, were they not?

24 A Well, we weren’t shipping anything.

25 Q You are being a bit evasive here, are you not? How close were you -- You were not very
26 close to the coal business at all.

27 A I was a member of the coal team and I would be perfectly aware whether or not we were
28 shipping coal to Edison Mission at the time, or not.

29 Q I want to focus on the phraseology. “We were not expecting to ship any additional coal.”
30 Could you look at bundle G3, please, at p.895? This should be an internal Enron e-mail
31 from Jez Peters. Can you read it? (After a pause) What this is is an internal e-mail dealing
32 with an invitation from Edison to tender for a ‘supply delivered stockpile Ferrybridge’.
33 This particular internal e-mail is dated August 30th. It refers to an invitation to tender that
34 had been made on the evening of 29th August.

1 A Right.

2 Q Enron then responded with a tender. So, can you please tell me on what basis is it that you
3 say that at this particular time Enron was not expecting to ship any additional coal to
4 Edison?

5 A Let me clarify that. Let me clarify that. There was no expectation at the time for us to be
6 shipping coal to Edison Mission on an E2E basis. That is my recollection at the time. Now,
7 if Edison Mission was in the market ...which -- I can't mention that. I wasn't aware that
8 they went to do that. But, they were probably one of twenty-five people that received an
9 offer.

10 Q You see, I would suggest to you that your recollection about the coal side of the business is
11 extremely faulty because in fact post-September 2000 Enron was shipping coal to Edison
12 and ----

13 A On a delivered basis? On a delivered basis?

14 Q To LBT?

15 A On a delivered basis - that is, to the port? That's on a CIF basis - that we were delivering on
16 a CIF basis. Not a delivered basis. Not on an E2E basis.

17 Q On a partial E2E basis. It was a hybrid arrangement.

18 A I'm curious about that arrangement because I was the person in charge of the trains at the
19 time. I don't recall doing an E2E.

20 Q It was an intermediary arrangement in which the transport element ended at LBT and did
21 not go right to the power station.

22 A That's called CIF.

23 Q No, it is not.

24 A That's called Cif sale.

25 Q No, it is not. It was an intermediary arrangement.

26 A Perhaps you know the INCOTERM for it? Perhaps you would've delivered stockpile --
27 delivered ex-stockpile ... Perhaps you can tell me what it was because if it's not -- if it's not
28 to the power station it's not E2E.

29 Q I think perhaps I was a bit too prompt in saying it was not, because it was a CIF
30 arrangement. But it was an intermediary arrangement ----

31 A That's called CIF. We sold coal CIF. We sold coal FOB. We bought FOB. We did all
32 kinds of things. E2E was one of the businesses we did.

33 Q The second reason why you are wrong is because Enron was receiving invitations to tender
34 from Edison and the example I have given you is an invitation to tender on an E2E basis.

1 A Of course we were receiving invitations from Edison Mission. Of course. It was in their
2 interests to do so. We were players in the coal market. Why not get a price? I would be
3 curious if we actually shipped that case. I don't think we did. I don't recall delivering that
4 case. I don't think we won.

5 Q Right. The second phrase that I wanted to ask you about in the same sentence is the bit that
6 follows: "-- stood no chance of winning the haulage tender". Again, the subject of the
7 sentence is the 'we'. Mr. Staley has given evidence that Enron did bid on the basis that
8 there was a chance of winning the tender.

9 A I would expect Stu Staley, as the director of Enron Coal Services Ltd., to say that. However,
10 having been intimately involved and responsible for the rail part of the business, and having
11 been intimately involved with all aspects of the delivery of coal and from ports to the
12 railway station -- the E2E power stations, I disagree. I did disagree with it.

13 Q All right. So, you disagree. If we move on to sub-paragraph (c) at the bottom of this page,
14 you say,
15 "The reasons why the bid was a non-serious one, i.e. was not likely to be attractive
16 to Edison, are clear --"
17 Really, this is a bit of speculation on your part, is it not?

18 A If I'm asked to tender for something and I respond with a non-conforming bid, in the real
19 world that bid is rejected.

20 Q That is not true either.

21 A Because I'm not responding to the tender in the proper fashion. We had no expectation of
22 getting any coal business out of this rail tender. This rail tender, for various reasons, was put
23 in, but there was no expectation of getting business from it. I don't know what else to say.
24 If you could point me to a document - an Enron document - or a communication between
25 Stu and George talking about how important this was, and how we were going to get in --
26 To be honest with you, the attitude of the Enron coal team towards Edison Mission was
27 dismissive, was derisory. We were arrogant. We said, "These idiots don't know what we're
28 doing. We're just going to get on with our business". That kind of thing. Okay? The
29 relationship with Edison Mission and Enron was not a positive one, and, to be honest with
30 you, the members of the team were very dismissive and derisory towards them.

31 Q I think the Tribunal have seen the documents. I do not need to go back to them. If we go on
32 to the next page, to para. 7 of your witness statement is just you placing your own
33 interpretation on certain facts, is it not?

1 A I want to clarify that - that Enron lost coal profits as a result of EWS' behaviour with regard
2 to the coal tender. I only maintained that Enron did suffer damage up until the point that the
3 E2E contract ended. I have always maintained that.

4 Q When did the E2E contract end?

5 A June 2000.

6 Q That is incorrect, is it not?

7 A In what sense?

8 Q It continued to be performed for some time after that.

9 A Perhaps you could actually illustrate that? The E2E contract ended in June 2000.

10 Q The arrangement whereby Enron supplied coal to Edison continued until 2001, did it not?

11 A That's something different, isn't it? That's not an E2E contract.

12 Q Right.

13 A That's different. I've always maintained up until June 2000 we had a legitimate claim and
14 with calculable damage. In fact, that is what we put in front of the Competition
15 Commission. We never argued the rail tender caused us any damage. We never argued that
16 it cost us a lot of tonnage. We never argued post 2000 that the rail tender had any effect on
17 Enron.

18 Q The reality is that Edison's coal requirements were being supplied by Enron until some date
19 in 2001.

20 A I think that's misleading actually because Edison had its own coal arrangements with
21 Powergen and they also procured their own ... tonnage on their own as well as of June 2000.

22 Q When the contract between Enron and Edison expired - and this is the contract for the
23 supply of coal - it would be necessary for Edison to find an alternative source of supply - in
24 other words, a replacement contract. Is that not correct?

25 A Replacing the bit that Enron was supplying?

26 Q Yes.

27 A Okay, so Enron is supplying on a CIF basis post June 2000, okay? Enron is not supplying
28 on an E2E basis but on a CIF basis. The argument stands. I'm sorry, if Enron is supplying
29 on a CIF basis that's not an E2E contract. That's on a CIF basis. We can't argue - we had
30 no E2E contracts post-June 2000, we then can't argue that we lost business as a result of not
31 having E2E contracts.

32 Q But the time at which Edison would need replacement supplies of coal would be as from the
33 point at which Enron's supplies under that contract ceased?

1 A My recollection is slightly different. We had some tonnage into Fiddler's Ferry carrying
2 over and some tonnage into Ferrybridge during the summer – June 2000. That's my
3 recollection. We had some cargos into LBT. That was all part of the work out between
4 Enron and Edison. The bottom line is we had no E2E contracts post June 2000. Did EWS
5 effect the performance of their contract? I've said yes. However, when Enron came to me
6 and said as a result of the loss of the rail tender we did not get additional business, I don't
7 think you can draw that conclusion. We said that as well. In fact, Enron never maintained
8 that when it submitted the competition complaint.

9 Q If you will forgive me, that is just a matter of speculation on your part?

10 A No, no, I was involved in the writing of the complaint as the chief witness, to the ORR. I
11 never maintained that the loss of the rail contract affected Enron. We never put that in
12 there. We put it in as a bye-line on a timeline, but we never maintained that the loss of the
13 rail contract caused us to lose additional business with Edison Mission, never; and we
14 never maintained within the company that it would ever have any effect on us.

15 Q I am afraid we are going to have to differ on that, because certainly my reading of your first
16 witness statement and also the response that you gave to the email from Mr. Lahnborg leads
17 me to a different conclusion?

18 A You're putting words in my mouth.

19 Q No, I am not, I am putting words in my own mouth. Can we move on to a different topic.
20 If you move on to para.8 of your statement, it is again a situation in which you are drawing
21 your own conclusions from facts. Is that not correct?

22 A Perhaps you could elaborate, I'm not sure I fully comprehend your statement?

23 Q Can you identify in para.8 any fact that you are giving evidence of?

24 A The figures by Mr. Ordoover that the rail contract has been nothing but a loss leader to get
25 Edison into a coal contract – if I remember correctly, was that the train of thought here?

26 Q I think actually that where you do get into a matter of fact is where you say:

27 "We would never have offered a discount that was not linked to the sale by Enron
28 of coal to Edison."

29 A In other words, we wouldn't have discounted rail if we threw in the coal.

30 Q Then when you get to the next bit you say:

31 "... there was never any suggestion that we had any prospect of selling increased
32 volumes of coal to Edison even if we won the tender."

33 A No.

34 Q Where do you get that from?

1 A Because the tender was for rail services and not for coal.

2 Q But it was in the context of Edison indicating that it was reconsidering its coal purchasing
3 requirements, or strategy, I should say. What was it wanting the haulage for?

4 A For the transport of coal.

5 Q In the context of a revised coal purchasing strategy?

6 A Right, okay.

7 Q So why do you say that there was no suggestion or, to use your own words:
8 “There was never any suggestion that we [Enron] had any prospect of selling
9 increased volumes of coal to Edison even if we won the tender.”

10 A This is an interesting logic chain, and I’m just trying to – you’ll have to give me some time
11 to think about it. What you’re effectively saying is that because Edison included Enron in a
12 tender they must have been offering an E2E deal. Is that my understanding of it?

13 Q No, I am putting a “foot in the door” theory.

14 A Pardon?

15 Q I am putting a “foot in the door” theory.

16 A ... once we have the rail tender we’re going to get coal as a result.

17 Q Yes, a recognised business technique?

18 A But that does not – you can’t draw that conclusion that had we won the tender we would
19 have gotten the coal. You can’t draw that conclusion.

20 Q This is really degenerating into just an argument, is it not? You are not giving evidence.

21 A I’m asked to comment on that statement and I stick by it.

22 Q Let us move to the section entitled “Enron’s business model” – this is p.843. Do we agree
23 that the Enron business model was a highly competitive option?

24 A In the context of the history, the term “Enron business model” is not used in many business
25 schools except only to suggest failure. I will say this much, that E2E was just one business
26 that Enron had in the coal business. We sold on an FOB basis, we sold on a CIF basis, I
27 bought coal in mines in South Africa and railways to the port. We did lots of things. E2E
28 was just one. To say that E2E was the only business that Enron’s coal team did is wrong.
29 We had E2E customers and here’s the point: Enron had no coal mine, Enron had no power
30 stations except for one small coal fired station in Wilton. What do you do if you want to get
31 into the coal business? You don’t own a coal mine if you don’t own a power station, okay.
32 You get somebody else’s order book and, yes, for sure, we can describe Enron’s business
33 model as a whole host of extrinsic and intrinsic options and make it very fancy but what this
34 really was was owning customer, owning the customer, and owning customer was to deliver

1 on an E2E basis. What we did was get Edison Mission's order book, and guess what, we
2 went out and bought ten times more coal than we needed for the power station, and that's
3 what you do. When you get someone else's order book you get optionality for mines, you
4 have the ability, and that's what we did.

5 THE CHAIRMAN: But you were a firm believer, were you not, in the E2E business model, as
6 was Mr. Staley?

7 A Absolutely, it's brilliant, if you think about it, we had nothing – you know the parable of the
8 stone soup - and we got everyone else to contribute. We got Edison Mission's order book,
9 and guess what, we prevented the stations from talking to the railway stations. We
10 prevented anyone from talking to the market. We controlled that, and as a result of
11 controlling that we got ten times more flow and we got legitimacy. If you are going to build
12 a mine and say, "I know we haven't got any power plants, but guess what, we have Edison
13 Mission's order book and we are controlling that, and if you want to get into Edison
14 Mission you have to sell us four times as much coal as you would and then maybe we'll get
15 some coal into the station". We did that, it was beautiful thing, I loved it, it was fun.

16 Q I think we have got your answer, I apologise for asking the question!

17 A It was fun ----

18 Q Wait for the next question from Mr. Lasok, if you do not mind?

19 A I loved it.

20 MR. LASOK: Could you turn to p.844 of your witness statement. Paragraphs 13 to 15 are really
21 about the period in 1999, are they not?

22 A Precisely.

23 Q Paragraph 16, the first sentence, there is a problem with that, which is that it is inconsistent
24 with the finding in the ORR's decision. For the Tribunal's reference, it is a finding at
25 bundle B1, p.15. If you go to the next page, at the end of para.16 you have got:

26 "Edison's acquiring of its own coal procurement and logistics team was much
27 more reflective of the standard business model prevalent throughout the utility
28 industry than was its previous short-term outsourcing with ECSL."

29 Every generator operating a coal fired power station had to have a coal team, did they not?

30 A In the relationship between Enron and Edison it was different, it was newer, it was different.
31 Actually, no, that's not true. If on a E2E model the whole idea that Enron had ----

32 THE CHAIRMAN: No, Mr. Kearney, I am going to ask Mr. Lasok to repeat the question, and
33 could you just answer it briefly, I think it was quite a simple one.

1 MR. LASOK: Every generator operating a coal fired power station had to have a coal team, did
2 they not?

3 A You have to have people that understood coal, yes.

4 Q The fact that you have got a coal team does not determine which sourcing strategy you are
5 going to use, whether it is DIY or E2E, does it?

6 A No.

7 Q In relation to para.17, I just wanted to ask you whether you were agreeing with what
8 Mr. Staley said at para.16 of his second witness statement. His second witness statement is
9 in bundle D1. 16 is actually about a point that you make about credit rating. If you have
10 got D1 at p.115.6 could you read para.16 and tell me whether there is anything in it that you
11 disagree with?

12 A (After a pause) I think we may be talking about two different things.

13 Q What comment would you like to make on para.16 of Mr. Staley's statement?

14 A I think we're talking about two different things. There was some mining company, a very
15 large public mining company, that would not sell to us. They would not take a credit risk
16 on us. This is just a fact, they would not take a credit risk, and it ... that was a very wise
17 thing. However, we definitely said at the time, and we know actually Enron's credit risk at
18 the time was completely mis-priced – we did offer that Enron was a much better credit than
19 shipping companies, than some mines they were shipping from. We definitely said that, but
20 what I'm trying to say is that utilities like Powergen or National Power is a very, very
21 respected long term credit in the market, a better credit rating than Enron, and it was
22 difficult for us to justify that we could get a better deal through E2E contracts than they
23 would be able to turn around. This is an argument that was thrown back to us quite a bit.

24 Q Which coal mines are you talking about?

25 A Pardon?

26 Q Can you name any of these coal mines?

27 A BHP Billiton.

28 Q Are you sure about that?

29 A That they would not sell us coal? It's not to say we did not buy BHP Billiton Coal, but
30 BHP Billiton would not take much credit risk with Enron. We did trade with BHP Billiton,
31 but they kept it very, very close.

32 Q Anybody else?

33 A That is my recollection.

34 Q That is your recollection?

1 A. Yes.

2 Q Anybody else?

3 A Pardon?

4 Q Anybody else? Any other mining company?

5 A If you look at what coal we were buying from people – BHP Billiton is the largest metal
6 mining company in the world and one of the largest coal companies in the world. They
7 were a substantial coal supplier in many different places.

8 Q Can we move on a bit. Perhaps you could put Mr. Staley away, as it were, and go back to
9 your witness statement, para.23 is again you drawing your own conclusions from the facts.

10 A True, I've drawn my conclusions, that is conjecture. That is conjecture.

11 Q Paragraph 24, if we go to the third line:

12 "To my knowledge and recollection, Edison was not looking to link rail haulage to
13 future coal sources in any way."

14 I think we have already explored that together, have we not?

15 A I think so, yes. I think we have explored that.

16 Q If you go to the next page, p.848, (c) the last sentence:

17 "We did not see any coal profits as arising from success on the Edison tender for
18 rail haulage."

19 Again, I think we have done that one to death, have we not?

20 Q I think that's an appropriate description.

21 THE CHAIRMAN: So do I.

22 MR. LASOK: You have got (e):

23 "I do not believe that a haulage only contract could have operated as a gateway to
24 providing more coal to Edison because ...

25 (i) it is my recollection that Ferrybridge was largely burning indigenous coal."

26 If I said to you that about 3.5 million tonnes of imported coal was hauled to Ferrybridge
27 between 2001 and 2004, is that something that you have got any knowledge about?

28 A If I recall correctly, Enron went bankrupt in November 2001. I don't know how much
29 indigenous coal – I don't know much imported coal Ferrybridge imported after the
30 cessation of the Enron contracts, because, to be honest with you, we weren't privy to those,
31 but at the time one of the big disputes that precipitated the Enron/EME dispute, if I recall,
32 and I was not principal to it, was that they had over-bought essentially. They over-bought
33 for Ferrybridge, they over-bought for Fiddler's Ferry.

1 Q In (ii) you say that it is your recollection that Edison was only burning Colombian coal. It
2 was burning Ferrybridge approved coal, was it not?

3 A At Ferrybridge, I am sorry, this should be clarified. My recollection is it was only burning
4 Colombian coal at Ferrybridge, but it referred to coal source directly from Drummond, and
5 also I believe it was burning some Polish coal as well. I remember shipping Polish coal to
6 them – Ferrybridge.

7 Q It just had to be Ferrybridge approved, did it not?

8 A Pardon?

9 Q It had to be Ferrybridge approved coal?

10 A Yes, Ferrybridge approved coal, yes.

11 Q That is right.

12 A No, no, I remember the difference between Ferrybridge approved and actually what coals
13 went to Ferrybridge.

14 Q Right, well, that is interesting.

15 A That is an interesting point, but (Laughter)

16 Q Then (iii) on the next page you say: “to the best of my knowledge, Max Crosland at Edison
17 would never have committed to purchasing coal over a long time period.” But the evidence
18 that we have received is that it was not Mr. Crosland’s decision, so how do you know that it
19 was Mr. Crosland’s decision?

20 A Well I had discussions with Max subsequent to the collapse of Enron, and he maintained it
21 was his decision and I think

22 Q Well he had power to make a recommendation, did he not? Or can you not give evidence
23 on that point?

24 A Well I can’t give evidence on that. What Mr. Crosland’s role within Edison Mission

25 Q If you go to para. 25, fifth line down, you say that British Energy did not have its own in-
26 house coal procurement team. Is that accurate?

27 A Let me explain that. They didn’t have a team set up that would go out into the market and
28 buy coal and bring it to the station. Of course they had people that dealt with coal at British
29 Energy ... coal procurement team ... a team that is responsible for sourcing, shipping,
30 putting to port ...

31 THE CHAIRMAN: Well I think you include a phrase a few lines further relating to other
32 companies who “wished to control their own procurement of coal and haulage directly in
33 the traditional manner”, is that what you mean?

34 A Precisely, yes.

1 MR. LASOK: If we look at the last line of para. 25: “By the Spring of 2000, Edison was not
2 interested in an E2E contract”. Again, you were not close enough to coal supply to have
3 direct knowledge of that, were you?

4 A Well, except for the fact that I had day to day contact with people ... who were aware of the
5 failing relationship between Enron and Edison Mission, so you’re right I was not privy to
6 their negotiation, I was not privy to the work out, but I certainly was privy to the attitude
7 and I would say the intention of Edison Mission.

8 Q And you missed ----

9 A I was also on the ... desk as well, and it wasn’t everyone had their own offices, it was open
10 plan where everyone worked together.

11 Q And you missed the August 29th request from Edison, that Enron supply coal on an E2E
12 basis?

13 A You know I think you are taking an incredibly minor exchange and blowing it up into a four
14 year coal deal. Of course Edison Mission would be out in the market asking for prices. I
15 don’t recall we actually delivered that cape and I believe we were probably one of the
16 twenty people who got the request. Why wouldn’t you ask Enron who were big players in
17 the coal business?

18 Q Could you go to p..850, please?

19 A I mean “Come to daddy” the email ends “come to daddy” -- that doesn’t mean we got the
20 business.

21 THE CHAIRMAN: What were you about to ask about, Mr. Lasok?

22 MR. LASOK: I was about to ask the witness to move on and come to ----

23 THE CHAIRMAN: I have just done so.

24 A Paragraph?

25 MR. LASOK: It is the end of para. 26, on p.850. In the last two sentences you say: “Edison had
26 no need or desire for Enron’s imported coal at Ferrybridge ...” Were you aware – well, I
27 have already put it to you, I do not think you were aware that Edison hauled 3.5 million
28 tonnes of imported coal to Ferrybridge between 2001 and 2004?

29 THE CHAIRMAN: Well I think you have already answered that by saying that Enron had gone
30 bust by then?

31 A Yes, I mean I wouldn’t have been aware of that.

32 MR. LASOK: Can we get to Enron’s dealings with Freightliner, please?

33 A Yes.

34 Q Do you agree that at the time Enron was concerned about EWS’s dominant position?

1 A Absolutely.

2 Q And it was concerned about EWS's abuse of the dominant position?

3 A Absolutely.

4 Q Do you agree that Enron thought that Freightliner offered the possibility of introducing
5 competition into the market?

6 A Absolutely.

7 Q But I want to take you to the second sentence of para. 28, it is the third line where you say:
8 "By the time of the Edison coal haulage tender, Enron had thrown its lot in with
9 Freightliner ..." I would suggest to you that that is not quite accurate. Enron saw that
10 Freightliner was an alternative provider of haulage services that Enron could use, but it also
11 gave Enron leverage of EWS in relation to possible future contracts with EWS. Do you
12 agree with that?

13 A The functioning of the market, absolutely, that was the whole idea of being in competition,
14 it would give us leverage.

15 Q And if you go to G2, p. 558 – do you have that?

16 A Yes.

17 Q This is an email from you to Mr. Staley amongst others, sent on May 12th 2000, and it deals
18 with the EWS proposed rate structure, which I think is set out in the succeeding pages, and
19 you say: "Advise we delay on contract as much as poss DRS is looking good". Is that
20 another instance of Enron looking to another possible source of competition that would give
21 it more leverage over EWS?

22 A Absolutely. One of the Contract.

23 Q We are talking in para. 28 actually of the period really August/September 2000. I just
24 wanted that connection to look at the last two sentences of para. 28 and the penultimate
25 sentence says:
26 "Freightliner's prices may have been slightly higher than EWS's, but we felt that
27 we received an excellent service from Freightliner and so derived very good value
28 from the arrangement."
29 But is it not ----

30 A ... we felt that we had negotiated a contract which would provide us with excellent service.
31

32 Q It only started hauling coal in January 2001.

33 A It was actually December 22nd, 2000.

1 Q Well I got my date from the ORR's report but it does not matter. The last sentence says:
2 "We did not regard ourselves as being disadvantaged whether in the Edison tender or more
3 generally by using Freightliner rather than EWS." But the ORR's finding was that Enron
4 was disadvantaged?

5 A We were disadvantaged but not by using Freightliner. I am curious, in fact I'm not sure I
6 understand. We were disadvantaged absolutely we were disadvantaged because we had no
7 negotiation for dealing with EWS. Once we got Freightliner in we had the ability to
8 negotiate. It didn't necessarily help us, we didn't get better rates from EWS.

9 Q I think at least on that point we are in agreement. I think there is just one last point that I
10 need to deal with, it is in connection with this business about renewal. I think it is said that
11 the renewal of the E2E agreement was undermined by EWS. Do you remember saying
12 that?

13 A Yes.

14 Q If EWS had not abused its dominant position, would you have said that Enron had a good
15 chance of winning E2E business from Edison?

16 A To be honest with you, it's not really my place to respond there.

17 Q I see.

18 A I think it coloured our relationship and I think it damaged our relationship, and I have said it
19 all along. Whether that would be a side factor I don't know. Did it play a role? I still think
20 to this day it played a role in not renewing the contract. But I can't say definitively that that
21 was the single issue because I worked for Enron not Edison Mission.

22 Q Okay, I think there is just one point that I need to put to you so that we are clear about it.
23 Could you look at G5, please? Page 1424 – this is your witness statement to the ORR and
24 you say at the end of para.20 that:

25 "EWS's behaviour played some role in undermining ECSL's position with regard
26 to the renewal of its supply of coal to EME's power plants."

27 I would suggest to you that contrary to what you said previously this is a reference to events
28 later in 2000 at which ECSL was unable to renew its relationship with Edison?

29 A Having written that, and having been there that is the wrong conclusion. It was referring to
30 the period up to June 2000.

31 Q The reason why I put that to you is that it does not make sense otherwise?

32 A What was that?

33 Q It does not make sense, does it?

1 A Sure it makes sense. We've lost the Edison Mission business in June 2000 and believe that
2 EWS's performance, the E2E contract, I believe that EWS's performance played some role
3 in that. You can't argue to Edison Mission that we are the best thing since sliced bread if we
4 can't deliver the coal, and to be honest with you we took that responsibility on ourselves
5 and Edison Mission took that risk that Enron would control every single aspect of its supply
6 chain. EWS's failure to perform during that contract from June 1999 to June 2000 was
7 directly impacted by EWS and that's what we put in the complaint.

8 Q You talk here about the renewal of the supply of coal. The supply of coal was not
9 terminated at the restructuring of the E2E agreement in 2000. It carried on and at a later
10 stage it would be necessary for Enron to renew its supply of coal to EME power plants, and
11 therefore I am suggesting to you that your current recollection is wrong and this sentence, at
12 the time that it was written was intended to refer to the renewal of a supply relationship with
13 Edison later in 2000?

14 A I can only categorically disagree. I know what they intended. Perhaps I should have been
15 more clear because to be honest with you I completely discounted, and almost forgot about
16 the Edison Rail tender, to be honest with you, by that point. It was such a minor event. You
17 are putting words in my mouth.

18 THE CHAIRMAN: Thank you very much, Mr. Lasok. Mr. Brealey, do you have any re-
19 examination?

20 MR. BREALEY: (After a pause) May I ask one question?

21 THE CHAIRMAN: Yes.

22 Re-examined by Mr. BREALEY

23 MR. BREALEY: Mr. Kearney, you have the Freightliner deal between Enron and Freightliner?

24 A Yes.

25 Q You have also got the Enron bid to Edison ----

26 A Yes.

27 Q -- where Enron proposed certain rates to Edison?

28 A Right.

29 Q What was the basis on which you quoted those rates?

30 A The basis of those rates was on the Freightliner contract. That was the only thing we could
31 go on.

32 MR. BREALEY: Thank you.

1 THE CHAIRMAN: Right, Mr. Kearney, thank you very much for attending. Could you pass on
2 our thanks to the person who has been assisting you with all the files, who has obviously
3 been very helpful; and to the Authorities – are you in Singapore?

4 A I'm in Singapore.

5 THE CHAIRMAN: Well would you thank the people in Singapore who have been helping you
6 and we bid you good night.

7 A Thank you very much, it is 11 o'clock, it is time for bed.

8 THE CHAIRMAN: We will adjourn until 10.30 on Monday. Hope you enjoy your vicarious
9 "burgers" over the weekend!

10 (Adjourned until 10.30 a.m. on Monday, 21st September 2009)

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