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Craig I. Smith
Attorney at Law
2824 Coventry Road
Cleveland, Ohio 44120
216-561-9410
wis29@yahoo.com

Via Next Day Delivery

December 12, 2008

FAX

Public Utilities Commission of Ohio
PUCO Docketing
180 East Broad Street, 13th Floor
Columbus, Ohio 43215

In Re: Case No. 08-0935-EL-SSO

Greetings:

Material Sciences Corporation files its Reply Brief in the above proceeding via fax on December 12, 2008. Docketing will receive for filing the original and necessary copies of the Reply Brief on December 15, 2008, the next business day.

Regards

Craig I. Smith

Craig I. Smith
Attorney for Material Sciences Corporation

BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of the Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company, for Authority to Establish a Standard Service Offer Pursuant to R.C. § 4928.143 in the Form of an Electric Security Plan	))))	Case No. 08-0935-EL-SSO

REPLY BRIEF BY MATERIAL SCIENCES CORPORATION

Craig I. Smith (0019207)
Attorney at Law
2824 Coventry Road
Cleveland, Ohio 44120
216-561-9410
wis29 @ yahoo.com
Attorney for Material Sciences Corporation

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I. INTRODUCTION

Material Sciences Corporation files its reply in support of its position the Electric Security Plan requires substantial modifications before approval, or rejection.

II. REPLY AND ARGUMENT

1. RC 4928.143 (C) (1) requires broad scope Commission review.

The Companies[1] contend SB 221 "radically" creates a new process for Standard Service Offer ("SSO") services. The Electric Security Plan ("ESP") mechanism, according to the Companies, offers customers electric generation, and other features or benefits without regard to RC Chapter 49. [2]

The Companies argue SB 221 requires narrow Commission adjudication because service costs no longer set rates, and, subject to constitutional protections, allows for ESP approval based on "whether the proposed ESP is more favorable, in the aggregate, than the expected results from a Market Rate Offer ("MRO")." [3] Commission review should exclude potential impacts of the plan on the Companies, other than looking backward for excessive earnings long after ESP approval, according to the Companies. [4]

The Companies caution the regulatory "paradigm" of SB 221 "*cannot require* [them] to accept a *different* ESP than the one proposed" (emphasis in quoted language).[5] Commission rejection to make a better ESP plan, or to address "parochial interests" of intervenors, could result in a SSO set at market rates.[6]

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[1] Companies refer to collectively Ohio Edison, CEI, and Toledo Edison
[2] Companies Br. pg. 1
[3] Companies Br. pg 1, FN 1, pg. 5-6
[4] Companies Br. pg. 4-5
[5] Companies Br. pg. 4
[6] Companies Br. pg. 4

OEG properly points out that under RC 4928.143(A) and RC 4928.143 (B)(2) (a) the Companies bear the burden of proof to show their ESP provides more favorable results than the MRO, recovers only prudently incurred costs, and meet state policies, including reasonably priced electric service and facilitating Ohio's effectiveness in the global economy.[7]

The Commission Staff believes SB 221 "contemplates" more than comparing ESP and MRO prices since Commission approval must effectuate state energy policies and further other Chapter 4928 goals.[8]

State policies guide the Commission in approving the Companies' ESP to ensure adequate, reliable, safe, efficient, nondiscriminatory, and reasonably priced retail electric service; [9] supplier, price, terms, conditions, and quality options for consumers to meet their needs; [10] consumers effective choices of suppliers; [11] encourage innovation and cost-effective supply and demand-side service; [12] promote effective customer choice through access to information on delivery system operations; [13] require flexible regulatory treatment to develop further competitive electric markets;[14] and, finally, facilitate Ohio's effectiveness in the global economy. [15] The Commission effectuated these polices through rule making as needed.[16]

The Companies' ESP may include other terms, conditions or charges as well to stabilize or provide more certain service that relate to limiting customer shopping,

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7 OEG Br., pg. 1-2
8 Staff Br., pg. 6
9 RC 4928.02 (A)
10 RC 4928.02 (B)
11 RC 4928.02 (C)
12 RC 4928.02 (D)
13 RC 4928.02 (E)
14 RC 4928.02 (G)
15 RC 4928.02 (N)
16 RC 4928.06 (A)

bypassable charges, standby, back-up, or supplemental power, default service, carrying costs, cost amortization, deferred and future recovery of deferred costs to stabilize or provide more certain service.[17] The SSO price may automatically increase or decrease under the ESP.[18] The ESP may provide for securitization of phase-in, deferrals. [19] The ESP may recover service costs incurred to provide the SSO relating to transmission, ancillary, congestion, or any related service.[20] The ESP may provide for single issue ratemaking, revenue decoupling, or other incentive ratemaking to modernize and make more reliable their delivery infrastructure. [21] Finally, the ESP may implement economic development, job retention, and energy efficiency programs, while allocating program costs among each of them.[22]

The scope of review expressed by the Companies unreasonably and unlawfully restricts the Commission's authority under SB 221 to approve, or modify and approve, the ESP application upon finding the plan *as approved* in the aggregate is more favorable than expected MRO results. [23] The remedies available for a Commission modified and approved ESP include termination of that plan through withdrawal, and filing a new plan or a MRO, by the Companies. [24] If terminated by withdrawal, the Companies most recent SSO continues, subject to increases or decreases in fuel costs, until ESP or MRO approvals occur.[25]

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[17] RC 4928.143 (B) (2) (d)
[18] RC 4928.143 (B) (2) (e)
[19] RC 4928.143 (B) (2) (f)
[20] RC 4928.143 (B) (2) (g)
[21] RC 4928.143 (B) (2) (h)
[22] RC 4928.143 (B) (2) (i)
[23] RC 4928.143 (C) (1)
[24] RC 4928.143 (C) (2) (a)
[25] RC 4928.143 (C) (2) (b)

The Companies' burden of proof requires showing reasonable and lawful proposals for all provisions within their ESP consistent with RC Chapter 4928 and Commission enacted rules.[26] Beyond comparing ESP and MRO price offerings, the Commission appropriately considers and balances "the competing interests of various stakeholders, a process which requires knowledge and understanding of the possible effects of decisions on various parties" in approving, modifying and approving, or rejecting the Companies' ESP.[27]

The Companies fail to meet its burden of proof that the filed ESP in the aggregate is more favorable than expected market based rates. The ESP requires substantial modification before approval, or rejection.

2. The ESP as proposed is less favorable than MRO expected results

A. The Companies overstate the costs of MRO default services

The Companies argue on a net present value basis the filed ESP is more favorable by at least $1.3 billion when compared to the expected results of a MRO.[28] The Companies overstated the expected MRO costs for default services. The Companies further support their positions by reference to Staff Witness Johnson's far lower $200 million net present value benefit to customers of the ESP over the expected MRO.[29] TE customers allegedly save $26.97 million, CEI customers $110.25 million, and OE

[26] See Case No. 08-777-EL-ORD, Finding and Order, dated September 17, 2008, subject to rehearing.
[27] Finding and Order, Case No. 08-777-EL-ORD, dated September 17, 2008, pg. 4-5, expressed in different context
[28] Companies Br., pg. 14-15
[29] Companies Br. pg. 15

customers $62.97 million over the three-year plan based on Mr. Johnson's determination. [30]

The Staff inappropriately concludes the Companies' ESP could meet a minimal approval test, but strongly argues that test alone becomes insufficient for Commission approval without modifications because SB 221 "contemplates" more than "a price on price" comparison." [31]

Indeed, the record supports Michael Schnitzer[32] recommended rejection of the ESP because the Companies rely on higher, outdated prices, and materially flawed quantitative comparisons to determine expected MRO results. Updated market conditions, and corrected comparison flaws completely eliminates the Companies' claimed ESP benefits in the aggregate. [33] The cumulative effect of all properly made adjustments reduces the ESP claimed benefits from $1,303.4 million to ($246.0) million.[34] An unbiased "apples to apples" comparison using FES[35] assumed risks under the ESP further reduces MRO costs annually by $22[illegible] million. This further reduction shows the claimed benefits of the ESP is ($841.9) million when compared to the MRO option.[36]

The record further supports Lane Kollen conclusion the ESP failed to meet the statutory test for approval. The ESP is more expensive by $1,692.6 million[37] using MRO prices of $63.45/MWh, $65.23/MWh, and $66.15/MWh during 2009, 2010, and 2011,

30 Derived from Companies Br. 15
31 Staff Brief, pg. 6
32 Testified for Constellation New Energy, Inc., and Constellation Energy Commodities Group, Inc.
33 Schnitzer Test., Competitive Supplier Ex. 2, pg. 32-34.
34 Schnitzer Test., Competitive Supplier Ex. 2, pg. 28-29, Table 4
35 FES means FirstEnergy Solutions, the affiliate generation supplier
36 Schnitzer Test., Competitive Supplier Ex. 2, pg. 29-32, Table 5
37 Kollen Test., OEG Ex. 2, pg. 3

determined after grossing up the transmission component for line losses, [38] using September 19, 2008 forward wholesale market prices, [39] and removing retail market premiums. [40]

The record also supports Stephen Baron finding that ESP charges resulted from unreasonably negotiated generation rates. POLR services obtained through RFP solicitations fully compensate the Companies for assuming the retail shopping risks without marked up retail prices. [41] The ESP marks up retail prices by 17% to 40% over wholesale generation prices to outsource those POLR risks to FES. [42] Companies' witness Jones estimates the retail margins paid by customers above wholesale market generation costs nearly $4 billion, or $22.86/MWh. [43]

The Companies speculate that increased risks of economic uncertainties offset the documented steep reductions in commodity prices since July 15, 2008. [44] The Companies further argue only use of July 15, 2008 forward prices contemporaneously compare all the terms and conditions of the ESP with expected results of the MRO. [45] Both positions undercut rather than support the findings presented by Companies' expert witnesses Dr. Jones and Mr. Graves, as adopted by Mr. Blank, to conclude the ESP is more favorable than an expected MRO. The Companies failed to present a record upon which the Commission may approve the ESP without significantly modified generation prices to accurately reflect expected economic and wholesale market conditions. Otherwise, the Commission should reject the ESP.

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[38] Kollen Test., OEG Ex. 2, pg. 8
[39] Kollen Test., OEG Ex. 2, pg. 11; Ex. 2 A update prices for October 10, 2008
[40] Kollen Test., OEG Ex. 2, pg. 12-13
[41] Baron Test., OEG Ex. 1, pg. 8
[42] Baron Test., OEG Ex. 1, pg. 9
[43] Baron Test., OEG Ex. 1, pg. 10
[44] Companies Br., pg. 16-20
[45] Companies Br., pg. 17

B. The Companies overstate Rider GEN rates, and use Rider GPI to create deferred generation costs recovered under Rider DGC far in excess of benefits received by customers.

The Staff describes the generation rate offers and phase-in deferrals as the core of the ESP Plan. [46] MRO prices properly derived are \$63.45/MWh, \$65.23/MWh, and \$66.15/MWh during 2009, 2010, and 2011.[47] ESP average base generation prices are in 2009: \$75.00/MWH with a phased-in price of \$67.50/MWH; in 2010: \$80.00/MWH with a phased-in price of \$71.50/MWH; and in 2011: \$85.00 with a phased-in price of \$75.50/MWH. Generation charges and phase-in credits are seasonally and voltage adjusted. [48]

The Companies propose recovering deferred amounts, not securitized, existing on December 31, 2010 under a non-bypassable DGC charge beginning January 1, 2011 set initially at an average rate of \$0.002009 per kWh, as subsequently adjusted. The average rider rate becomes \$0.003252 per kWh, as subsequently adjusted, to recover deferred accumulated balances as of December 31, 2012 starting January 1, 2013. [49]

The Staff correctly opposes creation of new generation-related deferrals that shift recovery far out to future periods. [50]

Staff recommends charging for generation at the lower phased-in generation discount rates with a mechanism to true up costs with a cap and floor on recovery.[51]

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[46] Staff Br., pg. 6
[47] Kollen Test., OEG Ex. 2, pg. 8, 11-13, Ex. A
[48] ESP App., Company Ex. 9A, pg 10
[49] ESP App., Company Ex. 9A, pg. 12
[50] Staff Br., pg. 6
[51] Staff Br., pg. 6

However, the Staff unreasonably sets Rider GEN prices (Rider GEN with the Rider GPI adjustments) at rates higher rates than expected MRO based on the record evidence.[52]

For example, TE industrial customers pay these phase-in generation prices during the plan's three-year term:

	2009 $/MWH		2010 $/MWH		2011 $/MWH	
MRO[53]	$63.35/MWH		$65.33/MWH		$66.15/MWH	
Rider GEN-Rider GPI[54]	Summer	Winter	Summer	Winter	Summer	Winter
GP	$74.484	$63.831	$78.898	$67.614	$83.312	$71.396
GSU	$72.386	$62.033	$76.676	$65.709	$80.965	$69.385
GT	$72.318	$61.975	$76.603	$65.648	$80.889	$69.321

The summer rates far exceed the expected MRO rates. Interestingly, the ESP winter rates closely approximate the expected MRO rates for 2009, but by 2011 also exceed the MRO rates expected.

Staff use of phase-in generation rates as proposed unreasonably charge customers. The Commission needs to further lower those generation rates before approving the Staff's proposal.

C. The ESP recovers unlawful and not prudently incurred costs under the FTE, FCA, and CCA riders.

[52] Staff Br., pg. 6
[53] Kollen Test., OEG Ex. 2, pg. 8, 11-13, Ex. A
[54] TE Rider GPI, Sheet 87, Rider GEN, Schedules 3a, 3b, and 3c

Riders FTE and FCA without record support assume that FES incurs 100% of those costs at plants dedicated to support ESP services.[55] Rider CCA implicitly assumes FES incurs costs of additional capacity purchases solely to serve SSO customers under the ESP.[56]

The riders recover different costs. Rider FTE increases ESP generation rates for SSO service only when FES' fuel transportation surcharges and environmental costs exceed $110 million over the three year plan period.[57] Fuel transportation surcharges total $60 million. The remaining $50 million applies to costs resulting from new or newly interpreted environmental laws or new taxes applying to FES after January 1, 2008.[58]

The FCA Rider recovers incremental fuel costs during 2011 that exceed 2010 levels.[59] Rider GEN includes fuel costs for 2009 and 2010.[60]

Rider CCA recovers the costs to meet MISO's planning reserve requirements between May through September beyond the committed to 1,000 MW capacity commitment during 2007-2011.[61]

The Staff correctly recommends rejection of Rider FCA because of uncertain scope and failure to receive forecasted fuel costs for 2011.[62]

The Staff also correctly recommends rejection of the FT (fuel transportation) portion of the FTE Rider for failure to receive supporting data.[63]

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[55] TE Schedule 3a, Sheet 110 (FTE), Sheet 115 (FCA)
[56] Companies Br., pg. 30-31, TE Schedule 4c, Sheet 111
[57] Companies Br., pg. 27-29
[58] Companies Br., pg. 27-29
[59] Companies Br., pg. 29-30
[60] Companies Br, pg. 29-30
[61] Companies Br, pg. 30-31
[62] Staff Br., pg. 19-20

RC 4928.143 provides for recovery of the Companies' incurred fuel costs to generate electricity, purchase power costs to purchase capacity and energy from suppliers, including affiliates, or CWIP related costs incurred for new generation or environmental expenditures of existing generation.[64]

Riders FTE, FCA and CCA recover specific costs incurred by FES to supply SSO generation under the ESP not allowed for under RC 4928.143. The Companies do not own generation that supplies electricity under the ESP

Further, the Companies fail to show the prudent nature of their decisions to agree to the terms of Riders FTE, FCA and CCA. FES may bill all rider FTE and FCA costs whether or not actually incurred at those generation plants dedicated to serve SSO customers under the ESP. Likewise the Companies imprudently agreed for FES to recover under Rider CCA its total costs for needed capacity purchases whether or not incurred as part of serving SSO customers under the ESP to meet additional MISO requirements during summer months.

Commission total rejection of Riders FTE, FCA and CCA is necessary as part of a modified and approved ESP.

III. Conclusion

SB 221 provides the Commission with broad discretion under RC 4928.143 to modify and approve, or reject, the ESP proposed by the Companies in the public interest to further state policies codified into law by the legislature. The result must be reasonably and fairly priced electric service under the ESP given expected future energy

[63] Staff Br., pg. 20-21
[64] RC 4928.143 (B) (1) (2)

market prices and economic conditions facing Ohio over the next three years. The ESP plan proposal based on July 15, 2008 market prices fall far short of meeting the required public interest.

Respectfully submitted

Craig I. Smith (0019207)
Attorney at Law
2824 Coventry Road
Cleveland, Ohio 44120
216-561-9410
wis29 @ yahoo.com
Attorney for Material Sciences Corporation

Certificate of Service

I hereby certify serving by electronic mail this initial brief on December 12, 2008 upon the listed persons and parties.

Craig I. Smith

James Burk
Mark Hayden
FirstEnergy Corporation
burkj@firstenergycorp.com
haydenm@firstenergycorp.com

David A. Kutik
Andrew J. Campbell
Jones Day
ajcampbell@jonesday.com
dakutik@jonesday.com

Sammel C. Randazzo
Lisa G. McAlister
McNees, Wallace & Nurick
sam@mwncmh.com
lmcalister@mwncmh.com

Leslie A. Kovacik
City of Toledo
Leslie.kovacik@toledo.oh.gov

Sheilah M. McAdams
Marsh & McAdams
Sheilahmca.aol.com

Paul S. Goldberg
City of Oregon
pgoldber@ci.oregon.oh.us

Paul Skaff
Perrysburg, Ohio
paulskaff@justice.com

Langdon D. Bell
Barth Royer
Bell & Royer Co., LPA
lbell@aol.com
barthroyer@aol.com

David Rinebolt
Ohio Partners for Afforded Energy
drinebolt@aol.com

Jeffrey L. Small
Jacqueline Roberts
Richard C. Reese
Gregory J. Poulos
Consumers' Counsel
small@occ.state.oh.us
Roberts@occ.state.oh.us
Roberts@occ.state.oh.us
Poulos@occ.state.oh.us

David F. Boehm
Michael L. Kurtz
Boehm, Kurtz & Lowry
dboehm@bkllawfirm.com
mkurtz @bkllawfirm.com

Gary A. Jeffries
Dominion Resources Services, Inc.
Gary.a.jeffries@dom.com

David L. Fein
Cynthia A. Fonner
Constellation Energy Group, Inc.
David.fein@constellation.com
Cynthia.a.fonner@constellation.com

John W. Bentine
Mark S. Yurick
Chester, Wilcox & Saxbe
myurick@cwslaw.com
jbentine@cwslaw.com

M. Howard Petri off
Stephen M. Howard
Vorys, Sater, Seymour and Pease LLP
mhpetricoff@vssp.com
smhoward@vssp.com

Henry Eckart, Esq.
henryeckhart@aol.com

Lance M. Keiffer
Toledo, Ohio
lkeiffer@co.lucas.oh.us

Brian J. Ballenger
Ballenger & Moore
ballengerlawbjb@sbcglobal.net

James E. Moan
Sylvania, Ohio
jimoan@hotmail.com

Thomas R. Hays
Sylvania, Ohio
hayslaw@buckeye-express.com

Steve Millard
Council on Small Enterprises
smillard@cosc.org

Damon E. Xenopoulos, Esq.
Garrett A. Stone
Michael K. Lavanga
Brickfield, Burchette, Ritts & Stone, P.C.
dex@bbrslaw.com
gas@bbrslaw.com
mkl@bbrslaw.com

Joseph P. Meissner
The Legal Aid Society of Cleveland
jpmeissn@lasclev.org

Sean W. Vollman
David A. Muntean
City of Akron
vollmse@ci.akron.oh.us
menteda@ci.akron.oh.us

F. Mitchell Dutton
FPL Energy Power Marketing, Inc.
Mitch.dutton@fpl.com

George H. Dunn
Schottenstein ZOX & Dunnco., LPA
gdunn@szd.com

Larry Gearhardt
Ohio Farm Bureau Federation
LGearhardt@ofbf.org

Craig G. Goodman
National Energy Marketers Assoc.
cgoodman@energymarketers.com

Nolan Moser
Trent A. Dougherty
Air & Energy Program Manager
nlan@theoec.org
trent@theoec.org

Dane Stinson
Bailey Cavalieri
Dane.stinson@baileycavalieri.com

James F. Lang
Laura McBride
Trevor Alexander
Calfee, Halter & Griswold
jlang@calfe.com
talexander@calfee.com
lmcbride@calfee.com

Theodore S. Robinson
Citizen Power
robinson@citizenpower.com

Richard Sites
Ohio Hospital Association
ricks@ohanet.org

Glenn Krassen
E Brett Breitschwerdt
Sally Bloomfield
Terrence O'Donnell
Bricker & Eckler
gkrassen@bricker.com
ebreitschwerdt@bricker.com
sbloomfield@bricker.com
todonnell@bricker.com

Nicholas C. York
Eric D. Weldele
Tucker Ellis & West
Nicholas.york@tuckerellis.com
Eric.weldele@tuckerellis.com

Robert J. Triozzi
Steven L. Beeler
City of Cleveland
sbeeler@city.cleveland.oh.us