

**BEFORE THE  
THE PUBLIC UTILITIES COMMISSION OF OHIO**

In the Matter of the Application of Ohio Power Company and Columbus Southern Power Company for Authority to Merge and Related Approvals	) ) ) )	Case No. 10-2376-EL-UNC
In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Authority to Establish a Standard Service Offer Pursuant to §4928.143, Ohio Revs. Code, in the Form of an Electric Security Plan.	) ) ) ) ) )	Case No. 11-346-EL-SSO Case No. 11-348-EL-SSO
In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of Certain Accounting Authority	) ) ) )	Case No. 11-349-EL-AAM Case No. 11-350-EL-AAM
In the Matter of the Application of Columbus Southern Power Company to Amend its Emergency Curtailment Service Riders	) ) ) )	Case No. 10-343-EL-ATA
In the Matter of the Application of Ohio Power Company to Amend its Emergency Curtailment Service Riders	) ) ) )	Case No. 10-344-EL-ATA
In the Matter of the Commission Review of the Capacity Charges of Ohio Power Company and Columbus Southern Power Company.	) ) ) )	Case No. 10-2929-EL-UNC
In the Matter of the Application of Columbus Southern Power Company for Approval of a Mechanism to Recover Deferred Fuel Costs Ordered Under Ohio Revised Code 4928.144	) ) ) ) )	Case No. 11-4920-EL-RDR
In the Matter of the Application of Ohio Power Company for Approval of a Mechanism to Recover Deferred Fuel Costs Ordered Under Ohio Revised Code 4928.144	) ) ) ) )	Case No. 11-4921-EL-RDR

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**REPLY BRIEF OF FIRSTENERGY SOLUTIONS CORP.**

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## **I. INTRODUCTION**

The Signatory Parties want the Commission to believe that it has a stark choice: approve an electric security plan for AEP Ohio which includes massive overcharges to SSO customers for generation service between January 1, 2012 and May 31, 2015, or be burdened with the uncertainty of litigation in multiple cases for the foreseeable future and potentially lose the alleged benefit of the conditional promise to transition to market-based SSO pricing starting June 1, 2015. This is nothing more than AEP Ohio's attempt to strong-arm the Commission into accepting a bad deal for retail customers and competitive markets. FES respectfully suggests that the Commission should reject the Partial Stipulation and exercise the Commission's existing authority to provide the best opportunity for customers to take advantage of the savings available in the competitive market. Although no one disputes the benefits of competition, the Signatory Parties offer no sound basis for delaying the benefits of market pricing to all retail customers for another three and a half years. They readily admit that SSO customers will pay millions more under the Proposed ESP than they would under an MRO. Indeed, Staff acknowledges that the Proposed ESP will force SSO customers to pay hundreds of millions more to AEP Ohio for generation service than they would under an MRO and, thus, that the Proposed ESP is quantitatively much worse than an MRO. In light of the massive cost burden imposed by the Proposed ESP, the Signatory Parties ask that the Commission accept illusory, contingent "qualitative" benefits as justifications for approval of the Proposed ESP. The Commission's statutory review of the Proposed ESP under R.C. § 4928.143(C) does not allow for such flights of fancy.

The Commission cannot approve a Proposed ESP based on unquantified benefits that may never occur, such as the transition to market-based pricing and the construction of the

Muskingum River 6 (“MR6”) gas unit.<sup>1</sup> The Commission also cannot credit as benefits of the Proposed ESP the “willingness” by AEP Ohio to satisfy Ohio law, such as AEP Ohio’s long-delayed transition to the corporate separation required by R.C. § 4928.17. The Commission also cannot credit as benefits of the Proposed ESP those alleged benefits that, if they do occur, have nothing to do with the Proposed ESP, such as AEP Ohio’s long-standing plan to use less coal and more natural gas or the termination of the AEP East Interconnection Agreement (a/k/a the “Pool Agreement”) that was initiated in December 2010. Finally, the Commission should not credit as a benefit of the Proposed ESP AEP Ohio’s “elimination” of proposals that are unlawful and anti-competitive, such as the many nonbypassable riders included in AEP Ohio’s initial filing and the absurd demand to charge \$355/MW-day to CRES providers in Case No. 10-2929-EL-UNC (the “10-2929 Docket”).

The Commission can provide the certainty and stability sought by the Signatory Parties by issuing three orders that comply with state law and policy and remedy long delayed deficiencies in AEP Ohio’s compliance: (1) an order rejecting the Partial Stipulation and the Proposed ESP in their entirety; (2) an order in the 10-2929 Docket reaffirming that the capacity price charged to CRES providers will track the RPM price<sup>2</sup>; and (3) an order requiring AEP Ohio to complete full corporate separation. As a result of the first order, “the provisions, terms, and conditions of [AEP Ohio’s] most recent standard service offer [would continue], along with any expected increases or decreases in fuel costs from those contained in that offer, until a subsequent offer is authorized pursuant to this section or section 4928.142 of the Revised Code,

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<sup>1</sup> In fact, the MR6 project could actually impose net costs on AEP Ohio’s customers, as the Partial Stipulation allows AEP Ohio to recover the above-market costs of such a facility in a new non-bypassable Generation Resource Rider (“GRR”).

<sup>2</sup> Unless further action is taken by the Commission, Ohio’s state compensation mechanism will remain RPM pricing.

respectively.”<sup>3</sup> This first order would freeze the current ESP in place, with no POLR charges and with only adjustments permitted for fuel costs. It would provide much more certainty to SSO customers than the Proposed ESP, which includes automatic price increases, fuel cost adjustments, arbitrary inter-class subsidies that adjust from year to year, nonbypassable riders with as-yet-undetermined costs, and anti-competitive restrictions on shopping. The second and third orders would position AEP Ohio to provide market-based pricing, which all Signatory Parties, except apparently AEP Ohio, appear to value and the law requires.

This approach is necessary because the Proposed ESP is not more favorable in the aggregate than the expected results of an MRO and the Partial Stipulation violates each prong of the Commission’s three-part test. As set forth below and in FES’ Initial Brief, the Commission’s statutory obligation to reject the Partial Stipulation and Proposed ESP, or at minimum to greatly modify them, is clear.

## **II. THE SIGNATORY PARTIES’ BRIEFS CONFIRM THAT THE PROPOSED ESP WILL COST CUSTOMERS MORE THAN AN MRO.**

### **A. All Parties Agree That SSO Customers Will Pay More Under The Proposed ESP Than They Would Under An MRO, And Reasonable Estimates Show That It Will Increase Costs By \$325 To \$800 Million.**

If the Commission approves the Proposed ESP as filed, SSO customers will pay hundreds of millions of dollars more for service than they would under an MRO between January 1, 2012 and May 31, 2015. The fact that SSO customers will pay more is undisputed. Staff agrees that the Proposed ESP “would, on a strictly quantitative basis, fail the aggregate test for each year of the plan.”<sup>4</sup> AEP Ohio states that the Proposed ESP will cost SSO customers at least \$108 million

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<sup>3</sup> R.C. § 4928.143(C)(2)(b).

<sup>4</sup> Post-Hearing Brief Submitted On Behalf Of The Staff Of The Public Utilities Commission Of Ohio (“Staff Brief”), p. 20.



more than an MRO on a net present value basis.<sup>5</sup> RESA also acknowledges that all analyses show the projected MRO price is more favorable than the Proposed ESP price.<sup>6</sup> Exelon and Constellation did not waste any time arguing the point.<sup>7</sup> IEU and OCC concur that SSO customers will pay hundreds of millions more to AEP Ohio for retail electric service than they would under an MRO.<sup>8</sup>

The only difference of opinion between the witnesses is over how much more SSO customers will be forced to pay to AEP Ohio under the Proposed ESP. The estimates are so unfavorable for AEP Ohio that its brief discussion of the required threshold issue that the ESP be more favorable than the expected results of an MRO is buried at pages 137-143 of its initial brief. AEP Ohio's low-ball calculation of the added cost the Proposed ESP will impose on SSO customers is \$108 million.<sup>9</sup> All other projections, including Staff's, agree that SSO customers will overpay for AEP Ohio's generation by at least \$325 million and perhaps more than \$1 billion.<sup>10</sup> Thus, "AEP Ohio the EDU" is proposing that SSO customers overpay "AEP Ohio the

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<sup>5</sup> Joint Initial Brief Of The Undersigned Signatory Parties ("AEP Ohio Brief"), p. 138.

<sup>6</sup> Retail Energy Supply Association's Post-Hearing Brief In Support Of The Stipulated Electric Security Plan Provided In The Stipulation And Recommendation Filed September 7, 2011 ("RESA Brief"), pp. 18-19.

<sup>7</sup> See generally Exelon Generation Company, LLC's Initial Post-Hearing Brief In Support Of The Stipulated Electric Security Plan Provided In The Stipulation And Recommendation Filed September 7, 2011 ("Exelon Brief"); Initial Trial Brief Constellation Newenergy, Inc. And Constellation Energy Commodities Group, Inc. ("Constellation Brief"), p. 6 ("Constellation has not conducted an analysis of the Stipulation as compared to an MRO . . .").

<sup>8</sup> Initial Post-Hearing Brief By The Office Of The Ohio Consumers' Counsel, The Appalachian Peace And Justice Network, And Ohio Partners For Affordable Energy ("OCC Brief"), pp. 33-34; Initial Brief Of Industrial Energy Users-Ohio ("IEU Brief"), pp. 19-21.

<sup>9</sup> Direct Testimony of William A. Allen on behalf of Columbus Southern Power Company and Ohio Power Company, AEP Ex. 4 ("Allen Direct"), Exhibit WAA-6.

<sup>10</sup> Post-Hearing Brief Of FirstEnergy Solutions Corp. ("FES Brief"), pp. 11-13, 16-21 (using Staff witness Johnson's market prices and Staff witness Fortney's methodology); IEU Brief, pp. 19-21.

generation company” for generation service by hundreds of millions of dollars. All that AEP Ohio offers in return is the false promise of “certainty.”

Parts of Staff’s Brief appear to have been written prior to the hearing and the Remand Order, as it erroneously claims an ESP price benefit of \$130 million for SSO customers.<sup>11</sup> Staff may have mistakenly believed at the time it agreed to sign the Partial Stipulation that SSO customers would see a benefit. However, this belief is not supported by the record and, most importantly, by Staff itself, which corrects this mistake later in its brief by admitting that the Proposed ESP fails quantitatively in every year.<sup>12</sup> As revealed on cross-examination of Mr. Fortney and Mr. Johnson, Staff’s calculation results in a substantial MRO price benefit to SSO customers of at least \$325 million, which is consistent with the low end of FES witness Schnitzer’s calculations (\$350 million).<sup>13</sup>

Because the witnesses’ calculations showing the high cost of the Proposed ESP disagree on exactly how high the cost is, RESA suggests that these estimates should be discounted as “too imprecise and uncertain to be conclusive.”<sup>14</sup> However, there is no uncertainty regarding whether the ESP price is higher than the MRO price. All of the witnesses, representing “multiple methodologies,” found the ESP price to be higher.<sup>15</sup> That is beyond conclusive; it is definitive. The Commission must give great weight to the fact that SSO customers will overpay for SSO service starting on January 1, 2012 if the Commission approves the Proposed ESP.

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<sup>11</sup> Staff Brief, p. 6.

<sup>12</sup> Staff Brief, p. 20, citing Staff witness Fortney’s testimony on cross-examination. *See* Tr. Vol. X, p. 1714.

<sup>13</sup> Tr. Vol. X, pp. 1695-1697; Testimony of Michael A. Schnitzer on behalf of FirstEnergy Solutions Corp., FES Exs. 3 and 4 (“Schnitzer Direct”), p. 28; FES Brief, pp. 12, 17-19.

<sup>14</sup> RESA Brief, p. 19.

<sup>15</sup> *See* RESA Brief, p. 19.

Moreover, RESA proposes a fool's errand, which is to give equal weight to the calculations performed by FES, Staff and AEP Ohio. FES' calculation takes into account all costs of the Proposed ESP. Staff's takes into account a number of the costs of the Proposed ESP. AEP Ohio's calculation ignores most costs of the Proposed ESP. The variation in results is thus easily explained by the quality and thoroughness of the work performed. The Commission can and should give most weight to the work performed by FES witness Schnitzer, as it is the most credible, fair and definitive and is supported by Mr. Fortney's calculation, when properly adjusted.

**B. AEP Ohio's Views On Its "MRO Price Test" Are Defective And Internally Contradictory, And Most Notably, Fail To Use A Competitive Price For Capacity In An MRO As Required by S.B. 221.**

AEP Ohio introduces its discussion of the MRO Price Test by stating that two prices must be estimated to determine the expected results of an MRO – a Competitive Benchmark Price and a generation SSO price.<sup>16</sup> AEP Ohio then explains that the Competitive Benchmark Price "is based on market data and includes the items that would be included by a supplier providing retail electric service to AEP Ohio customers. . . . The generation SSO price is a function of generation pricing from the Company's 2009-2011 ESP adjusted for certain generation related items."<sup>17</sup> AEP Ohio then devotes three pages of its brief to describing how AEP Ohio witness Thomas used a Competitive Benchmark Price that was not based on market data and a generation SSO price that was not adjusted for generation-related items.<sup>18</sup> As

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<sup>16</sup> AEP Ohio Brief, p. 139.

<sup>17</sup> *Id.* (internal citation omitted).

<sup>18</sup> *Id.*, pp. 140-42.

discussed in FES' Brief, AEP Ohio overstated the Competitive Benchmark Price and understated the generation SSO price (aka, the Legacy ESP Total Generation Service Price).<sup>19</sup>

Specifically, Ms. Thomas' calculation of a Competitive Benchmark Price includes capacity pricing that is not market-based. AEP Ohio does not explain why she ignored her own testimony and used capacity pricing that exists only on the pages of the Partial Stipulation.<sup>20</sup> As described by AEP Ohio, Ms. Thomas used two "capacity scenarios" drawn from Paragraph IV.2.b.1 of the Stipulation to create an Expected Bid Price weighted based on the Partial Stipulation's shopping caps.<sup>21</sup> By definition, a capacity price established in an ESP stipulation could never be the market-based capacity price used to price an MRO. If AEP Ohio prices its SSO load using an MRO, the price of capacity included in the market price should be based on market values and not some "made up" figure included in a negotiated, but unimplemented, partial settlement.

AEP Ohio implicitly recognizes the weakness in Ms. Thomas' invented capacity price when it states that the "Stipulation's capacity pricing, once adopted by the Commission, will establish the appropriate charges for use of AEP Ohio's capacity" for CRES suppliers and wholesale suppliers.<sup>22</sup> Thus, AEP Ohio recognizes that Ms. Thomas' Competitive Benchmark Price for the MRO depends upon the Commission adopting the Partial Stipulation. The converse is also true: if the Commission rejects the Partial Stipulation and AEP Ohio proceeds with an MRO, the Stipulation's capacity pricing will be completely irrelevant. As FES witness Schnitzer pointed out, the purpose of the ESP vs. MRO test is to compare two worlds: one with the Partial

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<sup>19</sup> FES Brief, pp. 37-41.

<sup>20</sup> See AEP Ohio Brief, p. 141; Direct Testimony of Laura J. Thomas on behalf of Columbus Southern Power Company and Ohio Power Company, AEP Ex. 5 ("Thomas Direct"), p. 4.

<sup>21</sup> AEP Ohio Brief, p. 141.

<sup>22</sup> AEP Ohio Brief, p. 151 (emphasis added).

Stipulation and the Proposed ESP and one without the Partial Stipulation and with an MRO.<sup>23</sup> Ms. Thomas combines these two worlds into a bizarre mishmash that lacks any relation to reality. Even after doing so, her ESP vs. MRO price test still comes out with the Proposed ESP as the loser.

Moreover, AEP never explains why a price for CRES providers that would result from the 10-2929 Docket would automatically apply to wholesale suppliers under an MRO. As FES pointed out in its initial brief, S.B. 221 requires the use of a competitive price for capacity in an MRO.<sup>24</sup> Otherwise, an MRO is not a Market Rate Offer. Under R.C. § 4928.142(C)(3), an MRO must include competitive market-based pricing for both energy and capacity procured for SSO supply.<sup>25</sup> As RESA explains, under an MRO, “rather than being based on the cost of service using the electric distribution utilities dedicated generation facilities, the competitive services were to be priced at market.”<sup>26</sup>

**C. None Of The Signatory Parties Provided A Reasonable Basis On Which To Exclude The Cost Of All Riders And AEP Ohio’s Most Recent Fuel Forecast From The Calculation Of The Proposed ESP Price.**

RESA attempts to cast doubt on Mr. Schnitzer’s calculations by describing them as “inherently speculations about future events.”<sup>27</sup> Of course, this is inherent in the statutory test itself, which requires that the Commission make a specific finding that the Proposed ESP, “including its pricing and all other terms and conditions, including any deferrals and any future recovery of deferrals, is more favorable in the aggregate as compared to the expected results that

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<sup>23</sup> Schnitzer Direct, pp. 10-11, 21-22.

<sup>24</sup> FES Brief, pp. 9-11.

<sup>25</sup> *Id.*

<sup>26</sup> RESA Brief, p. 21.

<sup>27</sup> *Id.*, p. 18.

would otherwise apply” if AEP Ohio implemented an MRO.<sup>28</sup> For the Commission to make this finding, it necessarily must make reasonable assumptions regarding what the costs will be of the Proposed ESP, including a reasonable estimate of all variable or undefined costs. The Commission also must make reasonable assumptions regarding what the expected result of an MRO would be. The Commission cannot abdicate this responsibility simply because RESA thinks it is too hard.

AEP Ohio’s approach is to ignore making any assumptions that are “too hard” unless those assumptions benefit AEP Ohio. For example, AEP Ohio states that “it is simply not possible” to estimate the value of the GRR and the PMR.<sup>29</sup> Of course, if there is any point in having either of these in the Proposed ESP, they must have some value to AEP Ohio and have an expected cost to AEP Ohio’s customers. Otherwise, there would be no point to including them in the Proposed ESP. Indeed, given AEP Ohio’s position to value the GRR and PMR riders at zero cost to customers, AEP Ohio then should not object to the Commission stripping these provisions from the Proposed ESP. While they remain in the Proposed ESP, however, the Commission must make a reasonable estimate of their cost.

AEP Ohio refuses to provide such an estimate, but FES witness Schnitzer does using AEP Ohio’s own forecasts and methodology. As Mr. Schnitzer testified extensively, he pulled together all reasonable assumptions regarding the GRR and PMR. For the GRR, he used AEP Ohio’s own cost estimates for the Turning Point project – which remain consistent with AEP Ohio’s development plans.<sup>30</sup> Staff witness Fortney did the same.<sup>31</sup> In fact, Mr. Fortney was

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<sup>28</sup> R.C. § 4928.143(C).

<sup>29</sup> AEP Ohio Brief, p. 161.

<sup>30</sup> Schnitzer Direct, pp. 12, 18; Tr. Vol. V, pp. 863-64. Mr. Schnitzer did not attempt to assign a cost to the MR6 project because he assumed it will not be in service until after June 1, 2015. Schnitzer Direct, p.

concerned that not including the Turning Point costs in the GRR estimate would result in an underestimate of the potential cost of the Proposed ESP.<sup>32</sup> AEP Ohio never explains why its own revenue requirement for the Turning Point project is not good enough for use in an estimate. AEP Ohio certainly has much to prove to gain Commission approval of Turning Point costs in the GRR. However, for as long as AEP Ohio seeks Commission approval of the GRR as one element of the Proposed ESP, then AEP Ohio should be able to defend the revenue requirement for this rider.

The same holds true for the PMR, which AEP Ohio also fails to defend. For the PMR, Mr. Schnitzer applied the same methodology that AEP previously used to assess the impact of pool termination and used AEP Ohio's own forecasted pool transfer prices.<sup>33</sup> As a result, his projection is that the PMR could result in costs of \$262-\$525 million.<sup>34</sup> On the other hand, AEP Ohio's analysis ignores the issue altogether on the basis that cost recovery is "speculative."<sup>35</sup> The uncertainty is the result of AEP Ohio's proposal, which includes a rider with no limitations and a cost of which it apparently had no idea or understanding until Mr. Schnitzer prepared his analysis. Given that AEP Ohio is unwilling to provide the Commission with a reasonable assumption concerning the cost of including the PMR in the Proposed ESP, Mr. Schnitzer's analysis is the only one available in the record (and is reasonably based on AEP Ohio's own

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12. He also did not assign a cost to the 350 MW of customer-sited projects that AEP Ohio witness Hamrock wants to include in the GRR. Schnitzer Direct, p. 18.

<sup>31</sup> Direct Testimony of Robert B. Fortney on behalf of the Staff of the Public Utilities Commission of Ohio, Staff Ex. 4 ("Fortney Direct"), Att. A; Tr. Vol. X, p. 1694.

<sup>32</sup> Tr. Vol. X, pp. 1694-95.

<sup>33</sup> Schnitzer Direct, p. 19 and fn. 40-41.

<sup>34</sup> Schnitzer Direct, p. 19.

<sup>35</sup> AEP Ohio Brief, p. 160.

methodology). As such, the Commission should reject AEP Ohio's "head-in-the-sand" approach and adopt Mr. Schnitzer's analysis as fair and reasonable.

With regard to AEP Ohio's failure to use its own internal estimates of future fuel costs, AEP Ohio defends its "head-in-the-sand" approach on the twin grounds that estimates are not required and do not matter.<sup>36</sup> On the first point, AEP Ohio points to prior SSO cases in which, according to AEP Ohio, the Commission did not require the use of forecasted data in the ESP vs. MRO test.<sup>37</sup> Yet the Commission's Order in Case No. 08-917-EL-SSO,<sup>38</sup> does not stand for the proposition that projections are not required. To the contrary, the Commission embraced Staff witness Hess's ESP vs. MRO test, which included several projections, including estimated purchased power costs and an annual non-FAC increase, as well as forecasted market prices.<sup>39</sup> AEP Ohio also cites to the Opinion and Order issued in Case No. 08-920-EL-SSO, but that opinion does not address any specific issues relating to fuel forecasts and simply concludes that the stipulated ESP in that proceeding passed the test.

Notably, regardless of AEP Ohio's legal position on whether estimates should be used, estimated figures were, in fact, included in Ms. Thomas' analysis. As discussed in FES' Initial Brief, however, she included estimates initially only for energy prices and then for environmental costs. Both were used for calculating her Competitive Benchmark Price. Thus, she included estimates only when they would help AEP Ohio's case. She then complained, without any apparent sense of irony, that it would be inappropriate to include changes to only

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<sup>36</sup> AEP Ohio Brief, pp. 148-49.

<sup>37</sup> AEP Ohio Brief, p. 148.

<sup>38</sup> AEP Ohio presumably is referencing the Commission's March 18, 2009 Opinion and Order.

<sup>39</sup> March 18, 2009 Order in Case No. 08-917-EL-SSO, at pp. 70, 72 and Staff Exh. 1A.



one factor.<sup>40</sup> Unlike Ms. Thomas, Mr. Schnitzer included all reasonable estimates in his ESP vs. MRO test, using AEP Ohio's own data and methodologies.

Including AEP Ohio's fuel cost estimates on both sides of the ESP vs. MRO test certainly matters, as made obvious by the substantial increase in the cost of the Proposed ESP after fuel costs are added to Mr. Fortney's calculation.<sup>41</sup> Instead of using AEP Ohio's own fuel cost estimates for 2012-14, AEP Ohio argues that Ms. Thomas' "sensitivity analysis" showed that including both increasing fuel and environmental costs would result in an increased ESP price benefit.<sup>42</sup> This is not accurate. Ms. Thomas' sensitivity analysis was designed merely to show how much the fuel costs would have to increase using the average of Mr. Schnitzer's environmental cost numbers to reach the same result that she showed in her direct testimony – results that showed that the ESP was more costly than an MRO by \$0.71/MWh.<sup>43</sup> On cross-examination, she admitted that one only needed a \$4/MWh increase in fuel costs to show that an MRO would cost less than the Proposed ESP.<sup>44</sup> Because AEP Ohio's actual fuel estimates are greater than \$4/MWh on average,<sup>45</sup> their use in the ESP vs. MRO test does not produce the result that Ms. Thomas and AEP Ohio suggests. In fact, as shown by Mr. Schnitzer, it provides the opposite result, *i.e.*, the Proposed ESP is more costly than an MRO. Thus, the Commission

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<sup>40</sup> FES Brief, p. 24.

<sup>41</sup> See FES Brief, p. 19-21.

<sup>42</sup> AEP Ohio Brief, p. 149; see Tr. Vol. XIII, p. 2352 (sensitivity analysis).

<sup>43</sup> Rebuttal Testimony of Laura J. Thomas on behalf of Columbus Southern Power Company and Ohio Power Company, AEP Ex. 23 ("Thomas Rebuttal"), Revised Exhibit LJT-R1; Tr. Vol. XIII, p. 2352-53. AEP Ohio similarly mischaracterizes Ms. Thomas' analysis at page 149 of its Brief when it says, "As shown in her Exhibit LJT-1, fuel costs would have to average more than \$40.25/MWh during the period January 2012-May 2015 to produce an adverse impact on her MRO Price Test." In fact, what that exhibit shows is how much fuel prices would have to increase to produce the same results that she obtained initially, *viz.*, a \$0.71/MWh cost.

<sup>44</sup> Tr. Vol. XIII, p. 2354.

<sup>45</sup> See FES Exh. 5 and Schnitzer Direct, Exh. MMS-4.

should rely upon the fair and reasonable analysis prepared by Mr. Schnitzer to find that the Proposed ESP will result in SSO customers overpaying AEP Ohio for generation service by \$350 to \$800 million.

**III. THERE ARE NO REAL “BENEFITS” OF THE PROPOSED ESP THAT WOULD OVERCOME THE INCREASED COST AND MAKE THE PROPOSED ESP MORE FAVORABLE.**

The Proposed ESP’s undisputed price tag puts the Signatory Parties in an untenable position – explaining how a plan that requires customers to pay more for electric service can possibly be seen as more favorable than a market-based outcome. The Signatory Parties’ responses are, not surprisingly, futile. First, they try to distort the standard for approving the Proposed ESP, but the standard is clearly set forth in the law. Second, they try to dress-up certain of the Proposed ESP’s provisions as benefits, but those provisions include legal requirements and actions that AEP Ohio had already committed to. The remaining provisions include terms that may never occur and that are simply not beneficial. Staff witness Fortney admitted that no one knows whether any of the alleged benefits which he identified as “qualitative benefits” will ever happen.<sup>46</sup> Therefore, the Proposed ESP itself provides no real “benefits,” and certainly no benefits that could overcome the \$325-800 million cost of the Proposed ESP’s SSO pricing.<sup>47</sup>

Moreover, the Signatory Parties’ generic claim that the Proposed ESP benefits customers by providing “certainty” contradicts the terms of the Partial Stipulation and AEP Ohio’s own analysis. By way of example, AEP Ohio throughout this proceeding was unable to forecast the costs associated with the GRR and the PMR during the proposed ESP period. Furthermore, as

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<sup>46</sup> Tr. Vol. X, pp. 1762-1763

<sup>47</sup> See FES Brief, p. 19 (Fortney’s calculation with POLR charge removed and Johnson’s market pricing results in ESP cost of \$325.5 million); Schnitzer Direct, p. 28.

described below, many of the alleged benefits are not certain to occur at all – including the incorporation of wholesale competition, corporate separation, grants to low-income customers and economic development, and unnecessary generation investments. All that is certain is that AEP Ohio customers would pay much less for generation service under an MRO.

**A. The Signatory Parties Cannot Avoid The Significance Of The Proposed ESP's Higher Price By Distorting The Legal Standard.**

The Commission cannot approve the Proposed ESP, with or without modifications, unless the Proposed ESP “so approved, . . . is more favorable in the aggregate as compared to the expected results that would otherwise apply under section 4928.142 of the Revised Code.”<sup>48</sup> However, AEP Ohio and the Signatory Parties attempt to divert the Commission’s attention to a different standard. The most obvious example is the Signatory Parties’ argument that the Proposed ESP is more favorable than AEP Ohio’s initial application for an ESP in this proceeding. For example, Exelon argues: “The question here is whether this Stipulation represents a reasonable compromise.”<sup>49</sup> That is not correct. The question is whether the Proposed ESP is more favorable in the aggregate than the expected results of an MRO. The statutory standard does not change because AEP Ohio filed an initial Application that was different from the current proposal and even more burdensome on SSO customers and competitive markets, nor does the statutory standard change because the current proposal is submitted as a partial stipulation. There are no exceptions to the statutory standard – and for good reason. If the Commission could approve the Proposed ESP because it is better than the original application, this would invite EDUs to submit out-of-this-world, totally unsupported

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<sup>48</sup> R.C. § 4928.143(C)(1).

<sup>49</sup> Exelon Brief, pp. 6, 9 (also concluding that “[t]he compromise embodied in the [Proposed] ESP is substantially better than the ESP proposed in AEP Ohio’s original application”); RESA Brief, p. 5 (“[T]his Stipulation represents a fundamentally different approach to standard service procurement and capacity pricing” from the initial ESP application).

initial proposals to set the bar, so that a settlement that incorporates any improvement over the initial proposal could be approved. That is not the law, nor should it be.

RESA tries to focus the Commission on the statute's requirement that the ESP "in the aggregate" must be better than an MRO.<sup>50</sup> RESA focuses on the word "aggregate" to suggest that, by its use of that word, the General Assembly was inviting the Commission to disregard any quantitative analysis of the Proposed ESP and to rest its decision instead on qualitative factors in analyzing the ESP vs. MRO test.<sup>51</sup> There are two problems with this. First, for this argument to be correct, the Commission would have to determine that the alleged qualitative benefits of the ESP somehow outweigh the quantified cost to customers. That, of course, begs the question as to how to do it. If there is no limit on the Commission's discretion, then the statutory test loses any meaning. If the Commission can just "deem" an ESP better because the Commission says so, how can that be meaningfully challenged or reviewed? It cannot, which is why such an interpretation makes no sense. Second, as applied in this case, the Commission must determine that the qualitative benefits of the Proposed ESP are worth more than the \$325 million – \$800 million cost of the Proposed ESP compared to an MRO sworn to by all credible witnesses. As discussed below, most of the qualitative benefits are not benefits to customers at all or not benefits of the Proposed ESP. Thus, for customers, it cannot be argued that the Proposed ESP is more favorable.

Staff suggests that the Proposed ESP is beneficial simply because it is an ESP, but this is unpersuasive and reflects a misunderstanding of the Commission's statutory obligation in

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<sup>50</sup> RESA Brief, pp. 17-18.

<sup>51</sup> RESA Brief, pp. 17-18; *see also* Staff Brief, p. 20 ("Ultimately, the qualitative benefits make an ESP better than an MRO in the aggregate.").

reviewing the Proposed ESP.<sup>52</sup> Staff not only ignores the statutory test, but is also setting up the false choice that, if the Commission rejects the Partial Stipulation, AEP Ohio's customers will be exposed to the allegedly undue risks of an MRO. That is not true. There is a difference between the ESP vs. MRO test that the Proposed ESP must (but does not) satisfy, and what happens next for AEP Ohio's customers. The Commission's decision here is not: (1) the Proposed ESP's higher prices starting in 2012 or (2) an MRO starting in 2012. The Commission has the authority to seek modifications to the Proposed ESP. AEP Ohio then has the ability to accept those modifications or withdraw its application.<sup>53</sup> If AEP Ohio withdraws the application, or if the Commission rejects the Proposed ESP, AEP Ohio's customers do not automatically receive the benefits of MRO pricing. Rather, AEP Ohio's current ESP will continue with adjustments for increases or decreases in fuel costs "until a subsequent offer is authorized pursuant to this [ESP] section or section 4928.142 of the Revised Code, respectively"<sup>54</sup> – which AEP Ohio has already assured investors is "not a bad news story for [AEP Ohio] at all."<sup>55</sup>

Staff's unsupported belief that a market-based MRO is something to fear is also inconsistent with Staff's testimony regarding the benefits of competitive markets.<sup>56</sup> For example, Staff argues that the (overly long) transition to market and corporate separation are

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<sup>52</sup> See Staff Brief, p. 8.

<sup>53</sup> See R.C. § 4928.143(C)(2).

<sup>54</sup> R.C. § 4928.143(C)(2)(b). RESA makes a related, confusing suggestion that AEP Ohio has the option to offer generation service "under an ESP-priced SSO based on its existing rates, which in the case of AEP Ohio is legacy generation, plus adjustments for fuel, transmission, and new generation investments including construction work in progress rather than a competitive market." RESA Brief, p. 12. While AEP Ohio has discretion to propose whatever it wants in an ESP application, subject to the limitations of R.C. § 4928.143(B), no such proposal is on the table and that is not what would be in place if the Proposed ESP is rejected.

<sup>55</sup> Direct Testimony of Tony C. Banks on behalf of FirstEnergy Solutions Corp., FES Ex. 1 ("Banks Direct"), p. 10-11 (quoting AEP Ohio CEO Mike Morris in a July 2011 investor earnings call).

<sup>56</sup> See Staff Brief, p. 8.

benefits of the Proposed ESP, once achieved.<sup>57</sup> If Staff truly believed that exposing customers to the market is some kind of a “threat,” Staff could not argue – as it does – that a transition to “full market pricing for generation service” is a “benefit” of the Proposed ESP.<sup>58</sup>

Further, Staff’s argument that “[e]ven if some of these attributes [of the Proposed ESP] could have been done separately, achieving them in one group is advantageous by enhancing the perception of stability in the state” is even less persuasive.<sup>59</sup> The record evidence and common sense counsel that the state will benefit most from lower electricity prices that are promoted by an effective competitive market.<sup>60</sup> Rather than living under a “perception of stability,” AEP Ohio’s customers and the state’s economy deserve actual stability and the benefits of competition. But the Partial Stipulation and the Proposed ESP prevent customers from receiving these benefits for at least another three and a half years.

**B. The Transition To Market Is Required By Law, Not The Proposed ESP; The Proposed ESP Serves Only To Unnecessarily Prolong That Transition.**

The most common “benefit” cited by the Signatory Parties is that the Proposed ESP provides a transition to corporate separation and competition,<sup>61</sup> and a transition that is faster than could otherwise be accomplished.<sup>62</sup> But, neither are benefits of the Proposed ESP and neither

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<sup>57</sup> See Staff Brief, p. 6.

<sup>58</sup> Staff Brief, p. 6.

<sup>59</sup> See Staff Brief, p. 8.

<sup>60</sup> See FES Brief, pp. 123-24.

<sup>61</sup> See Constellation Brief, p. 7 (“AEP Ohio’s willing transition of its SSO load into the competitive market, as contained in the Stipulation, is a significant benefit to rate payers and the public interest that cannot be achieved as quickly under an MRO and is not required under an ESP.”); RESA Brief, pp. 12-13 (AEP Ohio’s “commitment to move to a competitive bid auction is a substantial benefit to consumers that may not be achieved as quickly outside this Stipulation.”); Staff Brief, p. 6 (describing as a benefit as a “transition to complete corporate separation and full market pricing for generation services that is materially quicker than what would be possible otherwise”), 9 (“path is being cleared for competitive auctions to serve AEP Ohio’s SSO load”).

<sup>62</sup> See, e.g., RESA Brief, p. 5; Staff Brief, p. 20 (quoting Staff witness Fortney and describing the benefit as the “change in business model to a competitively bid SSO in 2015”).

are certain under the Proposed ESP. First and foremost, it cannot be said that corporate separation is a benefit of the Proposed ESP when corporate separation is required by Ohio law. The General Assembly mandated corporate separation of generation services over ten years ago, and the Commission ordered AEP Ohio to achieve full, structural corporate separation over ten years ago.<sup>63</sup> Therefore, the Partial Stipulation's provisions regarding AEP Ohio's overdue separation is not a "benefit" of the Partial Stipulation but a requirement of Ohio law.<sup>64</sup>

Similarly, termination or modification of the Pool Agreement also is not a benefit of the Partial Stipulation. The pool members gave notice of termination in December 2010, well before the Partial Stipulation was signed, and were not prompted by the Partial Stipulation.<sup>65</sup> As Mr. Nelson testified, "we envisioned pool termination occurring without the stipulation."<sup>66</sup> As the pool members gave notice of termination well in advance of the Partial Stipulation, termination of the pool is not a "benefit" of the Partial Stipulation.

The Signatory Parties' assertion that the transition to market is a benefit of the Proposed ESP overlooks that the Proposed ESP contains at least two contingencies before a Competitive

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<sup>63</sup> R.C. § 4928.17; *see also* Tr. Vol. VI, p. 985 (Constellation witness Fein acknowledging that S.B. 3 would have required AEP Ohio to complete corporate separation at some point prior to the filing of the Partial Stipulation); *In the Matter of the Applications of Columbus Southern Power Company and Ohio Power Company for Approval of Their Electric Transition Plans and for Receipt of Transition Revenues*, Case Nos. 99-1729-EL-ETP and 99-1730-EL-ETP, Opinion and Order at p. 24-25 (Sept. 28, 2000).

<sup>64</sup> At the same time AEP Ohio argues that corporate separation is a benefit of the Proposed ESP, AEP Ohio continues to argue that the Commission need not review the details ahead of time because "the impact on ratepayers of generation divestiture will be established through the adoption of the Stipulation and fully implementing the requirements of R.C. 4928.17." *See* AEP Ohio Brief, p. 73. This is nonsensical. The Commission cannot understand the "impact on ratepayers" of AEP Ohio's proposed corporate separation when no one other than AEP Ohio knows how corporate separation will happen. The Commission is charged and entitled to consider the structure of AEP Ohio's corporate separation in order to ensure that ratepayers' interests are furthered in the transition.

<sup>65</sup> Tr. Vol. V, pp. 692-93.

<sup>66</sup> Tr. Vol. V, p. 693.

Bid Process (“CBP”) may occur: corporate separation and pool modification or termination.<sup>67</sup>

Of course, there is no testimony or evidence that establishes that either of these are necessary preconditions to a CBP, *i.e.*, that it is not possible to have a CBP before corporate separation and changes to the pool occur. For example, AEP Ohio spends 5-6 pages discussing pool termination and modification.<sup>68</sup> Although it appears that AEP Ohio is trying to argue that pool termination or modification needs to be done upon corporate separation, nowhere does AEP Ohio explain why corporate separation or pool termination/modification is necessary before AEP Ohio can conduct a CBP. The Commission need look no further than the Stipulation submitted by Duke Energy Ohio and all of the intervenors in its pending ESP proceeding to see that a CBP can be incorporated into an ESP prior to the completion of corporate separation.<sup>69</sup> Not only is the “transition to market” completely contingent on these events, and therefore quite possibly illusory, but there is also no penalty or consequence to AEP Ohio for failing to meet the contingencies.

The Signatory Parties also argue that the Proposed ESP provides a “benefit” because it would achieve a transition to competitive markets more quickly than an MRO. For this argument, the Signatory Parties rely on the “blend” required by R.C. § 4928.142 for EDUs that owned or operated generation as of July 1, 2008. They argue that, without the Proposed ESP, “the full benefits of competition would not be realized until year six of the transition.”<sup>70</sup> The Signatory Parties’ argument overlooks the clear statutory ability of the Commission to accelerate

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<sup>67</sup> Stip., § IV.1(t); FES Brief, pp. 93-94.

<sup>68</sup> See AEP Ohio Brief, pp. 75-80.

<sup>69</sup> See Stipulation, Case No. 11-3549-EL-SSO (filed October 24, 2011).

<sup>70</sup> See, *e.g.*, Exelon Brief, p. 14.



the MRO blending period beginning in the second year.<sup>71</sup> As a result, AEP Ohio’s customers could enjoy the benefit of wholesale competition from a CBP through an MRO after two years, while also preserving the Commission’s discretion to transition from current ESP pricing at a different pace. The Proposed ESP prevents SSO customers from accessing the benefits of wholesale competition for at least another three and a half years (and they may not access these benefits at all). The Proposed ESP’s contingent, three-and-a-half-year transition is not a “benefit.”

In portraying these provisions of the Proposed ESP as a benefit, it is AEP Ohio’s customers’ eventual arrival at a fully competitive market that actually reflects benefits to customers. This benefit is acknowledged by all parties. This, of course, begs the question, “If a fully competitive market is so good, why don’t we get there sooner?” The Signatory Parties provide no good answer. RESA says that it “understands that there are unique factors associated with AEP’s structure which inhibit an immediate move,”<sup>72</sup> but none of those “factors” are ever described or justified by RESA – or anyone else. Exelon simply states that June 2015 is the “most realistic date for full transition to competition,” citing its witness’s own testimony.<sup>73</sup> There is no evidence to establish that any barriers prevent AEP Ohio from incorporating a CBP into its SSO offer before AEP Ohio wants to.<sup>74</sup> AEP Ohio simply thumbs its nose and says, “you

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<sup>71</sup> Tr. Vol. X, p. 1709; R.C. § 4928.142(E); *In the Matter of the Application of Duke Energy Ohio for Approval of a Market Rate Offer to Conduct a Competitive Bidding Process for Standard Service Offer Electric Generation Supply, Accounting Modifications, and Tariffs for Generation Service.*, Case No. 10-2586, 2011 WL 1827190, ¶ 15 (May 04, 2011). RESA also mischaracterizes IEU witness Murray’s testimony on this point. See RESA Brief, p. 23. Although RESA’s citation does reference a six-year transition, RESA omits reference to Mr. Murray’s earlier testimony that the Commission could shorten the time for blending. See Tr. Vol. XI, pp. 1877-78.

<sup>72</sup> RESA Brief, p. 13.

<sup>73</sup> Exelon Brief, pp. 8-9.

<sup>74</sup> See Tr. Vol. V, pp. 720-721 (AEP Ohio witness Nelson acknowledged that there is nothing “explicit[]” in the Pool Agreement that would preclude a wholesale power procurement auction, and stating that he

can't make me.”<sup>75</sup> The fact of the matter is that AEP Ohio can either structure its rates to meet (and beat) an MRO, or it can recognize what the FirstEnergy Ohio utilities recognized in 2008 and Duke Energy Ohio recognized in 2011 – the best way to structure an ESP to beat an MRO is to have a CBP. There is no need to delay allowing all of AEP Ohio's customers the real, undisputed benefit of competitive markets. The “glide path” laid down by the Proposed ESP and the Partial Stipulation is nothing more than an opportunity for AEP Ohio to charge above-market prices and to be insulated from meaningful competition in the meantime.

**C. The “Elimination” Of Nonbypassable Riders Is Not A Benefit Because The Riders Do Not And Could Not Exist.**

Another “benefit” that the Signatory Parties argue is reflected in the Proposed ESP is the “elimination” or “withdrawal” of certain nonbypassable riders that were originally proposed in AEP Ohio's initial ESP application.<sup>76</sup> There are at least two reasons why this is wrong. First, as noted, the benefits that the Signatory Parties should be touting are the benefits relative to an MRO, not an overly aggressive initial ESP application that had little to no relationship to reality. The Signatory Parties' interest in focusing on a comparison to the initial application here is not surprising because there is no provision for any such riders in an MRO.<sup>77</sup> Therefore, the “elimination” of these riders does not reflect any benefit over an MRO. Second, the riders were not “eliminated;” they were never approved and they could not have been approved. As numerous Signatory Parties acknowledged, the nonbypassable generation-related riders had no

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“wouldn't waste [his] time” to perform any analysis of whether such a procurement would have any impact on the pool members); FES Ex. 12.

<sup>75</sup> See, e.g., AEP Ohio Brief, p. 18-19.

<sup>76</sup> See Staff Brief, p. 6; Exelon Brief, p. 6; Constellation Brief, pp. 8, 12; RESA Brief, pp. 5, 16.

<sup>77</sup> See R.C. § 4928.142.

basis in Ohio law and violated the state's policy to ensure effective competition.<sup>78</sup> Similarly, AEP Ohio points to the elimination of POLR charges as an example of benefits that are “not readily quantified yet are nevertheless of significant value.”<sup>79</sup> The Commission rejected any such charges in AEP Ohio's current ESP<sup>80</sup> and, in its initial ESP application here, AEP Ohio sought to use the same discredited methodology to support a POLR charge. The elimination of charges that would not be available under an MRO and could not be charged in an ESP is not a “benefit” by any reasonable definition of the term.

**D. There Is No Evidence That The GRR, Turning Point Project Or MR6 Project Are Benefits Of The Proposed ESP And, In Fact, The Only Evidence Is To The Contrary.**

Given that every witness who testified about it said that there is no need for additional generation in Ohio, it is impossible to understand how the potential for *any* recovery – not to mention nonbypassable recovery – for AEP Ohio-owned generation is a benefit to anyone other than AEP Ohio. Notably, “[r]ejecting AEP Ohio's automatic recovery for new generation under the” GRR was cited as one of the benefits of the Proposed ESP by CRES Signatory Parties in their briefs.<sup>81</sup> Exelon's witness testified that it would, in fact, “oppose the construction of any additional power plants as unnecessary and not being able to satisfy the statutory criteria.”<sup>82</sup> However, other Signatory Parties do try to argue that the GRR is a benefit, including AEP Ohio's

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<sup>78</sup> See, e.g., Exelon Brief, p. 13; Constellation Brief, p. 8, 12; RESA Brief, p. 16.

<sup>79</sup> AEP Brief, p. 138.

<sup>80</sup> See Remand Order.

<sup>81</sup> See Constellation Brief, pp. 8, 12-13 (emphasis added, also touting the limitations of the GRR); see also RESA Brief, pp. 16-17 (GRR now limited to two projects and noting that AEP Ohio must in a separate application demonstrate need and adherence to statutory standards).

<sup>82</sup> Tr. Vol. VI., p. 1039.

brief argument that the GRR will enhance reliability and provide a cost-based hedge.<sup>83</sup> Not only is there no evidence of either such “benefit,” the record evidence counsels to the contrary.

First, there is no evidence that the GRR does or could meet the statutory requirements under R.C. § 4928.143(B)(2). Most obviously, AEP Ohio must establish in this proceeding that there is a “need” for the Turning Point solar project and the MR6 project so that they may be included in the GRR.<sup>84</sup> AEP Ohio provided no evidence that either facility was needed<sup>85</sup> and, in fact, the evidence resoundingly confirms that there is no need for any new generation in AEP Ohio’s territory, specifically, and Ohio, generally. Rather, AEP Ohio and PJM are both capacity long for the foreseeable future.<sup>86</sup>

Second, the evidence establishes that generation investments provided outside of the competitive market can have significant negative consequences for AEP Ohio’s customers and Ohio’s economy.<sup>87</sup> The competitive market is an important guide in ensuring that generation investments are appropriate and cost-effective, while properly keeping the risk of such

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<sup>83</sup> AEP Ohio Brief, p. 6.

<sup>84</sup> See R.C. § 4928.143(B)(2)(b), (c).

<sup>85</sup> See AEP Ohio Brief, pp. 49-52 (discussing the GRR, but omitting any support for the material requirements of such a rider).

<sup>86</sup> See, e.g., Schnitzer Direct, pp. 41-43 (also concluding that “AEP Ohio has significant reserve margins and does not need new generation dedicated to serve its AEP Ohio load.”); Tr. Vol. VI, p. 968; Tr. Vol. VI, p. 1037; Tr. Vol. IV, pp. 555-556. There are additional reasons that the GRR cannot be approved which were not addressed by the Signatory Parties. For example, the fact that the GRR is a “placeholder” is insufficient to save it or to remedy its harms. The statutory requirements for ESPs explicitly require that evidence of the costs of the riders and the “need” for additional generation must be established in this proceeding. See R.C. § 4928.143(B)(2)(b), (c). “Placeholders” also can adversely affect competition because of the uncertainty it would create for potential suppliers in assessing the competitive market in Ohio. Accordingly, the GRR cannot and should not be approved even as a placeholder. Testimony of Jonathan A. Lesser on behalf of FirstEnergy Solutions Corp., FES Ex. 2 (“Lesser Direct”), p. 63. Further, the Turning Point project could not be approved as part of the GRR because it is a renewable energy facility. Ohio law requires that renewable energy costs must be bypassable in accordance with R.C. § 4928.64, whereas the GRR is proposed to be nonbypassable.

<sup>87</sup> See FES Brief, pp. 134-35.

investments on the investors, rather than customers.<sup>88</sup> FES witness Lesser explained that recovery of generation costs through a nonbypassable rider “would further foreclose competition, contrary to state policy.”<sup>89</sup> FES witness Schnitzer explained how approval of the GRR transfers these risks from investors to customers:

The electricity supply business is inherently risky, because the future is uncertain with respect to those things that will determine the future market price of electricity: load growth, fuel prices, environmental costs, new technology, and so forth. The proposed GRR would improperly allocate risk (including the risk associated with technological choices, excess supply problems, and cost overruns) to consumers rather than to investors. Not surprisingly, the regulatory process significantly underestimates these risks when making long-term resource commitments because customers, and not investors, largely bear these risks. In these risky electricity markets, unfavorable and unforeseen investment outcomes are common. Unfortunately, in regulated markets, retail customers bear the responsibility of paying for those mistakes.<sup>90</sup>

FES witness Schnitzer also estimated that the above-market costs associated with such uneconomic investments totaled \$60 million in the first year alone, and the costs could continue for years.<sup>91</sup> Unnecessary and uneconomic investments that would represent additional cost burdens to Ohio businesses struggling to compete cannot be described as a “benefit.”

Third, there is no clarity as to the scope or parameters of the projects. For example, AEP Ohio has suggested, and again suggests in its Brief, that the existing Muskingum River 5 (“MR5”) unit could be included in the costs added to the GRR.<sup>92</sup> AEP Ohio witness Hamrock also believes that AEP Ohio’s costs to develop up to 350 MW of customer-sited combined heat

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<sup>88</sup> See Schnitzer Direct, pp. 37-39.

<sup>89</sup> Lesser Direct, p. 48.

<sup>90</sup> Schnitzer Direct, pp. 37-38.

<sup>91</sup> Schnitzer Direct, pp. 38-39.

<sup>92</sup> See AEP Ohio Brief, p. 73 (suggesting a potential transfer of MR5 “subject to being retained by the electric distribution utility should a nonbypassable charge for the life of the facility be approved for MR6 prior to completing the structural corporate separation”); see also FES Brief, p. 133, fn. 603.

and power, waste energy recovery, and distributed generation resources may be recovered through the GRR, although this contravenes the express terms of the Partial Stipulation.<sup>93</sup> The uncertainty regarding what costs might be recovered through the GRR leaves the Commission and other interested parties unable to fully assess the impact of the GRR on AEP Ohio's customers and on Ohio. Thus, simply approving the GRR as a "placeholder" rider "would cast a cloud of uncertainty over competitive markets."<sup>94</sup> It is also important to note that while the GRR is not a "benefit" of the Partial Stipulation, it remains a cost of the Partial Stipulation because the GRR costs are incurred whether these facilities benefit customers or not.

Fourth, AEP Ohio's planned development of the Turning Point project cannot be considered a benefit because the project was planned and provided for prior to the Partial Stipulation. AEP Ohio was required to make a commitment to invest \$20 million in Turning Point as a result of CSP's 2009 SEET proceeding, without any conditions requiring guaranteed nonbypassable cost recovery.<sup>95</sup> Therefore, there is no basis on which to credit the Turning Point project as a benefit stemming from the Proposed ESP. To the contrary, the Proposed ESP harms customers and competitive markets by converting what the statute requires to be bypassable cost recovery under R.C. § 4928.64(E) into a nonbypassable rider.

Lastly, as with other purported benefits of the Proposed ESP, there is no certainty that the generation investments will be made. Staff witness Fortney admitted that there was no certainty of the completion of, for example, the MR6 unit.<sup>96</sup> AEP Ohio witness Hamrock also made clear

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<sup>93</sup> Tr. Vol. V, pp. 865-67; Stip. § IV.1.d.

<sup>94</sup> Lesser Direct, p. 63.

<sup>95</sup> Tr. Vol. VI, pp. 864-865.

<sup>96</sup> Tr. Vol. X, pp. 1762-63.

that the MR6 unit will be built only if it makes economic sense.<sup>97</sup> AEP Ohio's development of the MR6 unit is neither dependent upon nor required by the Partial Stipulation.<sup>98</sup> Accordingly, the GRR cannot be deemed a "benefit" of the Proposed ESP when there is no need for the facilities, the unnecessary investments will be uneconomic and damaging to Ohio's economy, and there is no certainty that the investments will be made in any regard. In short, the GRR, Turning Point project and MR6 project are not benefits of the Proposed ESP. To the contrary, if these facilities are built and funded through the GRR, they are likely to result in significant above-market costs to be recovered from AEP Ohio's customers.

**E. "Commitments" And Consideration Of Other Generation Investments Are Not Benefits, Particularly When They Are Already Part Of AEP Ohio's Business Plan And Should Be Made In The Competitive Market.**

The Signatory Parties suggest that the Proposed ESP is beneficial because it commits "AEP Ohio to do a substantial fleet transformation and fuel diversification utilizing Ohio shale gas," and because "[h]aving AEP enter into competitively priced long term shale gas contracts with Ohio producers promotes investment and employment growth in Ohio."<sup>99</sup> They apparently do not understand that the Partial Stipulation does not obligate AEP Ohio to do anything that it wasn't going to do anyway.

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<sup>97</sup> Tr. Vol. V, pp. 857-859.

<sup>98</sup> Tr. Vol. V, pp. 857-859. AEP Ohio erroneously argues that rejection of the GRR would preclude the possibility of the Commission approving the MR6 unit or the Turning Point project. AEP Ohio Brief, pp. 51-52. To the contrary, rejection of the GRR would mean that these projects would be developed under existing market conditions and regulatory incentives – i.e., they would be developed if they make economic sense and not as uneconomic investments under the Partial Stipulation. Regardless of whether the Commission approves the GRR as a place holder, the MR6 unit may be constructed as part of AEP's long-term business plan to transition from coal to gas. Plus, the Turning Point project presumably may be constructed so that AEP Ohio – and the future AEP GenCo – can satisfy its R.C. § 4928.64 benchmarks and recover its costs on a bypassable basis through AEP Ohio's Alternative Energy Rider.

<sup>99</sup> Staff Brief, p. 7; *see also* AEP Ohio Brief, pp. 84-86.

First, AEP Ohio admitted that its “commit[ment]” to fleet transformation is an AEP-wide business objective that pre-dated the Partial Stipulation and will continue with or without it.<sup>100</sup> Therefore, it cannot be said to be a benefit of the Proposed ESP. Second, the “commit[ment]” includes no detail and imposes no requirements on AEP Ohio to do anything.<sup>101</sup> AEP Ohio admitted that shale gas contracts will only be entered into if economically justified and prudent, which, obviously, are the only contracts it can enter into now.<sup>102</sup> AEP Ohio’s agreement to “pursue” customer-sited combined heat and power and waste energy recovery resources, is similarly vague, open-ended, and not a requirement on AEP Ohio to do anything.<sup>103</sup> Moreover, Staff’s suggestion of an economic benefit of such commitments is totally unsupported in the record.<sup>104</sup> To the contrary, AEP Ohio’s investments in generation resources should be left to the discretion of AEP Ohio and its investors to respond to the signals sent by the competitive market for generation service.<sup>105</sup> Without competitive market signals guiding such decisions, unnecessary and uneconomic investments will be made, which will raise prices for customers and hurt the economy.<sup>106</sup> Uneconomic generation investments should not be so recklessly included in a proposal simply because allegedly qualitative benefits are needed to overcome the significant burden imposed on customers by the Proposed ESP. Such investments will only increase the price paid by customers.

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<sup>100</sup> See Tr. Vol. V, pp. 855-856.

<sup>101</sup> See Stip., § IV.2(a).

<sup>102</sup> Tr. Vol. V, pp. 857-860.

<sup>103</sup> Staff Brief, p. 7; AEP Ohio Brief, p. 85.

<sup>104</sup> Staff Brief, p. 7.

<sup>105</sup> See R.C. § 4928.17.

<sup>106</sup> See FES Brief, pp. 134-35.



AEP Ohio has failed to even address FES' arguments that the MTR unreasonably and unfairly subsidizes certain customer classes.<sup>107</sup> Instead, AEP Ohio claims that the MTR manages the transition to market rates.<sup>108</sup> This argument fails, because even if a transition mechanism to market was appropriate, there is no reason why shopping customers who are already paying market prices should pay the charge. Similarly, there is no reason why AEP Ohio should receive an additional \$24 million in MTR charges in 2012 if the intent of the rider is to "smooth" the transition to market.<sup>109</sup> The MTR is unreasonable and unfair, and should be rejected.

**F. The Signatory Parties Claim Other Benefits Without Acknowledging They Are Contingent And Uncertain.**

The Signatory Parties tout the proposed grants to Partnership With Ohio ("PWO") and the Ohio Growth Fund ("OGF") as unqualified "benefits" of the Proposed ESP.<sup>110</sup> However, the Signatory Parties fail to mention that the grants are contingent on AEP Ohio's earnings. If AEP Ohio does not achieve a 10% return on equity, the requirement for the grants disappears.<sup>111</sup> The Signatory Parties also fail to mention that the PWO grant represents a decrease in funding from prior years. AEP Ohio currently provides \$5 million a year to PWO without any contingencies, but under the Proposed ESP, the funding would decrease by 40%, if it is provided at all.<sup>112</sup> Gifts that may never be made can hardly be credited as unqualified "benefits" of the Proposed ESP.

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<sup>107</sup> FES Brief, p. 115

<sup>108</sup> AEP Ohio Brief, p. 40.

<sup>109</sup> Although Mr. Allen recognized the MTR charge of \$24 million as a cost under the Proposed ESP, Ms. Thomas did not include this charge in her analysis. Allen Direct, p. 18.

<sup>110</sup> See Staff Brief, p. 12 (there also is no record evidence to support Staff's assertion that the grant to OGF facilitates the state's economy); RESA Brief, p. 23.

<sup>111</sup> See Stip., § IV.1(u).

<sup>112</sup> Tr. Vol. VI, pp. 930-931.

Similarly, the only “commitment” made to Grove City and Hilliard to get them to sign the Partial Stipulation is possible funding for a pilot program for LED lighting.<sup>113</sup> Yet this program must first be approved as a component of AEP Ohio’s next Energy Efficiency and Peak Demand Reduction Portfolio Program for 2012-14, and there is no evidence or even a suggestion that the proposed program passes the total resource cost test and will be approved by the Commission.

**G. The “Elimination” of Admitted Shopping Barriers Is Not A Benefit Because Such Barriers Violate State Policy And Others Would Not Be Eliminated Until 2015.**

The Signatory CRES Parties tout as a benefit of the Proposed ESP the removal of certain AEP Ohio policies that they acknowledge have served as barriers to shopping in AEP Ohio’s territory.<sup>114</sup> As set forth in detail in FES’ Initial Brief, state law and policy requires competition. Therefore, none of the barriers – those that will be “removed” and the additional barriers that continue<sup>115</sup> – should exist in the first place.<sup>116</sup> In any event, the Proposed ESP’s impact on shopping barriers is not as rosy as the Signatory Parties would have the Commission believe. Other than AEP Ohio’s agreement to provide customer information, the only barrier to actually

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<sup>113</sup> See AEP Ohio Brief, pp. 84-85; Stip., § IV.1.(w).

<sup>114</sup> See Constellation Brief, pp. 13-14; RESA Brief, pp. 6, 15-16.

<sup>115</sup> The Proposed ESP provides that certain existing barriers to competition in AEP Ohio’s service territory would continue: (1) above market capacity charges and the “queue” for capacity; (2) switching fees; (3) burdensome minimum stay requirements related to switching; (4) the elimination of certain rate schedules from the shopping tariff, which forces shopping customers to lose distribution discounts; and (5) the failure to offer billing options provided by other Ohio utilities. Banks Direct, pp. 53-56.

<sup>116</sup> The fact that these shopping barriers have been in place in AEP Ohio’s service territory also refutes Exelon’s unsupported assertion that, “[a]s evidenced by a lack of shopping in the AEP Ohio service territory, customers preferred the AEP Ohio rates to competitive rates.” Exelon Brief, p. 9. This assertion is totally unsupported and contradicts the testimony of Exelon’s own witness, as well as other CRES providers, that AEP Ohio has had corporate policies to discourage competition. FES Brief, p. 89 (citing Tr. Vol. VI, p. 1036; Tr. Vol. IV, pp. 538-539); see also Tr. Vol. VI, pp. 978-980 (Constellation witness Fein acknowledging the existence of shopping barriers that have “been on the books [in AEP Ohio’s] tariffs).

be removed as of January 1, 2012, is the 90-day notice requirement for a certain subset of customers.<sup>117</sup> Other barriers would remain in place until June 2015, including the 12-month minimum stay and the minimal seasonal stay for residential and small commercial customers.<sup>118</sup> Of course, as discussed further in Section V, the biggest barrier to competition for all customers – AEP Ohio’s proposed RPM-capacity price caps – also would be imposed until June 2015. Those caps and the ceiling they place on shopping for all customers renders the removal of the 90-day notice requirement for a certain subset of customers meaningless because so few new customers will be able to shop anyway.<sup>119</sup>

#### **H. Staff’s Reference to Transmission Cost Savings Should Be Stricken.**

In a list of benefits of the Proposed ESP, including the inaccurate “\$130 million cost savings” refuted by Staff’s own testimony, Staff argues that the Proposed ESP “saves ratepayers millions in transmission costs.”<sup>120</sup> This argument should be stricken and disregarded. There is absolutely no record evidence that the Proposed ESP has any impact on transmission costs, not to mention a positive impact. No witness addressed the impact of the Proposed ESP on transmission costs and no exhibits were admitted regarding any such impact. Staff provides no citations to support these statements, and there are none. Staff appears to have mistakenly copied this language from its post-hearing brief filed in Case No. 10-388-EL-SSO. Accordingly, the Commission should disregard Staff’s assertion.

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<sup>117</sup> Stip., § IV.1(s).

<sup>118</sup> See Constellation Brief, pp. 14-15.

<sup>119</sup> See FES Brief, pp. 100-102.

<sup>120</sup> See Staff Brief, pp. 8, 10 (also later stating that “[t]ransmission costs are avoided leading to more reasonably priced electricity”).

**IV. ABOVE-MARKET CAPACITY PRICING IS NOT A “BENEFIT” OF THE PROPOSED ESP AND IS UNSUPPORTED AND IMPROPER.**

Every one of the Signatory Parties has claimed that the resolution of the 10-2929 Docket constitutes a “benefit” of the Proposed ESP.<sup>121</sup> AEP Ohio was forced to create this “benefit” because even its own analysis shows that an MRO is more favorable to customers.<sup>122</sup> As discussed in detail below, the resolution of the 10-2929 Docket is not a “benefit” of the ESP, and AEP Ohio’s above market capacity pricing proposal should not be considered by the Commission.

**A. The Partial Stipulation Does Not Offer “Discounted” Capacity Prices, But Instead Increases Capacity Prices Dramatically.**

AEP Ohio touts as a benefit of the Partial Stipulation (but not the Proposed ESP) its provision of “discounted capacity prices to competitive suppliers for all of AEP Ohio’s generation portfolio.”<sup>123</sup> This “discounted capacity” argument was adopted by other parties in their briefs.<sup>124</sup> This doublespeak is worthy of inclusion in George Orwell’s *1984*. The only capacity compensation mechanism for AEP Ohio for load transferred to a CRES supplier which has ever been in place since AEP Ohio joined PJM is RPM pricing.<sup>125</sup> This RPM based pricing was recently affirmed by both FERC and the Commission. To change the status quo and impose capacity pricing which is four times higher than RPM pricing is not offering a “discount.” Instead, it is a dramatic and unwarranted price increase, and is certainly not a “benefit” of the Partial Stipulation.

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<sup>121</sup> See e.g., AEP Ohio Brief, p. 87; Exelon Brief, p. 10; RESA Brief, p. 13; Constellation Brief, p. 10; Staff Brief, p. 10.

<sup>122</sup> See Thomas Direct, Ex. LJT-3.

<sup>123</sup> AEP Ohio Brief, p. 16.

<sup>124</sup> See, e.g., Staff Brief, p. 10.

<sup>125</sup> AEP Ohio Brief, p. 90.

## **1. Capacity has been priced at RPM since AEP Ohio joined PJM.**

AEP Ohio's recent attempts to change from its historical use of RPM pricing have not been successful. FERC rejected AEP Ohio's request to adopt cost-based pricing based on a recent Commission decision.<sup>126</sup> The Commission entry relied on by the FERC was issued December 8, 2010, in the 10-2929 Docket ("10-2929 Entry"). In the 10-2929 Entry, the Commission formally adopted the current capacity charges established by the three-year RPM capacity auction conducted by PJM as the state capacity compensation mechanism.<sup>127</sup> As shown by this authority, despite recent unsuccessful efforts by AEP Ohio, RPM pricing is the current law in Ohio and is the only pricing mechanism which has ever been in place.

The briefs of AEP Ohio and Staff both claim that the "discounted" capacity pricing contained in the Proposed ESP constitutes a benefit of the Partial Stipulation in the amount of \$856 million.<sup>128</sup> Specifically, Staff claims that "AEP Ohio will provide discounted capacity prices to competitive suppliers for increasing portions of AEP Ohio's generation portfolio in order to support growth of robust competitive supply options for customers and to resolve the

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<sup>126</sup> FERC Entry dated January 20, 2011, Case No. ER11-2183-000; Direct Testimony of Roy J. Shanker on behalf of FirstEnergy Solutions Corp., FES Ex. 14 ("Shanker Direct"), p. 13.

<sup>127</sup> 10-2929 Entry. AEP Ohio argues that an August 11, 2011 scheduling entry in the 10-2929 Docket somehow adopted cost-based capacity pricing in Ohio. *See* AEP Ohio Brief, p. 92. Just as it did regarding the POLR charge in Case No. 08-917-EL-SSO, AEP Ohio attempts to read a procedural entry as somehow limiting or binding the Commission's authority regarding the substantive issue of law. This is flawed for two reasons. First, the language of the August 11, 2011 Entry references the "capacity cost pricing/recovery mechanism." *Id.* at ¶ 6. This phrasing does not reference AEP Ohio's full embedded cost-based proposal, it instead relates to the cost of capacity to CRES providers. Therefore, the Attorney Examiner's use of this phrasing was entirely appropriate. Second, it is not credible to argue that a paragraph in a scheduling entry was meant to somehow overturn or limit the 10-2929 Entry, which expressly considered the issue and adopted RPM pricing as Ohio's state compensation mechanism for capacity. 10-2929 Entry ¶ 4. If the Attorney Examiner had intended to limit testimony to only cost-based proposals he would have done so expressly, not through a coded message that only AEP Ohio understood. Moreover, a scheduling entry issued by the Attorney Examiner cannot overturn the decision of the Commission on December 8, 2010. Just as the Commission rightfully determined in Case No. 08-917-EL-SSO, AEP Ohio's hyper-technical reading of the August 11, 2011 scheduling entry in the 10-2929 Docket should be rejected.

<sup>128</sup> AEP Ohio Brief, p. 96; Staff Brief, p. 6, 10.

pending capacity compensation case for AEP Ohio.”<sup>129</sup> Not only does this argument completely ignore the un rebutted testimony at hearing regarding this dramatic price increase, it also ignores the testimony from Staff’s own witnesses Dr. Choueiki and Mr. Fortney. Other than AEP Ohio, every Signatory Party who presented testimony regarding capacity pricing, including RESA, OEG, Constellation, and Exelon, agreed that capacity pricing should be based on RPM prices.<sup>130</sup> Dr. Lesser explained why raising prices inappropriately, but not raising them as high as was originally proposed, is not a benefit of the Partial Stipulation:

Again, therefore, equating a ‘benefit’ to CRES customers from not recovering monies for which it has no right to collect in the first place, is specious. One might as well argue that the thief who stole your wallet, but not your watch, ‘benefitted’ you, because he could have stolen the watch too.<sup>131</sup>

To create the illusion of “discounted” capacity pricing, Mr. Allen calculated the difference between AEP Ohio’s proposed, allegedly cost-based capacity charge of \$355.72/MW-day and RPM market rates for the limited amount of market-based capacity made available during each year of the Partial Stipulation.<sup>132</sup> Mr. Allen’s alleged “benefit” was thus measured relative to AEP Ohio’s capacity price proposal (which is contrary to decisions by the FERC and the Commission) and was not measured relative to an MRO.<sup>133</sup> AEP Ohio’s Proposed ESP calculates the “benefit” of the “discounted” capacity as having a net present value of \$856 million.<sup>134</sup>

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<sup>129</sup> Staff Brief, p. 10.

<sup>130</sup> See Tr. Vol. IV, pp. 539-540 (RESA); Tr. Vol. III, p. 236 (OEG); Tr. Vol. VI, pp. 970-971, 982-983 (Constellation); Tr. Vol. VI, pp. 1043-1044 (Exelon).

<sup>131</sup> Lesser Direct, p. 26.

<sup>132</sup> Tr. Vol. III, p. 433-435; AEP Ohio Brief, p. 94.

<sup>133</sup> AEP Ohio Brief, p. 96.

<sup>134</sup> Allen Direct, Ex. WAA-6. AEP Ohio compares the amounts of RPM capacity available under the Partial Stipulation to the loads of Toledo Edison Company, Dayton Power & Light Company; and Duke

However, Staff witness Choueiki testified that AEP Ohio's proposal to use cost-based rates was "not reasonable."<sup>135</sup> He also found that "to the extent there is a transparent forward capacity price available in the market, such a price should be used."<sup>136</sup> Mr. Fortney agreed with this analysis, and agreed that Staff supported pricing at RPM.<sup>137</sup> Mr. Fortney explained in detail why he did not believe that the "discounted" capacity pricing should be considered to be a "benefit" of the Partial Stipulation.

Q. So would it be fair to say that -- would it be fair to say that if one was going to have a benefit calculated from not having to pay a capacity price of \$355, one would have to assume that AEP was entitled to charge that amount?

A. I play the lottery and occasionally when one of the jackpots gets fairly high I take out my pad of paper and I write down what I'm going to spend the money on, who I might leave it to, and who I might give it to, and I guess, for example, if I took my pad of paper out and I put Ms. Grady's name down, she's a nice person, it probably isn't much of a benefit to her unless I actually win the lottery and until I actually give her a million dollar check.

So I know you like yes or no answers, so I think the answer to your question is yes, I think when you are going to compare two things, one of the things has to be a certain.

Q. And you didn't attempt to calculate that benefit because you didn't think it was a benefit, did you?

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Energy-Ohio. *See* AEP Ohio Brief, p. 96. AEP Ohio fails to recognize that by making this argument it is illustrating just how many customers will be prevented from accessing the market-based capacity prices that the rest of Ohio's customers enjoy. As Mr. Banks explained, "the disturbing flip side is that in its first year, the [Proposed] ESP would effectively prohibit AEP Ohio customers in a level encompassing double the load of The Cleveland Electric Illuminating Company from shopping – approximately three times the load of Toledo Edison and the vast majority of AEP Ohio's customers." Banks Direct, p. 5.

<sup>135</sup> Direct Testimony of Hisham M. Choueiki on behalf of the Staff of the Public Utilities Commission of Ohio, Staff Ex. 2 ("Choueiki Direct"), p. 4.

<sup>136</sup> Choueiki Direct, pp. 4, 7-8.

<sup>137</sup> Tr. Vol. X, p. 1707.

A. It may be a meaningful number for AEP. I do not believe it's a meaningful number for the comparison of the MRO to the ESP.<sup>138</sup>

As shown by Staff's testimony, there is simply no "benefit" associated with the alleged "discounted" capacity pricing for three reasons. First, the only right price for capacity is the RPM market-based price, as discussed in detail below and in Dr. Choueiki's testimony. Second, a four-fold increase in capacity prices cannot be considered in any way a "discount" encouraging shopping in AEP Ohio's territory. Instead, this is a cost to AEP Ohio's customers of \$1.27 billion.<sup>139</sup> Third, the Proposed ESP does not offer any "benefit," because Ohio has never adopted AEP Ohio's purported cost-based pricing structure. In light of these factors, the position taken by Staff on brief is incorrect, and FES respectfully suggests that the position taken by Staff in its sworn testimony be accepted instead. There is no "benefit" associated with the Partial Stipulation's capacity pricing.

**B. The Statutory ESP vs. MRO Test Requires That The Commission Compare The Proposed ESP To A Market-Based MRO.**

Ms. Thomas also used capacity pricing from the Partial Stipulation to create the competitive benchmark price used in her ESP vs. MRO test.<sup>140</sup> This assumption is flawed because the proposed capacity pricing from the Partial Stipulation is irrelevant to the Commission's consideration of the pricing that should have been included in the test. As explained in FES' Brief at pages 9-11, market-based capacity prices must be used in the ESP vs. MRO test as a matter of law. R.C. § 4928.142(C) clearly reflects that the comparable MRO should include competitive market-based pricing for the procurement of SSO supply, "including the costs of energy and capacity" procured through the competitive process.

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<sup>138</sup> Tr. Vol. X, p. 1707-1708.

<sup>139</sup> Lesser Direct, p. 10-11.

<sup>140</sup> Thomas Direct, p. 9.



**C. There Is Only One Right Price For Capacity: The RPM Market-Based Price.**

As shown in FES' Brief at pages 51-61, the only right transfer price for capacity is the RPM market-based price. The reasons why RPM transfer pricing is the most appropriate method to price capacity are discussed below, and then AEP Ohio's misguided attacks on RPM pricing are addressed in detail.

First, due to AEP Ohio's FRR election, CRES providers are obligated to purchase capacity from AEP Ohio for any load in AEP Ohio's FRR area.<sup>141</sup> Because AEP Ohio has historically charged CRES suppliers the RPM price for capacity, CRES providers had no reason to make their own FRR election during this period.<sup>142</sup> AEP Ohio is now attempting to change the rules of the game by changing to capacity charges of \$255/MW-day, which is roughly four times higher than RPM prices during this period.<sup>143</sup> The biggest problem with this proposal, among many, is that the Reliability Assurance Agreement ("RAA") does not permit a CRES provider to make its own election into AEP Ohio's FRR territory during the period from the present through May 31, 2015. This means that CRES providers who relied on AEP Ohio's express position regarding RPM capacity pricing in Case No. 08-917 *et al.*, are being asked to pay these above-market rates for the period in which they don't have the ability to avoid AEP's unilateral increase in prices by providing their own capacity.<sup>144</sup> This is anti-competitive and improper.

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<sup>141</sup> FES Brief, p. 51.

<sup>142</sup> AEP Ohio Brief, p. 90.

<sup>143</sup> Banks Direct, p. 12.

<sup>144</sup> FES Brief, p. 52.

Second, capacity rates in PJM are normally set via the RPM auction process.<sup>145</sup> Offers in this auction are subject to price caps based on the resource's avoided cost rate.<sup>146</sup> Suppliers cannot make offers at their full embedded costs.<sup>147</sup> Nothing in the RAA provides for AEP Ohio or any supplier participating under the FRR alternative to recover its full embedded cost of capacity.<sup>148</sup> As nothing in the RAA authorizes the recovery of full embedded costs, AEP Ohio's proposal to institute a negotiated value based on those full embedded costs is inappropriate.

Third, from a policy perspective, in the long run RPM prices maximize economic efficiency.<sup>149</sup> Pricing at anything other than RPM in the long term would create distorted incentives encouraging CRES providers to divert capacity into AEP Ohio's FRR region in order to obtain the higher capacity payments.<sup>150</sup> In the short run, pricing capacity at the negotiated rate would simply divert resources from CRES providers to AEP Ohio and cause shopping customers to pay more than they should for capacity.<sup>151</sup>

Every one of AEP Ohio's attacks center on the unsupported premise that it is entitled to recover its costs, and AEP Ohio insists that everything must be viewed through that prism. However, nothing in Ohio law or the RAA guarantees that any Load Serving Entity ("LSE") will be guaranteed recovery of its full embedded costs. AEP Ohio ignores this essential distinction, and as a result all of its arguments lack merit.

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<sup>145</sup> FES Brief, p. 52; Shanker Direct, p. 7.

<sup>146</sup> FES Brief, p. 52; Shanker Direct, p. 8.

<sup>147</sup> FES Brief, p. 52-53; Shanker Direct, p. 8.

<sup>148</sup> FES Brief, p. 53; Shanker Direct, p. 9, 11.

<sup>149</sup> FES Brief, p. 55.

<sup>150</sup> Shanker Direct, p. 19. As the Partial Stipulation returns to RPM pricing on May 31, 2015, and CRES providers are "locked in" to AEP Ohio's FRR plan until after that date, the long term impact of this provision is mitigated.

<sup>151</sup> FES Brief, p. 56, 59.

**1. RPM prices are the best market-based prices for capacity and are supported by every party presenting testimony on this issue other than AEP Ohio.**

AEP Ohio argues that RPM prices are not an accurate reflection of the market because RPM is a “regulated market” and includes certain factors which could result in a downward bias in auction clearing factors.<sup>152</sup> AEP Ohio’s arguments miss the point. The issue is not whether RPM prices are purely market driven, or whether RPM prices are the exact prices which would be present in a perfect market. Instead, the issue is whether RPM prices are the best estimate of market prices which are available. The answer to that is a conclusive, un rebutted, yes. Every party other than AEP Ohio who presented testimony on this issue agreed that RPM prices were the best evidence of market rates available.<sup>153</sup> Most notably, Staff testified that AEP Ohio’s proposal to use cost-based rates was “not reasonable,” and supported pricing at RPM.<sup>154</sup>

AEP Ohio next argued that its claimed “RPM flaws” would not apply in the context of a cost-based rate established by a regulator. This argument does not make sense, and when asked this question at the hearing Dr. Shanker correctly identified it as a non-sequitur.<sup>155</sup> The RPM model attempts to replicate a market price of capacity, and is the closest approximation to the market value of capacity available.<sup>156</sup> Any purported “flaws” in RPM pricing would not be present in a rate based on costs because a rate based on cost wouldn’t attempt to replicate the competitive market in any respect.<sup>157</sup> Thus, this comparison is faulty.

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<sup>152</sup> AEP Ohio Brief, p. 101.

<sup>153</sup> See Shanker Direct, p. 16; Tr. Vol. IV, pp. 539-540 (RESA); Tr. Vol. III, p. 236 (OEG); Tr. Vol. VI, pp. 970-971, 982-983 (Constellation); Tr. Vol. VI, pp. 1043-1044 (Exelon).

<sup>154</sup> Choueiki Direct, p. 4; Tr. Vol. X, p. 1707.

<sup>155</sup> Tr. Vol. VI, p. 1117.

<sup>156</sup> Shanker Direct, p. 18; FES Brief, p. 55.

<sup>157</sup> See Tr. Vol. VI, p. 1117.

AEP Ohio did not present any evidence suggesting that another market price would be more appropriate than RPM pricing, and did not present any evidence suggesting that RPM prices taken as a whole (including factors which would tend to put upward pressure on prices) were not a reasonable reflection of how the market would value capacity. Indeed, AEP Ohio witness Pearce expressly admitted that RPM pricing is a type of market-based capacity pricing.<sup>158</sup> Dr. Pearce also admitted that RPM pricing is transparent.<sup>159</sup> In light of these admissions from AEP Ohio's own witnesses, it is difficult to understand why AEP Ohio attacks what it recognizes is a transparent market-based pricing mechanism.

As the testimony regarding the market-based nature of RPM pricing from Dr. Shanker and others is unrebutted by AEP Ohio, AEP Ohio's unwarranted attacks on RPM pricing lack merit.

**2. RPM prices are already known during the Proposed ESP term, and are four times lower than the \$255/MW-day pricing contained in the Partial Stipulation.**

AEP Ohio next attacks RPM prices as being volatile, and claims that a cost-based rate would not be volatile.<sup>160</sup> As a preliminary matter, while RPM prices do vary from year to year during the Proposed ESP, they are known and effectively fixed, so there is no applicable concept of volatility as the term is typically used. RPM prices through May of 2015 are known with certainty and were extensively discussed in testimony.<sup>161</sup> As such, there is no uncertainty in RPM prices for the entire period in which AEP Ohio claims to substitute the "certainty" of its above-market negotiated price of \$255/MW-day for RPM pricing. The reality is that other than

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<sup>158</sup> Tr. Vol. II, p. 177.

<sup>159</sup> Tr. Vol. II, p. 177.

<sup>160</sup> AEP Ohio Brief, p. 101.

<sup>161</sup> See Schnitzer Direct, p. 21; FES Brief, p. 49-50.

minor adjustments reflecting load variation or incremental procurement, RPM pricing will be fixed at a level that is about a quarter of the “certain” AEP Ohio proposal through May 2015, when AEP Ohio has agreed to use RPM pricing.

Additionally, although AEP Ohio attacks the volatility of the RPM system, it somehow fails to acknowledge that AEP Ohio and other Signatory Parties are classifying the transition to RPM market-based pricing in 2015 as a benefit of the Partial Stipulation.<sup>162</sup> It is disingenuous to claim that RPM prices are inappropriately volatile in one section of a brief, only to then claim that they are beneficial to customers later in that same brief. FES agrees with the latter position taken by the Signatory Parties: RPM pricing is beneficial to customers. It is not inappropriately volatile, and is not volatile in any respect during the term of the Proposed ESP.

To the extent AEP Ohio claims that the change in RPM prices constitutes volatility during the Proposed ESP term, even though those prices are known prior to the start of the Proposed ESP term, this argument is still misguided. It is un rebutted that AEP Ohio’s proposed \$255/MW-day price is nearly four times higher than RPM prices during the Proposed ESP term.<sup>163</sup> Mr. Nelson admitted that at no time since RPM came into effect through May 2015 has the RPM price been at or above \$255/MW-day in the PJM unconstrained region.<sup>164</sup> Customers are much better off paying prices which are “volatile” when they are dramatically lower than the “stable” rates contained in the Partial Stipulation. Further, at a basic level, volatility in prices is not an evil in and of itself. Price movements send appropriate messages to market participants,

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<sup>162</sup> See AEP Ohio Brief, p. 96, 145; Staff Brief, p. 10; Constellation Brief, p. 10; RESA Brief, p. 10; Exelon Brief, p. 10.

<sup>163</sup> Banks Direct, p. 12.

<sup>164</sup> Tr. Vol. XII, p. 2183.

*e.g.*, to build more capacity when prices are high.<sup>165</sup> These signals are another of the many benefits of competitive markets.

### **3. Use of RPM pricing does not constitute a transfer of wealth to CRES providers.**

AEP Ohio claims that the use of RPM pricing would constitute “a transfer of wealth” from AEP Ohio, and would constitute a “subsidy” to CRES providers who purchase that capacity without paying AEP Ohio’s inflated full-embedded costs.<sup>166</sup> This argument rests entirely on the presumptions that: (a) AEP Ohio is entitled to recover the full embedded cost of its capacity; and (b) any compensation mechanism which doesn’t provide for the recovery of these costs constitutes a subsidy to CRES providers.<sup>167</sup> This argument is refuted in detail in FES’ Brief at pages 58-60. The key points of this discussion are briefly summarized below.

AEP Ohio’s claim that market-based pricing constitutes a subsidy completely ignores how we came to this point. As acknowledged in AEP Ohio’s Brief, AEP Ohio has voluntarily made an FRR election ever since the RPM was established in June of 2007.<sup>168</sup> AEP Ohio’s FRR election continues through the planning year 2014/2015.<sup>169</sup> For this entire period, AEP Ohio has been compensated at the RPM price.<sup>170</sup> Indeed, AEP Ohio used RPM prices to its benefit in the past, including most recently in its 2009-2011 ESP.<sup>171</sup> As shown by these undisputed facts, AEP Ohio used RPM prices for years to transfer capacity under its FRR election, and now claims that a transfer at anything other than its full-embedded costs would constitute a subsidy to CRES

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<sup>165</sup> Tr. Vol. VI, p. 1121.

<sup>166</sup> AEP Ohio Brief, p. 101-02.

<sup>167</sup> AEP Ohio Brief, p. 91.

<sup>168</sup> AEP Ohio Brief, p. 90.

<sup>169</sup> AEP Ohio Brief, p. 90.

<sup>170</sup> AEP Ohio Brief, p. 90.

<sup>171</sup> Schnitzer Direct, p. 22-23.

providers. It is not persuasive for AEP Ohio to claim that the FRR election it made, and the RPM prices it relied upon, are now suddenly a subsidy to CRES providers.

AEP Ohio's position is also completely unsupported as a matter of law or economics.<sup>172</sup> Transferring capacity at market prices is the only result that avoids subsidies, as the payments are equal to the opportunity costs that AEP Ohio has for a market disposition (not an assumed regulatory disposition) of the capacity.<sup>173</sup> If AEP Ohio were to sell this capacity into the market, the best approximation of what it would receive is the RPM price.

AEP Ohio's position is also inaccurate, because it assumes that AEP Ohio's full embedded cost calculation is correct.<sup>174</sup> As explained in detail in FES' Brief at pages 69-74, AEP Ohio's calculation dramatically overstates AEP Ohio's true cost of capacity.

Finally, AEP Ohio's position is hypocritical.<sup>175</sup> AEP Ohio claims that any payment below its full embedded costs would mean it is subsidizing CRES providers. However, after it separates its generation assets as required by the Partial Stipulation, it would no longer be recovering its full embedded cost-based rate. The only distinction between these two periods appears to be that during the bulk of the ESP period, AEP Ohio didn't want to charge RPM prices, and once the FRR election terminates AEP Ohio does want to charge RPM prices. This transparent hypocrisy should be rejected.

#### **4. CRES providers had no reason to self-supply into AEP Ohio's territory by making their own FRR elections.**

Apparently recognizing that changing the historic compensation mechanism after CRES providers were prevented from making their own FRR elections is problematic, AEP Ohio

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<sup>172</sup> FES Brief, p. 59.

<sup>173</sup> Shanker Direct, p. 17.

<sup>174</sup> FES Brief, p. 59.

<sup>175</sup> FES Brief, pp. 59-60.

developed an argument that CRES providers could have elected to self-supply into AEP Ohio's FRR plan in the past as opposed to relying on AEP Ohio's capacity.<sup>176</sup> However, as discussed in detail above, the only efficient market price for capacity is RPM pricing, and this is the pricing structure which has been used by AEP Ohio ever since it made an FRR election in 2007. As such, CRES providers had no reason to elect to self-supply into AEP Ohio's FRR region as opposed to the PJM market in general.<sup>177</sup> It is only this potential exercise of market power by AEP Ohio that raises the issue of why CRES providers would have been motivated to self-supply. The obvious answer is that CRES providers only would have been motivated to self-supply had they anticipated such inappropriate and anti-competitive behavior by AEP Ohio. Attempting to put the "blame" on CRES providers for failing to anticipate AEP Ohio's illegitimate behavior says much more about AEP Ohio than it does about the CRES providers. It is hard to contemplate a world where all market participants are expected to act in anticipation of anti-competitive violations by others.

AEP Ohio's argument also fails because PJM is a regional marketplace, which provides capacity to several states, including Ohio. Recent PJM auctions have shown that there is a substantial amount of excess capacity in this region.<sup>178</sup> In fact, PJM has already procured more than enough capacity for all of the load-serving entities in PJM, including AEP Ohio, for the entire ESP period and has a reserve margin that exceeds its target.<sup>179</sup> As PJM is long on capacity, there is no reason why the Commission should impose a dramatic price increase on Ohio customers in order to incentivize new capacity in Ohio by forcing LSEs to make their own

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<sup>176</sup> AEP Ohio Brief, pp. 93, 102.

<sup>177</sup> Shanker Direct, p. 7.

<sup>178</sup> Schnitzer Direct, p. 41.

<sup>179</sup> Schnitzer Direct, p. 42.



FRR elections into AEP Ohio's FRR region.<sup>180</sup> Indeed, there is no record evidence establishing that any new capacity would be incentivized by such a structure, as the excess capacity in PJM suggests that LSEs would simply bid their existing excess capacity into AEP Ohio's FRR region to obtain the higher prices rather than building new capacity in Ohio.<sup>181</sup>

Finally, AEP Ohio implies that CRES providers did not make an FRR election into AEP Ohio's FRR plan due to some unexplained and unquantified "potential penalties" associated with an FRR election.<sup>182</sup> As a preliminary matter, AEP Ohio has not quantified these costs, and so it is not feasible to determine the potential impact these costs could have on the decision to make an FRR election. This argument also is deficient because it misses the larger point: AEP Ohio has priced capacity at RPM ever since it made an FRR election.<sup>183</sup> By making this choice, and by repeatedly making an FRR election even after recent RPM results became known, AEP Ohio effectively discouraged CRES providers from making this election. There was simply no need to do so, because capacity would be priced at RPM whether bid into the auction or not. Also, AEP Ohio conveniently ignores that the best estimate of the price for its capacity without an FRR election is the RPM price. AEP Ohio must now live with the strategic choice it made to make the FRR election.

## **5. Cost-based capacity pricing would not lead to lower prices in Ohio.**

As discussed in detail above, adopting either AEP Ohio's cost-based capacity proposal or the Partial Stipulation's negotiated \$255/MW-day proposal would lead to a dramatic increase in

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<sup>180</sup> It is also illustrative to note that AEP Ohio is extremely long on capacity. AEP Ohio's reserve margin was about 55% in 2009, 37% in 2010, and is expected to gradually decline to about 28% by 2016, even after assuming 2.0 GW in plant retirements. Schnitzer Direct, pp. 42-43. These margins are well above PJM's target installed reserve margin of 15-16%. Schnitzer Direct, p. 43.

<sup>181</sup> Schnitzer Direct, pp. 42-43; Shanker Direct, p. 19.

<sup>182</sup> AEP Ohio Brief, p. 102.

<sup>183</sup> AEP Ohio Brief, p. 90.

costs over the long term. During his re-direct examination, Dr. Shanker discussed the potential long-term impact of a non-market capacity price. He concluded that a cost-based rate would inappropriately incentivize CRES providers to divert resources into AEP Ohio's region to displace AEP Ohio's capacity, and that this would distort markets.<sup>184</sup> AEP Ohio quoted this section, and emphasized a portion of the following text:

In the original testimony that I provided I discussed how a likely result would be if prices were very high and AEP on retail, let's say the 350 level, there would be an incentive for people to withdraw assets from the rest of PJM where they're properly -- not properly, where they are valued at, say, 150 in the hypothetical, and to direct them into AEP, and with the result being the prices would actually rise in the rest of PJM from the distortion of the resources.<sup>185</sup>

AEP Ohio then distorted what Dr. Shanker actually said, which is that prices within PJM would rise, and claimed that "Ohio customers would get lower prices for capacity but residents of another State might not keep their lower prices."<sup>186</sup> This is incorrect. Dr. Shanker did not state that prices in Ohio would fall if Ohio adopted a cost-based capacity price. Prices would not fall for AEP Ohio customers because, if AEP Ohio's view prevailed, capacity in AEP Ohio would be priced at AEP Ohio's costs. Further, LSEs making an FRR election would be paid for their capacity at that same cost-based price established by AEP Ohio under the proposed new state compensation mechanism. Therefore it would not matter how much excess capacity was bid into AEP Ohio's FRR region. The dramatic price increase for capacity would merely transfer some portion of these windfall profits from AEP Ohio to the LSE making the FRR

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<sup>184</sup> Tr. Vol. VI, pp. 1156-57.

<sup>185</sup> AEP Ohio Brief, p. 103 (citing Tr. Vol. VI, p. 1156-57)( emphasis added).

<sup>186</sup> AEP Ohio Brief, p. 103.

election. Ohio customers would see no benefit whatsoever, and instead would see the dramatic price increase currently proposed by AEP Ohio.

**6. No transition period to RPM pricing is necessary or appropriate.**

AEP Ohio claims that a “transition period” to RPM pricing is warranted as a result of its previous FRR election.<sup>187</sup> This argument conflicts both with logic and the record. First, as discussed in detail above, the status quo is RPM pricing. Therefore, AEP Ohio is not asking for a transition to market, but is instead asking for a transition from market, to a negotiated figure for forty-one months which is four times market price, and then back to market. Second, also as discussed above, AEP Ohio made its FRR election voluntarily, and presumably in what it believed to be its best interests. There is no reason to punish customers and prevent shopping because AEP Ohio may have made a poor choice. Finally, CRES providers and customers are “locked in” until May 31, 2015 as a result of AEP Ohio’s choice and past positions.<sup>188</sup> As explained by Dr. Shanker in detail, it is anticompetitive to ask CRES providers and Ohio customers to pay dramatically increased rates for capacity during a period in which AEP Ohio’s actions have effectively precluded them from making other arrangements for capacity.<sup>189</sup>

**D. Even If Cost-Based Capacity Pricing Were Proper, And It Is Not, AEP Ohio’s Calculation Is Incorrect.**

As explained in detail in FES’ brief at pages 61-73, AEP Ohio’s calculation of its purported capacity costs is significantly overstated. AEP Ohio’s calculation is incorrect because

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<sup>187</sup> AEP Ohio Brief, p. 104.

<sup>188</sup> FES Brief, p. 52; Shanker Direct, p. 7.

<sup>189</sup> AEP Ohio quotes testimony from Dr. Shanker at hearing regarding the timing of the cost-based rate on the anti-competitive nature of AEP Ohio’s proposal. As recognized by AEP Ohio in its brief, this portion of Dr. Shanker’s testimony was focused solely on the anti-competitive nature of imposing such changes while CRES providers were “locked-in” to purchasing capacity from AEP Ohio. *See* AEP Ohio Brief, p. 104. Dr. Shanker did not agree that a cost-based rate would ever be appropriate, and disputed cost-based pricing for capacity in his testimony. *See, e.g.*, Shanker Direct, p. 11. As such, this testimony should not be read as an approval of cost-based capacity charges in any respect.

S.B. 3 requires that all generation plant investment after January 1, 2001, be recovered solely in the market, and AEP Ohio inappropriately seeks to recover post-2000 costs through its capacity price.<sup>190</sup> AEP Ohio's calculation is also incorrect because Dr. Pearce inappropriately included pre-2001 stranded costs in his capacity cost calculation.<sup>191</sup> Finally, AEP Ohio's calculation is incorrect because AEP Ohio's formula rate fails to include an offset for energy revenue.<sup>192</sup>

Dr. Lesser analyzed each of these deficiencies in detail, and determined that AEP Ohio's actual capacity cost is \$57.35/MW-day. AEP Ohio has contested Dr. Lesser's conclusions and has claimed that Dr. Lesser's calculations should be rejected for a variety of reasons. AEP Ohio's position is incorrect, and each of these issues is discussed in detail below.

**1. S.B. 3 requires that all generation plant investment after January 1, 2001 be recovered solely in the market, and AEP Ohio inappropriately seeks to recover post-2000 costs through its capacity rate.**

AEP Ohio has not contested that it is seeking to recover post-2000 generation costs through its capacity charge.<sup>193</sup> AEP Ohio has admitted that under S.B. 3, all generation plant investment after January 1, 2001 was to be recovered solely in the market.<sup>194</sup> AEP Ohio also admitted that "[a]s part of the settlement in Case No. 99-1729-EL-ETP and 99-1730 EL-ETP ("ETP Cases"), AEP Ohio agreed not to pursue SB 3's opportunity for recovery of stranded generation investment."<sup>195</sup> These admissions conclusively establish that AEP Ohio's proposed

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<sup>190</sup> FES Brief, pp. 61-64, 67-68.

<sup>191</sup> FES Brief, pp. 66-67.

<sup>192</sup> FES Brief, pp. 68-70.

<sup>193</sup> See AEP Ohio Brief, pp. 118-124.

<sup>194</sup> R.C. § 4928.01(A)(28); AEP Ohio Brief, p. 118; FES Brief, pp. 61-64.

<sup>195</sup> AEP Ohio Brief, p. 118.

capacity cost calculation is contrary to law and inappropriate, and that AEP Ohio's proposed formula rate must be rejected for all purposes.

Despite these conclusive admissions, AEP Ohio has offered several arguments suggesting that post-2000 investment may be properly included in its capacity cost calculation. Each lacks merit, as discussed below.

**a. S.B. 3 contained no exception for “wholesale” prices**

AEP Ohio claims that, because the capacity charges at issue are “wholesale” prices, S.B. 3 and the Commission's orders in the ETP Cases are not relevant.<sup>196</sup> AEP Ohio failed to cite any authority in support of its position because there is no such authority. S.B. 3 was not limited to retail charges. Instead, the statute expressly prohibits the recovery of post-2000 investment as sought by AEP Ohio.<sup>197</sup>

This argument also ignores the retail application of the charges at issue. AEP Ohio has made an FRR election which forces customers to purchase their capacity from AEP Ohio. Therefore, this is not simply a wholesale charge which stands in a vacuum. Instead, it is a charge which will be directly applicable to every shopping customer forced to pay AEP Ohio's above-market capacity charges through no choice of their own or of their CRES provider.

In light of AEP Ohio's conclusive admissions above regarding S.B. 3 and the ETP Cases, and AEP Ohio's failure to cite any authority which would justify excluding purported “wholesale” charges from the scope of S.B. 3, this argument should be rejected.

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<sup>196</sup> AEP Ohio Brief, pp. 118-19.

<sup>197</sup> See R.C. § 4928.17(A).

**b. Past Commission approval of environmental expenses does not authorize recovery of post-2000 investment.**

AEP Ohio next argues, *once again without citation to authority*, that the Commission has “not excluded any significant generation plant costs from the Companies’ retail SSO rates.”<sup>198</sup> This argument is curious because AEP Ohio has repeatedly admitted its generation rates are not cost-based.<sup>199</sup> As AEP Ohio’s generation rates are not based on costs, there could not have been any specific cost-based recovery through past generation rates.

Presumably, AEP Ohio intended to reference only “specific recovery of environmental compliance investments” instead of generation costs in total.<sup>200</sup> AEP Ohio never explains how past recovery for specific environmental investments somehow means that it has been allowed to recover post-2000 investments. Instead of providing this analysis, AEP Ohio argues that its plants would not have been as profitable without these investments.<sup>201</sup> This is simply irrelevant. S.B. 3 required that AEP Ohio’s generation compete in the competitive market. Nothing in S.B. 221 changed this express requirement.

This argument also fails for a more practical reason. AEP Ohio admits that it has already been compensated for the environmental compliance costs.<sup>202</sup> However, Dr. Pearce did not subtract this prior cost-recovery when calculating AEP Ohio’s capacity charge.<sup>203</sup> This means that AEP Ohio is seeking to recover for the same environmental compliance costs twice: once through the EICCR and once through a capacity charge. This double recovery violates basic

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<sup>198</sup> AEP Ohio Brief, p. 119.

<sup>199</sup> See, e.g., Direct Testimony of David M. Roush, AEP Ex. 2 (“Roush Direct”), pp. 8-9.

<sup>200</sup> AEP Ohio Brief, p. 119.

<sup>201</sup> AEP Ohio Brief, p. 120. AEP Ohio also failed to present any evidence quantifying these expenses, showing how these expenses increased or maintained energy output, or that these expenses were not required by environmental regulations.

<sup>202</sup> AEP Ohio Brief, pp. 119-20.

<sup>203</sup> See Direct Testimony of Kelly D. Pearce, AEP Ex. 3, Ex. KDP-1.

ratemaking principles, and is simply a further illustration of the overreaching nature of AEP Ohio's calculation. Moreover, it illustrates why Dr. Lesser's exclusion of post-2001 investment from his capacity charge calculation is correct.

**2. AEP Ohio waived the opportunity to recover stranded costs, and now improperly seeks to recover stranded costs through its capacity charge.**

AEP Ohio does not contest that it includes stranded costs in its capacity charge.<sup>204</sup> However, AEP Ohio argues that it should be able to recover stranded costs because the ETP Cases were based on then-forward projections of market prices and net book value.<sup>205</sup> AEP Ohio does not quantify the amount, if any, by which the ETP-era analysis was allegedly incorrect.<sup>206</sup> As AEP Ohio has not quantified the impact of this alleged error, it is unclear what impact AEP Ohio believes this has on Dr. Lesser's argument, or why it believes this argument is relevant.

Leaving aside AEP Ohio's failure to quantify the impact of this change, AEP Ohio offers no legal basis suggesting that S.B. 3 and the ETP Cases now offer it a second bite at the apple. Instead, AEP Ohio only claims that S.B. 221 "now involves several cost-based rate adjustments" in an ESP.<sup>207</sup> AEP Ohio never explains why these unrelated cost-based rate adjustments which are specifically authorized by statute allow it to recover for stranded costs not authorized by statute. There is good reason for this failure to cite authority, because nothing in S.B. 3 or S.B. 221 allow for a "do over" of the ETP Cases based on current knowledge. This makes sense, because allowing for a retrospective review of stranded costs would mean that AEP Ohio could constantly be changing the definition of which costs were stranded based on then current market prices. This is not the law in Ohio. S.B. 221 expressly stated that either an ESP or an MRO

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<sup>204</sup> AEP Ohio Brief, p. 120.

<sup>205</sup> AEP Ohio Brief, pp. 120-122.

<sup>206</sup> AEP Ohio Brief, pp. 120-122.

<sup>207</sup> AEP Ohio Brief, p. 123.

“shall exclude any previously authorized allowances for transition costs.”<sup>208</sup> AEP Ohio acknowledged that S.B. 3 prohibits recovery of stranded costs, and that it waived the right to recovery for stranded generation costs as part of the ETP Cases.<sup>209</sup> These admissions are conclusive, and establish that AEP Ohio cannot legally include stranded costs in a cost-based capacity calculation.

Finally, AEP Ohio argues that because it is only seeking to recover stranded costs from 2012-2015, and it was not permitted to charge a market rate in the past, that it should be permitted to collect stranded costs now.<sup>210</sup> Even if this is true – and one ignores AEP Ohio’s express agreement to waive recovery of stranded costs in the ESP Cases – it is irrelevant. Under S.B. 3, S.B. 221, and the ETP Cases, AEP Ohio is no longer permitted to recover stranded costs. These authorities do not allow for recovery of costs now, even if only for a “brief” time. AEP Ohio has offered no authority to the contrary. Moreover, this ignores AEP Ohio’s responsibility in this situation. If AEP Ohio had followed Ohio law and separated its generation assets it could have gone to market in the past. Instead, it chose to remain vertically integrated and to pursue an ESP in Case No. 08-917-EL-SSO. As AEP Ohio made this choice, AEP Ohio may not credibly claim that S.B. 221 caused it not to recover market rates.

**3. AEP Ohio’s formula rate fails to include an offset for energy-related sales.**

As explained in detail in FES’ Brief at pages 68-70, Dr. Lesser concluded that AEP Ohio’s formula rate overstated capacity costs by failing to include an offset for energy-related sales. AEP Ohio recovers a portion of its fixed costs when it makes energy-related sales for resale because revenues received from those sales that exceed AEP Ohio’s variable O&M plus

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<sup>208</sup> R.C. § 4928.141(A).

<sup>209</sup> AEP Ohio Brief, p. 118.

<sup>210</sup> AEP Ohio Brief, pp. 122-23.



fuel costs recover a portion of its embedded capacity costs.<sup>211</sup> Thus, AEP Ohio recovers a portion of its embedded costs twice: first, through its embedded capacity cost and second through off-system energy sales.<sup>212</sup> Dr. Lesser found that AEP Ohio overstated its capacity costs by \$248 million by failing to include an offset for energy sales.<sup>213</sup>

AEP Ohio has not contested that it recovers a portion of its capacity costs through energy sales. Instead, AEP Ohio argues that Dr. Lesser's calculation of that margin was incorrect. As discussed in detail below, AEP Ohio's arguments each fail.

**a. No fuel deferral adjustment is necessary or appropriate.**

AEP Ohio argues that Dr. Lesser should have included an adjustment of \$130 million because the actual expenditures for fuel by AEP Ohio were \$130 million more than the amount reported in Account 501 due to fuel deferrals.<sup>214</sup> As explained in detail in FES' brief, this was not an error.<sup>215</sup> On cross-examination Mr. Nelson admitted that the very fuel deferrals on which he based his opinion were already going to be recovered on a non-byassable basis through the PIRR.<sup>216</sup> Because AEP Ohio would automatically recover these deferrals through the PIRR even if all customers shopped, including them again in the cost-based capacity price to be charged to CRES suppliers would result in double-recovery of these costs. Accordingly, no adjustment to Dr. Lesser's calculation is necessary or appropriate.

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<sup>211</sup> Lesser Direct, p. 24.

<sup>212</sup> Lesser Direct, p. 24.

<sup>213</sup> Lesser Direct, p. 27.

<sup>214</sup> AEP Ohio Brief, p. 106.

<sup>215</sup> FES Brief, p. 72.

<sup>216</sup> Tr. Vol. XII, p. 2205.

**b. The Interconnection Agreement does not authorize a double recovery through energy sales.**

AEP Ohio next attacks Dr. Lesser's energy offset calculation by claiming that the Interconnection Agreement requires AEP Ohio to share energy revenue with other AEP entities.<sup>217</sup> As a preliminary matter, AEP Ohio and the other AEP entities gave each other notice on December 17, 2010 that they were terminating the Interconnection Agreement.<sup>218</sup> As a result of this decision, it is unclear whether this "sharing" of energy margins will continue in the future.

Leaving aside the uncertain nature of the continued sharing of energy margins, double recovery is still improper, whether it is shared with other entities or not. By failing to include a credit for the impact of energy receipts on capacity costs, AEP Ohio has overstated its capacity costs, and its sharing of this double recovery does not impact the conclusion that it is a double recovery.

AEP Ohio's position is also inappropriate because it assumes that the Interconnection Agreement would require an absurd result. When customers stay with AEP Ohio, they have a first call on AEP Ohio's energy at cost.<sup>219</sup> Under AEP Ohio's reading of the Interconnection Agreement, when those same customers shop, that energy is then sold in a manner that gives customers in other states a first call on the profits from that energy, despite the fact that these margins are earned on energy which would otherwise be sold to Ohio customers.<sup>220</sup> This is not symmetric or supportive of retail competition, and would result in a windfall to customers in other jurisdictions.<sup>221</sup> Mr. Schnitzer concluded that other jurisdictions have made modifications

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<sup>217</sup> AEP Ohio Brief, pp. 106-107.

<sup>218</sup> AEP Ohio Brief, p. 76.

<sup>219</sup> Tr. Vol. VII, p. 1400.

<sup>220</sup> Tr. Vol. VII, p. 1400.

<sup>221</sup> Tr. Vol. VII, p. 1400.

to prevent such absurd results, and that Ohio should do the same to the Interconnection Agreement. As Mr. Schnitzer put it:

“When you're asking yourself how should retail competition be implemented, is it reasonable to leave in place an agreement which says if you don't shop, you get the benefit of low-cost energy at cost, and if you do shop, costs for Ohio collectively go up by roughly \$500 million a year, that to me is not a reasonable agreement to be operating under in this kind of a world and it would be reasonable to modify it.”

Tr. Vol. VII, p. 1401.

Indeed, AEP Ohio witness Nelson admitted that the pool's operating committee already has agreed to modification of the Pool Agreement to reflect customer shopping.<sup>222</sup> This modification was necessary because, when the Pool Agreement was developed, it did not envision customer shopping.<sup>223</sup> Although Mr. Nelson confessed that he had not conducted an analysis of the impact of a CBP on the Pool Agreement,<sup>224</sup> it is clear that, because AEP Ohio has made the FRR election, a CBP would have no impact on AEP Ohio's provision of capacity under the Pool Agreement through May 31, 2015.<sup>225</sup> AEP Ohio agreed that the Pool Agreement does not explicitly preclude AEP Ohio from participating in a wholesale power procurement auction for its SSO load.<sup>226</sup> Nevertheless, Mr. Nelson recognized that a CBP likely would require another meeting of the pool operating committee because, as with existing retail shopping, the

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<sup>222</sup> Tr. Vol. V, pp. 717-18.

<sup>223</sup> Tr. Vol. V, p. 718.

<sup>224</sup> Mr. Nelson did testify that a CBP prior to corporate separation could create a financial exposure for AEP Ohio, which he explained simply meant that AEP Ohio might make less money from the generation it now sells to captive SSO customers. Tr. Vol. V, p. 724. He agreed that AEP Ohio could suffer less of a financial impact if it participated in the CBP. Tr. Vol. V, pp. 724-25.

<sup>225</sup> Tr. Vol. V, pp. 718-19, 721.

<sup>226</sup> FES Exh. 12.

Pool Agreement does not envision the supply of SSO load through a CBP.<sup>227</sup> Any potentially adverse impact of a CBP on AEP Ohio under the Pool Agreement could be resolved through that pool operating committee meeting, as suggested by Mr. Schnitzer. Indeed, Mr. Nelson agreed that a CBP likely would “put the nail in the coffin” of the 40%/60% margin sharing AEP Ohio relies upon in its Brief.<sup>228</sup> This is not a hypothetical exercise, as claimed by AEP Ohio, since AEP Ohio and the other pool members already have adjusted the Pool Agreement to reflect real-world retail shopping.<sup>229</sup>

AEP Ohio clearly stated that it anticipated terminating the Interconnection Agreement without the Partial Stipulation.<sup>230</sup> Despite this admission, AEP Ohio assumes a massive transfer of dollars from AEP Ohio to out-of-state AEP affiliates who are short on energy. This doesn’t make sense, because AEP Ohio is a net seller of energy into the pool at prices which are below market. Therefore, AEP Ohio would have the Commission ignore the cost to OPCo associated with selling energy into the pool at below-market prices, while at the same time preventing CSP from benefiting from the pool by buying energy at below-market prices. This result doesn’t make sense. Dr. Lesser and Mr. Schnitzer’s calculation of AEP Ohio’s energy margin was correct, and AEP Ohio’s position lacks merit.

**c. AEP Ohio’s proposed “shared basis” for energy resale margins lacks record support of any kind.**

AEP Ohio also claims that Dr. Lesser should not have credited all energy margins to customers, and instead should have “shared” these margins with AEP Ohio.<sup>231</sup> AEP Ohio

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<sup>227</sup> Tr. Vol. V, pp. 721-23.

<sup>228</sup> Tr. Vol. V, p. 723; AEP Ohio Brief, pp. 106-107, 109.

<sup>229</sup> AEP Ohio Brief, p. 109; Tr. Vol. V, pp. 717-718.

<sup>230</sup> Tr. Vol. V, p. 693.

<sup>231</sup> AEP Ohio Brief, p. 107.

references an explanation from Dr. Pearce in support of this argument, but nothing in Dr. Pearce's testimony addresses this issue.<sup>232</sup> At no point does Dr. Pearce explain why a sharing of energy margins would be appropriate, much less a justification for his proposed 50% sharing margin when customers are paying for 100% of the cost of the capacity used to create these margins. As AEP Ohio has failed to provide any record evidence establishing that any sharing of this margin is necessary or appropriate, the argument must be rejected for lack of evidence.

**4. AEP Ohio's actual capacity cost is \$57.35/MW-day and customers receive no "benefit" by paying a higher price.**

As explained above, each of AEP Ohio's criticisms lack merit. AEP Ohio has overstated its claimed capacity cost of \$355.72/MW-day significantly, and its true capacity cost is \$57.35/MW-day.<sup>233</sup> AEP Ohio uses an artificially inflated capacity compensation mechanism, which has never been adopted in Ohio, to claim that its customers receive a benefit of \$856 million because the Partial Stipulation does not require them to pay the inappropriate above-market capacity charge originally proposed by AEP Ohio. AEP Ohio also claims, without citation or explanation, that the blend of RPM pricing and the \$255/MW-day negotiated pricing could possibly be below RPM prices at some unidentified point.<sup>234</sup> This comparison to AEP Ohio's litigation position, as opposed to the results of an MRO based on competitive prices, is invalid as a matter of law and should be rejected. As correctly explained by Staff witness Fortney's lottery example, simply because AEP Ohio would have liked to charge this above-

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<sup>232</sup> See AEP Ohio Brief, p. 107; Pearce Direct, p. 10 (only referencing the size of AEP Ohio's proposed energy credit); Pearce Direct, Ex. KDP-3 (providing the calculation for this credit without explanation).

<sup>233</sup> Lesser Direct, p. 30.

<sup>234</sup> AEP Ohio Brief, p. 122. AEP Ohio fails to acknowledge that no customers will ever pay the proposed "blended" capacity charge. Customers will pay either RPM prices or \$255/MW-day. AEP Ohio also fails to acknowledge that RPM prices are below the "blended" capacity charge in every year of the Proposed ESP by definition, since \$255/MW-day is higher than RPM prices for the entire relevant period.

market rate does not make the actual above-market costs of the Partial Stipulation a “benefit” to customers.

**E. The Negotiated Capacity Price Is Not A Benefit Of The ESP, And The “Certainty” Accompanying This Above-Market Price Is Not Beneficial To Customers.**

Several parties have claimed that the Partial Stipulation’s resolution of the 10-2929 Docket constitutes a benefit of the Partial Stipulation, and that it is a reasonable settlement of the litigation positions in that case. There are two fundamental flaws in that argument. First, the 10-2929 Docket is separate from the Proposed ESP’s SSO provisions that the Commission is comparing to an MRO. Even if there were a benefit associated with settling this case (which there is not), it is not a benefit of the Proposed ESP. Second, regulatory certainty for customers and litigants does not outweigh \$1 billion in higher prices for customers.<sup>235</sup>

**1. The resolution of the 10-2929 Docket is not a “benefit” of the Proposed ESP.**

AEP Ohio witness Allen calculated the difference between AEP Ohio’s proposed, allegedly cost-based capacity charge and RPM market rates for the limited amount of market-based capacity made available during each year of the Partial Stipulation as having a net present value of \$856 million.<sup>236</sup> Some parties have relied on this supposed “benefit” as a benefit of the Partial Stipulation.<sup>237</sup>

Even if Mr. Allen’s calculation was correct (which it is not, as discussed above), and resolution of the 10-2929 Docket is a benefit of the Partial Stipulation, resolution of the 10-2929 Docket is not a benefit associated with the Proposed ESP. The 10-2929 Docket is a separate case

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<sup>235</sup> Lesser Direct, p. 11 (finding that AEP Ohio is imposing a \$1.27 billion cost on customers who are not eligible to obtain market capacity prices).

<sup>236</sup> Allen Direct, WAA-6; Tr. Vol. III, p. 433-435.

<sup>237</sup> See, e.g., Staff Brief, p. 6, 10.

from the Proposed ESP, and the resolution of the 10-2929 Docket is not a benefit of the Proposed ESP when compared with an MRO. AEP Ohio acknowledged the essential difference in these two points in its brief by separating its analysis regarding the capacity pricing issue (AEP Ohio Brief, Section V) from its analysis regarding the ESP vs. MRO test (AEP Ohio Brief, Section VI). While FES vigorously disagrees that the resolution reached by the parties in the 10-2929 Docket constitutes a benefit in any respect, under no circumstances can it be considered a benefit of the Proposed ESP.

## **2. Regulatory certainty does not outweigh higher prices.**

Several parties have claimed that the regulatory certainty associated with the Partial Stipulation is significant, and that avoiding the litigation that AEP Ohio repeatedly threatens is worthwhile.<sup>238</sup> RESA, Exelon, and Constellation refer to the resolution of the 10-2929 Docket as removing a “cloud” on the Ohio retail electric market and providing clarity to CRES providers.<sup>239</sup> Avoiding litigation regarding a charge that these same parties agree should not ever have been proposed is not worth \$1 billion in excess costs to customers as compared to an MRO.<sup>240</sup> This “regulatory certainty” is also not worth artificially limiting competitive choice in Ohio until May 31, 2015.

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<sup>238</sup> See, e.g., AEP Ohio Brief, p. 99 (referencing AEP Ohio threat of litigation for confiscatory regulation arising from a fully-litigated decision on capacity pricing); Exelon Brief, pp. 7, 10; RESA Brief, pp. 13-14; Constellation Brief, p. 10.

<sup>239</sup> RESA Brief, p. 14 (citing Exelon at Tr. Vol. VI, pp. 1013-1015); Constellation Brief, p. 10.

<sup>240</sup> See Lesser Direct, p. 10.

**V. THE PARTIAL STIPULATION UNREASONABLY DELAYS FOR THREE AND A HALF MORE YEARS THE OPPORTUNITY FOR EFFECTIVE COMPETITION, WHICH INCREASES COSTS TO AEP OHIO CUSTOMERS BY \$1 BILLION.**

**A. The Signatory Parties Recognize The Benefits Of Competition.**

The Signatory CRES Parties' Briefs provide an excellent summary and confirmation that a competitive market for retail electric service benefits "customers and the public interest."<sup>241</sup> Exelon acknowledges that "under such a process, customers will have the opportunity to choose less costly options rather than be captive to one provider."<sup>242</sup> Exelon also acknowledges that, under a competitive process:

All power generation units will have to compete on a best-price basis with other resources in the market for the right to serve default customer load. Such competition will yield lower default service rates and will foster competition at the retail level by giving customers a fixed-rate default offer that they can readily compare to retail offers.<sup>243</sup>

Similarly, Constellation argues that "[p]ublic procurement of energy and capacity would result in AEP Ohio's customers receiving the lowest priced electricity along with the most innovative service options. Competitive bidding would also encourage retail and wholesale competition development and investment in Ohio."<sup>244</sup>

The problem, of course, is that their conclusion that the Partial Stipulation "benefits consumers through competitive procurement of both energy and capacity"<sup>245</sup> actually describes only the last twelve months of a fifty-three month above-market rate plan. The Partial

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<sup>241</sup> Exelon Brief, p. 6.

<sup>242</sup> Exelon Brief, p. 6.

<sup>243</sup> Exelon Brief, pp. 6-7; *see also* RESA Brief, p. 10 (supporting Exelon's arguments and testimony regarding the benefits of competition).

<sup>244</sup> Constellation Brief, p. 9 (emphasis added).

<sup>245</sup> Exelon Brief, p. 7.



Stipulation and the Proposed ESP block wholesale and retail competition, with all the benefits that everyone lauds, until June 2015. Wholesale competition is blocked, as described in Section III above, through the Proposed ESP's delayed use of a CBP to procure SSO supply until June 2015, without any good reason for the delay. Retail competition is blocked through the Partial Stipulation's caps on RPM-priced capacity and the above-market capacity price for all customers in excess of the caps.

**B. The Signatory Parties Cannot Credibly Claim That The RPM Price Caps Will Not Constrain Shopping.**

Despite substantial evidence (including their own witnesses' admissions to the contrary), the Signatory Parties try to argue that the arbitrary, negotiated \$255/MW-day capacity price will not effectively preclude retail competition above the caps. AEP Ohio's own executive admitted that "the thought and the theory is that the shopping will be constrained to the discounted RPM price," and that AEP Ohio "should see no more shopping than the 20%, 30%, 40% levels that are included in the stipulation."<sup>246</sup> RESA witness Ringenbach similarly agreed that the \$255/MW-day price would limit or constrain shopping.<sup>247</sup> Constellation witness Fein agreed that a 200% increase in capacity prices over RPM prices "would adversely affect shopping."<sup>248</sup> Staff witness Fortney also agreed that a higher capacity price would discourage shopping by limiting CRES providers' ability to make as good an offer.<sup>249</sup>

The Signatory Parties look primarily to AEP Ohio witness Allen's testimony that CRES providers *could* have headroom at the \$255/MW-day capacity price to argue that the RPM price caps do not constrain shopping. At best, and without fixing any of the errors in his calculation,

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<sup>246</sup> Banks Direct, p. 36, Exs. TCB-8 and -9 (emphasis added).

<sup>247</sup> Tr. Vol. IV, p. 543-44.

<sup>248</sup> Tr. Vol. VI, pp. 970-971.

<sup>249</sup> Tr. Vol. X, pp. 1693-1694.

Mr. Allen’s testimony concluded that the \$255/MW-day price would leave “headroom” of less than 1% margin.<sup>250</sup> When his calculation is corrected to include certain costs that AEP Ohio witness Thomas testified should be included in a competitive price,<sup>251</sup> that 1% headroom disappeared, and in fact, became negative.<sup>252</sup>

Regardless, as FES explained in its Initial Brief, Mr. Allen’s testimony lacks any credibility.<sup>253</sup> Given his lack of any experience with CRES providers, he has no basis to opine that such economically irrational behavior – offering a product in a competitive market below market price – is something that a CRES provider would actually (as opposed to theoretically) do.<sup>254</sup> FES witness Schnitzer clearly testified that when capacity is priced at \$255/MW-day, the CRES cost-to-serve exceeds the Proposed ESP price-to-compare and, as a result, CRES providers would have to serve customers at a loss in order to provide customers with savings from the price-to-compare.<sup>255</sup> In addition, Ms. Thomas’ calculation of the market costs of a CRES provider when capacity is priced at \$255/MW-day is virtually identical to that of Mr.

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<sup>250</sup> Tr. Vol. XII, pp. 2158 (confidential).

<sup>251</sup> Mr. Allen excluded a risk adder and an administration cost charge that Ms. Thomas had included. *See* Rebuttal Testimony of William A. Allen on behalf of Columbus Southern Power Company and Ohio Power Company, AEP Exs. 20A and 20B (“Allen Rebuttal”), p. 8 (removing the Transaction Risk Adder and Retail Administration Charge from Ms. Thomas’ analysis); Thomas Direct, Ex. LJT-1 (including these charges). These were charges that Ms. Thomas believed represented likely charges – and reasonable values for those charges – that would be included in a wholesale supplier’s bid for SSO load. Thomas Direct, Ex. LJT-1.

At best, the analyses of AEP Ohio’s witnesses are inconsistent; at worst, they are disingenuous. When attempting to calculate an MRO price, Ms. Thomas had no problems with adding certain adders and administrative costs. But when it came to comparing CRES providers’ costs with the SSO price, Mr. Allen jettisoned those charges to squeeze those costs in below the SSO price. Such obvious analysis skewing, game-playing lacks any credibility and should be rejected.

<sup>252</sup> FES Brief, pp. 98-99.

<sup>253</sup> *See* FES Brief, pp. 98-100; AEP Ohio Brief, p. 111.

<sup>254</sup> *See* FES Brief, p. 98.

<sup>255</sup> Schnitzer Direct, p. 36.

Schnitzer's calculation.<sup>256</sup> Therefore, the same conclusion can be reached using AEP Ohio's own calculation of CRES market costs. There can be no clearer evidence of the Partial Stipulation's negative impact on retail competition in AEP Ohio's service territory.<sup>257</sup>

The Signatory Parties also argue that the Proposed Stipulation does not limit shopping because CRES providers could offer long term contracts that would include capacity priced at \$255/MW-day initially and at RPM prices later.<sup>258</sup> First, of course, neither CRES providers nor customers have the "option" to receive RPM-priced capacity during any given year of the Proposed ESP. A customer entering into such a contract is not guaranteed to be eligible for RPM-priced capacity in subsequent years. That uncertainty alone would constrain shopping. Exelon acknowledged in a separate context that uncertainty in pricing hinders shopping. "Stated simply and as a practical matter, it is difficult to quote retail prices to potential customers with the caveat that the actual rate is subject to the final resolution of FERC proceedings."<sup>259</sup> The same holds true for uncertainty in the possibility of later receiving RPM-priced capacity. "If customers don't know [what price they would receive], they are less likely to shop."<sup>260</sup> Therefore, CRES providers and customers are left with the limited and constrained shopping "available" at the \$255/MW-day price.<sup>261</sup> Given the number of CRES suppliers who offered

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<sup>256</sup> See Thomas Direct, Ex. LJT-1.

<sup>257</sup> AEP Ohio also relies upon Dr. Lesser's comparison of AEP Ohio's net, energy-related production costs and its net remaining base generation revenues to concoct a "headroom" argument (AEP Ohio Brief, pp. 111-12), but this reliance is unfounded. Dr. Lesser did not show, as suggested by AEP Ohio, that the capacity price paid by SSO customers is \$335.50/MW-day. To the contrary, Dr. Lesser's analysis simply shows the unlikelihood that AEP Ohio is charging SSO customers \$355/MW-day. Lesser Direct, pp. 37-38. Plus, his analysis had nothing to with the headroom that may be available to CRES providers.

<sup>258</sup> See AEP Ohio Brief, p. 111.

<sup>259</sup> Exelon Brief, p. 11.

<sup>260</sup> Banks Direct, p. 29.

witnesses, one would expect that if such a transaction were likely, one of them would have spoken about that possibility in detail.

Indeed, the possibility of these inadequate contingencies and the (at best) less than 1% headroom available at the \$255/MW-day capacity price undermine the Signatory Parties' reliance on RESA witness Ringenbach's statement that her company is *making offers* at the \$255/MW-day capacity price.<sup>262</sup> This hearsay statement is completely unsupported; no one knows any of the details of such offers or any contingencies underlying it. Notably, Ms. Ringenbach did not see fit to include any evidence of such offers into her direct testimony or RESA's Initial Brief. As AEP Ohio's executive admitted, CRES suppliers and Staff recognized, and Mr. Schnitzer calculated, the \$255/MW-day capacity price will limit or constrain shopping.

AEP Ohio's reference to the 1,500 commercial and industrial customers who have switched since September 7, 2011<sup>263</sup> also has no relevance to whether customers will shop if they instead receive the \$255/MW-day price for capacity. By switching now, those customers likely will receive RPM-priced capacity during the term of the current ESP. Given the availability of allotments as of the beginning of 2012, it is likely that those customers who are already in the queue would get the remaining allotments available as of January 1, 2012 (at the expense of the unused allotment for residential customers). Further, as AEP Ohio witness Allen admitted, the

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<sup>261</sup> Staff's suggestion that the Partial Stipulation's two different (and discriminatory) capacity prices provide "optionality" for CRES providers should be disregarded. Staff Brief, p. 18 ("The stipulation includes two levels of discounted capacity to CRES providers that provide sufficient optionality for a CRES provider to compete through shopping.") The two capacity prices provide no "options" to CRES providers or customers. Either customers seeking to shop will be charged RPM prices or they will pay four-times more under the arbitrary, negotiated price. To the extent Staff intends to refer, as others do, to the idea that "CRES providers have the option to structure multi-year contracts with customers that could allow them to purchase capacity at \$255/MW-day in 2012 and/or 2013 and at RPM in the remaining years of the contract" (Staff Brief, p. 18), FES had refuted, and again refutes above, that unrealistic "option."

<sup>262</sup> See AEP Ohio Brief, p. 110.

<sup>263</sup> See AEP Ohio Brief, p. 110.

terms of those 1,500 customers' contracts are unknown.<sup>264</sup> The contracts may include provisions that would allow the customers to void the contracts if they are unable to get RPM-priced capacity. As such, the 1,500 customers provide no evidence that retail competition would occur at the Partial Stipulation's \$255/MW-day price for capacity.

AEP Ohio's other allegedly supporting citations do not substantiate its arguments. For example, AEP Ohio cites Signatory CRES Party witnesses as supporting the Partial Stipulation because the capacity prices would be less than AEP Ohio had originally proposed.<sup>265</sup> First, as noted above, this is not the standard for approval of the Proposed ESP or the Partial Stipulation. Moreover, of course, both witnesses also testified that the "reduced" \$255/MW-day price would limit or constrain shopping.<sup>266</sup> AEP Ohio also is disingenuous in describing IEU witness Murray's testimony regarding the impact of the capacity price caps.<sup>267</sup> Mr. Murray did not acknowledge, as AEP Ohio suggests, that the Partial Stipulation does not impose a literal or absolute cap on shopping. Rather, Mr. Murray testified that, in his judgment "a CRES provider couldn't economically make an offer at \$255 a megawatt-day" and that such offers were possible if a CRES provider wanted to take a "loss leader."<sup>268</sup>

The Signatory Parties completely overreach<sup>269</sup> in arguing that the \$255/MW-day capacity price will not limit or constrain retail competition. Their arguments lack any merit or support, and are contradicted by their own testimony and statements. The caps on RPM-priced capacity

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<sup>264</sup> Tr. Vol. XII, p. 2083.

<sup>265</sup> AEP Ohio Brief, pp. 98-99.

<sup>266</sup> Tr. Vol. IV, pp. 543, 544; Tr. Vol. VI, pp. 970-71.

<sup>267</sup> See AEP Ohio Brief, pp. 112-113.

<sup>268</sup> See Tr. Vol. XI, pp. 1885-1886.

<sup>269</sup> For example, Staff suggests that the Partial Stipulation's \$255/MW-day capacity price that is four times higher than market will "support growth of robust competitive supply options for customers." Staff Brief, pp. 10-11 (emphasis added); see also Exelon Brief, p. 15 (Partial Stipulation "provides significant pro-competitive benefits").

reflect only minimal increases above current shopping levels and would maintain shopping levels in AEP Ohio's service territory that are the lowest in the state.<sup>270</sup>

**C. The Signatory Parties Ignore The Significant Adverse Impacts On Governmental Aggregation, Which Represents Residential Customers' Most Significant Opportunity To Shop.**

FES' Initial Brief thoroughly explained how the Partial Stipulation would violate the Commission's charge to "encourage and promote large-scale governmental aggregation."<sup>271</sup> AEP Ohio, at best, is apathetic about governmental aggregation and none of the Signatory Parties has any interest in governmental aggregation.<sup>272</sup> Not surprisingly, the Signatory Parties devote no attention to governmental aggregation. In fact, AEP Ohio's Brief does not even mention governmental aggregation. Only Staff referred to governmental aggregation and it was fleeting and easily dismissed. Specifically, Staff cites AEP Ohio witness Allen's suggestion in rebuttal that governmental aggregation has continued or increased since the Partial Stipulation was filed.<sup>273</sup> However, as shown in FES' Initial Brief, Mr. Allen's rebuttal testimony was not credible because he failed to understand that, in accordance with Ohio law, the November ballot initiatives were submitted in early August 2011 – well before the Partial Stipulation was signed and when AEP Ohio provided all capacity at RPM market-based prices.<sup>274</sup>

Governmental aggregation provides significant benefits for residential and smaller commercial customers, who without the aggregation of their interests may not be able to secure

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<sup>270</sup> See FES Brief, pp. 100-101.

<sup>271</sup> R.C. §§ 4928.02(K), 4928.20; *see also* O.A.C. 4901:1-35-03(C)(6), (7).

<sup>272</sup> Tr. Vol. VI, p. 846; Tr. Vol. III, pp. 398-399; *See* Tr. Vol. VII, p. 975 (no Constellation aggregation contracts); Tr. Vol. VI, p. 1041 (no Exelon aggregation contracts); Tr. Vol. IV, p. 558 (no Direct Energy aggregation contracts); Tr. Vol. IV, p. 558 (no aggregation contracts involving any RESA members); Tr. Vol. VI, p. 1041 (no Exelon aggregation contracts).

<sup>273</sup> Staff Brief, p. 19.

<sup>274</sup> *See* R.C. § 3501.02 (requiring ballots be certified 90 days before general election).

such benefits in the competitive market. These potential benefits are illustrated by the discounts provided to the only two communities in AEP Ohio's service territory to have completed the process, and whose customers enjoy a 5-6% discount off the price-to-compare for residential customers and a 15% discount for small commercial customers.<sup>275</sup> As Staff recognizes, under the Partial Stipulation, governmental aggregation customers "will have the same access to RPM priced capacity as any other customer"<sup>276</sup> – which is little to none. Yet, the right of customers in governmental aggregation programs to shop should be "promote[d]," not ignored or, as is more likely here, discouraged. The only way to "encourage and promote" governmental aggregation and allow other communities in AEP Ohio's territory to enjoy the benefits of governmental aggregation in the context of the Partial Stipulation is to reject it or, at minimum, to exclude governmental aggregation customers from the limitations of the Partial Stipulation's RPM-priced capacity caps.

**D. FES' "Motives" Reflect Ohio Law And The Process Through Which Competition Provides Benefits.**

As the record readily shows, AEP Ohio does not like competition.<sup>277</sup> Its antipathy shows through in its discussion of FES. AEP Ohio suggests that FES' concerns with the Partial Stipulation and its Proposed ESP carry less weight because FES allegedly has "tunnel vision" in favor of competition.<sup>278</sup> Yet, AEP Ohio's attempt to attack FES is only an attack on competition and further demonstrates AEP Ohio's anticompetitive aims.

Competition is Ohio law – not some newfangled product that FES has a patent on. The Commission should be concerned, because AEP Ohio clearly is not, that the Partial Stipulation

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<sup>275</sup> Banks Direct, p. 32; *see also* AEP Ex. 10 (City of Reynoldsburg ordinance).

<sup>276</sup> Staff Brief, p. 19.

<sup>277</sup> *See* FES Brief, pp. 89-91.

<sup>278</sup> AEP Ohio Brief, pp. 113-118.

and its Proposed ESP do not conform to the *state law and policy* that seeks to “ensure effective competition in the provision of retail electric service.”<sup>279</sup> The Commission should be concerned, because AEP Ohio clearly is not, that the Partial Stipulation and the Proposed ESP do not conform to the Commission’s mission to “facilitat[e] an environment that provides competitive choices.”<sup>280</sup>

The fact that it is FES that serves as the party in this proceeding that seeks to ensure compliance with those requirements and goals – together with IEU, OCC, and others – is of no consequence. Yes, FES is interested in providing service to AEP Ohio customers on a wholesale and a retail basis. Yes, FES can and should be able to provide that service now. Yes, FES is capable of providing real and material competition to AEP Ohio within the next three and a half years in which the Partial Stipulation seeks to preclude competition. But FES’ interests in these regards do not undermine its arguments. Rather, FES’ interests emphasize its efforts to ensure CRES providers have the ability to compete in AEP Ohio’s territory and to illustrate how the competitive market benefits customers. FES wants to compete because it can offer lower prices to AEP Ohio’s customers – such as the two governmental aggregation customers in AEP Ohio’s territory that enjoy a 5% and 15% discount to residential and small commercial customers, respectively.<sup>281</sup> Competition will challenge AEP Ohio, FES and other CRES providers to more effectively and efficiently provide retail generation service. These are the exact forces that benefit customers.

The significant adverse impact of the Partial Stipulation on shopping in AEP Ohio’s territory, as demonstrated by FES, adversely affects all CRES providers and their ability to

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<sup>279</sup> R.C. § 4928.02(H).

<sup>280</sup> *See Banks Direct*, p. 5.

<sup>281</sup> *See FES Brief*, p. 117; *see also* AEP Ex. 10.



effectively compete in accordance with Ohio law. Apparently it is lost on AEP Ohio that competition benefits all customers, whether they be FES' shopping customers, AEP Retail's shopping customers, or AEP Ohio's non-shopping customers.<sup>282</sup>

AEP Ohio does not bother to explain how the Partial Stipulation furthers the specific factors that the Commission could consider in limiting competition. (AEP Ohio's listing of the issues in the Commission's mission statement is notable for the same reason.<sup>283</sup>) The only factor that the Partial Stipulation promotes is the financial benefit of AEP Ohio – with a total absence of evidence that without the Partial Stipulation service reliability or stability is in any way harmed.

**E. The Partial Stipulation Represents A Continuation Of AEP Ohio's Past Practices, And The Signatory Parties Do Not Justify The Three And A Half Year Delay To Both Wholesale And Retail Competition.**

Because they cannot and do not dispute that competition benefits customers, the Signatory Parties argue around the failures of the Partial Stipulation and the Proposed ESP to provide those benefits. The Signatory Parties' briefs continue to beat the drum of the "glide-path" to market. They argue that three and a half years provides AEP Ohio with a "reasonable" time to effect corporate separation and position itself for a wholesale CBP. First, there is no record evidence that AEP Ohio could not compete in a wholesale CBP for service starting in 2012 – nor do any of the Signatory Parties present any argument that AEP Ohio cannot.<sup>284</sup> If, in

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<sup>282</sup> AEP Ohio also attacks Mr. Banks' testimony by suggesting that his view is that anything anticompetitive is automatically bad. *See* AEP Ohio Brief, pp. 113-118. This suggestion pulls one sound bite from Mr. Banks' deposition and ignores Mr. Banks' testimony earlier in his deposition that AEP Ohio's inquiry was too limited in scope. Tr. Vol. VII, p. 1289. It also ignores Mr. Banks' testimony at hearing that the Commission can take into account other noncompetitive factors, when permitted by the statute. Tr. Vol. VII, p. 1289; *see also* R.C. § 4928.143(B)(2)(d).

<sup>283</sup> *See* AEP Ohio Brief, pp. 116-117.

<sup>284</sup> Indeed, AEP Ohio's own actions show AEP Ohio could conduct a wholesale CBP immediately. In Case No. 08-917-EL-SSO, AEP Ohio proposed to purchase incremental power on a "slice of system" basis for between 5% and 15% of its load. *See* Case No. 08-917-EL-SSO, Opinion and Order, March 18,

fact, AEP Ohio is unable to situate itself for wholesale competition prior to June 2015 – and that is not a fact, as set forth in the record evidence – then, at a bare minimum, AEP Ohio’s customers should be allowed access to retail competition.

Since 2000, Ohio law has required competition for electric generation service. Ohio law also requires the Commission to promote governmental aggregation. There is no basis in the law, in state policy, or in the record to establish any basis on which to allow AEP Ohio to continue to block wholesale competition (by not including a CBP) and at the same time block its customers’ ability to effectively shop on the retail level (through the many restrictions on shopping, especially the capacity pricing). Similarly, there is no basis to approve the Partial Stipulation’s guarantee to AEP Ohio of: (a) above-market SSO generation revenues; and/or (b) a defined SSO customer base in order ostensibly to protect AEP Ohio’s financial health. AEP Ohio had the opportunity to present such evidence, but it did not. There is no such evidence.

Finally, recent events show the potential benefits to customers associated with wholesale competition. After the most recent FirstEnergy utilities’ auction results were released, Chairman Snitchler said “The wholesale generation auction process continues to yield positive results.”<sup>285</sup> He went on to say that “[c]ompetition and market forces have clearly been shown to help keep electric generation costs low for FirstEnergy customers.”<sup>286</sup> AEP Ohio claims the FirstEnergy utilities’ auction results are substantially similar to the Competitive Benchmark prices it

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2009, p. 15. The fact that AEP Ohio requested a CBP in 2008 conclusively establishes that nothing prevents AEP Ohio from conducting a CBP for its load today.

<sup>285</sup> PUCO press release dated October 26, 2011. Available at

<http://www.puco.ohio.gov/puco/index.cfm/media-room/media-releases/puco-accepts-results-of-firstenergy-auction1/> (last accessed Nov. 17, 2011).

<sup>286</sup> *Id.*

developed through Ms. Thomas.<sup>287</sup> The most recent FirstEnergy auction results are therefore particularly revealing, because AEP was an active participant in these auctions, winning five tranches at a tranche weighted average price of \$52.80/MWh.<sup>288</sup> Notably, these auction results are well below the \$57.47/MWh price from the January 2011 auction for the FirstEnergy utilities,<sup>289</sup> which AEP Ohio acknowledges was approximately \$2.92/MWh less than AEP Ohio's expected bid price.<sup>290</sup> In light of these new auction results showing even lower prices, which AEP successfully participated in, it appears that AEP Ohio's expected bid price is significantly overstated. It also appears that Chairman Snitchler was correct, and that competition has once again kept generation costs low to the benefit of Ohio customers. AEP's participation in these auctions shows that AEP likes competitive markets in Ohio, so long as that competition doesn't take place in AEP Ohio's service territory.

**VI. THE SIGNATORY PARTIES CANNOT REASONABLY DISPUTE THAT THE NEGOTIATIONS WERE IMPROPERLY EXCLUSIONARY AND INSUFFICIENT.**

**A. No One Disputes That The Residential Customer Groups Were Excluded, And The Arguments Regarding FES Are Not Credible.**

While AEP Ohio takes pains to detail the communications and alleged position of FES before FES was excluded, neither AEP Ohio nor any other Signatory Party provides any arguments to rationalize, explain or refute the exclusion of residential customer groups. Exelon notes in passing that different types of interested parties signed on in support of the Partial Stipulation, including residential customers.<sup>291</sup> However, as set forth in briefs of those parties

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<sup>287</sup> AEP Ohio Brief, p. 156.

<sup>288</sup> Case No. 10-1284, Auction Manager Report dated November 16, 2011, p. 5 (Table 2).

<sup>289</sup> AEP Ohio Brief, p. 152.

<sup>290</sup> Thomas Direct, p. 10; AEP Brief, p. 156.

<sup>291</sup> Exelon Brief, p. 5.

who oppose the Partial Stipulation, residential customer groups were affirmatively excluded from the final negotiations and do not support the Partial Stipulation – most notably including OCC. To the extent Exelon’s misguided reference is based on the presence of two municipalities as Signatory Parties, FES’ Initial Brief resoundingly discredited the municipalities’ efforts to represent residential customers here.<sup>292</sup> To the extent Exelon’s reference is based on its suggestion that Staff’s interests are global, Staff’s support also is not enough.<sup>293</sup> Indeed, the logical extension of this argument is that it is unnecessary to have any non-AEP Ohio party support a stipulation if Staff has signed on in support. The Commission has never held that view, nor has the Ohio Supreme Court. As described in FES’ Initial Brief, the exclusion of the residential customer groups in conjunction with the terms and conditions of the Partial Stipulation that unduly burden residential customers should raise the Commission’s concern.<sup>294</sup> For this reason alone – and independent of any other issues involving the negotiations (and there are several), the Partial Stipulation should be not be afforded weight.

As to FES, AEP Ohio’s Brief goes into a dramatic “he said, he said” argument that lacks credibility in response to FES’ rebuttal.<sup>295</sup> AEP Ohio argues that FES witness Banks’ rebuttal testimony was narrowly crafted to deal only with whether FES physically walked out of the meeting in the afternoon of August 26. This argument overlooks the fact that Mr. Banks clearly testified more broadly – in addition to refuting the idea that FES walked out of the meeting – that FES did nothing at the August 26th afternoon meeting to indicate that it was no longer interested

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<sup>292</sup> See FES Brief, pp. 138-141.

<sup>293</sup> See Exelon Brief, p. 5.

<sup>294</sup> See FES Brief, pp. 138-141.

<sup>295</sup> See AEP Ohio Brief, pp. 24-25.

in talking about settlement.<sup>296</sup> Unfortunately for AEP Ohio, its own witness said the same thing. Although it argues in its Brief that “[i]n that meeting, FES conveyed the same message that it did not intend to continue negotiating under the majority’s framework,”<sup>297</sup> Mr. Hamrock clearly testified that he did not see any communication from FES that stated that FES was choosing to stop participating in settlement negotiations.<sup>298</sup> Mr. Hamrock also previously testified that AEP Ohio continued to reach out to parties that were not participating after August 30th, but he did not recall any such communications with FES.<sup>299</sup> It was only on re-direct, after discussions with counsel, that Mr. Hamrock claimed, for the first time, that FES “specifically walked out of that [August 26th afternoon] session and said that they were no longer interested in that framework [being discussed].”<sup>300</sup> Mr. Hamrock’s re-direct testimony lacks credibility and was directly refuted by FES and earlier by Mr. Hamrock. Indeed, AEP Ohio’s suggestion that FES had indicated that, during a meeting in the morning of August 26, it was no longer interested in discussing settlement is rebutted by the facts and logic. If FES had said that in the morning of August 26, why was FES present during a meeting that afternoon? As discussed in FES’ Initial Brief, FES’ exclusion is significant despite the fact that other CRES parties signed on to the Partial Stipulation.<sup>301</sup> Unlike FES, however, the unaffiliated Signatory Party CRES providers

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<sup>296</sup> See Tr. Vol. VII, p. 1186 (“Q: And did FirstEnergy Solutions at that meeting indicate that they were no longer interested in talking about settlement? A: No, we did not.”).

<sup>297</sup> AEP Ohio Brief, p. 25.

<sup>298</sup> Tr. Vol. VI, p. 872.

<sup>299</sup> Direct Testimony of Joseph Hamrock on behalf of Columbus Southern Power Company and Ohio Power Company, AEP Ex. 8 (“Hamrock Direct”), p. 9; Tr. Vol. VI, pp. 872-874.

<sup>300</sup> Tr. Vol. VI, p. 941.

<sup>301</sup> FES Brief, pp. 141-144.

are: not based in Ohio; not currently active in AEP Ohio's service territory; and not currently active in governmental aggregation anywhere in Ohio.<sup>302</sup>

Some of the Signatory Parties make more generic challenges to the exclusion of the non-signatory parties in a “blame the victim” type attack that does not make sense. RESA states that the non-signatory parties' exclusion from the talks “was by their own decision,” but its only authority for that absurd sentiment is the cross-examination of AEP Ohio witness Hamrock, which provides no support for the idea that the non-signatory parties excluded themselves.<sup>303</sup> AEP Ohio attempts to make much of the fact that the non-signatory parties signed a joint defense agreement.<sup>304</sup> AEP Ohio argues that allowing the non-signatory parties into the negotiations “would be like having the other team in the opponent's locker room during a pregame meeting when strategy was being discussed and developed . . . .”<sup>305</sup> This only confirms that it was the Signatory Parties that were excluding the non-signatory parties from the locker room (as opposed to RESA's suggestion that the excluded parties excluded themselves). Moreover, regardless, the fact that certain parties entered into a joint defense agreement says nothing more than that these parties had identified a common interest in what the ESP should look like – and not look like. The locker room analogy illustrates that AEP Ohio viewed the non-signatory parties as adverse before the Partial Stipulation was signed, and that it took measures to keep the Signatory Parties out of the final negotiations.

AEP Ohio's suggestion that it offered an olive branch prior to the signing of the Partial Stipulation is also disingenuous and was rebutted in FES' Initial Brief. Such as it was, the olive

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<sup>302</sup> FES Brief, pp. 141-144.

<sup>303</sup> RESA Brief, p. 8.

<sup>304</sup> AEP Ohio Brief, p. 26.

<sup>305</sup> AEP Ohio Brief, p. 26.

branch came in after 10 p.m. at night, less than twelve hours before the hearing was scheduled to begin the next morning.<sup>306</sup> Such an offer provides “no real or effective opportunity to review, respond to, or negotiate regarding the Partial Stipulation – which spans approximately 30 pages, and involves completely new provisions and different numbers.”<sup>307</sup> Not only were residential customer groups and FES excluded from settlement negotiations, but the rushed manner in which the Partial Stipulation was reviewed and considered raises additional concerns. The Partial Stipulation does not satisfy the first prong of the Commission’s test for the reasonableness of settlement stipulations.

**B. The Signatory Parties Implicitly Recognize That The Partial Stipulation Does Not Satisfy The Commission’s Test Because The Negotiations Involved Little To No Analysis Of The Partial Stipulation’s Terms.**

AEP Ohio specifically acknowledges that one of the factors to be considered regarding the first prong of the Commission’s test for settlement stipulations is “the detail in which the issues in the case were discussed.”<sup>308</sup> AEP Ohio also admits that the Signatory Parties agreed that they would establish after the Partial Stipulation was signed that the Proposed ESP passed the ESP vs. MRO test.<sup>309</sup> Thus, AEP Ohio admits that no such analysis was performed during negotiations before the Partial Stipulation was signed. The Signatory Parties signed on with no understanding of whether the Proposed ESP would pass the statutory test or, for example, that the Proposed ESP would cost customers millions of dollars more than an MRO.

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<sup>306</sup> See Banks Direct, p. 58.

<sup>307</sup> Banks Direct, p. 58.

<sup>308</sup> AEP Ohio Brief, p. 28.

<sup>309</sup> AEP Ohio Brief, p. 30.

AEP Ohio also attempts to minimize IEU witness Murray's testimony regarding the state of negotiations and the Signatory Parties' lack of knowledge or analysis.<sup>310</sup> However, that testimony stands on its own and is based on the Signatory Parties' own discovery responses. While AEP Ohio wants to excuse these negotiation deficiencies on the lack of a statutory requirement that all parties execute their own ESP vs. MRO test, the fact of the matter is that no one performed such a test before the Partial Stipulation was signed, no one assessed the impact of the Partial Stipulation on shopping, no one provided or requested updated shopping data, and the vast majority of the Signatory Parties did not see significant components of the Partial Stipulation before the Partial Stipulation was signed.<sup>311</sup> AEP Ohio also argues that the Signatory Parties were aware of AEP Ohio's testimony in support of the initial ESP application "demonstrating" that the initial ESP was more favorable in the aggregate, and that AEP Ohio's "compromises" "could only improve" the favorable result.<sup>312</sup> This argument is totally unsupported by the record and a bold misrepresentation. Many, if not most, of the Signatory Parties filed testimony in opposition to the initial ESP application. Indeed, it can only be said that the vehement opposition to the initial ESP application required AEP Ohio to begin negotiations seeking approval of an alternative proposal. Accordingly, it cannot be said that the Signatory Parties' analysis satisfies the Commission's standard for serious bargaining that includes an assessment of "the detail in which the issues in the case were discussed."

## **VII. CONCLUSION**

The Commission should reject AEP Ohio's attempts to institute the Proposed ESP, which unnecessarily limits wholesale competition, and the Partial Stipulation, which unjustifiably limits

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<sup>310</sup> See AEP Ohio Brief, pp. 28-30.

<sup>311</sup> See FES Brief, pp. 145-148.

<sup>312</sup> AEP Ohio Brief, p. 30.



retail competition. There is no basis on which to limit for another three and a half years either form of competition – and certainly not both forms of competition. Competition is required by Ohio law and provides significant benefits and lower costs to customers. These benefits and cost savings of competition within AEP Ohio’s territory are large, on the order of \$1 billion or more, and of particular importance to AEP Ohio’s customers and Ohio’s economy now, as the country struggles to right itself in a challenging economy. Other Ohio utilities’ customers receive these benefits; AEP Ohio’s customers deserve them, too.

As set forth in FES’ Brief and this Reply Brief, the Partial Stipulation and the Proposed ESP fail to meet the statutory standard for an ESP<sup>313</sup> and fail to meet the Commission’s standards for a reasonable settlement stipulation.<sup>314</sup> Therefore, the Commission should reject them both based on any of their flaws, including:

**1. The Proposed ESP is not more favorable in the aggregate than the expected results of an MRO.**

- It is undisputed that the Proposed ESP will cost customers more than the expected results of an MRO. The most reasonable estimates show that the Proposed ESP will result in additional costs of \$325-\$800 million.
- AEP Ohio and other Signatory Parties’ attempts to compare the Proposed ESP to AEP Ohio’s litigation position fail to satisfy the statutory ESP vs. MRO test that requires the Commission to compare the Proposed ESP to a market-based MRO.
- Under an MRO, the price of capacity included in the market price is based on market values as required by S.B. 221, and not the “made up” figure included the Partial Stipulation that AEP Ohio relied upon.

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<sup>313</sup> R.C. § 4928.143(C)(1).

<sup>314</sup> *In the Matter of the Application of Duke Energy Ohio, Inc. for Approval of the Establishment of Rider BTR and Associated Tariff Approval*, Case No. 11-2641-EL-RDR *et al.*, Opinion and Order (May 25, 2011) at p. 9; *see also Indus. Energy Consumers of Ohio Power Co. v. Pub. Util. Comm.*, 68 Ohio St.3d 559, 561 (1994); *In the Matter of the Application of 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. 10-388-EL-SSO, Opinion and Order (Aug. 25, 2010) at p. 20.

- AEP Ohio’s quantification of “benefits” relative to AEP Ohio’s initial and unreasonable requests are without merit and should be dismissed.
- None of the Signatory Parties’ attempts to create qualitative “benefits” changes the Proposed ESP into a more favorable option or outweighs its increased cost relative to an MRO.
- The alleged “benefits” either do not relate to the Proposed ESP, are uncertain, and/or are not actually beneficial.

**2. The Partial Stipulation and the Proposed ESP are not the product of serious bargaining among capable, knowledgeable parties.**

- Intervenors representing residential customers (OCC and APJN) were excluded from settlement negotiations, along with FES, which represents AEP Ohio’s immediate competition, and these exclusions should trigger the Supreme Court’s concerns expressed in *Time Warner*.<sup>315</sup>
- The evidence reflects that the Signatory Parties conducted little to no analysis of the Partial Stipulation’s or Proposed ESP’s terms or their impact on AEP Ohio’s customers.

**3. The Partial Stipulation and the Proposed ESP do not, as a package, benefit ratepayers and the public interest.**

- The Proposed ESP is reasonably estimated to cost customers \$325-\$800 million more than the expected results of an MRO and approximately \$1 billion more than a fully competitive ESP offer.
- The Proposed ESP unnecessarily delays wholesale competition for three and a half more years for no good reason.
- The Partial Stipulation’s caps on RPM-priced capacity will preclude the vast majority of AEP Ohio’s customers from enjoying the benefits of retail competition for three and a half more years.
- The Proposed ESP incorporates an unsupported, “placeholder” GRR that would only impose uneconomic and unnecessary generation costs on AEP Ohio’s customers.
- The Proposed ESP incorporates an unsupported, “placeholder” PMR which would inappropriately make customers responsible for the impact of AEP Ohio’s decision to terminate the AEP Power Pool and could cost Ohio customers more than \$525 million.<sup>316</sup>

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<sup>315</sup> *Time Warner AxS v. Pub. Util. Comm.*, 75 Ohio St.3d 229, 233 fn.2 (1996).

<sup>316</sup> See FES Brief, p. 29, 32.

- The Proposed ESP and the Partial Stipulation improperly burden residential customers through subsidized rate increases and limits on governmental aggregation.
- The Partial Stipulation and the Proposed ESP would provide AEP Ohio with approximately \$1 billion in improper above-market revenues that would harm Ohio's economy and would cause the loss of thousands of Ohio jobs.

#### **4. The Partial Stipulation and the Proposed ESP violate important regulatory principles and practices.**

- The Partial Stipulation and the Proposed ESP violate state policy, including the state's policy to offer nondiscriminatory prices, to ensure effective competition in the provision of retail electric service, and to facilitate the state's effectiveness in the global economy.
- The Partial Stipulation and the Proposed ESP do not encourage or promote governmental aggregation and, in fact, preclude governmental aggregation.
- The Partial Stipulation will impose discriminatory capacity prices on shopping customers, while offering a third (and unknown) capacity price on non-shopping customers.
- The Proposed ESP includes other discriminatory components, including an arbitrarily limited shopping credit.
- The Partial Stipulation's arbitrary \$255/MW-day capacity price violates sound economic theory and state policy by instituting anti-competitive charges, including charges that AEP Ohio waived the right to recover or charges that AEP Ohio must recover through the competitive market.
- The Proposed ESP violates state law, which requires that the costs of renewable energy be recovered on a bypassable basis, when the GRR would allow for nonbypassable cost recovery of the Turning Point project.

In sum, there are a myriad of independent reasons why the Commission should reject the Partial Stipulation and the Proposed ESP. If the Commission were able to identify any basis on which to approve the Partial Stipulation or the Proposed ESP, the Commission should institute the modifications identified in FES' Initial Brief,<sup>317</sup> to ensure that the plans fall closer in line with state law and policy.

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<sup>317</sup> See FES Brief, pp. 148-152.

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s/ Laura C. McBride

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I hereby certify that a copy of the foregoing *Reply Brief of FirstEnergy Solutions Corp.* was served this 18th day of November, 2011, via e-mail upon the parties below.

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