

**BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO**

In the Matter of the Commission's)	
Investigation of Ohio's Retail Electric)	Case No. 12-3151-EL-COI
Service Market.)	

**COMMENTS OF
INDUSTRIAL ENERGY USERS-OHIO**

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I. INTRODUCTION

On December 12, 2012, the Public Utilities Commission of Ohio ("PUCO" or "Commission") issued an Entry initiating an investigation regarding the health, strength and vitality of the competitive retail electric service market and actions that the Commission may take to enhance the health, safety and vitality of that market. As part of the investigation, interested parties have been given an opportunity to respond to numerous questions regarding default service as well as Ohio's corporate separation requirements. Based on the content of the questions, it appears that this investigation may impact the ultimate price paid as well as the size and scope of the "customer choice" opportunity available to Ohio consumers. Accordingly, the Industrial Energy Users-Ohio ("IEU-Ohio") respectfully submits answers to and comments on such questions for the Commission's consideration.

The answers and comments which follow identify the many opportunities available to the Commission to remove barriers that are presently blocking consumers from acting on the full opportunity to reduce and stabilize their electric bills. The most significant barriers that are presently in place are barriers which the Commission itself has erected over the objections of consumers and competitive suppliers. IEU-Ohio

answers and comments invite the Commission to promptly eliminate these barriers just as IEU-Ohio urged, in the first place, the Commission to not allow the barriers to be erected. Among other things, the barriers provide an unreasonable and unlawful advantage to the competitive generation business of some incumbent electric distribution utilities or their affiliates, conflict with the policy set forth in Section 4928.02, Revised Code and work to transfer massive amounts of consumers' wealth to some incumbent utility beneficiaries or their affiliates through a combination of above-market compensation and non-bypassable charges.

IEU-Ohio appreciates the opportunity provided by this investigation. Hopefully, this investigation will help to shine more light on the barriers that are working against the public interest and cause the Commission to take action to eliminate such barriers.

II. RESPONSES TO THE COMMISSION'S QUESTIONS

A. MARKET DESIGN

- (a) Does the existing retail electric service market design present barriers that prevent customers from obtaining, and suppliers from offering, benefits of a fully functional competitive retail electric service market? To the extent barriers exist, do they vary by customer class?**

Neither the above question nor the Entry issued on December 12, 2012 that initiated the investigation in Case No. 12-3151-EL-COI identifies the intended meaning of the phrases "existing retail electric service market design" or defines the "benefits of a fully functional competitive retail electric service market" which are referenced in the question. These phrases have no standardized meaning. Accordingly, the following response will focus on the legal and regulatory structure created by Chapter 4928, Revised Code, as it relates to retail "customer choice" and the Public Utilities Commission of Ohio's ("Commission") implementing the reforms enacted by the

General Assembly. Those reforms focus on remedying the anti-competitive structure of the retail electric market and empower customers by freeing them to select their supplier of competitive retail electric services (“CRES”).

Chapter 4928, Revised Code, and similar restructuring efforts implemented by the Federal Energy Regulatory Commission (“FERC”) were adopted based on a common finding. Restructuring of the electric sector was commenced purposefully because of the ability of dynamically efficient competition to better protect and serve the public interest than could any of the many versions of traditional rate-base-rate-of-return regulation. While the fundamental purpose of traditional economic regulation has always been to simulate the forces provided by a competitive market,¹ traditional economic regulation had, in its application, shown itself to be a highly dysfunctional and inferior tool when subjected to a public interest test. The massive amount of “stranded cost” that was approved by state regulators with the commencement of retail competition stands as compelling proof of the degree to which traditional regulation had detached itself from the public interest. But, restructuring the electric sector to enable a competitive market was not without challenges. At its inception, the evolution towards “customer choice” had to displace and overcome the legal barriers that kept willing buyers and sellers apart and it included specific evolutionary or transitional mechanisms.

Initially, the restructuring set forth in Chapter 4928, Revised Code, required: (1) service unbundling along functional lines; (2) identification of CRES; (3) elimination of the Commission’s supervisory and regulatory authority over CRES (with very limited

¹ Jonathan A. Lesser and Leonardo R. Giacchino, *Fundamentals of Energy Regulation*, 17 (2007). (“The fundamental purpose of economic regulation – regardless of the chosen means – is to simulate the allocation of resources that would occur in a dynamically efficient market.”)

exceptions); (4) equating unbundled retail transmission prices to those authorized by FERC; (5) retention of traditional economic regulation for non-competitive retail electric services; (6) comparable and non-discriminatory distribution and transmission services; (7) corporate separation requirements designed to eliminate the incumbent's advantage and make providers of competitive services compete based on merit as judged by consumers; (8) a "one and done" opportunity for incumbent electric distribution utilities ("EDU") to collect "transition revenue" with discounts to transition charges designed to encourage consumers to switch to a CRES provider (at least 20% by the midpoint of the "market development period"); (9) transmission owners to transfer control over their facilities to a regional transmission organization ("RTO") that can maintain reliability and prevent transmission owners from favoring their own or affiliated capabilities; (10) changes that shifted direct tax burdens from electric utilities to consumers to position the utilities for successful participation in the competitive market; (11) consumer education; (12) certification requirements for CRES providers; and (13) proactive Commission attention to the policy set forth in Section 4928.02, Revised Code. Eventually, Chapter 4928, Revised Code, was modified by the General Assembly to add supply and demand portfolio mandates and establish two alternative means by which EDUs may be compensated for CRES provided to retail customers not served by a CRES provider.

The design set forth by the General Assembly contains, with the exception of the portfolio requirements in Sections 4928.64 and 4928.66, Revised Code, no significant structural barriers to CRES commerce between retail buyers and sellers. It also provides the Commission with the authority to move other services into the CRES category.

However, the Commission's implementation of the General Assembly's design has uniquely and unlawfully authorized one EDU (AEP-Ohio)² to increase the compensation it collects from retail consumers and to erect or maintain such barriers. The anti-competitive consequences of the Commission's actions will persist for at least six years unless the Ohio Supreme Court rules otherwise. To make matters worse, the increases in compensation which have been authorized by the Commission have been accompanied by a parade of time-differentiated, self-reconciling, electric-bill-destabilizing recovery mechanisms (or "riders") that transfer business and financial risk from the EDU or its affiliates to consumers who have no means to control or manage such risks. Even under the dysfunctional forms of traditional economic regulation, these results would have been abhorrent to important regulatory principles and the law. Many of these riders also permit AEP-Ohio to inflate any compensation subject to deferred collection through significantly above-market carrying charges which increase the deferred balance at a compounding rate.

The Ohio Supreme Court has, on occasion, held that the Commission has unlawfully increased electric bills and erected barriers to customers seeking to lower their electric bills through customer choice. On such occasions, the Commission has exercised its discretion to delay or avoid providing consumers with a meaningful remedy. One example of the Commission's response or lack thereof to the Ohio Supreme Court's rulings is provided below.

On March 18, 2005, CSP and OP ("AEP-Ohio") filed an application for authority to recover costs of at least one 600 MW Integrated Gasification Combined Cycle ("IGCC") generating facility in Meigs County, Ohio through a three-phase recovery

² As used herein, AEP-Ohio refers to either Ohio Power Company ("OP") and Columbus Southern Power Company ("CSP") combined or OP after the merger with CSP left it as the surviving entity.

scheme.³ The application was solicited by the Commission through its decision in AEP-Ohio's rate stabilization plan ("RSP") case. Despite protests from consumers, the Commission authorized AEP-Ohio to recover approximately \$24 million associated with Phase I of AEP-Ohio's IGCC proposal over a 12-month period.⁴ The Commission also ordered AEP-Ohio to refund all Phase I charges if AEP-Ohio did not engage in a continuous course of construction of the proposed facility over a five-year period commencing with the date of the Commission's decision.⁵

On March 13, 2008 (almost two years following the Commission's IGCC decision), the Ohio Supreme Court overturned the Commission's Order allowing AEP-Ohio to recover the IGCC Phase I costs.⁶ The Ohio Supreme Court ruled that the evidence assembled by the Commission did not support the Commission's ruling that the IGCC generating unit would provide distribution/ancillary services.

On September 17, 2008, the Office of the Ohio Consumers' Counsel ("OCC") filed a request with the Commission requesting that the Commission direct AEP-Ohio to refund the \$24 million and on January 8, 2009, an Entry was issued directing AEP-Ohio to "provide a detailed statement outlining the status of the construction of the IGCC facility, including whether AEP-Ohio is engaged in a continuous course of construction

³ *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Authority to Recover Costs Associated with the Construction and Ultimate Operation of an Integrated Gasification Combined Cycle Electric Generating Facility*, PUCO Case No. 05-376-EL-UNC, Application (March 18, 2005) (hereinafter, "*AEP-Ohio IGCC Proceeding*"). AEP-Ohio also applied for Ohio Power Siting Board ("OPSB") approval of the IGCC Project, which the OPSB approved (with conditions) on April 23, 2007. *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for a Certificate of Environmental Compatibility and Public Need for the Great Bend IGCC Project in Meigs County, Ohio*, PUCO Case No. 06-30-EL-BGN, Opinion, Order, and Certificate (April 23, 2007).

⁴ *AEP-Ohio IGCC Proceeding*, Opinion and Order at 11 (April 10, 2006).

⁵ *Id.* at 16-17.

⁶ *Indus. Energy Users-Ohio v. Pub. Util. Comm.*, 117 Ohio St.3d 486, 2008-Ohio-990.

on the IGCC facility” by February 7, 2009.⁷ On February 6, 2009, AEP-Ohio filed the update required by the Attorney Examiner. AEP-Ohio stated that it had not commenced construction of the IGCC facility. Thereafter, the Commission did nothing.

In September 2009, IEU-Ohio filed a motion asking the Commission to require AEP-Ohio to refund IGCC-related revenues collected from customers or to show cause why an immediate refund should not be required. IEU-Ohio provided the Commission with an integrated resource plan filed by an AEP-Ohio affiliate, Appalachian Power Company (“APCo”), at the Virginia State Corporation Commission that contained information pertaining to the entire eastern segment (which includes Ohio) of AEP-Ohio’s parent company. The Virginia integrated resource plan stated that AEP-Ohio had no plans to initiate construction of any IGCC plant prior to June 28, 2011. Subsequent to the filing of the integrated resource plan, APCo also made a filing in Virginia indicating that plans to move forward with the IGCC facility had been abandoned.

On June 28, 2011, five years after the Commission’s illegal IGCC decision and more than three years after the Ohio Supreme Court ruled the Commission violated the law, a joint motion was filed by IEU-Ohio, OCC, the Ohio Energy Group (“OEG”), and Ohio Partners for Affordable Energy (“OPAE”) requesting that the Commission proceed in the case. The joint movants noted that AEP-Ohio had requested that the Commission not proceed on remand until five years had passed from the Commission’s Entry on Rehearing (issued June 28, 2006) and that five years had now passed. The joint motion requested that the Commission direct AEP-Ohio to refund the \$24 million with interest.

⁷ *AEP-Ohio IGCC Proceeding*, Entry at 3 (January 8, 2009).

The Commission has not acted on the Ohio Supreme Court's IGCC ruling or the various motions filed by consumer groups requesting that the Commission do so.

Current events also provide examples of the Commission's willingness to permit EDUs to obtain permission to collect above-market compensation for generation-related services and block or impede, through non-bypassable charges, the ability of customers to obtain lower electric bills from the market. In the wake of the Commission's favorable response to AEP-Ohio's efforts to increase electric bills further above market and block "customer choice", two other EDUs (Duke Energy Ohio or "DE-Ohio" and The Dayton Power and Light Company or "DP&L") presented their own demands for above-market compensation and barriers to "customer choice." In these "me too" applications, the EDUs seek authority to: increase their generation-related compensation by unreasonably and unlawfully leveraging their role as a default service provider; transfer their competitive sector business and financial risks to retail consumers; evade Commission-approved settlement commitments; evade corporate separation requirements; and erect "customer choice" barriers all to the disadvantage of Ohio's retail electric consumers.

(b) Does default service provide an unfair advantage to the incumbent provider and/or its generation affiliate(s)?

If corporate separation requirements are properly implemented and maintained and RTOs are properly discharging their considerable duties, neither the incumbent EDU nor its affiliates should obtain an advantage (unfair or otherwise) from default service.

Despite the importance of the corporate separation requirements, the Commission has chosen, often over the objections of stakeholders, to ignore failed

compliance with such requirements. Instead, the Commission has rewritten Ohio law by approving another transition period thereby delaying the required compliance. The Commission has also chosen to ignore proposals to fully and completely use a competitive bidding process (“CBP”) to set or test the default generation supply price so as to prevent AEP-Ohio from obtaining an anti-competitive, anti-consumer, unfair and therefore unlawful advantage. In doing so, the Commission effectively invited other EDUs or their affiliates to seek a similar undue and unlawful advantage and, as indicated above, other EDUs have accepted the Commission’s invitation.

RTOs are charged with critically important monitoring and policing functions that are designed to proactively prevent or reactively remedy anti-competitive conduct arising due to concentration of market power through incumbency, affiliation or otherwise. However, PJM Interconnection, L.L.C. (“PJM”), the RTO on which Ohio retail electric consumers most depend, has refused to discharge its duties in circumstances where the consequences are visited upon retail customers.

For example, IEU-Ohio recently approached PJM to request assistance regarding the specification of peak load contribution (“PLC”) factors by incumbent EDUs (load serving entities or “LSEs” in PJM-speak). A PLC attaches to each retail customer for purposes of determining each customer’s responsibility for the regional capacity obligation which is part of the PJM organized wholesale market design. A retail customer’s PLC factor is the controlling billing determinant for capacity under PJM’s Reliability Assurance Agreement (“RAA”).⁸ The process by which PLCs are developed and assigned to retail customers is neither transparent nor standardized. And despite the compliance audit responsibilities which the RAA assigns to PJM, IEU-Ohio

⁸ The RAA is available via the Internet at <https://www.pjm.com/~media/documents/agreements/raa.ashx> (last checked January 25, 2013).

discovered that PJM makes no effort to examine or test the methods by which incumbent suppliers identify PLCs. More pointedly, PJM's administration of the RAA provides no check against an incumbent supplier that uses its PLC specification role to benefit itself or an affiliate.⁹

(c) Should default service continue in its current form?

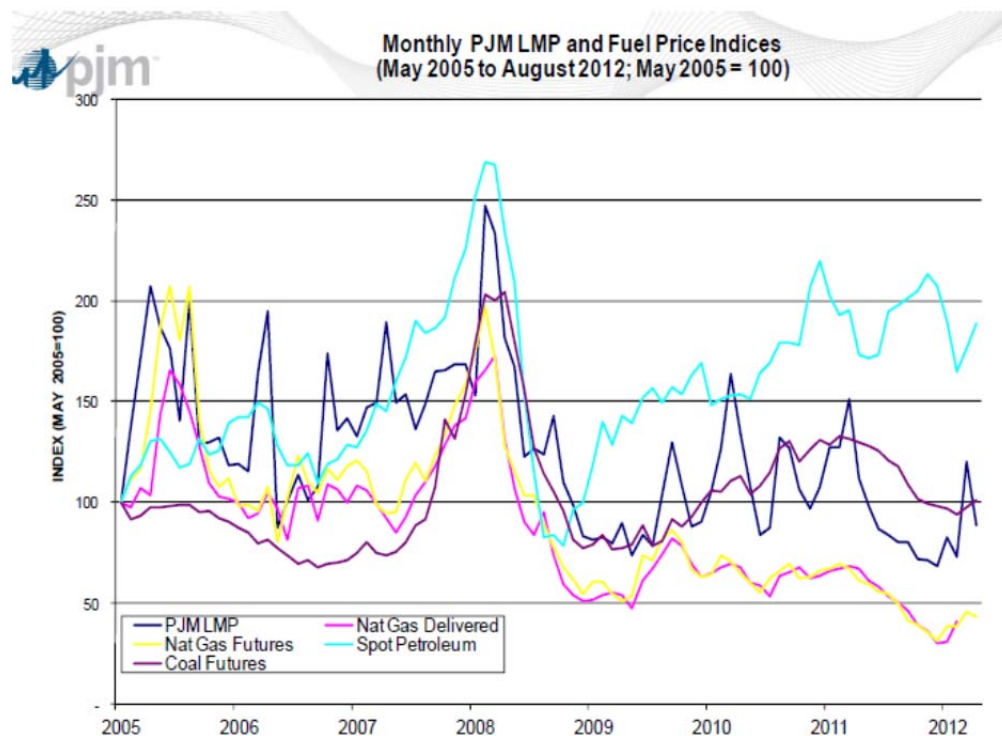
There is no standard current form for default service. Thus, answering this question presents challenges.

Ohio law provides EDUs with the right to propose the means by which they will serve as the default CRES or standard service offer ("SSO") supplier. In response, the Commission has, on an *ad hoc* basis, exercised discretion to approve or modify and approve, sometimes unlawfully, individual EDU proposals. The Commission's *ad hoc* and individualized response to each proposal shows a pro-regulation bias that the Commission has applied to favor the electric security plan ("ESP") option which the Commission has held is "inherently" better than the market rate offer ("MRO") option. Additionally the Commission has resorted to counting non-quantifiable, qualitative "benefits" for purposes of conducting the MRO v. ESP test and approving an ESP that is designed to favor the incumbent or its affiliate even in circumstances where the Commission has acknowledged that the ESP is not better for consumers in the aggregate based on a quantified benefits approach.

Over the last few years, wholesale electric prices have declined. This decline has been influenced by a number of things, including the supply and price of natural gas

⁹ In recent cases where IEU-Ohio has asked the Commission to address the problems created by the lack of transparency and standardization that are presently associated with the PLC specification process, the Commission declined.

and conditions in the general economy. The graph¹⁰ below indicates the relative changes in monthly natural gas prices and PJM's average locational marginal price ("LMP") of electricity, essentially a spot electricity price, using the year 2005 as the base year. From 2005, natural gas prices have dropped significantly and electric prices have generally trended down as well, subject to typical seasonal (summer/winter) fluctuations.



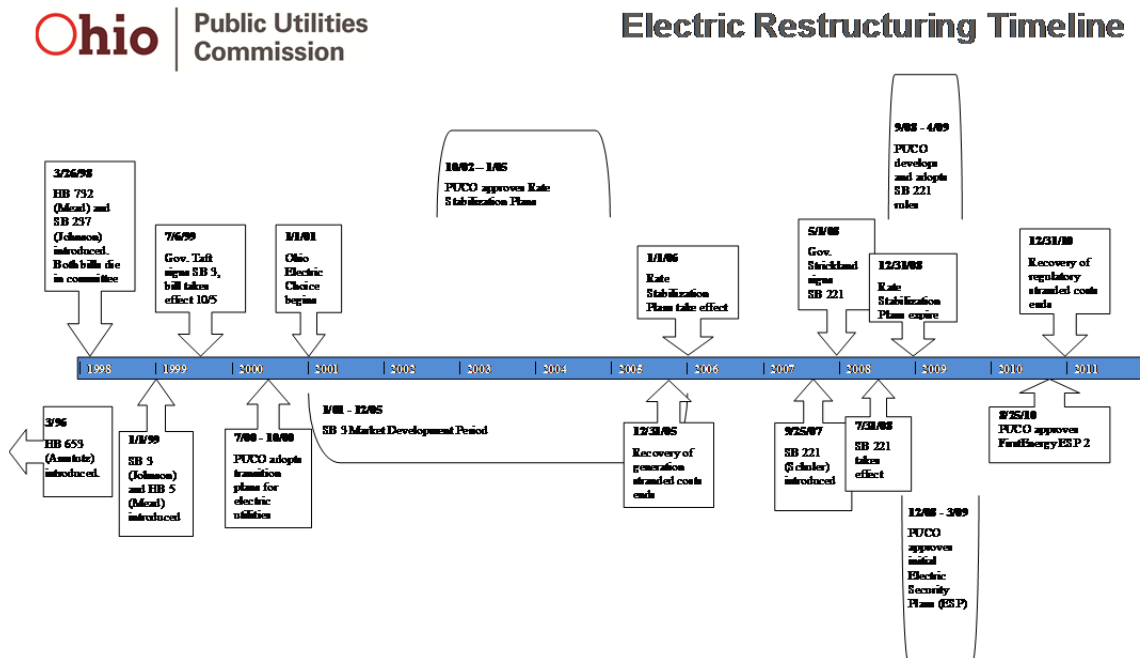
During this period of wholesale price decline, the Commission has, in some cases, authorized the full and complete use of an independently conducted CBP to determine the proper amount of compensation for default generation supply. The CBP process allows numerous suppliers to compete for this opportunity as in the case of a

¹⁰ *What's Ahead: Natural Gas Prices & the Impact on Electricity Rates ... Gas & Power Relationships in the PJM Wholesale Electric Power Market Impacting Over 60,000,000 Million in 13 States* - Andrew Ott, Senior Vice President, Markets, PJM Interconnection LLC, Norristown, PA , Manufacturers' Educational Council, 17th Annual Ohio Energy Management Conference (February 19, 2013) (Mr. Ott's complete Power Point presentation is available via the Internet at: <https://www.mecseminars.com/sites/default/files/presentation-files/Tuesday%20-%20Whats%20Ahead%20Natural%20Gas%20Prices%20and%20Electricity%20Rates%20-%20Ott.pdf>) (last checked March 1, 2013).

competitive market. Where the CBP has been fully and completely used for this purpose, the trend in the default electric supply price has followed the trend of wholesale prices. More specifically, the default supply prices for retail customers of the FirstEnergy Corp. (“FirstEnergy”) EDUs and DE-Ohio have declined or remained stable because of the use of a CBP to set the default generation supply prices. For other electric consumers in Ohio, however, electric prices and bills have gone up or stayed at levels significantly above market largely as a result of the Commission’s contested authorization of “administratively determined” default generation supply prices and a process that effectively allows the incumbent EDU to obtain a default generation supply monopoly. In the case of AEP-Ohio which serves customers in over 60 counties, the Commission’s actions sanctioned higher and more volatile prices accompanied by “now and later” non-bypassable barriers to the benefits otherwise available through “customer choice.” The consequences of the Commission’s actions are shown in the typical residential bill graph provided herein in the pages that follow: the Commission’s failure to fully and completely use a CBP has allowed AEP-Ohio’s default service electric bills to become the highest in Ohio, rise while wholesale prices are declining and provide AEP-Ohio’s competitive generation business with an undue, unlawful and unfair advantage relative to other competitive generation suppliers.

When Ohio changed the legal framework applicable to the electric utility sector to implement a “customer choice” vision, it provided a “one and done” opportunity for incumbent electric utilities to obtain “transition revenue” (sometimes called “stranded costs”) to help them prepare to compete based on merit. Below is an illustration from testimony presented by the Commission to the Ohio House Public Utilities Committee

on September 29, 2011.¹¹ The illustration shows the transitional electric restructuring timeline established by Ohio law.



Ohio law and the above timeline clearly indicate that the opportunity for incumbent utilities to recover generation “stranded costs” ended no later than December 31, 2005. And, Ohio law states that once this opportunity ends, the generation business of each incumbent electric utility must be fully on its own in the competitive market.

But, neither the obvious implications of the above timeline nor the content of Ohio law has retarded the appetite of some EDUs for yet another transition and more “transition revenue.” For example, AEP-Ohio has, since January 2011, prosecuted a successful campaign before the Commission to insulate its competitive generation business from the discipline of the market, newly obtain hundreds of millions of dollars in “transition revenue” outside the period specified by Ohio law and block customer

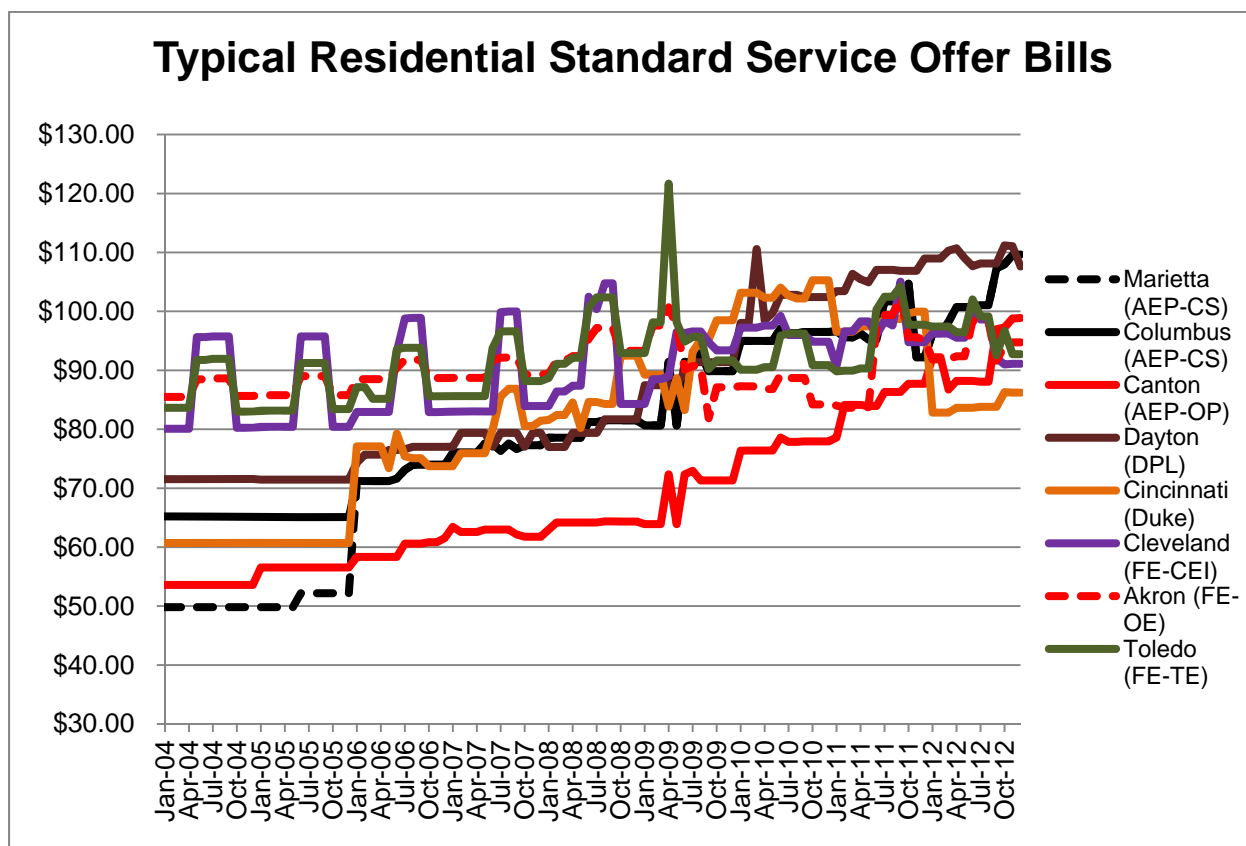
¹¹ The slides from the Commission’s September 29, 2011 presentation are available via the Internet at <http://www.puco.ohio.gov/puco/index.cfm/consumer-information/consumer-topics/legislative-testimony> (last checked February 25, 2013).

access to the lower electric bills available from CRES providers including AEP-Ohio's unregulated affiliate.

As already discussed, the Commission's conceptual embrace of AEP-Ohio's proposals to raise electric bills and block shopping has also inspired DP&L and DE-Ohio to ask the Commission to give them what the Commission has given AEP-Ohio. The actions already taken by the Commission and their implications as they relate to the proposals by DP&L and DE-Ohio score to well over \$2 billion in above-market compensation for the incumbents' competitive generation business. This above-market compensation is provided through a confusing array of non-bypassable charges that work to increase the total bill for electricity while depriving customers of the full opportunity to reduce their electric bills by turning to a CRES provider.

The up/down conflicts in the default service retail electricity pricing trend lines have become more observable in the last 12 months. These same conflicts have also caused the relative position of the default supply prices of Ohio's EDUs to change substantially.

Contrary to the situation that existed when Ohio's law was changed to provide consumers with the opportunity to select their electricity supplier, customers in the distribution service area of AEP-Ohio now pay some of the highest electric bills in Ohio. The graph below shows the relative changes in the "typical" SSO electric bill for residential customers based on information published by the Commission. And, this change in relative position of Ohio's EDUs can be traced directly to differences in the extent to which a CBP or other market-based pricing information is used **or not used** to establish an EDU's default generation supply compensation and the extent to which the Commission has approved above-market, **non-bypassable** generation-related charges.



Again, the default service problems that have materialized are not inherent in the approach spelled out by Ohio law. The problems have arisen as a result of the choices made by the Commission as it has been presented with opportunities to address default service proposals, issues and problems.

This question and the others that focus on default service also suggest that the Commission has inverted the “customer choice” priorities contained in Chapter 4928, Revised Code.

Where consumers receive utility services through a network of physical facilities that are mostly used in common, the physical performance of the network must be balanced to maintain reliability (ability of the network to reliably satisfy demand in real time and on a sustained basis). In an Ohio electricity context, the reliability-related system balancing function is performed by PJM. The economic responsibility for

imbalances is, in turn, assigned through a formalized system that collects and pays out revenue. Because of the hierarchically dependent relationship between the wholesale and retail market segments and the preemptive superiority of PJM's FERC-sanctioned determinations, bulk service reliability and the allocation of economic responsibility for default service functions are necessarily driven by the structure of the organized wholesale market.

Suppliers that take on default retail electric service responsibility are obligated to provide an unspecified quantity of goods or services at an unspecified time. If the default supplier does not act to manage the volume and timing risks associated with the default service responsibility, bulk system reliability will nonetheless be maintained by the RTO and maintained in ways that are designed to remedy the anti-competitive structure of the electric industry. The RTO's reliability-related actions will then manifest themselves in the system of financial settlements that are part of the organized wholesale market. In this circumstance, the EDU would merely function to bill and collect funds from customers receiving default service in an amount sufficient to pay the RTO invoice.

Because of the nature of default service and the hierarchically dependent relationship between the wholesale and retail market segments, it is nearly impossible to use default service as the primary means of enabling a market-based system that requires suppliers to focus on the wants and needs of ultimate customers. Yet, the Commission appears to be focusing on default service as though it is the primary means of providing consumers with the benefits of a competitive electric market. This Commission-adopted prioritization is upside down relative to the "customer choice" priorities established by the letter and spirit of Ohio law, which is focused on enabling

competition that is focused on customers (rather than the wants and needs of regulators or incumbent utilities).

The Commission's upside down prioritization of goals is also in conflict with the fundamental priorities of economic regulation. Whether the economic or financial consequences of balancing a utility network are assigned or allocated to ultimate customers through traditional rate base, rate of return regulation or a market-based system of economic regulation, these alternative means have a common goal. The fundamental purpose of economic regulation – regardless of the chosen means – is to simulate the allocation of resources that would occur in a dynamically efficient market.¹²

The Commission's *ad hoc* determinations regarding default electric service can be divided into two categories. In the first category, there are two EDUs that are presently employing a CBP to assign the physical responsibility for providing default supply and establish the compensation that must be collected to balance default service supply and demand. In the other category, there are EDUs for which the Commission has administratively determined default supply compensation. As discussed herein, these administratively determined compensation structures also include features that erect barriers to customer choice, provide the incumbent's competitive generation business with an unfair advantage and work hard against the letter and spirit of Ohio law.

The Commission's approval of above-market administratively determined prices and non-bypassable charges to establish the SSO also provide the incumbent EDU with an unfair advantage through its relationship with residential customers receiving

¹² Jonathan A. Lesser and Leonardo R. Giacchino, *Fundamentals of Energy Regulation*, 17 (2007). (“The fundamental purpose of economic regulation – regardless of the chosen means – is to simulate the allocation of resources that would occur in a dynamically efficient market.”)

assistance through the Universal Service Fund (“USF”) and customers with “reasonable arrangements” approved pursuant to Section 4905.31, Revised Code.

Residential customers receiving assistance from the USF may be unable to obtain service from a CRES provider unless or until the Director of the Ohio Development Services Agency (“ODSA”) acts on their behalf through the aggregation authority delegated to the Director by Section 4928.53, Revised Code. Thus, when the Commission authorizes above-market default SSO generation supply prices, these residential customers may be captive to the above-market consequences. Since the bill payment assistance is funded by the consumers paying USF charges, the above-market price paid by residential customers receiving USF assistance flows into the electric bills of all customers. The above-market consequence is compounded through the USF structure, hurting customers receiving USF bill payment assistance, hurting all other customers and providing the incumbent EDU with an unfair and unwarranted advantage.

Section 4905.31, Revised Code, gives the Commission authority to approve an electric “reasonable arrangement” between a utility and a customer at the request of the utility, a mercantile customer or a group of mercantile customers.

Reasonable arrangements are generally customer-specific arrangements where the price, terms and conditions are customized to meet the needs of the customer. For decades, these arrangements have been used for economic development and retention purposes and particularly for large manufacturers that often have specialized service and price needs. Unless the Commission approves a reasonable arrangement, customers are subject to the standard rate schedules generally available to the public.

As discussed below, there are standard electric rate schedules for shopping and non-shopping electric customers.

The reasonable arrangement statute permits the Commission to provide an EDU participating in a reasonable arrangement with the ability to recover a shortfall in revenue that occurs because of the reasonable arrangement. In such circumstances, the Commission allows the EDU to collect this shortfall (delta revenue) from other customers, generally through a non-bypassable charge. Delta revenue is essentially the revenue difference between the revenue produced by the reasonable arrangement and the “otherwise applicable rate schedule.” Thus, the delta revenue measurement question becomes: What is the otherwise applicable rate schedule?

The Commission’s measurement of delta revenue has generally been based on the difference between the reasonable arrangement revenue and the EDU’s otherwise applicable SSO rate schedule. Where the Commission has authorized above-market compensation for an EDU (such as in the case of AEP-Ohio, DE-Ohio and DP&L), the use of the otherwise applicable SSO rate schedule provides the incumbent EDU with an unfair advantage because it unreasonably inflates the amount of “delta revenue”.

There is no good reason why the otherwise applicable SSO default service rate schedule must be used for purposes of defining the delta revenue amount.

Each EDU has two sets of standard rate schedules. One set is for shopping customers and the other set of standard rate schedules is for non-shopping customers. The rate schedules applicable to shopping customers are generally for just the distribution or distribution and transmission service provided by the incumbent EDU. A shopping customer obtains generation supply from a CRES provider — not the incumbent EDU.

The existence of two different standard rate schedules (one for shopping and one for non-shopping customers) gives the Commission the opportunity to measure delta revenue based on a shopping customer reference point. And, in present circumstances, the use of the standard shopping customer rate schedule to define delta revenue will almost certainly produce a lower amount of “delta revenue.” Since the shopping customer standard rate schedule allows the customer to obtain generation supply from the market and since market prices for electricity are presently at relatively low levels, the Commission can (and should) use the shopping customer standard rate schedule to measure delta revenue to both get the best outcome for the reasonable arrangement customer and to reduce the amount of the shortfall that may get passed on to other customers in the form of delta revenue charges.

The potential for the SSO standard rate schedule to make the revenue shortfall or “delta revenue” higher than it should be is greater in circumstances where the Commission has administratively determined default generation supply prices and where the Commission has added non-bypassable charges to the mix.

In FirstEnergy’s and DE-Ohio’s service areas, the default generation supply price is based on a CBP and, as a result, the generation supply prices have tracked the decline in electric prices observable in the wholesale market. When a CBP was introduced in DE-Ohio’s service area, residential non-shopping customers saw their electric bills drop by about 17%.¹³

In AEP-Ohio’s and DP&L’s service area, the Commission has established default generation supply prices at levels well above prevailing market prices and has allowed

¹³ Information regarding the results of this DE-Ohio CBP are available through the Commission’s website including the following Internet address: <http://www.puco.ohio.gov/puco/index.cfm/media-room/media-releases/duke-energy-auction-leads-to-lower-electric-prices-in-2012/> (last checked February 28, 2013).

the EDU to collect a portion of this above-market premium through non-bypassable charges. In such circumstances, the EDU obtains an unfair advantage where delta revenue is measured based on the otherwise applicable rate schedule for non-shopping customers.

(d) Does Ohio's current default service model impede competition, raise barriers, or otherwise prevent customers from choosing electricity products and services tailored to their individual needs?

As explained herein, the individual and very different decisions that the Commission has made regarding the default service offerings of EDUs have not produced a common default service model.

In some cases, the Commission has approved ESPs that contain explicit provisions to prevent customers from choosing electricity products and services tailored to their individual needs while increasing the default service prices further above market. Where they exist, these provisions insulate the competitive lines of business of the incumbent or its affiliates from the discipline of customer choice, thereby effectively creating a deregulated monopoly. These Commission-approved provisions also equip the incumbent or its affiliates with an anti-competitive advantage that they can then use to obtain market share outside their traditional service area.

The barriers and the inflated prices authorized by the Commission through its *ad hoc* SSO decisions also ripple through customers' bills in a variety of ways.

As discussed above, customers receiving USF assistance are generally captive to state government's unwillingness to procure better service and lower bills through the market. Where the Commission has authorized EDUs to further increase SSO prices above market and collect a "shopping tax" through non-bypassable charges, the electric

bills of these vulnerable customers rise as does the amount of funding assistance that must be collected from other customers. A similar consequence occurs in the case of reasonable arrangement customers that may not be permitted to shop as a result of limitations in their Commission-approved reasonable arrangements. Thus, the customer choice barriers and above-market compensation which have been approved by the Commission in some ESP cases impose a double penalty on consumers, Ohio's economic development and retention objectives and the public interest.

In other cases, where a CBP has driven the compensation for default generation supply and the selection of suppliers for such supply, structural barriers have been eliminated or significantly reduced. And, where competitive bidding has been adopted to establish compensation for default supply of competitive services, the customers receiving USF assistance and the customers who fund such assistance have received flow-through benefits.

While the Commission's default service-related questions tend to focus on default generation supply, this is not the only area where the role assigned to the incumbent is interfering with the ability of customers to freely select the products and services that meet their needs.

Ohio's supply side and demand side portfolio mandates call on the incumbent EDU to manage a massive program of government intervention in ways that work hard against the market's ability to allocate resources efficiently and in accordance with consumers' preferences. Ohio's portfolio mandates are incompatible with a market-based approach and they fortify the power of incumbency through things like "lost revenue" and "shared savings" allowances that are only available to the incumbent EDU.

As the Commission considers what, if any, barriers have been created as a result of the default supplier role assigned to an EDU, IEU-Ohio encourages the Commission to expand its view to include the anti-competitive/pro-monopoly effects of Ohio's portfolio mandates.

(e) Should Ohio continue a hybrid model that includes an ESP and MRO option?

As explained herein, the Commission's SSO-related decisions have produced very different outcomes. As a consequence, there is no common default service model in Ohio.

In practice, the Commission has displayed a strong bias against the MRO option. The Commission' resorting to qualitative benefits to overcome the quantitative aggregate disadvantage of a proposed ESP (as compared to the MRO) and the Commission's unlawful and EDU-friendly approvals of ESPs have effectively written the MRO option and the "benefit in the aggregate" test out of the law.

(f) How can Ohio's electric default service model be improved to remove barriers to achieve a properly functioning and robust competitive retail electric service electricity market?

Below is a non-exhaustive list of actions that could be taken to remove barriers to a properly functioning and robust competitive retail electric service market. These items are not new. IEU-Ohio has previously urged or is currently urging the Commission to act on these opportunities in other Commission proceedings.

Through the rehearing process or otherwise, barriers to a properly functioning, robust electric service market can be removed by eliminating all generation-related non-bypassable charges and not approving any new generation-related non-bypassable charges. If not eliminated entirely, the Commission should exempt customers that elect

to return to default service supply at a market-based price provided by the EDU or that waive their right to return to EDU default supply from such non-bypassable charges. As explained herein, it is the Commission's decisions – not Ohio law – that are creating such barriers and the Commission can and should act to take down the barriers that have arisen because of the Commission's decisions.

Barriers to a properly functioning, robust electric service market can be removed by using the authority delegated to ODSA to obtain generation supply for customers receiving USF assistance in cases where such supply is not already being procured through a CBP. Here again, all generation-related non-bypassable charges should be eliminated or be waived.

Barriers to a properly functioning, robust electric service market can be removed by using the continuing jurisdiction of the Commission over existing reasonable arrangements to encourage customers to use the market to help Ohio advance its economic development and retention goals and reduce delta revenue. In such circumstances, the Commission should signal that it is willing to entertain requests to eliminate shopping limitations in Commission-approved reasonable arrangements.

Barriers to a properly functioning, robust electric service market can be reduced by the Commission signaling that newly-proposed reasonable arrangements should rely upon the market to obtain CRES and, where reasonably possible, to reduce any "delta revenue" that might otherwise occur by relying on the otherwise applicable SSO tariff.

Barriers to a properly functioning, robust electric service market can be reduced by enforcing current corporate separation requirements. Ohio's corporate separation requirements have been in place for well over a decade and the requirements are mandatory. The Commission has given some EDUs more time to delay compliance

with structural separation requirements and in doing so has provided such EDUs with an unfair, unreasonable and unlawful advantage.

Barriers to a properly functioning, robust electric service market can be reduced by the Commission's enforcement of the statutory requirement that the generation business segment of each EDU and EDU affiliate be fully on its own in a competitive market. Here again, the Commission has authorized ESPs that are specifically designed to insulate the competitive generation business of EDUs and their affiliates from the discipline of the competitive market. The Commission's actions are incompatible with Ohio law and provide the benefited generation businesses with an unfair, unreasonable and unlawful advantage.

Barriers to a properly functioning, robust electric service market can be removed or reduced by not approving proposals that make customers captive to transmission service provided by the incumbent EDU. Customers or their suppliers should be free to source transmission service directly from the RTO.

Barriers to a properly functioning, robust electric service market can be reduced by holding RTOs accountable for such things as properly and transparently discharging their audit and oversight responsibilities regarding compliance with the RAA and the process by which "LSEs" identify customer-specific PLCs.

Barriers to a properly functioning, robust electric service market can be reduced or eliminated by using a CBP to establish the level of carrying costs associated with deferred compensation mechanisms. The EDU average embedded debt-based carrying charge rate typically allowed by the Commission is generally 200 basis points or more higher than debt rates readily available in financial markets. Opportunities to leverage the ability of the financial market to reduce the carrying charge component of

regulatory assets exist and not acting on such opportunities provides the incumbent EDU with an unfair advantage.

Barriers to a properly functioning, robust electric service market can be reduced or eliminated by reducing the return on equity component of an EDU's compensation where cost recovery mechanisms work alone and combine to transfer business or financial risks to an EDU's customers.

Barriers to a properly functioning, robust electric service market can be reduced or eliminated by repealing the portfolio mandates in Sections 4928.64 and 4928.66, Revised Code, and, in the meantime, by measuring compliance to include all the things that Ohio law requires the Commission to count for compliance purposes.

- (g) Are there additional market design changes that should be implemented to eliminate any status quo bias benefit for default service?**
- (h) What modifications are needed to the existing default service model to remove any inherent procurement (or other cost) advantages for the utility?**

As discussed herein, there are significant opportunities for the Commission to eliminate barriers to a robust, fully functioning retail electric service market by focusing on the barriers that the Commission has itself created. IEU-Ohio urges the Commission to remove the barriers that the Commission has approved through the ESP process and then assess what, if any, incremental improvements may be necessary.

- (i) What changes can the Commission implement on its own under the existing default service model to improve the current state of retail electric service competition in Ohio?**

As discussed herein, there are significant opportunities for the Commission to eliminate barriers to a robust, fully functioning retail electric service market by focusing on the barriers that the Commission has itself created. Some of the opportunities are

more specifically discussed and identified in the above responses. IEU-Ohio urges the Commission to act on these opportunities.

(j) What legislative changes, if any, including changes to the current default service model, are necessary to better support a fully workable and competitive retail electric service market?

As discussed herein, there are significant opportunities for the Commission to eliminate barriers to a robust, fully functioning retail electric service market by focusing on the barriers that the Commission has itself created. Some of the opportunities are identified in the above responses. IEU-Ohio urges the Commission to act on these opportunities and then assess what, if any, incremental improvements may be necessary through legislative or regulatory channels.

(k) What potential barriers, if any, are being created by the implementation of a provider's smart meter plans? Should CRES suppliers be permitted to deploy smart meters to customers? Should the Commission consider standardizing installations to promote data availability and access?

The Commission has the authority to declare metering, billing and collection services competitive services so that a broader scope of customer choice can drive innovation. The Commission should explore opportunities to expand the scope of CRES rather than picking "smart meters," particular technologies or capabilities that then must be deployed through an incumbent EDU.

Where possible, measurement of billing determinants should be standardized based on measurement practices in the wholesale market to facilitate "apples to apples" comparisons and to better predict actual bill outcomes.

(l)¹⁴ Should the Commission consider standardized billing for electric utilities?

Where possible, measurement of billing determinants should be standardized based on measurement practices in the wholesale market to facilitate “apples to apples” comparisons and to better predict actual bill outcomes.

(m) Do third party providers of energy efficiency products, renewables, demand response or other alternative energy products have adequate market access? If not, how could this be enhanced?

As discussed above, Ohio’s portfolio mandates are a massive form of government intervention that blocks comparable and non-discriminatory market access for all suppliers of products or services that can help consumers reduce their energy intensity and act on their preferences for conventional and unconventional resources.

(n) Does an electric utility have an obligation to control the size and shape of its native load so as to improve energy prices and reduce capacity costs?

Answering this question requires a brief discussion of the term “native load.”

Generally, the term “native load” is used to describe the retail customer load for which the electric utility has an obligation to construct and operate facilities to reliably meet the needs of the customer. The use of the term began in an era when retail customers in Ohio received bundled generation, transmission and distribution service from the electric supplier to which they were assigned by Ohio’s certified service area law that begins at Section 4933.81, Revised Code. That era ended in Ohio more than a

¹⁴ The numbering assigned to the questions by the Commission is in error. Corrected numbering has been used for purposes of responding to the questions.

decade ago. Electric restructuring in Ohio changed the historical meaning of “native load.”

Under Ohio’s current unbundled service legal structure, each EDU is obligated to construct and operate distribution facilities to reliably meet the needs of retail customers. As a general proposition and with the exception of the duties created by Ohio’s portfolio mandates, an EDU has no obligation or opportunity to control the size and shape of its “native load” even if to do so might improve energy prices and reduce capacity prices. And the Commission has no authority under Ohio law to regulate the size and shape of customers’ load.¹⁵ Of course, differences in the size and shape of load, native or otherwise, can be reflected in the time differentiated prices charged by the EDU or authorized by the Commission so as to better inform customers about the billing significance of choices about the level and timing of consumption.

Under Ohio law, an EDU can only function as a default supplier of generation supply and a supplier of distribution service with certain service area rights. Under Ohio law, the Commission has, with very limited exceptions, no authority to regulate or supervise the provision of any service declared to be competitive. Under Ohio law and excluding the duties created by Ohio’s portfolio mandates, an EDU has no obligation or opportunity to control the size and shape of native load so as to improve energy prices and reduce capacity costs. Likewise, neither an EDU nor the Commission has the right to directly or indirectly deprive consumers of their ability to access CRES providers to improve energy prices and reduce capacity prices.

¹⁵ *Ohio Manufacturers Association v. Public Utilities Commission of Ohio*, 46 Ohio St. 2d 214 (1976).

B. CORPORATE SEPARATION

- (a) Whether an electric utility should be required to disclose to the Commission any information regarding the utility's analysis or the internal decision matrix involving plant retirements, capacity auction, and transmission projects, including correspondence and meetings among affiliates and their representatives?**

The term "electric utility," as it relates to the Commission's jurisdiction, gives the Commission authority over the EDU distribution function. Ohio law specifically bars, with very limited exceptions, the Commission's regulation or supervision of services, such as generation service, which are declared competitive. Unbundled transmission service is subject to the exclusive jurisdiction of FERC as is the sale of electricity for resale. With timely and proper compliance with Ohio's and FERC's corporate separation requirements, the opportunity for the Commission to obtain the information identified in the above question depends on the authority of FERC and FERC-regulated RTOs.

- (b) Should a utility's transmission affiliate be precluded from participating in the projects intended to alleviate the constraint or should competitive bidding be required?**

The subject area identified in the question is within the exclusive jurisdiction of FERC. With regard to this subject and questions about the opportunity for transmission providers to participate in projects intended to alleviate constraints, IEU-Ohio has supported FERC's efforts to eliminate any incumbent provider right of first refusal ("ROFR") advantage. The need for project participation bans may exist in cases where the utility has failed to comply with corporate separation requirements.

- (c) How long should a utility be permitted to retain their injection rights?**

As presented, the question cannot be answered.

(d) As fully separate entities, does a utility's distribution affiliate have a duty to oppose the incentive rate of return at FERC?

A utility may have a fiduciary duty to oppose an incentive rate of return if the proposal is adverse to the interests of its shareholders. Otherwise, the question cannot be answered without speculating about the meaning of the words in the question. It would be helpful if the Commission would clarify this question as part of this investigation.

As the Commission knows, the transmission affiliates of some EDUs have sought and obtained incentive returns on common equity for some projects. The incentive return, of course, increases the cost of the project as it is incorporated in rates and charges for transmission service. Accordingly, awarding incentive returns has and will continue to work to increase the delivered price of electricity. But more importantly, the method by which the transmission service revenue requirement is assigned or allocated through the transmission ratemaking process at FERC can cause transmission rate outcomes to mismatch the costs and benefits associated with transmission projects. More specifically, some transmission entities (including those affiliated with AEP-Ohio) have continued to push transmission project cost allocation methods that socialize the cost responsibility for transmission projects in ways that impose excessive costs on Ohio electricity consumers relative to the benefits of the projects. Accordingly, the potential significance of an incentive rate of return on the delivered price of electricity in Ohio needs to be considered in conjunction with the method used to allocate or assign costs through the transmission ratemaking process.

(e) Is there a potential for consumers to be misled by a utility's corporate separation structure?

Responses to prior questions include opinions and information related to the corporate separation requirements which have not been fulfilled as required by Ohio law. The potential for consumers to be misled exists in this area and others as a matter of fact. It increases where corporate separation requirements are not consistently obeyed and the need for consumer education is ignored.

(f) Are shared services within a 'structural separation' configuration causing market manipulation and undue preference?

Responses to prior questions include opinions and information related to the corporate separation requirements which have not been fulfilled as required by Ohio law. The potential for market manipulation and undue preferences exist in this area and others as a matter of fact. It increases where corporate separation requirements are not consistently enforced and obeyed.

(g) Should generation and competitive suppliers be required to completely divest from transmission and distribution entities, maintain their own shareholders and, therefore, operate completely separate from an affiliate structure?

The Commission's authority to investigate and address this subject area is addressed by Ohio law. The Commission has, with very limited exceptions, no authority to regulate or supervise competitive services such as generation. Also, other federal and state agencies are empowered to address corporate relationships that result in excessive concentrations of horizontal or vertical market power. A divestiture requirement may be appropriate to prevent such concentrations and as a remedy to the damage caused by such concentrations.

(h) Are there PJM tariffs or FERC rules that would mitigate market power and/ or facilitate retail electric service competition?

There are Ohio laws, Commission rules, PJM tariffs and FERC rules that, if properly implemented, can and will mitigate undue concentrations of horizontal and vertical market power and facilitate wholesale as well as retail electric service competition. For example, PJM's RAA is a FERC-approved agreement that establishes the means by which generation capacity service is to be valued and priced within PJM's regional organized wholesale market.¹⁶ The purpose of the RAA is expressed in Article 2 (emphasis added):

ARTICLE 2 -- PURPOSE

This Agreement is intended to ensure that adequate Capacity Resources, including planned and Existing Generation Capacity Resources, planned and existing Demand Resources, Energy Efficiency Resources, and ILR will be planned and made available to provide reliable service to loads within the PJM Region, to assist other Parties during Emergencies and to coordinate planning of such resources consistent with the Reliability Principles and Standards. ***Further, it is the intention and objective of the Parties to implement this Agreement in a manner consistent with the development of a robust competitive marketplace.*** To accomplish these objectives, this Agreement is among all of the Load Serving Entities within the PJM Region. Unless this Agreement is terminated as provided in Section 3.3, every entity which is or will become a Load Serving Entity within the PJM Region is to become and remain a Party to this Agreement or to an agreement (such as a requirements supply agreement) with a Party pursuant to which that Party has agreed to act as the agent for the Load Serving Entity for purposes of satisfying the obligations under this Agreement related to the load within the PJM Region of that Load Serving Entity. Nothing herein is intended to abridge, alter or otherwise affect the emergency powers the Office of the Interconnection may exercise under the Operating Agreement and PJM Tariff.

Despite the clear and pro-competitive purpose of the RAA, the Commission has nonetheless cited the RAA in its decisions authorizing AEP-Ohio to collect significantly

¹⁶ The RAA is available *via* the Internet at <http://www.pjm.com/~media/documents/agreements/raa.ashx> (last checked February 25, 2013). The RAA is a FERC-approved tariff and is designated as PJM's Rate Schedule No. 44.

above-market compensation for generation capacity services and to do so through non-bypassable charges imposed on shopping and non-shopping retail customers. As explained above, the Commission's actions in this regard, coupled with the Commission's refusal to fully and completely rely on a CBP or the results of other CBPs conducted in Ohio to determine AEP-Ohio's default generation supply compensation, have caused AEP-Ohio's retail electric prices to become the highest and the least avoidable in Ohio. And, the Commission's use of the RAA to provide AEP-Ohio's generation business with an anti-competitive and undue advantage has provoked DE-Ohio to demand that the Commission apply the RAA to give DE-Ohio's generation business a similar anti-competitive and undue advantage.

III. CONCLUSION

For the reasons discussed above, IEU-Ohio urges the Commission to promptly act to remove the barriers that the Commission has allowed to be inserted between retail consumers and CRES providers ready and willing to help consumers realize the full electric bill reduction and stabilization benefits that are presently available in the market but for such barriers. Among other things, the barriers provide an unreasonable and unlawful advantage to the competitive generation business of some incumbent electric distribution utilities or their affiliates, conflict with the policy set forth in Section 4928.02, Revised Code and work to transfer massive amounts of consumers' wealth to some incumbent utility beneficiaries or their affiliates through a combination of above-market compensation and non-bypassable charges.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing *Comments of Industrial Energy Users-Ohio* was served upon the following parties of record this 1st day of March 2013, via electronic transmission, hand-delivery or first class U.S. mail, postage prepaid.

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