

**BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO**

In the Matter of the Application of Ohio)
Edison Company, The Cleveland Electric)
Illuminating Company, and The Toledo)
Edison Company for Authority to) Case No. 14-1297-EL-SSO
Provide for a Standard Service Offer)
Pursuant to R.C. 4928.143 in the Form of)
an Electric Security Plan.)

**SECOND SUPPLEMENTAL TESTIMONY OF EDWARD W. HILL
ON BEHALF OF THE
OHIO MANUFACTURERS' ASSOCIATION ENERGY GROUP**

August 10, 2015

1 **Introduction, Purpose and Summary of Conclusions**

2 **Q. Please state your name, title and business address.**

3 A. My name is Edward W. Hill, Ph.D. I recently retired as the Dean of the Maxine
4 Goodman Levin College of Urban Affairs at Cleveland State University and Professor of
5 Economic Development. My current address is 1121 Forest Rd., Lakewood, Ohio 44107.

6 **Q. Have you provided written testimony before in this proceeding?**

7 A. Yes, I provided written direct testimony on December 22, 2014, and supplemental
8 written testimony on May 11, 2015. My testimony addressed the policy implications that
9 I believe the Public Utilities Commission of Ohio (Commission) should consider
10 regarding the request of Ohio Edison Company (Ohio Edison), The Cleveland Electric
11 Illuminating Company (CEI), and The Toledo Edison Company (Toledo Edison)
12 (collectively, the Companies) for approval of an Economic Stability Program (Program),
13 which includes shifting the financial risk of operating generation plants onto their
14 customers through a rider and the utilization of a power purchase agreement (PPA) to
15 subsidize portions of the generation capacity owned by the Companies' affiliate,
16 FirstEnergy Solutions. I explained that the proposal shifts the risk of owning and
17 operating generating capacity to customers, including those customers who choose to
18 shop and purchase their generation from alternative suppliers or generators other than the
19 Companies' affiliate, FirstEnergy Solutions. I also addressed, in response to the Attorney
20 Examiner's Entries dated March 23, 2015 and May 1, 2015, whether and how the
21 Commission's factors set forth in the recent AEP Ohio Order regarding AEP's electric

1 security plan and request for cost recovery associated with a PPA¹ should be considered
2 in evaluating the Companies' request for future cost recovery associated with a PPA.²

3 **Q. What is the purpose of your second supplemental testimony in this proceeding?**

4 A. Pursuant to the established procedural schedule,³ I am testifying in response to the
5 Supplemental Stipulation and Recommendation that was filed on May 28, 2015 by the
6 Companies and signatory parties in this proceeding (Supplemental Stipulation)⁴ and the
7 Second Supplemental Stipulation and Recommendation that was filed on June 4, 2015 by
8 the Companies and signatory parties in this proceeding (Second Supplemental
9 Stipulation)⁵ (collectively, Supplemental Stipulations). Both Supplemental Stipulations
10 modify and adopt the initial Stipulation and Recommendation filed by the Companies and
11 signatory parties in this proceeding on December 22, 2014 (Stipulation).⁶ In the
12 Supplemental Stipulations, the Companies continue to raise new issues, offer new
13 arguments, expand the carefully crafted coalition of supporters, and, when considered
14 together with the initial Stipulation, further its attempt to influence the public policy

¹*In the Matter of the Application of Ohio Power 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. 13-2385-EL-SSO, et al., Opinion and Order at 25 (February 25, 2015) (AEP Ohio Order).

²*In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company and The Toledo Edison Company for Authority to Provide for a Standard Service Offer Pursuant to R.C. § 4928.143 in the Form of an Electric Security Plan*, Case No. 14-1297-EL-SSO (ESP IV Proceeding), Entry at 2 (March 23, 2015) and Entry at 10 (May 1, 2015) (citing AEP Ohio Order).

³ ESP IV Proceeding, Entry at 4 (July 2, 2015), modifying the schedule established at the June 2, 2015 Prehearing Conference, Transcript at 93, 95-96.

⁴ ESP IV Proceeding, Supplemental Stipulation and Recommendation (May 28, 2015) (Supplemental Stipulation).

⁵ ESP IV Proceeding, Second Supplemental Stipulation and Recommendation (June 4, 2015) (Second Supplemental Stipulation).

⁶ ESP IV Proceeding, Stipulation and Recommendation (December 22, 2014), as modified by the Errata filed on January 21, 2015 (Stipulation).

1 process in ways that are harmful for the state of Ohio. Accordingly, I offer an analysis of
2 the multiple stipulations, the supporters of those stipulations, and the cumulative effect of
3 the multiple stipulations on the business community in Ohio.

4 **Q. Have you had an opportunity to review the Supplemental Stipulation and Second**
5 **Stipulation, both of which modify the Stipulation?**

6 A. Yes. I have reviewed all of the stipulations that have been filed to date, as well as
7 relevant portions of the Companies' Plan termed at different times *Powering Ohio's*
8 *Progress*, Electric Security Plan IV, and ESP IV. I have also reviewed the supplemental
9 testimony of Eileen Mikkelsen (multiple filings), filed on behalf of the Companies, which
10 claim to support the various stipulations.⁷

11 **Q. Which provisions contained in the Supplemental Stipulations are new to the**
12 **Companies' initial ESP IV Plan and Stipulation?**

13 A. The Supplemental Stipulations modify various provisions of Rider ELR (the
14 interruptible program), create a new pilot program for certain customers regarding
15 transmission costs, and create a new time-of-use proposal for certain customers. In
16 exchange for these new or modified provisions, the Supplemental Stipulations add two
17 additional entities to the group of 12 entities that were signatory parties to the Stipulation,
18 all of which have agreed to either support or not oppose the Companies in their request
19 for approval of the Companies' ESP IV Application (Signatory or Non-opposing Parties).
20 These Signatory or Non-opposing Parties state that they joined the Companies in

⁷ ESP IV Proceeding, Supplemental Testimony of Eileen M. Mikkelsen (December 22, 2014) (Mikkelsen Supplemental Testimony), Third Supplemental Testimony of Eileen M. Mikkelsen (June 1, 2015) (Mikkelsen Third Supplemental Testimony), and Fourth Supplemental Testimony of Eileen M. Mikkelsen (June 4, 2015) (Mikkelsen Fourth Supplemental Testimony).

1 supporting the proposed ESP IV Application after “a serious compromise of complex
2 issues.”⁸ However, the Signatory or Non-opposing Parties extracted payments, rate
3 discounts, and/or customer-specific special programs from the Companies through
4 several new provisions added to the ESP IV Application through the stipulations, many
5 of which are on topics that did not appear in the Companies’ original ESP IV Application
6 and were not discussed in pre-filed testimony. After successfully extracting benefits
7 from the Companies, the Signatory or Non-opposing Parties agreed to recommend
8 approval of the Companies’ proposed ESP IV Application (as modified by the
9 stipulations), including the Economic Stability Program and establishment of the Retail
10 Rate Stability Rider (Rider RRS) associated with the PPA.⁹

11 While the Supplemental Stipulations, as well as the corresponding third and fourth
12 supplemental testimony of Ms. Mikkelsen, tout the additional issues addressed in the
13 Supplemental Stipulations (that adopt the entirety of the initial Stipulation¹⁰) as small and
14 narrow, the fact of the matter is that both Supplemental Stipulations raise additional
15 matters that have not been presented previously.

⁸ Supplemental Stipulation at 1, 5, and Second Supplemental Stipulation at 1, 2, adopting Stipulation in its entirety; see Stipulation at 5.

⁹ Supplemental Stipulation at 1, 5, and Second Supplemental Stipulation at 1, 2, adopting Stipulation in its entirety; see Stipulation at 6.

¹⁰ Supplemental Stipulation at 1 and Second Supplemental Stipulation at 1.

1 **Q. Are the benefits extracted from the stipulations available to all customers or all**
2 **parties to the proceeding?**

3 A. No. Several benefits only pertain to the interests of a specific Signatory or Non-
4 opposing Party or are only available to specific Signatory and Non-opposing Parties, or
5 their members.

6 For example, under the Supplemental Stipulation, the Stipulating and Non-opposing
7 Parties propose a new, small-scale pilot program for some of the Signatory and Non-
8 opposing Parties and their members, which allows those pilot participants to opt-out of
9 the Companies' Rider NMB and obtain all transmission and ancillary services directly
10 through PJM's Open Access Transmission Tariff (OATT), or indirectly through a
11 certified retail electric supplier. It is not clear whether the costs associated with the
12 implementation of this pilot program will be passed on to other customers, nor is it clear
13 whether any costs included in Rider NMB that are not paid for by opt-out pilot
14 participants will be borne by other customers.

15 As another example, under the latest stipulation filed (i.e., Second Supplemental
16 Stipulation), the Stipulating and Non-opposing Parties propose to deploy a Commercial
17 High Load Factor ("HLF") Experimental Time-of-Use Rate Proposal that will be
18 available for only commercial customers that have headquarters located in Ohio and have
19 at least 30 facilities in the Companies' service territories (with each facility consuming at
20 least 1.5GWh annually). Refrigeration must also be a major portion of the customer's
21 load. Furthermore, each of the customer's participating facilities must have interval

1 metering, must have an average monthly load factor during the preceding 12 months of
2 70% or higher, and must be served under the Companies' GS or GP rate schedules.¹¹

3 The Experimental Time-of-Use Rate was not included in the Company's ESP IV
4 Application, the Stipulation, or the Supplemental Stipulation. It appears for the first time
5 in the Second Supplemental Stipulation and adds one Signatory Party to the overall
6 settlement. Ms. Mikkelsen states that the provision will give a customer that meets the
7 specified narrowly-tailored criteria an opportunity to reduce its overall energy bills with
8 the "[r]ecovery of differences, if any, between revenues collected to provide this
9 generation service and the cost associated with providing this generation service" from
10 other customers through Rider GCR.¹² The amount or impact on Rider GCR is not
11 disclosed.¹³

12 **Q. What are some of the other benefits that only pertain to the interests of specific**
13 **Signatory or Non-opposing Parties?**

14 A. In addition to the new programs created and the special rate programs continued that
15 are, essentially, limited to only Signatory or Non-opposing Parties, various payments are
16 promised to a few Signatory Parties associated with energy efficiency and assistance

¹¹ See Second Supplemental Stipulation at 1-2.

¹² Mikkelsen Fourth Supplemental Testimony at 2; see also Response of the Companies to OCC-16-INT-601, attached hereto at EWH Supplemental Attachment A at 1.

¹³ See Response of the Companies to OCC-15-INT-590 and RESA/EPSC-2-INT-16, attached hereto at EWH Supplemental Attachment A at 2-3.

1 programs.¹⁴ The stipulations and supporting testimony show that these Signatory Parties
2 will receive approximately \$15.31 million in payments.¹⁵

3 **Q. Do ratepayers pay for the cumulative benefits available to the Signatory and**
4 **Non-signatory Parties?**

5 A. Yes, for the most part. The costs associated with providing the special rate
6 discounts will be recoverable from ratepayers through Rider DSE1, Rider EDR(e), Rider
7 EDR(i), and Rider DRR,¹⁶ the costs associated with implementing and running the energy
8 efficiency programs or audits will be recoverable from ratepayers through Rider DSE,¹⁷
9 the costs associated with funding the Community Connections program will be
10 recoverable from ratepayers,¹⁸ and any net costs associated with providing the new
11 experimental time-of-use rate will be recovered from ratepayers through Rider GCR.¹⁹

12 **Q. Have you been able to quantify the costs of the cumulative benefits of the**
13 **stipulations that will be paid for by ratepayers, most of which will not be receiving**
14 **the direct benefits delineated in the stipulations?**

15 A. The stipulations only provide partial information about the cost shifting and payments
16 that are proposed during the ESP IV. I received some supplemental information from

¹⁴ See, e.g., Stipulation Sections B and C.

¹⁵ List of benefits compiled based upon Stipulation at 10-15 and Mikkelsen Supplemental Testimony at 4-5.

¹⁶ Supplemental Stipulation at 2-3; Mikkelsen Third Supplemental Testimony, Attachment EMM-3 at 2; Stipulation at 9-10; Mikkelsen Supplemental Testimony at 3-4.

¹⁷ Stipulation at 10-12; Mikkelsen Supplemental Testimony at 4-5.

¹⁸ Mikkelsen Supplemental Testimony at 10 (Although not stated in the Stipulation, Ms. Mikkelsen's Supplemental Testimony asserts that the Companies will not seek to recover from other ratepayers the \$7.1 million in funds designated to assist at-risk populations. There is no similar commitment made regarding the recovery of the \$5.1 million in payments to the CHN from the Community Connections program funding).

¹⁹ Mikkelsen Fourth Supplemental Testimony at 2; see also supra n.13.

1 discovery responses given by the Companies. Unfortunately, however, the overall
2 financial impact upon the customers that cannot receive the settlement benefits that are
3 only attainable by a few Signatory or Non-opposing Parties are not made clear in the
4 material submitted.²⁰

5 From the information that we have been able to obtain to date through the testimony and
6 discovery responses, I have been able to quantify some of the costs that will be borne by
7 the ratepayers due to the cumulative impact of the stipulations. From the special
8 programs, payments, and rate discounts, ratepayers may be responsible for \$228.2
9 million.²¹ Any projected costs assessed to ratepayers through Rider RRS would be in
10 addition to the direct benefits received by the Stipulating or Non-opposing Parties.

²⁰ For example, it is not clear who will bear the cost of administrative oversight of some of the new programs. Although the Companies claim in response to PUCO-DR-33, Part 10, attached hereto at EWH Supplemental Attachment A at 4-6, that they will not seek recovery of administrative costs for the new transmission Pilot Program that would permit certain customers to opt out of Rider NMB, the Companies did not include such a guarantee in the Supplemental Stipulation or filed testimony. Nonetheless, the Companies admitted that there are administrative activities associated with the Pilot Program's implementation. See response to PUCO-DR-33, Part 9, attached hereto at EWH Supplemental Attachment A at 4-6. If those activities are completed by employees of the Companies (regulated distribution companies) or costs are allocated to the distribution business, the labor and costs of such activities may be borne by ratepayers. See also *supra* n.13, and the Response of the Companies to RESA/EPSC-1-INT-34, attached hereto at EWH Supplemental Attachment A at 7, regarding the Experimental Time-of-Use Rate Proposal (the participants of the Experimental Time-of-Use Rate Proposal will not pay the same cost for capacity as standard service customers).

²¹ See Stipulation at 7-8, 9-10, 10-15 and Mikkelsen Supplemental Testimony at 3-5; Supplemental Stipulation at 2-3; Mikkelsen Fourth Supplemental Testimony at 2; Response of the Companies to: OMAEG-3-INT-46(b); OMAEG-4-INT-88; OCC-12-INT-296; OCC-12-INT-300; OCC-15-INT-578; OCC-15-INT-579; OMAEG-5-INT-118; and OMAEG-5-INT-119, respectively attached hereto at EWH Supplemental Attachment A at 8-15. See also Response of the Companies to OMAEG-3-RPD-021, Attachment 1 (Confidential); OMAEG-4-RPD-32, Attachment 1 (Confidential); and PUCO-DR-30(a) (Confidential), respectively attached hereto at EWH Supplemental Attachment B at 1-7 (Confidential).

1 **Q. Do economic development discounts and incentives provide benefits to all**
2 **ratepayers?**

3 A. If structured properly, yes. Economic development incentives can help companies
4 lower production costs, control or provide increased certainty over their operating costs,
5 speed the opening of a plant, and influence the design of plant and equipment. Economic
6 development incentives can be used to bring fallow land into use and they can be used to
7 provide a trained workforce. In other words, a public benefit should be identifiable and
8 the incentive should pass the “but for” test—but for the incentive the operation would not
9 have opened.

10 Incentives may be appropriate for economic development reasons, but the incentives need
11 to be uniformly applied and available to all similarly situated customers. The criteria for
12 qualifying for the incentives and discounts should not be so narrowly tailored that they
13 are discriminatory or only apply to one or a few companies. Economic development
14 incentives also should be restricted to companies that primarily sell goods and services to
15 out-of-state customers or have their goods and services bundled into these exported goods
16 and services. These firms are considered to be part of the economic base of the state.

17 The selection of the recipients of narrowly defined economic development incentives
18 should not be made by a private company that is in a position to provide one of its
19 customers with a competitive advantage over another company in its service territory.
20 This is especially true if there is a quid-pro-quo as is the case in the proceeding currently
21 pending before the Commission. Most importantly, the state of Ohio should not be

1 delegating its economic development strategy and authority to a privately owned electric
2 utility.

3 What is presented in the stipulations is not a set of economic development incentives.
4 Instead, the incentives are targeted price reductions and discounts that are being offered
5 by the Companies through the regulatory process to only those customers or groups that
6 have been invited to join the exclusive club or coalition formed by the Companies, and
7 the costs of such discounts and incentives are being largely passed on to the broad pool of
8 ratepayers in the Companies' service territories who were not invited to join the club
9 formed by the Companies. Typically, in operating competitive markets, the decision to
10 offer a discount is up to the provider and that provider and its stockholders absorb the
11 discount in expectation of other gains, such as increased sales volumes tied to efficiencies
12 of scale or using slack production capacity, or to prevent the loss of the customer. The
13 cost of these discounts is not typically passed onto other customers unless the provider
14 has some form of market power. Also, in competitive markets, cost shifting does not
15 occur to customers in a defined geographic area using the regulatory powers of the state.

16 While incentives may reduce the expenses and provide associated benefits to the
17 Signatory or Non-opposing Parties that are receiving the incentive, such discounting
18 becomes problematic when the cost of the incentive is then passed on to other customers
19 or other classes of customers.

20 The value of incentives should not be shifted to other customers or established in a
21 manner that is tailored to discriminate among competitive customers, unjustly choosing
22 winners and losers. Economists consider such cost shifting to be a form of cross-

1 subsidization where parties that lack market power are paying for incentives offered to
2 parties that have market power. Such cross-subsidies are inherently market distorting.

3 There is no longer an integrated generation, transmission, and distribution power market
4 in Ohio. Electric generation in Ohio is now a competitive service. The only remaining
5 natural monopoly is in the distribution system. Regulatory policy should be very careful
6 not to allow the existence of a natural monopoly in the distribution system to be used as
7 leverage to protect non-competitive firms in the other two components of electric service.

8 **Q. Will the costs of the stipulations be borne equally and fairly by all ratepayers?**

9 A. No. From reviewing the stipulations, testimony, and applicable tariff schedules, it
10 appears that some of the costs or charges to ratepayers for the settlement programs and
11 rate discounts will be paid for by only certain commercial rate schedules, mainly the
12 General Service (GS) and General Primary (GP) customers in the Companies' service
13 territories, some costs will be paid for by all ratepayers in the Companies' service
14 territories, and some costs will be borne by all ratepayers in the Companies' service
15 territories except for the customers receiving the direct benefits.²² If this occurs, then
16 certain customers or classes will pay a disproportionate share of the benefits outlined in
17 the stipulations.

²² See generally, Ohio Edison Company, P.U.C.O. No. 11, Sheets 101 (Rider ELR, Effective June 1, 2015), 115 (Rider DSE, Effective July 1, 2015), and 116 (Rider EDR, Effective June 1, 2011 and July 1, 2015, depending on section); The Cleveland Electric Illuminating Company, P.U.C.O. No. 13, Sheets 101 (Rider ELR, Effective June 1, 2015), 115 (Rider DSE, Effective July 1, 2015), and 116 (Rider EDR, Effective June 1, 2011 and July 1, 2015, depending on section); and The Toledo Edison Company, P.U.C.O. No. 8, Sheets 101 (Rider ELR, Effective June 1, 2015), 115 (Rider DSE, Effective July 1, 2015), and 116 (Rider EDR, Effective June 1, 2011 and July 1, 2015, depending on section), respectively attached hereto as EWH Supplemental Attachment A at 16-57; see also, Response of the Companies to OCC-13-INT-345; OCC-15-INT-580; OCC-15-INT-581, respectively attached hereto as EWH Supplemental Attachment A at 58-60.

1 **Q. Are there other Signatory or Non-opposing Parties that indirectly benefit from**
2 **the stipulations?**

3 A. Yes, given that the Supplemental Stipulations adopt the Stipulation and the ESP IV
4 Application, as modified by the stipulations,²³ beneficiaries to the stipulations include
5 those who benefit from the establishment of a rider to recover from ratepayers all costs
6 associated with the generating plants subject to a purchase power agreement between the
7 regulated utility and unregulated affiliate. Rider RRS provides the regulated entities' (the
8 Companies') parent company, FirstEnergy Corp., with a guaranteed return on the
9 generation assets owned by FirstEnergy Solutions that are included in the PPA
10 transaction that forms the basis of Rider RRS.²⁴ Beneficiaries of the stipulations would
11 include the Companies, Ohio Power, and their affiliates.²⁵

12 **Q. Are the Supplemental Stipulations in the public interest?**

13 A. No. In addition to the discussion above regarding costs of incentives and the unfair
14 cross-subsidization of costs to a select group of customers, the Supplemental Stipulations
15 are also not in the public interest because they adopt the Companies' Application with
16 regard to the Economic Stability Program and Rider RRS, as well as the associated PPA.
17 As explained in my Supplemental Testimony, the proposed PPA requires the Companies
18 to purchase all of the power from uncompetitive generating plants owned by its affiliate,
19 FirstEnergy Solutions, and pass on the costs of fuel and any plant upgrades, plus a return,
20 to ratepayers. The output from the generating units will be sold into the regional

²³ See supra n.9.

²⁴ See generally, Testimony of Stephen E. Strah at 4-5 (August 4, 2015).

²⁵ Stipulation at 25 (Ohio Power Signature Page).

1 wholesale market, and any losses or profit resulting from the sale will be passed on to all
2 customers in the Companies' service territories through Rider RRS. The Companies
3 have projected that there will be no profit in the first three years covered by all three
4 stipulations.

5 Although the Companies assert that the Stipulation, which is adopted by the
6 Supplemental Stipulations in its entirety,²⁶ preserves the competitive retail market, an
7 overall settlement that includes the PPA proposal prevents a completely free market from
8 evolving and, therefore, is not in the public interest.

9 More specifically, the Supplemental Stipulations are not in the public interest for two
10 reasons. First, they adopt a scheme that will provide one certified retail electric supplier
11 in Ohio with a competitive advantage in the Ohio market as its uneconomic generating
12 plants will be subsidized by the Companies' ratepayers through approval of the Economic
13 Stability Program and associated PPA. Second, the Supplemental Stipulations and the
14 PPA will deter entry into the power generation portion of the market by new competitors.
15 Typically, if a market participant cannot compete in a competitive market, it will fail.
16 Subsidizing an existing market participant in the hope that it may be able to compete at
17 some point in the future is not in the public interest, nor is it good public policy. It will
18 only deter entry and keep prices higher than they would be in a competitive market. The
19 PPA can best be described as a coin-flip bet that FirstEnergy Corp. is making, one where
20 it's "heads I win and tails you lose."

²⁶ See *supra* n.9.

1 By examining the algebra behind the logic of the proposal, the inequities of the proposal
2 become apparent:

3 Let p_C represent the price paid for by consumers, p_{FE} the price charged by FirstEnergy
4 Solutions, and p_A is the price charged by alternative suppliers.

5 Also let the production cost of energy be represented by c_{FE} for FirstEnergy Solutions
6 and c_A for the alternative producers.

7 If $p_C = p_A = p_{FE}$ then the market is at a short-term equilibrium and there is no incentive to
8 change suppliers. This can only be a stable solution over time only as long as $c_A = c_{FE}$.

9 However, the Companies have informed the Commission that its affiliate could not sell
10 the output from the generating plants covered by the PPA for a profit, implying that for
11 some fraction of its capacity its production cost is higher than the cost of competitors.
12 Therefore, $c_{FE} > c_A$.

13 Now let t_{FE} represent the tax or surcharge imposed by the Companies through the
14 proposed regulation (Rider RRS) on all customers if the net costs outweigh the revenues
15 that the plants obtain in the market; then $t_{FE} = f(c_{FE} - c_A)$. This equation notes that as the
16 cost differential increases between the plants in question and alternative sources of
17 generating capacity the tax increases automatically.

18 There is a secondary effect to this dynamic that offers greater pause, which is the power
19 of precedent. If the PPA is approved and other generating assets become uncompetitive
20 then the Commission has established a precedent that will be used to bring those assets

1 under regulatory protection with an assured rate of return on capital. This will affect not
2 just the Companies' affiliated generating assets but all generating plants located in the
3 state of Ohio; after all, what is fair for one must be fair for all. In this case, allow **b** to
4 represent the decimal fraction of non-competitive generating assets expressed in terms of
5 kilowatt-hours and **(1-b)** is the fraction that is competitive; then **b + (1-b) = 1.00**.

6 Then: $t_{FE} = f(b)$ meaning that the tax (or costs) imposed by the Companies, and others in
7 similar situations, will be a function of the portion of generating capacity that falls under
8 a PPA and its successors and as **b** increases, so does t_{FE} .²⁷ In other words, as **b** increases,
9 or as the portion of the state's generating fleet that is not price competitive in the
10 wholesale markets increases, the tax will increase. This will effectively deter entry and
11 investments by competitors in generating capacity.

12 Then: $p_C = p_A + t_{FE} = p_{FE}$.

13 The algebra states that as the production cost differential increases compared to that of
14 alternative producers, the imposed tax increases proportionately, thereby redistributing
15 income from customers located in the Companies' service territories to FirstEnergy
16 Solutions and FirstEnergy Corp.'s shareholders. Heads, FirstEnergy Solutions wins; tails
17 FirstEnergy Solutions' competitors lose. No matter what, FirstEnergy Solutions'
18 customers will have, at best, market electric rates; but, more likely, they will have higher
19 electric rates than if a competitive generating market existed. The second conclusion I
20 reach is that entry into the state by alternative energy producers will be deterred because

²⁷ The actual function is nested: $t_{FE} = f(b)$ with $b = g(c_i - c_A)$, where c_i is the operating cost at power plant *i*.

1 the precedent provided by the PPA will eliminate their pricing advantage held by new
2 entrants. The PPA is a way of using the regulatory power of the state to create political
3 market power in the electric market for the legacy generators. Deterring entry and
4 investment in the state of Ohio is not in the public's interest.

5 **Q. Have you been able to quantify the costs of the indirect benefits attributed to the**
6 **Signatory or Non-opposing Parties that benefit from the establishment of Rider**
7 **RRS, which was adopted by the Supplemental Stipulations?**

8 A. No. As explained in my previous testimony,²⁸ Ms. Mikkelsen appears to value the
9 PPA provision of the ESP IV Application at \$2.0 billion in favor of customers, but
10 recognizes that that benefit may not come to fruition, and if it does, it will not occur
11 during the term of ESP IV.²⁹ The stipulations appear to adopt the Companies' proposed
12 Rider RRS in its entirety with one modification. The Supplemental Stipulations' blanket
13 adoption of the Companies' Application with regard to the Economic Stability Program
14 and Rider RRS, as well as the associated PPA (with one modification), adds costs to the
15 proposed overall settlement that will be borne by ratepayers, and, as explained above, is
16 not in the public interest.³⁰

²⁸ Hill Supplemental Testimony at 16.

²⁹ See Mikkelsen Supplemental Testimony at 2.

³⁰ See, e.g., Supplemental Testimony of Ramteen Sioshansi at 2; Supplemental Testimony of James F. Wilson at 3-4; Direct Testimony of Steven Ferrey at 12 (all filed May 11, 2015).

1 **Q. Why do you believe the Companies, through the Supplemental Stipulations,**
2 **increased the size of what you have termed a “redistributive coalition”?**

3 A. In my previous testimony, I explained how the Stipulation formed a redistributive
4 coalition, which is a relatively small group that promotes policies for their mutual
5 financial benefit.³¹

6 The redistributive coalition was assembled to present to the Commission and to the
7 public the façade not only of broad support for the ESP IV, but of a broad range of
8 benefits flowing to the classes of customers represented by the Signatory or Non-
9 opposing Parties. The stipulations and testimony are careful to state that the participation
10 of the members of the redistributive coalition indicates broad support and benefits
11 flowing to the classes that they represent. Unfortunately, the benefits only flow to the
12 Signatory or Non-opposing Parties.

13 While the Companies imply that the outcome was universal, the stipulations are clear
14 that the provisions only apply to the entities that were involved in the negotiations and
15 the benefits derived only apply to the Signatory or Non-opposing Parties. In her
16 testimony, Ms. Mikkelsen asserts: “As can be seen from this list, the Signatory Parties
17 represent varied and diverse interests including large industrial customers, small and
18 medium businesses, mercantile customers, colleges and universities, low income
19 residential customers, organized labor and a large municipality.”³² The façade of
20 universality, however, is apparent later in her testimony: “The Signatory Parties represent

³¹ Hill Supplemental Testimony at 14.

³² Mikkelsen Supplemental Testimony at 6.

1 a broad range of interests including the Companies, another Ohio electric distribution
2 utility, organized labor, various consumer groups (themselves representing a broad range
3 of customer classes and varied interests), and a large municipality.”³³

4 Ms. Mikkelsen then concludes that given the group of Signatory Parties that make up the
5 coalition, the stipulation as a package benefits customers and the public interest.³⁴ As I
6 have stated before, this is a carefully crafted coalition designed to look as if it represents
7 broad groups, rather than the specific entities that they actually represent.

8 The Supplemental Stipulations merely add two more entities to that redistributive
9 coalition by adding additional provisions that are for the benefit of the Signatory or Non-
10 opposing Parties.

11 **Q. How does the concept of a redistributive coalition apply?**

12 A. Here, the Companies have assembled a coalition to promote a policy that benefits
13 their affiliate, FirstEnergy Solutions, and the other coalition members. The benefit to the
14 Companies consists of a subsidy to pay for its affiliated company’s underperforming
15 generation. This benefit to the Companies has been valued at \$3 billion by one expert
16 witness for a non-signatory party, the Office of the Ohio Consumers’ Counsel.³⁵

17 The large heterogeneous group that has to pay for the majority of this proposed policy, as
18 well as the other costs embedded in the stipulations, consists of the remaining

³³ Id. at 7.

³⁴ Id. at 8.

³⁵ See Direct Testimony of James F. Wilson at 12 (December 22, 2014).

1 commercial, industrial, and residential ratepayers of northern Ohio who are not members
2 of the redistributive coalition. This large ratepayer group would be very difficult and
3 expensive to organize for purposes of advocating the group's interests.

4 Further, the costs of learning about and understanding the impact of the proposals set
5 forth in the various stipulations and the ESP IV Application are substantial because these
6 costs are opaque, buried in a series of riders that are beyond the ability of a typical
7 ratepayer to understand, and provided through an evolving regulatory process that needs
8 to be constantly monitored. Non-members of the redistributive coalition are further
9 disadvantaged by the large, complicated, last minute submittals to the Commission.
10 Additionally, many of the provisions embedded in the stipulations are written in ways
11 that are extremely difficult to disentangle, including the wholesale adoption of the
12 Companies' large ESP IV Application with limited exceptions.

13 Economists and political theorists who have developed public choice theory anticipated
14 the dense and opaque nature of these sorts of submittals with another concept: *rational*
15 *ignorance*.³⁶ A redistributive coalition can raise the costs of obtaining and understanding
16 information that relates to their proposed actions by making submittals as opaque and
17 technical as possible. The term "rational ignorance" was coined to describe the
18 reasonable disengagement of the public from trying to understand technical information
19 and expert testimony where the cost of obtaining the knowledge is high and the return to
20 individuals from their effort is low, even if the collective impact is large. Rational
21 ignorance also explains how members of a redistributive coalition will focus on the direct

³⁶ Downs, Anthony. *An Economic Theory of Democracy*. New York: Harper Row, 1957.

1 impact of payments and benefits to them or their members without acknowledging the
2 full impact of the proposed redistribution on the public at large. This is a point to keep in
3 mind when the Commission's three part test of the reasonableness of the multiple
4 stipulations is discussed below: the calculation used by the members of a redistributive
5 coalition is their net benefit, not society's net benefit.

6 **Q. Does the expansion of the redistributive coalition through the Supplemental**
7 **Stipulations improve the overall settlement or address your previously stated**
8 **concerns?**

9 A. No. The cost of organizing the group and adding two more parties to the group is
10 small relative to the benefits received by the Signatory or Non-opposing Parties. The
11 costs associated with providing incentives to a group of parties, much of which are
12 funded by ratepayers that have been excluded from the settlement, are far outweighed by
13 the returns.

14 The actual cost of organizing the redistributive coalition will not be borne significantly
15 by the organizer, the Companies. These costs will instead be passed on to ratepayers in
16 the form of various costs or expenses of the regulated utility. Therefore, the direct or
17 lasting expense incurred by the organizer, the Companies, is minimal. Some of the
18 coalition members receive cost reductions, a predictable financial benefit, some obtain
19 benefits that will be passed on to the members of their organizations, and others find
20 funds to support their organizations' missions. Many coalition members may be able to
21 use the windfalls to pay for their administrative expenses. Nonetheless, while many of
22 these pass-through benefits may be socially beneficial or meritorious to a relatively small
23 group of beneficiaries, it is at the expense of a much larger group. Accordingly, the

1 overall settlement, as a package, does not benefit most ratepayers and is not in the public
2 interest.

3 **Q. How do you think the coalition members were selected?**

4 A. The list of signatories was carefully constructed. The Companies stated that the
5 members of the redistributive coalition “represent varied and diverse interests including
6 large customers, small and medium businesses, mercantile customers, colleges and
7 universities, low income residential customers, organized labor, and a large
8 municipality.”³⁷ However, the list also raises a series of questions: how are they
9 representative? Did they represent their peers and similar organizations in the negotiation
10 process? Were they able to obtain similar benefits for their peers or at the exclusion of
11 their peers? Generally speaking, the answers to the last two questions are no: they
12 represented themselves and the incentives they obtained are for their organizations or
13 companies alone.

14 For example, why is the City of Akron a direct beneficiary while other communities with
15 low-income populations, such as Toledo, are excluded? Why are private colleges and
16 universities beneficiaries, while public colleges and universities are excluded? Why are
17 COSE's members eligible for audits, while small business members of other chambers of
18 commerce or organizations are left out? Why would a grocer that is able to meet certain
19 requirements receive an operating cost advantage over its competitors?

³⁷ See Mikkelsen Supplemental Testimony at 2.

1 The simple answer is that not all customers were invited to become members of the
2 coalition. This is a political coalition assembled to provide a veneer of inclusion and the
3 image of universal support in exchange for a limited set of pre-defined financial benefits.
4 In exchange, the members of the coalition (i.e., Signatory or Non-opposing Parties) have
5 committed to endorse the totality of the ESP IV Application, including Rider RRS. The
6 Supplemental Stipulations adopted the Stipulation in its entirety, which includes the
7 statement: “each Signatory Party agrees to and will support the reasonableness of the ESP
8 IV and this Stipulation before the Commission, and to cause its counsel to do the
9 same.”³⁸

10 The redistributive coalition is being used by the Companies, and their parent company,
11 FirstEnergy Corp., as a broad representation of the economy in a political process. The
12 Commission, however, is being asked to adopt a settlement that chooses winners and
13 losers among competitors. Why is this good public policy?

14 **Q. From your perspective is there anything illegal about creating and using a**
15 **“redistributive coalition” to your benefit?**

16 A. There is nothing illegal about forming a redistributive coalition; it is a political
17 coalition designed to extract a favorable outcome from a regulatory or legislative
18 proceeding for its members. It just has to be recognized for what it is, and for what it is
19 not. It is not a bargaining body that represents all of the Companies’ ratepayers or the
20 public interest.

³⁸ Stipulation at 18.

1 The Companies imply that the negotiations that took place between the members of its
2 redistributive coalition were “fair.” However, there is nothing supporting this conclusion
3 in the record. Ms. Mikkelsen’s Testimony supporting the Supplemental Stipulations does
4 not address the negotiations of the Signatory or Non-opposing Parities or fairness. The
5 testimony supporting the Supplemental Stipulations merely asserts that each stipulation
6 continues to meet the Commission’s criteria and refers to the Supplemental Testimony
7 supporting the initial Stipulation. In the referenced Supplemental Testimony, Ms.
8 Mikkelsen references the Commission’s criteria when considering the reasonableness of a
9 stipulation: “a stipulation must satisfy three criteria: (1) the stipulation must be the
10 product of serious bargaining among capable, knowledgeable parties; (2) the stipulation
11 must not violate any important regulatory principle or practice; and (3) the stipulation
12 must, as a package, benefit ratepayers and the public interest.”³⁹ Ms. Mikkelsen then
13 explains how she believes that the initial Stipulation meets those criteria. Ms. Mikkelsen,
14 however, fails to address the Commission’s criteria in her Third and Fourth Supplemental
15 Testimony as they relate to the Supplemental Stipulations.

16 **Q. Do you agree with Ms. Mikkelsen’s conclusion?**

17 A. No. There is no evidence in the record that the Supplemental Stipulations satisfy the
18 Commission’s three-prong test. First, in my reading of the Supplemental Stipulations,
19 which adopt the Stipulation and supporting testimony, there is no evidence that the first
20 criterion has been met, as there is no evidence that all or most of the Signatory or Non-

³⁹ See Supplemental Testimony of Eileen M. Mikkelsen at 2; see also Third Supplemental Testimony of Eileen M. Mikkelsen at 3 and Fourth Supplemental Testimony of Eileen M. Mikkelsen (referencing the above-mentioned factors).

1 opposing Parties were knowledgeable of all provisions of the Companies' ESP IV
2 Application that they have agreed to through the Stipulations.

3 Furthermore, there is no evidence in the record that the claimed additional supporters of
4 the Companies' ESP IV Application are actual supporters of the Application and/or the
5 stipulations or that they are even knowledgeable of the contents of the Application and/or
6 multiple stipulations.⁴⁰ For instance, the President and CEO of FirstEnergy Corp., Chuck
7 Jones, published an article in the *Cleveland Plain Dealer*, stating that "the supporters ...
8 include many residential, commercial, industrial and low-income customers, as well as
9 organized labor, communities and schools." Many of the cited "supporters" in the article
10 are not Signatory or Non-opposing Parties to the multiple stipulations, and it is unknown
11 what, if any, incentives or benefits that any such "supporters" may have received to voice
12 their support for the Companies' proposal. It is also unknown what the "support" is truly
13 based upon. For instance, did those "supporters" understand that the Companies' motive
14 came at an expense to the Companies' ratepayers?

15 Mr. Jones explained the purpose of the Companies' proposal and settlement pending
16 before the Commission in his July 27, 2015 interview with *Plain Dealer* reporter John
17 Funk: "Jones said FirstEnergy's future is at risk if it cannot persuade the state's Public
18 Utilities Commission to *force ratepayers* to cover the full costs of electricity from two of

⁴⁰ "Powering Ohio's Progress' rate plan is about preserving vital power plants for Ohio customers: Chuck Jones (Opinion)," *Cleveland Plain Dealer* (August 2, 2015), attached hereto at EWH Supplemental Attachment A at 61-63; see also list of claimed supporters in the Companies' cover letter filed with Stipulation (December 22, 2014) and Response of the Companies to OMAEG-3-INT-27; OMAEG-3-INT-28; OMAEG-3-INT-29; OMAEG-3-INT-30; OMAEG-3-INT-31; OMAEG-3-INT-32; OMAEG-3-INT-33; OMAEG-3-INT-34; OMAEG-3-INT-35; OMAEG-3-INT-36; OMAEG-4-INT-68; OMAEG-4-INT-69; OMAEG-4-INT-72; OMAEG-3-INT-25; OMAEG-4-INT-73; OMAEG-4-INT-74; and OMAEG-4-INT-75, attached hereto as EWH Supplemental Attachment A at 64-80.

1 its huge coal and nuclear plants, *even if other sources of electricity, such as natural gas,*
2 *would be cheaper for consumers.*” Funk reported that in an interview with the
3 newspaper’s editorial board Jones stated: “I am trying to save a company.”⁴¹

4 Second, the parties did not represent a diverse group of customers or certain classes of
5 customers as they only represented themselves. It is my understanding that the second
6 criteria fails as the Commission has recently stated that it disfavors direct payments of
7 funds to intervenors, even if those funds are to be refunded to ratepayers.⁴² This appears
8 to be the case with many of the funds provided to organizations in the stipulations. This
9 policy position would also apply to the provisions contained in the Supplemental
10 Stipulations, as well as the Stipulation, that are only available to one or more of the
11 Signatory or Non-signatory parties at the exclusion of other customers.

12 Finally, it is clear that the Supplemental Stipulations do not meet the third criterion of
13 benefiting ratepayers and the public interest. The Supplemental Stipulations do not
14 benefit ratepayers as a whole and are not in the public interest. Providing benefits to
15 carefully selected members of a redistributive coalition cannot be deemed to benefit all
16 ratepayers, similarly-situated ratepayers who were not included in the bargaining process,

⁴¹ Funk, John, “FirstEnergy wants Ohio to end deregulation, return to state-controlled rates,” *Cleveland Plain Dealer* (July 28, 2015, updated July 29, 2015) (emphasis added), attached hereto at EWH Supplemental Attachment A at 81-83.

⁴² See *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Authority to Recover Costs Associated with the Ultimate Construction and Operation of an Integrated Gasification Combined Cycle Electric Generation Facility*, Case No. 05-376-EL-UNC, Order on Remand at 11-12 (February 11, 2015) (“The Commission notes that provision l.b. of the Stipulation includes direct payments to intervenors of funds to be refunded to ratepayers. * * * However, the Signatory Parties to this Stipulation and parties to future stipulations should be forewarned that such provisions are strongly disfavored by this Commission and are highly likely to be stricken from any future stipulation submitted to the Commission for approval.”)

1 or the public interest as a whole. The bargains struck will result in most of the
2 redistributive coalition's benefits being paid for by the vast majority of ratepayers: those
3 who were not part of the bargaining and those who will not receive the direct payments
4 and other benefits extracted by the members of the redistributive coalition. If enacted,
5 the broad pool of electricity users will pay a *de facto* tax enabled and enforced by the
6 Commission to benefit the redistributive coalition assembled by the Companies,
7 including the organizer, the Companies, which are the largest beneficiaries, as well as
8 their affiliate.

9 **Q. Why is such a redistributive coalition a problem for policy makers?**

10 A. The problem is that those who stand to lose from policies promoted by a
11 redistributive coalition are part of a large, heterogeneous group, one that is difficult and
12 expensive to organize in opposition to the proposed redistribution.

13 Information that is missing from the cumulative settlement, including testimony
14 supporting the Supplemental Stipulations that adopt the Stipulation, include models and
15 estimates on the losses that will be incurred by companies that are not part of the
16 redistributive coalition when faced with higher prices triggered by the redistributive
17 features of the stipulations and Economic Stability Program; deterred investment by new
18 power generators; the impact of embargoing the importation of power from out-of-state
19 generators; cost-shifting that will take place from the members of the redistributive
20 coalition to those not invited to join the coalition; and the expected net benefits to be
21 enjoyed by the Companies or their parent company from the increase in revenues versus
22 the costs it will incur during the three-year period covered by the stipulations and the 15-
23 year period covered by the PPA.

1 One loss will be indirect, but it will directly affect the economy of the state of Ohio. This
2 is the loss in Gross State Product and employment associated with operating and sales
3 cost increases that are part of the elasticities associated with the cost of electricity.⁴³ The
4 price elasticity of demand for electricity that will be experienced by all other
5 manufacturers in the region with the increases in electric prices that will be necessary to
6 fund the provisions of the stipulations, including Rider RRS, has not been considered.
7 My concerns about the price elasticity of demand for electricity among manufacturers
8 generally were addressed in my previous testimony and will not be repeated here.
9 However, it is important to note that the additional provisions of the Supplemental
10 Stipulations exacerbate my original concerns.

11 **Q. Do the Supplemental Stipulations include programs for demand reduction and**
12 **energy efficiency programs that could reduce electricity demand in Northern Ohio?**

13 A. Yes, the Supplemental Stipulations include demand reduction programs, including an
14 interruptible program and a time-of-use rate proposal.⁴⁴ These are in addition to the
15 amounts of money promised to support the administration of energy efficiency programs,
16 which will benefit a small number of ratepayers, in the Stipulation.

17 The Companies were proponents of legislation in the Ohio General Assembly to revise
18 and/or freeze energy efficiency and peak demand reduction programs that were part of

⁴³ The elasticity associated with Gross Product is the percent change in value added in a manufacturing sector divided by the percent change in the cost of electricity. The elasticity in the number of jobs in the manufacturing sector is the percent change in the number of jobs divided by the percent change in the cost of electricity. These can also be expressed in their instantaneous forms, the ration of the natural logarithms of each variable.

⁴⁴ Supplemental Stipulation at 1-2; Second Supplemental Stipulation at 1-2; Mikkelsen Fourth Supplemental Testimony at 2.

1 the energy efficiency portfolio in Ohio.⁴⁵ Proponents of the legislation argued that
2 energy efficiency should compete without subsidy with other forms of generation in an
3 open, unsubsidized market. Through the various stipulations and ESP IV Application,
4 the Companies propose additional energy efficiency and peak demand reduction
5 programs and argue for a generation subsidy because certain generation facilities cannot
6 compete in the open market.

7 The Companies also argue that its affiliated subsidized generation can be complemented
8 with a modest and highly selective subsidy to promote energy efficiency and peak
9 demand reduction programs. The Companies want to replace independent public
10 administration and a broader efficiency mandate with certain administrators running a far
11 smaller funding vehicle for the efficiency plans.

12 The energy efficiency programs included in the stipulations have been carved out to
13 entice specific signatories to join the redistributive coalition and provide political support
14 for the package of rates and riders that are the true substance of *Powering Ohio's*
15 *Progress Plan*. The efficiencies gained through the series of *ad hoc* small initiatives will
16 not make a serious difference in the regional demand for electricity. But they will result
17 in shifting costs to the ratepayers who were not allowed to become signatory parties, if
18 the redistributive coalition persuades the Commission to adopt the stipulations and ESP
19 IV.

⁴⁵ See testimony submitted to the Senate Public Utilities Committee regarding SB 58 (the predecessor to SB 310) by Leila L. Vespoli on behalf of FirstEnergy Corp. in support of Revisiting Ohio's Energy Efficiency Mandates (April 9, 2013), attached hereto at EWH Supplemental Attachment A at 84-90; see also "No retreat: the governor enters the energy debate and sends the right message to lawmakers," *Akron Beacon Journal* (May 3, 2014) and "Kasich should work against deeply flawed Ohio Senate Bill 310: editorial," *Cleveland Plain Dealer* (May 2, 2014), attached hereto at EWH Supplemental Attachment A at 91-93.

1 **Q. What is the cumulative effect of the stipulations on energy policy?**

2 A. The submission of the stipulations has effectively confused the order of public policy
3 making in regard to the future of electric energy production and cost, and serves only to
4 distract the Commission (and the State) from answering the most important questions
5 about Ohio's energy future:

6 • What is the proper energy-producing footprint? Is it energy produced within the
7 borders of the state or is it the PJM footprint?

8 • What is the best and least cost way of resolving uneconomic power generating
9 assets to ensure the integrity of the power transmission and distribution systems
10 and truly guarantee reliable power? This has to go beyond the Companies'
11 service territories.

12 • How can Ohio and the PJM footprint accommodate industry-scale proof of
13 concept energy experiments to comply with mandates to lower CO₂ and
14 particulate emissions in power generation?

15 • Should low-income utility voucher programs or special interest programs
16 provide for statewide access and equity? Should they be tax-based programs
17 voted on by the Ohio General Assembly, as opposed to programs and costs
18 embedded in utility specific rates for select geographic areas of the state and only
19 for a select group of beneficiaries?

20 The *de facto* taxation and redistribution measures that are proposed in the stipulations
21 properly belong to the Ohio General Assembly, not the Commission.

22

1 **Conclusion**

2 **Q. Have your prior recommendations to the Commission with regard to the**
3 **Companies' "Powering Ohio's Progress" strategy, set forth in its Fourth Electric**
4 **Security Plan, changed in any way as a result of the Supplemental Stipulations?**

5 A. No. I continue to recommend that the Commission reject the Companies' request for
6 the establishment of a rider and the utilization of a power purchase agreement to
7 subsidize portions of the aging, inefficient power plants owned by their affiliate,
8 FirstEnergy Solutions. I also continue to recommend that the Commission reject any
9 proposals that are detrimental to Ohio businesses and economic growth, and that are not
10 in the public interest, including incentives that are neither uniformly applied nor available
11 to all similarly situated customers. The redistributive features of the stipulations that shift
12 costs to companies that are not part of the redistributive coalition will cause those
13 companies to face higher operating costs and be less competitive.

14 **Q. Does this conclude your second supplemental testimony?**

15 A. Yes.

CERTIFICATE OF SERVICE

The undersigned hereby certifies that a true and accurate copy of the foregoing document was served on August 10, 2015 by electronic mail upon the persons listed below.

/s/ Rebecca L. Hussey

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