DYNEGY EXHIBIT NO. 2

BEFORE THE PUBLIC UTILITIES COMMISSION OF OHIO

In The Matter of the Application Seeking Approval of Ohio Power Company's Proposal to Enter into an Affiliate Power Purchase Agreement For Inclusion in the Power Purchase Agreement Rider	)	Case No. 14-1693-EL-RDR
In The Matter of the Application of Ohio Power Company for Approval of Certain Accounting Authority	)	Case No. 14-1694-EL-AAM

SUPPLEMENTAL DIRECT TESTIMONY OF

DEAN ELLIS

VICE PRESIDENT, REGULATORY AFFAIRS, DYNEGY INC.

IN OPPOSITION TO AEP OHIO'S SETTLEMENT AGREEMENT

Filed: December 28, 2015

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SUPPLEMENTAL DIRECT TESTIMONY OF
DEAN ELLIS**

INTRODUCTION

Q. WHAT IS YOUR NAME AND BUSINESS ADDRESS?

A. My name is Dean Ellis and my business address is 601 Travis Street, Suite 1400, Houston, TX 77002.

Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?

A. I am employed by Dynegy Inc. ("Dynegy"). My title is Vice President, Regulatory Affairs. I am responsible for overseeing the development and advancement of Dynegy's wholesale and retail regulatory and environmental policy. I also oversee Dynegy's governmental and legislative affairs activities.

Q. ARE YOU THE SAME DEAN ELLIS WHO PREVIOUSLY TESTIFIED IN THIS PROCEEDING?

A. Yes. Earlier in this proceeding, I provided testimony opposing Ohio Power Company's ("AEP Ohio") amended application that was filed on May 15, 2015.

PURPOSE OF THIS SUPPLEMENTAL TESTIMONY

Q. WHAT IS THE PURPOSE OF THIS SUPPLEMENTAL TESTIMONY?

A. This supplemental testimony is offered on behalf of Dynegy to respond to the December 14, 2015 proposed Joint Stipulation and Recommendation ("Stipulation"). AEP Ohio's proposal in its amended application was to enter into a power purchase agreement ("PPA") with AEP Generation Resources Inc. ("AEPGR") for the generation output of several of its generating units ("PPA units") or in the case of the jointly owned units the allocated portion owned by AEPGR.

AEP Ohio in turn would net revenues received from selling the output and capacity from the designated units or parts of units against the costs incurred by AEPGR and return on equity paid to AEPGR. AEP Ohio would then bill or credit retail customers for the net of costs to revenues. As stated in my initial direct testimony, Dynegy opposes AEP Ohio's proposal for the PPA as well as AEP Ohio's proposal to net revenues received and costs incurred related to AEP Ohio's Ohio Valley Electric Corporation ("OVEC") entitlement, for which AEP Ohio already has a direct contractual relationship through an existing agreement. The Stipulation does nothing to change Dynegy's opposition to the proposal.

STIPULATED PPA PROPOSAL

Q. WHY DOES DYNEGY OPPOSE THE STIPULATED PPA PROPOSAL?

A. As I stated in my initial direct testimony, Dynegy opposes arrangements or constructs that are designed to distort the markets in a manner that assure benefits to one market participant and therefore inappropriately disadvantage other market participants. With its incorporation of AEP Ohio's PPA proposal and OVEC entitlement proposal, the Stipulation is just such an arrangement. If approved by the Commission, the Stipulation will have a direct impact for years on Dynegy's ability to compete with AEPGR and AEP Ohio in the wholesale markets. Under the proposed PPA, AEPGR will have all its costs covered plus a guaranteed 10.38% rate of return. All other merchant generators, including Dynegy, must compete for sales and bear the risk of lost revenues if they do not competitively price their generation output. The Stipulation provides AEPGR with an advantage over other merchant generators, placing other existing merchant generators, jobs and tax revenue at risk. Further, because the design of the PPA remains cost plus, AEPGR and AEP Ohio have no financial incentive to act in an economically rational manner for the purchased output from the PPA units or the OVEC entitlement. Including the PPA units and the OVEC entitlement in the PPA rider will effectively encourage the continued operation of less efficient, less cost effective plants and discourage the modernization of generation sited in Ohio.

Q. DOES THE STIPULATION HARM THE PUBLIC?

A. Yes, in addition to harming Dynegy and other merchant generators, the Stipulation harms the public in three ways. First, AEP Ohio's customers must pay a significant subsidy to AEPGR. Second, the subsidy creates a disincentive for AEP Ohio and AEPGR to operate the subsidized units efficiently and to competitively market the units output in the PJM market. Third, the subsidy will act as a barrier to new market participants who must put their own capital at risk to build or purchase generation units with no guaranteed rate of return to compete against AEPGR's subsidized units.

Q. WHAT COMMITMENTS IN THE STIPULATION HAS AEP OHIO MADE WITH RESPECT TO THE JOINTLY OWNED UNITS?

A. As I explained in my initial direct testimony: Conesville unit 4; Stuart units 1-4; and Zimmer unit 1 are only partially owned by AEPGR – the other owners are Dynegy and The Dayton Power & Light Company ("DP&L"). OVEC is owned by numerous entities in addition to AEP Ohio, including DP&L, FirstEnergy and Duke. The PPA generating units partially owned by AEPGR are commonly referred to as Joint Owned Units ("JOUs") and are covered by Joint Operating Agreements ("JOAs"). At page 23 of the Stipulation and with regard to the units co-owned with

Dynegy (and DP&L), AEP Ohio has stated that it will open a docket at the PUCO by March 30, 2017 that will identify and remove any barriers to retiring, refueling or repowering those units. Additionally, AEP Ohio has stated if it cannot get the co-owners (Dynegy and DP&L) to commit to the retirement, refueling or repowering of those units, it will report by January 1, 2024 the steps it has taken to consolidate ownership.

Q. DOES THE STIPULATION ADDRESS YOUR CONCERNS WITH THE EFFECTS OF THE PPAS ON THE JOINT OWNERSHIP?

A. No, as mentioned above, there are three owners of the joint-owned PPA units. The ownership is fractional in nature, where each owns a share of the unit. Each owner offers (bids) its fractional share into the PJM energy and capacity markets, and each owner receives its share of the market revenues. On the cost side, the operations costs are split amongst each owner in proportion to their fractional share. Should one owner receive an out-of-market subsidy such as the PPA rider, it will greatly distort the ownership arrangement. For example, if AEPGR were to receive an out-of-market PPA at above-market rates, the perverse effect would be that the PPA owner would be at a significant cost advantage, with the non-PPA owner at a disadvantage. Said differently, if one were to co-own a business with a business partner, and that partner were to receive a guaranteed, above-market subsidy, the subsidized partner would become agnostic to the prices at which the business sells its product eliminating any incentive for the subsidized partner to improve efficiency in operations. The result would be an increase in the cost of operations for the joint owners ultimately putting the non-subsidized partner's ability to compete in jeopardy. In the case of AEPGR, it will not only receive its costs under the PPA but also a set return on equity of 10.38% - both disincentives to the efficient operation and capital investment in the PPA units. AEPGR will also have less incentive to consider any consolidation of ownership of the joint-owned PPA units with the long-term PPA in place. Approval of the Stipulated PPA proposal will also discourage efforts to maximize efficiency, reliability and profitability of the units due to diverging motivations and objectives of the joint owners.

Q. DOES THE STIPULATION PROVIDE AEPGR AND AEP OHIO WITH ADEQUATE INCENTIVE TO MANAGE THE PPA UNITS EFFICIENTLY AND COST-EFFECTIVELY OR TO RESPOND TO MARKET SIGNALS?

A. Typically, a merchant generator has a direct financial incentive to bid its capacity and energy into the market at prices that will be attractive to buyers yet attempt to cover operating costs and maximize margins to ensure the continued life of the asset. That requires merchant generators to carefully control costs, and carefully watch market pricing of a power market that fluctuates greatly depending on weather and economic activity. By contrast a regulated generator operating on a cost of service basis is not concerned about arriving at a price that will both attract buyers and recover its costs. It strives to keep its costs at the rates established and approved by the regulator (who generally sets rates based on units shown to be used and useful).

The PPA and PPA rider construct is a hybrid of the competitive and regulated merchant generator constructs that awards AEPGR for years with the best elements of being an unregulated merchant generator without the down side of being a regulated cost of service generator. Under the Stipulation, AEPGR will be guaranteed a competitive market rate of return for years but without the risk of not making that return because of weak sales, increasing costs, or low priced competition. On the other hand, AEPGR will not have the risk typically associated with cost of service regulation that requires the units to be used and useful and to operate under set rates. And under the PPA, if costs go up, AEPGR can simply pass through those increased costs to its affiliate (AEP Ohio) which in turn will pass on the cost increases to its customers through the non-bypassable PPA rider.

Simply put, the combination of the PPA and the PPA rider eliminates much of the cost focus and discipline required of a merchant generator to ensure cost recovery plus an appropriate return over the continued life of the asset. For example, if low gas prices and warm weather this winter depress prices in the Duke Ohio Zone, Dynegy will have to reduce or possibly eliminate its margin, carefully control costs and carefully watch the market in order to make a profitable sale into the market for the 46.5% portion of the Zimmer plant it owns. By contrast, with the stipulated PPA proposal in place, AEPGR will simply bill AEP Ohio its costs for its 25.4% portion of Zimmer plant and collect its 10.38% rate of return.

Q. DO YOU BELIEVE THE CREDITS LISTED ON PAGE 5 OF THE STIPULATION PROVIDE A PROPER INCENTIVE TO AEP OHIO AND AEPGR TO MANAGE THE PPA UNITS EFFICIENTLY, COST-EFFECTIVELY AND WITH MAXIMUM MARKET PROFITABILITY?

A. No. AEP Ohio's projections attached to AEP Ohio witness Allen's December 14, 2015 direct testimony predict annual credits under the PPA rider under the majority of scenarios for planning years 2020/2021 through 2023/2024 in amounts that exceed the trigger conditions for AEP Ohio's payments. Assuming AEP Ohio believes in its forecasts, it is logical then to conclude that AEP Ohio negotiated this provision believing it would not have to make any additional credit payments to customers for those planning years. The additional credits are not an incentive that will assure AEP Ohio and AEPGR manage the PPA units efficiently, cost-effectively or in a manner that responds to market signals. A true incentive would be to make AEP Ohio guarantee its projections. Without a proper incentive, AEP Ohio could easily engage in market behavior that would distort prices, such as offering its capacity or energy in the market at prices that do not reflect the actual cost of operations, suppressing the market clearing price for the co-owners of the PPA units along with owners of other generating units.

Q. ARE THERE ANY PARTICULAR RISKS FOUND IN THE STIPULATED PPA AND PPA RIDER CONSTRUCT THAT COULD RESULT IN LARGE OPERATING COSTS BEING PICKED UP BY THE CAPTIVE CUSTOMERS?

A. Yes. AEPGR has contracted for capacity performance products in PJM. Under the PJM capacity performance program, generators are paid bonuses for assuring delivery, however, if deliveries are not made there are very significant penalties. There are no force majeure or reasonable effort exceptions to failing to make a capacity performance guarantee. If a merchant generator fails to deliver on a capacity performance contract the generator will pay the penalty. Needless to say, merchant generators are motivated to take great efforts to avoid failing to perform. By contrast, under the stipulated PPA and PPA rider construct, if AEPGR makes a reasonable effort to deliver but was unable to any resulting PJM performance penalties may be passed on to AEP Ohio's customers. Using Conesville units 5 and 6 as an example, if the approximately 810 MWs bid into the auctions as capacity performance products fail to deliver when called upon, the penalties assessed by PJM could be as high as $128 million annually.[1] The magnitude of this penalty and the potential ability of AEP Ohio to pass this cost

[1] PJM Capacity Performance annual stop loss = 1.5 x net CONE x UCAP x 365 days, or 1.5 x $288.95/MW-day x 810 MW x 365 days = $128 million

through to customers would put the joint owners at extreme odds when it comes to decisions around reliability investments.

OTHER PROVISIONS OF THE STIPULATION

Q. ARE THERE PROVISIONS IN THE STIPULATION OTHER THAN THE OVEC AND PPA PROPOSAL THAT DYNEGY OPPOSES?

A. Yes. It is anticompetitive to have ratepayers finance the addition of natural gas firing to the Conesville units 5 and 6 while competitors like Dynegy would have to finance any such investments through their own working capital. Further, it appears that the co-firing as structured by AEP Ohio may just be window dressing. As detailed below, the limits AEP Ohio has placed in the Stipulation as to the coal heat input are close to the units' current coal heat input which would negate the use of natural gas.

Q. CAN YOU EXPLAIN NATURAL GAS CO-FIRING OF A COAL FIRED PLANT?

A. Natural gas co-firing of a coal-fired power plant generally allows the plant to operate on coal, natural gas or a combination of the two simultaneously.

Q. WHAT IS REQUIRED TO ADD CO-FIRING CAPABILITY TO A COAL PLANT?

A. Generally speaking, natural gas will need to be brought to the site (if not already present), appropriate piping, values, pressure regulators, meters, filters for the natural gas supply will need to be installed along with piping and nozzles added to the boiler (if not already present) and necessary control system upgrades will be required including the burner management system and flame scanner systems. Burner modifications may also be required along with any necessary modifications to the emissions control equipment.

Q. WILL A CO-FIRED PLANT TEND TO FAVOR ONE FUEL SOURCE OVER THE OTHER FUEL SOURCE WHEN OPERATING?

A. Yes. Generally speaking, plants originally designed and built to operate on coal are most efficient and cost effective while burning coal. There are many operational challenges in operating a coal plant strictly on gas, including boiler temperatures. In general, because of the poor efficiency related to the increased heat rate needed while firing natural gas in a co-fired unit, operating this type of plant solely on gas is usually the least likely operating mode if it is operated on gas at all. With a guaranteed cost recovery, though, AEP Ohio could dispatch the PPA units at below market pricing in order to run the units on natural gas with the ratepayers making up the lost revenues.

Q. HOW MUCH DOES IT COST TO ADD CO-FIRING CAPABILITY TO A COAL FIRED PLANT?

A. The costs vary by site. As mentioned above, natural gas will need to be brought to the site if not already there and depending on the distance of the natural gas source, this can be a significant cost. Additionally, boiler modifications will need to be made. If the source of natural gas is close, it is possible that the cost to add co-firing to the Conesville Units 5 and 6 could be minimal relative to other capital projects. For example, if natural gas is already onsite, and the boiler already has some natural gas firing capability, then the cost could be minimal, perhaps only several hundreds of thousands of dollars. In contrast, if natural gas is not available at the site, the cost of the pipeline to do so could be tens of millions of dollars alone, with the actual work at the plant small relative to the pipeline.

Q. IS THIS CHANGE A CONVERSION?

A. Co-firing of these units will be more of an "addition" than a "conversion." "Conversion" generally refers to changing the fuel from one type (such as coal) to another type (such as natural gas). And as described above, co-firing does not necessarily mean that natural gas will be used.

Q. AS A CO-OWNER IN CONESVILLE UNIT 4, DOES DYNEGY HAVE ANY PLANS TO ADD NATURAL GAS CO-FIRING TO THAT UNIT?

A. No. As I indicated above, plants originally designed and built to operate on coal are most efficient and cost effective while burning coal. Dynegy did not purchase its interest in the Conesville unit 4 to operate that unit in a manner that would disadvantage the unit in competing in the wholesale markets. If AEPGR and AEP Ohio truly intend to operate the Conesville units 5 and 6 on natural gas, they will put those units at a disadvantage in the wholesale markets. It does not appear that AEPGR and AEP Ohio intend to operate the units on natural gas based on its historical heat input for those units compared to the heat input limitation of 28,737,180 MMBTUs that is at page 19 of the Stipulation.

Q. WHAT IS HEAT INPUT?

A. Heat input is basically the energy contained in the fuel (coal or gas) put into the boiler for combustion to convert thermal energy to electrical energy. Heat input can be measured on a one million British Thermal Unit (MMBTU) basis.

Q. IS THERE A RELATIONSHIP BETWEEN HEAT INPUT AND THE AMOUNT OF ELECTRICITY THAT IS PRODUCED?

A. Yes. Setting aside other variables, an increase in heat input translates to an increase in generated electricity.

Q. HAS AEP OHIO MADE ANY COMMITMENTS REGARDING HEAT INPUT IN THE STIPULATION?

A. Yes. AEP Ohio agreed to limit the heat input from *coal* (emphasis added) to 28,737,180 MMBTUs per year, after adding co-firing capability in 2017 until 2030.

Q. WHAT IS THE HISTORICAL HEAT INPUT OF THE PLANT?

A. In looking at publicly-available data on the US EPA website from its air and markets data[2],

[2] http://ampd.epa.gov/ampd/

Conesville units 5 and 6 have had a historical heat input as shown in Table 1 below.

Year	Actual Heat Input (million MMBTU)
2008	55.7
2009	40.9
2010	36.2
2011	46.3
2012	34.2
2013	39.8
2014	44.1
2015	29.5[3]

Table 1: Historical Heat Input of Conesville Units 5 and 6

Q. HOW DOES THE AEP OHIO HEAT INPUT LIMIT IN THE STIPULATION COMPARE TO THE HISTORICAL HEAT INPUT OF THE PLANT?

A. As can be seen above, the heat input of Conesville units 5 and 6 has been generally declining over the past 8 years. Chart 1 below shows the historical heat input, a linear trend line of that heat input and the AEP Ohio proposed heat input limit.

[3] Annualized. The actual heat input through the third quarter 2015 is 22.1 million MMBTU.

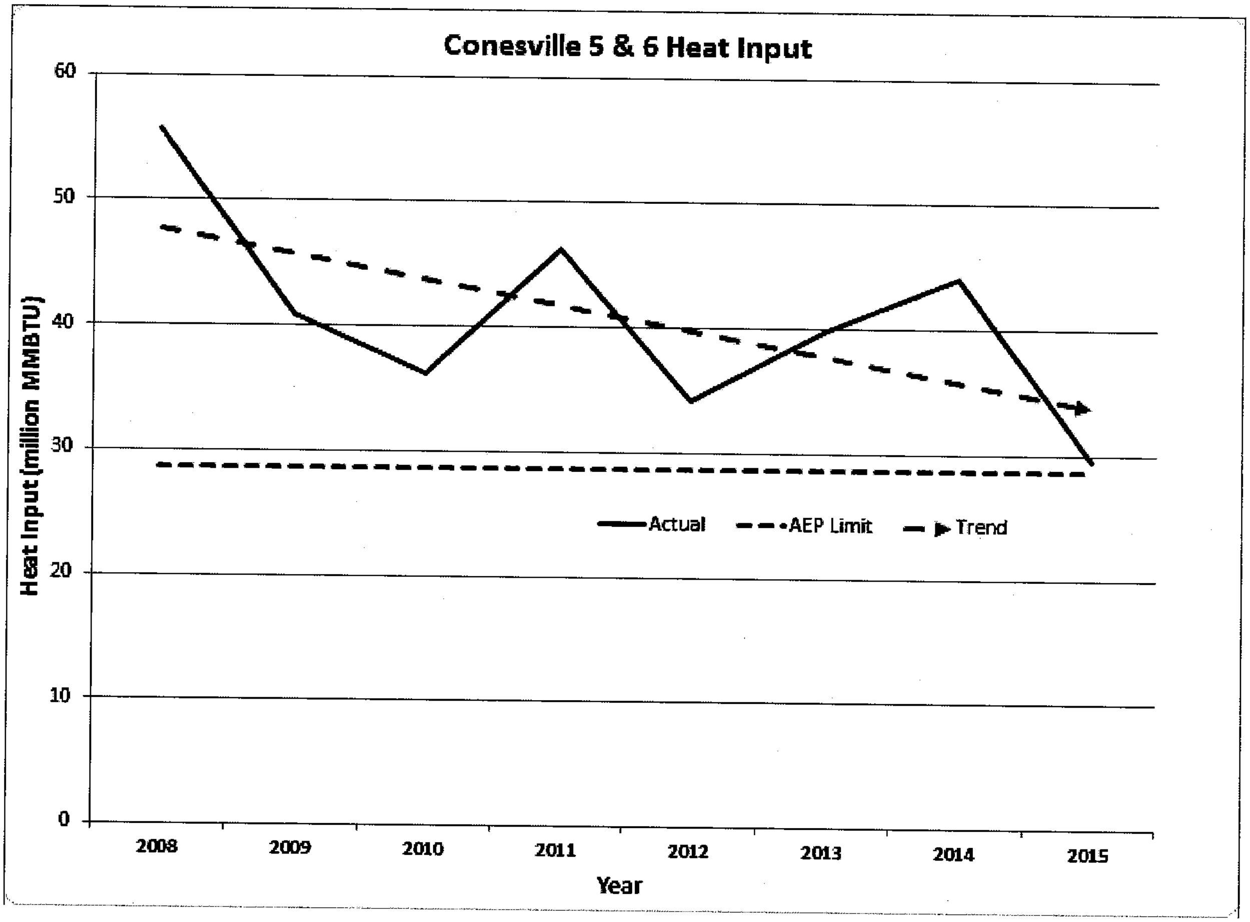

Chart 1: Historical Heat Input of Conesville Units 5 and 6
Linear Trend Line of that Heat Input, and Proposed Heat Input Limit

Q. WHAT CONCLUSIONS CAN YOU DRAW ABOUT AEP OHIO'S COMMITMENT TO CO-FIRE THE UNITS AND THE HEAT INPUT LIMIT?

A. Again, the heat input of the Conesville units 5 and 6 has been steadily declining over the past 8 years. In fact, the projected heat input for 2015 (when annualized using the actual first three quarters of this year) is estimated to be nearly the same as AEP Ohio's proposed limit in the Stipulation. The decline is generally consistent with the overall decline of coal-fired generation output nationwide including the PJM market[4] as natural gas-fired generation has become more economic and cost competitive, along with overall flat-to-declining electric demand largely attributable to economic conditions and energy efficiency programs. Given that natural gas prices are projected to remain at all-time lows for the foreseeable future, it is reasonable to expect that the heat input will either remain at AEP Ohio's proposed limit or even fall below that level without the addition of co-firing with natural gas. In other words, AEP Ohio and AEPGR have given up nothing in exchange for the commitment to limit the coal heat input to the Conesville units 5 and 6. It will very likely continue to operate in the same manner as today and with the same emissions.

Q. IS THERE VALUE IN AEP'S PLEDGE TO MAINTAIN AN OHIO NEXUS OF OPERATIONS AS TO THE PPA UNITS?

A. The Stipulation, at page 16, includes a statement that AEP "will maintain" its nexus of operations relating to the operation and support of the PPA units in Ohio over the term of the PPA rider. As written, this statement also appears to be window dressing. Dynegy can also claim it maintains a nexus of operations in Ohio related to the units it operates in Ohio including Zimmer, Stuart and Conesville. Dynegy maintains a nexus of operations in the Northeast related to the operation of the units there and has a nexus of operations in Illinois related to the units it operates in Illinois. And regardless of what is said in the Stipulation, AEP will maintain a nexus of operations in Ohio as to the PPA units so long as it has any ownership of or support role in those units. A more meaningful commitment would be one that specified minimum employment levels and minimum capital investment requirements.

[4] https://www.eia.gov/todayinenergy/detail.cfm?id=23252

Q. IS AEP REQUIRED TO MAINTAIN ITS CORPORATE HEADQUARTERS IN COLUMBUS, OHIO UNDER THE TERMS OF THIS STIPULATION?

A. No. Under the terms of the Stipulation, AEP states that it only "intends" to maintain its corporate offices in Columbus for the term of the PPA rider; nothing obligates or otherwise requires AEP to keep its headquarters in Columbus. More importantly, there is no commitment to maintain current employment levels in Ohio, so even if the headquarters is kept in Ohio there is not a pledge that current operations could not be moved out or that employment would not be reduced.

CONCLUSION

Q. WHAT IS YOUR RECOMMENDATION TO THE COMMISSION IN REGARDS TO THE STIPULATION?

A. As I stated in my initial direct testimony, AEP Ohio's request in this proceeding would shift the financial downside of running these plants from AEP's investors to the ratepayers of AEP Ohio. And if AEP Ohio were truly interested in providing a financial hedge to consumers, there are other effective and less costly ways to do so, including issuing a request for proposal ("RFP") for the capacity and energy over the period in question. The RFP could take on a variety of forms, including a fixed-price option, a variable-priced option, or a combination of both. The Stipulation ignores all other options and instead focuses on providing benefits to one current market participant – AEPGR. In fact, should the Commission disallow any costs to be recovered through the PPA rider, it will harm the financial wherewithal of the regulated utility and not the merchant generator. The Commission should reject the Stipulation and AEP Ohio's application in this proceeding.

Q. DOES THIS CONCLUDE YOUR TESTIMONY?

A. Yes.

CERTIFICATE OF SERVICE

The Public Utilities Commission of Ohio's e-filing system will electronically serve notice of the filing of this document on the parties referenced on the service list of the docket card who have electronically subscribed to the case. In addition, the undersigned certifies that a courtesy copy of the foregoing document is also being served (via electronic mail) on the 28th day of December 2015 upon all persons/entities listed below:

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