

**BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO**

In The Matter of the Application of Ohio Edison Company, The Cleveland Electric 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)
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) **Case No. 14-1297-EL-SSO**
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INITIAL BRIEF OF THE CITY OF CLEVELAND

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INTRODUCTION AND BACKGROUND

On August 4, 2014, the Ohio Edison Company, the Cleveland Electric Illuminating Company (“CEI”), and the Toledo Edison Company (collectively the “Companies”) filed an Application for a fourth electric security plan (“ESP IV”) with the Public Utilities Commission of Ohio (“PUCO” or the “Commission”) seeking authority for a 15-year term Power Purchase Agreement (“PPA”) with the Companies’ affiliate, FirstEnergy Solutions Corp. (“FES”), for all of FES’s generation, plus a minimum, guaranteed rate of profit to FES paid by the captive ratepayers, pursuant to a Retail Rate Stability Rider (“Rider RRS”). On December 1, 2015, the Companies filed a Third Supplemental Stipulation and Recommendation (“Stipulation III”), which in part, reduced the term to eight years and the guaranteed profit to 10.38%. The Companies’ current electric security plan will expire in May 2016.

On December 1, 2014, the PUCO permitted the City of Cleveland (“Cleveland”) to intervene in this matter. Cleveland opposes the ESP IV and Stipulation III because both proposals represent a bailout and result in an unfair, negative financial impact on captive ratepayers, such as Cleveland and its residents, while the Companies and FES receive an unfair advantage in the market in violation of Ohio law and public policy.

A. The City of Cleveland

Cleveland relies on CEI to deliver the electric power necessary for various Cleveland-owned facilities and street lighting. Residents and businesses living or located in Cleveland rely on CEI for power as well. CEI has approximately 180,000 residential, commercial, and industrial customers within Cleveland that collectively consume more than 4.5 million MWh per year at a cost of \$400 million annually. In street lighting alone, Cleveland consumes over 21,000 MWh per year at a cost of about \$1.7 million to CEI. Cleveland's municipal electric aggregation program provides about 47,000 distribution service customers to CEI. The Companies' ESP IV and this proceeding will have an impact on Cleveland, its residents and businesses.

B. The PPA and Rider RRS

The Companies propose Rider RRS will include all the costs and revenues from the FES-owned power stations as follows:

- The Davis-Besse nuclear power station ("Davis-Besse plant")
- The W.H. Sammis power stations ("Sammis plant")
- The Ohio Valley Electric Corporation power stations ("OVEC") (limited to FES's interest in OVEC)

Direct Testimony of Hisham M. Choueiki, Ph.D., P.E. ("Choueiki"), Sept. 18, 2015, pg. 4; see also Direct Testimony of Garrett Cole ("Cole"), Dec. 22, 2014, pg. 4-5. The proposed PPA will obligate the Companies to purchase all the output from the FES power plants, at cost, sell the output in the PJM markets, and use the revenues to cover the costs of the plants and the guaranteed profit of 10.38% to FES over an 8-year term. Choueiki at pg. 5; Cole at pg. 4; Stipulation III. "The difference between the revenues and the costs will be netted as a credit or a debit in Rider RRS." Choueiki at pg. 5.

STANDARD OF REVIEW

Pursuant to R.C. §4928.143, the Commission may approve, modify and approve, or deny the Application.

[T]he commission by order shall approve or modify and approve an application filed under division (A) of this section if it finds that the electric security plan so approved, including its pricing and all other terms and conditions, including any deferrals and any future recovery of deferrals, is more favorable in the aggregate as compared to the expected results that would otherwise apply under section 4928.142 of the Revised Code. Additionally, if the commission so approves an application that contains a surcharge under division (B)(2)(b) or (c) of this section, the commission shall ensure that the benefits derived for any purpose for which the surcharge is established are reserved and made available to those that bear the surcharge. Otherwise, the commission by order shall disapprove the application.

R.C. §4928.143(C)(1). The utility has the burden of proof in the proceeding. Id.

LAW

An Ohio electric plan may include “[a]utomatic recovery of any of the following costs of the electric distribution utility, provided the cost is prudently incurred: . . . the cost of purchased power supplied under the office, including the cost of energy and capacity, and including purchased power acquired from an affiliate . . .” R.C. §4928.143(B)(2). Unreasonable charges are prohibited.

Every public utility shall furnish necessary and adequate service and facilities, and every public utility shall furnish and provide with respect to its business such instrumentalities and facilities, as are adequate and in all respects just and reasonable. All charges made or demanded for any service rendered, or to be rendered, shall be just, reasonable, and not more than the charges allowed by law or by order of the public utilities commission, and no unjust or unreasonable charge shall be made or demanded for, or in connection with, any service, or in excess of that allowed by law or by order of the commission.

R.C. §4905.22.

ARGUMENT

The price of natural gas has dropped and flattened since the Companies prepared and filed their Application. See Deposition Testimony of Judah Rose (“Rose”), Oct. 23, 2015, pg. 10-13. Had the CEI ratepayers been subject to the ESP IV since August 2014, Cleveland would be overpaying, excessively so, for electricity today. And yet, the Companies continue to promote an outdated and unsupported plan that guarantees significant, increased costs to the captive ratepayers while it caps the FES investment and protects an absolute profit to FES. If the wholesale pricing remains near current levels, there will be large, unmitigated and unfair costs to the captive ratepayers. The ESP IV is flawed because it: 1) lacks a diligent, prudent procurement process; 2) proposes unfair and excessive risks to the ratepayers; 3) guarantees a profit to FES shareholders; and 4) disrupts the market to FES’s advantage and discretion. The Commission should deny the Application and Stipulation III.

A. ESP IV Fails On Adequate, Reliable, and Reasonably Priced Electric Services

When the Companies applied for their ESP III in 2008, the PUCO ruled in favor of a deregulated energy service pricing.¹ In the FirstEnergy MRO 2008, the PUCO held,

Chapter 4928 of the Revised Code provides a roadmap of regulation in which specific provisions were put forth to advance state policies of ensuring access to adequate, reliable, and reasonably priced electric service in the context of significant economic and environmental challenges. In reviewing the Companies’ application for an MRO, the Commission is aware of the challenges facing Ohioans and the electric power industry and will be guided by the policies of the state as established by the General Assembly in Section 4928.02, Revised Code, as amended . . .

¹ See In the Matter of the Application of Ohio Edison Companies, the Cleveland Electric Illuminating Companies, and the Toledo Edison Companies for Approval of a Market Rate Offer to Conduct a Competitive Bidding Process for Standard Service Offer Electric Generation Supply, Accounting Modifications Associated with Reconciliation Mechanics, and Tariffs for Generation Service, Case No. 08-936-EL-SSO, Opinion and Order (Nov. 25, 2008) (“FirstEnergy MRO 2008”); In the Matter of the Application of Ohio Edison Companies, the Cleveland Electric Illuminating Companies, and the Toledo Edison Companies for Authority to Establish a Standard Service Offer Pursuant to Section 4928.143, Revised Code in the Form of an Electric Security Plan, Case No. 08-935-EL-SSO, Opinion and Order (Dec. 19, 2008) (“FirstEnergy ESP III 2008”).

FirstEnergy MRO 2008, at 5. The PUCO also applied the law to FirstEnergy’s ESP III.

The Commission believes that the state policy codified by the General Assembly in Chapter 4928, Revised Code, sets forth important objectives which the Commission must keep in mind when considering all cases filed pursuant to that chapter of the code. Therefore, in determining whether the ESP meets the requirements of Section 4928.143, Revised Code, the Commission takes into consideration the policy provisions of Section 4928.02, Revised Code, and we use these policies as a guide in our implementation of Section 4928.143 . . .

FirstEnergy ESP III 2008, at 8.

The ESP IV deviates from the current plan and the Commission’s goal of transitioning the Ohio electric distribution companies toward a fully-competitive retail-market construct. See Choueiki, pg. 7-9 (regarding the status of retail competition in the FirstEnergy service area). The ESP IV is a bailout. The Companies and FES propose to shift all the financial risk to the captive ratepayers and FES receives a guaranteed profit, also paid by the captive ratepayers. Direct Testimony of Joseph P. Kalt, Ph.D. (“Kalt”), Dec. 22, 2014, pg. 8 (“The proposed ESP of the Companies represents a return through the back door to old-style ratemaking that uses the captivity of local ratepayers to insulate generation owners from risk.”).

Under the ESP IV, the captive ratepayers must purchase power from FES plants, fund improvements to or debt for FES’s power plants, and ensure the profit. There is no ceiling to the exposure or to the amount of risk that the Companies and FES shift to the captive ratepayers.

“[T]he proposed PPA and Rider RRS plan is unambiguously contrary to the interests of the general ratepaying public of Ohio served by the Companies. The proposed plan would shift very large risks from FES’ debt and equity investors onto the Companies’ captive ratepayers. The economics of the Companies’ own calculations showed that their proposed plan would burden the Companies’ captive ratepayers with \$220 million of uncompensated risk. It would do this without any compensating benefits or return to the general ratepaying public. The plan, in short, is what is commonly called a ‘bailout’.”

Second Supplemental Testimony of Joseph P. Kalt, Ph.D. (“Kalt Supp. II”), Dec. 30, 2015, pg. 3-4. The ESP IV is unilateral to the benefit of Companies and FES. Choueiki, pg. 13, “The

Companies and FES did not, in Staff's opinion, commit to sharing the financial risk associated with Rider RRS with its distribution customers." Id. The unfair risk results in unreasonable charges imposed on the captive ratepayers at FES' discretion.

The Stipulation III does not alleviate the unfair risk to the captive ratepayers. "The plan continues to be an unambiguous bailout that would benefit FES' stockholders and lenders." Kalt Supp. II, at pg. 6

The Third Stipulations' projected captive ratepayer benefits are based on significantly out-of-date input assumptions. Simply accounting for the changes in fuel and power markets over the past eighteen months shows that the Companies' latest claims of ratepayer benefit are grossly unrealistic. . . . It is clear from up-to-date inputs that the proposed rate plan of FES' Ohio utility affiliate Companies promises to impose hundreds of millions of dollars of net harm on the Companies' captive ratepayers.

The Companies proposed ESP would also undermine the federally-regulated competitive wholesale power markets of PJM. It would do so by using Ohio state regulation to force captive retail ratepayers to subsidize the subject plants' participation in the PJM wholesale markets. This subsidization will benefit the shareholders and lenders who own less efficient producers (i.e., Davis-Besse and Sammis), but will come at the expense of newer, more efficient and cost-effective generators that would otherwise supply additional power and/or enter the federally-regulated wholesale market. In the absence of a subsidy, the Companies' captive rate payers in Ohio will pay lower prices and the nation's energy production will have lower total cost to the economy.

Kalt Supp. II, at pg. 23-24.

The ESP IV and the Stipulation III provide no reliability or reasonableness for the price of electric service. "[I]f the projected net-generation of the plants corresponds to what we have actually witnessed on average . . . captive ratepayers will realize a net present value loss \$201 million." Kalt Supp. II, pg. 21-22. The Stipulation III will result in a massive, negative financial impact on Cleveland and its residents, which impact is unreasonable considering the financial state of CEI's Cleveland-based customers.

B. The ESP IV Lacks a Diligent Procurement Process

In a long-term asset investment, such as the PPA's 15-year or 8-year term, alternative supply sources developed under a request for proposals ("RFP") and/or an Integrated Resource Plan ("IRP") provide information to regulatory bodies to review the prudence of the investment decisions. Cole at pg. 5. Under a RFP or an IRP, the provider has an opportunity to analyze and compare available, varying, or new fuel resources and to develop the appropriate economic, credit, regulatory, or other risk strategy for the provider and for the ratepayer. Cole at pg. 5-6. "It is a very common practice for sizable regulated utilities, like FirstEnergy, to demonstrate the prudence of their resource decisions with the use of an RFP, IRP or both." Cole at pg. 6.

Under the PPA, the Companies make no real effort to establish actual energy cost to FES, let alone external sources, varying, or new fuel sources. For FES to profit, the Companies must be obligated to purchase all power produced from FES's power plants. The actual cost of energy will be determined by the market, plus the costs of the power stations, plus the profit to FES. The "transfer of these costs to the retail ratepayers appears to be unilateral having no prudent procurement process or resource plan to support the decision in comparison to other potential supply alternatives." Cole at pg. 7.

Under the Stipulation III, the Companies benefit from the PPA even more so since the Companies propose a severability provision at Section V.(B)(3)(c) Severability Provision, which, if accepted, would serve to make FES whole at the expense of the captive ratepayer consistent with retroactive ratemaking. (Simply stating that a provision does not violate the law does not excuse a provision and its intended results from actually violating Ohio law.) The ratepayers, not FES, will cover the risk regardless of how a court determines FES' bailout plan.

CERTIFICATE OF SERVICE

I hereby certify that a true and accurate copy of the Initial Brief of the City of Cleveland has been electronically filed with the Public Utilities Commission of Ohio and has been served by electronic mail, upon the parties identified below, on this 16th day of February, 2016.

/s/ Kate E. Ryan

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Summary: Brief Initial Brief of the City of Cleveland electronically filed by Kate E. Ryan on behalf of The City of Cleveland