

**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 |) | Case No. 14-1297-EL-SSO |
| 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. |) | |

**REPLY BRIEF OF
DYNEGY INC.**

PUBLIC VERSION

February 26, 2016

TABLE OF CONTENTS

| | | |
|------|---|----|
| I. | INTRODUCTION | 1 |
| II. | THERE IS CERTAINTY IN OHIO AS TO ELECTRICITY | 3 |
| A. | The Davis-Besse, Sammis and OVEC plants are not closing | 3 |
| B. | Rider RRS is not needed for fuel diversity | 6 |
| C. | Rider RRS is not needed for grid reliability..... | 7 |
| D. | Price signals from the PJM markets are incentivizing new generation in Ohio..... | 9 |
| III. | THE PROPOSED OVERSIGHT IS NOT SUFFICIENT TO PROTECT THE WHOLESALE MARKETS | 10 |
| A. | The proposed oversight for Rider RRS is different from the oversight imposed on traditional, regulated utilities | 10 |
| B. | The proposed oversight is insufficient | 12 |
| C. | The Companies should be required to bid into the PJM markets no lower than actual cost | 14 |
| IV. | IF THE COMMISSION APPROVES RIDER RRS, IT SHOULD CONDITION ITS APPROVAL OF RIDER RRS ON A COMPETITIVE BID PROCESS FOR THE UNDERLYING PPA | 15 |
| A. | The underlying transaction benefits FES and its balance sheet | 16 |
| B. | The Commission should condition any approval of Rider RRS on competitively bidding the underlying PPA | 20 |
| V. | CONCLUSION..... | 23 |
| | CERTIFICATE OF SERVICE | 24 |

I. INTRODUCTION

The record evidence in this proceeding contradicts the claims by Ohio Edison Company, The Cleveland Electric Illuminated Company, and The Toledo Edison Company (collectively the “Companies”) that their Retail Rate Stability rider (“Rider RRS”) proposal will benefit ratepayers and is in the public interest. In its initial brief, Dynegy Inc. (“Dynegy”) noted the fatal flaws of Rider RRS: it violates state law, it subsidizes FirstEnergy Solutions Corp. (“FES”) at the expense of competitor Ohio merchant generators, it harms both the wholesale and retail energy markets, and it exposes ratepayers to significant costs, among other faults. Dynegy submits its reply brief to emphasize three points regarding the Companies’ initial brief.

First, the Companies’ repeated insinuation that the Sammis and Davis-Besse plants face imminent threat of closure, with attendant risks to Ohio’s generation supply and impacts on the local economy, is not borne out by the facts. Testimony by the Senior Vice President, Fossil Operations and Environmental at FirstEnergy Generation, LLC, a wholly owned subsidiary of FES, and other evidence of record firmly establishes that neither these plants nor the Ohio Valley Electric Corporation (“OVEC”) plants will close. Indeed, the Companies continue to invest in the Sammis and Davis-Besse plants, which can realize significant additional revenue as a result of PJM Interconnection L.L.C.’s (“PJM”) new capacity performance program. As the plants are not at risk of shuttering, the Companies’ claim that Rider RRS is needed for grid reliability rings hollow, particularly because PJM has other means at its disposal—such as the Reliability Must Run contract—to support grid reliability without any need for Rider RRS. Finally, generation certainty is assured by the development of new generation within Ohio and PJM. The fact that new generation is incentivized to build in Ohio demonstrates that PJM’s existing price signals are working and will continue to work unless disrupted by Rider RRS.

Second, the level of oversight that the Stipulation¹ proposes for Rider RRS is insufficient to protect the wholesale markets. The Companies have claimed throughout this proceeding that they welcome “rigorous” oversight over Rider RRS, but in reality their proposal contemplates only minimal oversight over the Companies and no oversight at all over FES. This is plainly insufficient and is significantly narrower than the oversight that the Commission would exercise if FES was a traditional regulated cost-of service utility. Notably, the Companies ignored the recommendations of Commission Staff with respect to the level of Commission oversight, betraying any claim that their proposal provides for “rigorous” supervision. This should be reason enough for the Commission to reject Rider RRS. If Rider RRS is approved, and the Companies bid capacity into the PJM markets, the Commission should at a minimum follow PJM’s recommendation and require the Companies to bid capacity at actual costs into the market to avoid any price suppressive effect.

Third, the Commission should reject Rider RRS in its entirety for all the above reasons, but if it rules otherwise, it should condition any approval of Rider RRS on competitively bidding the underlying power purchase agreement (“PPA”). This will allow merchant generators to compete with FES on an equal and fair basis and better protect the Companies’ ratepayers. Competitive bidding is strongly favored and routinely practiced in Ohio, notably through the Companies’ SSO procurement auctions. Most importantly, other merchant generators have expressed their willingness to compete with FES. For example, Exelon projects its offer would save ratepayers more than \$2 billion over the proposed term sheet with FES. Likewise, Dynegy would be interested in participating in a competitive bidding process for a PPA to include in

¹ A partial Stipulation and Recommendation was filed in this proceeding on December 22, 2014, and supplemented on May 28, June 4, and December 1, 2015. For ease, those filings will be referred to collectively as “the Stipulation.”

Rider RRS if the Commission conditions its approval of Rider RRS on competitively bidding the PPA.

Absent competitive bidding, Rider RRS is simply a subsidy to FES that provides certainty to FES by transferring the market risk to the Companies' ratepayers. FES may need Rider RRS for its balance sheet, but Ohio ratepayers neither need nor want it. The Commission should remove Rider RRS from the Companies' proposed ESP IV or otherwise at a minimum, condition any approval on a competitive bid process.

II. THERE IS CERTAINTY IN OHIO AS TO ELECTRICITY

Throughout this proceeding, the Companies have tried to create the impression that their Retail Rate Stability Rider ("Rider RRS") proposal is necessary because allegedly there is a great deal of uncertainty as to whether Ohio will have reliable electric service and stable prices. The record evidence shows just the opposite. Ohio has reliable electric service, stable retail pricing and a new wave of gas-fired generation plants that will compliment Ohio's existing coal and nuclear plants.

A. The Davis-Besse, Sammis and OVEC plants are not closing.

The Companies, as they have done throughout this proceeding, claim in their initial brief that the future of the plants is uncertain and that the Davis-Besse, the Sammis and OVEC plants are financially challenged.² Turning first to this claim as to the OVEC plants, the record is clear that FES on its own, cannot close the OVEC plants as its entitlement share is less than five percent and there are multiple other owners (called sponsoring companies) who would have to

² Companies Initial Brief at 5 and 29. *See, also*, Transcript ("Tr.") Volume ("Vol.") 1 at 97-99; Tr. Vol. 2 at 404-405.

agree.³ Also, Companies witness Mikkelsen reluctantly testified that there is greater certainty with respect to the continued operation of the OVEC plants.⁴

Regarding the Davis-Besse and Sammis plants, the Companies point to historical profit/loss information for the plants to support their claim that FES may close the Davis-Besse and Sammis plants in the short-term.⁵ That evidence is insufficient to show that those two plants are in financial need, especially as the Companies' witness Don Moul testified repeatedly that a plant retirement decision is based on a snapshot of one year, looking at whether the plant is recovering its avoidable cost going forward and taking the cost of any necessary future capital expenditures, and overlaying that information with the balance sheet of the company.⁶

The record of the Davis-Besse and Sammis plants' going forward costs and revenues show that those plants will not close. FE witness Don Moul testified that FES may "reach a point where these plants aren't covering their avoidable costs, at which point we would have to make a decision as to whether to continue to invest in them and to keep them online or choose to shut the units down."⁷ P3/EPSA witness Dr. Joseph Kalt⁸ testified that the Sammis and Davis-Besse plant [REDACTED]

[REDACTED] Even the Companies' witness Donald Moul indicated that the plants [REDACTED].¹⁰ That

³ Tr. Vol. 2 at 405, 407.

⁴ Tr. Vol. 2 at 407.

⁵ Companies Initial Brief at 125.

⁶ Tr. Vol. 32 at 6630.

⁷ Tr. Vol. 10 at 2202.

⁸ Dr. Kalt is the Ford Foundation Professor (Emeritus) of the International Political Economy at the John F. Kenney School of Government, Harvard University. He also works as a senior economist with Compass Lexecon, an economics consulting firm. P3/EPSA Ex. 5 at 1.

⁹ P3/EPSA Ex. 2 at 42-44.

¹⁰ Tr. Vol. 10 at 2202.

explains why FES has not announced that either of the plants are retiring and why FES continues to invest in both plants.¹¹ The investments include a steam generator for Davis-Besse, a 600 million dollar project,¹² which as Mr. Moul said was a once in a lifetime event for a nuclear facility.¹³ All of this evidence collectively leads to the conclusion that Davis-Besse and Sammis will not close in the near term.

The plants will also receive a significant revenue boost through PJM's new capacity performance program. PJM has run a Base Residual Auction for delivery year 2018/2019, a transition auction for delivery year 2016/2017 and a transition auction for delivery year 2017/2018 under the capacity performance design.¹⁴ The result was a significant increase in capacity prices for all capacity resources in PJM and particularly for capacity resources in the western part of PJM, including Ohio.¹⁵ The implementation of capacity performance, as intended, has resulted in generators receiving millions of dollars in additional revenue, in exchange for higher expectations around performance during extreme system events. [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

¹⁶

This and other evidence in the record show that the Davis-Besse, Sammis and OVEC plants are not in financial need and will not close in the near term. FES also has the benefit of being the affiliate of a major corporation. As the Senior Vice President, Fossil Operations and

¹¹ P3/EPSCA Ex. 1 at 41, citing Hardin Direct Testimony at 10.

¹² Tr. Vol. 32 at 6606.

¹³ Tr. Vol. 10 at 2200.

¹⁴ IMM Ex. 2 at 3.

¹⁵ IMM Ex. 2 at 3.

¹⁶ Tr. Vol. 9 at 1986-1987.

Environmental at FirstEnergy Generation, LLC (Don Moul) testified, FirstEnergy Corp. could borrow money to invest in the plants and he did not rule out FirstEnergy Corp. financing any necessary capital investments in the plants if Rider RRS was not approved.¹⁷ The plants are not in financial need and are not going to close. Ohio (and PJM) already have certainty. There is no need for Rider RRS.

B. Rider RRS is not needed for fuel diversity.

The Companies claim that coal-fired assets and nuclear assets contribute to generation resource diversity, thereby “precluding the potentially catastrophic overreliance on a single type of fuel supply such as natural gas.”¹⁸ The fact that the plants are not closing moots the Companies’ argument that the plants are necessary for fuel diversity. Also refuting the Companies’ claim that the Sammis and Davis-Besse plants are necessary to avoid a “potentially catastrophic overreliance” on natural gas is the fact that Dynegy owns approximately 2,700 megawatts of baseload coal-fired generation in Ohio.¹⁹ Those plants are operating today along with Dynegy’s Ohio-based natural gas-fired generation plants.

Regardless, even if the plants were at risk of closing (which they are not), the Companies presented no evidence establishing that there will be a significant impact on Ohio and PJM’s generation mix if the Sammis plant and/or the Davis-Besse units retired. Staff witness Dr. Choueiki agreed that the Ohio generation mix consisted of approximately 68 percent coal, 17 percent natural gas and 12 percent nuclear as of November 2014.²⁰ This mix shows that even if the Sammis plant and Davis-Besse units closed, the Ohio generation mix would still predominantly favor coal with natural gas a distant second. As P3/EPSCA witness Dr. Kalt

¹⁷ Tr. Vol. 10 at 2199.

¹⁸ Companies Initial Brief at 130.

¹⁹ Company Ex. 184 at 103-104.

²⁰ Tr. Vol. 30 at 6206.

testified, “it would take a significant shift toward natural gas resources to materially change the proportion of coal-fired resources.”²¹

Another witness for the Companies (Dr. Makovich) acknowledged that PJM had approximately 70,000 megawatts of installed coal-fired capacity meaning that the Sammis plant is approximately 3.0 percent of that capacity.²² Likewise, PJM has approximately 30,000 megawatts of installed nuclear capacity of which Davis-Besse is approximately 3.0 percent.²³ So even if the Sammis and Davis-Besse plants closed, PJM would still have approximately 97,000 megawatts of installed coal and nuclear capacity in addition to the new natural gas-fired generation coming online.

Even if the plants were at risk of closing (which they are not), the current mix of fuel diversity in Ohio and PJM does not justify Rider RRS.

C. Rider RRS is not needed for grid reliability.

The Companies’ claim that Rider RRS is necessary to avoid “potentially catastrophic reliability issues.”²⁴ The Companies believe that it is not feasible for renewables and natural gas to “supplant” Ohio’s coal and nuclear baseload generation assets.²⁵ The Companies also believe that the continued operation of baseload fuel diverse generating plants will provide increased assurance for reliability of the customers on the Companies’ system.²⁶ The key to the Companies’ argument is assuming that the Sammis and Davis-Besse plants will close without Rider RRS. But as noted above and in other briefs, those plants are no more at risk of closure

²¹ P3/EPSCA Ex. 1 at 37.

²² Tr. Vol. 17 at 3502-3503.

²³ Tr. Vol. 17 at 3503 to 3504.

²⁴ Companies Initial Brief at 56.

²⁵ *Id.* at 62.

²⁶ *Id.* at 63.

than the OVEC plants are at risk of closure, and the OVEC plants are not going to close. With new gas-fired generation coming on-line in Ohio coupled with existing coal and nuclear units, Ohio generation units will contribute to grid reliability.

The Commission should also note that PJM has overall responsibility for monitoring and maintaining grid reliability.²⁷ As part of the market operator function, PJM coordinates and directs the operation of the transmission grid and plans transmission expansion improvements to maintain grid reliability in the PJM region.²⁸ New generators must go through PJM's interconnection process which addresses any needed transmission upgrades.²⁹ For units that may be deactivated, PJM has a process for studying grid reliability and can provide a Reliability Must Run ("RMR") contract for any units determined necessary to maintain reliability.³⁰

The RMR contract is a viable option to ensure grid reliability. For example, FES has accepted RMR contracts previously for certain units, including the Ashtabula 5, East Lake 1-3 and Lake Shore 18 units.³¹ And the Companies have not foreclosed using RMR again. The Companies' witness Donald Moul testified that FES would be willing to evaluate any RMR offer for Davis-Besse and Sammis should the need arise.³² Although he considered RMR a "stop-

²⁷ PJM operates a centrally dispatched, competitive wholesale electric power market that, as of June 30, 2015, had installed generating capacity of 176,741 megawatts (MW) and 944 members including market buyers, sellers and traders of electricity in a region including more than 61 million people in all or parts of Delaware, Illinois, Indiana, Kentucky, Maryland, Michigan, New Jersey, North Carolina, Ohio, Pennsylvania, Tennessee, Virginia, West Virginia and the District of Columbia. Company Ex. 76, Quarterly State of the Market Report for PJM: January through June, at page 3.

²⁸ Company Ex. 76, Quarterly State of the Market Report for PJM: January through June, at page 3.

²⁹ See e.g. Interconnection Service Agreement Among PJM Interconnection, LLC and Carroll County Energy LLC and AEP Ohio, Inc., Sierra Club Ex. 59 (administrative notice taken, Tr. Vol. 16 at 3411).

³⁰ Exelon Ex. 1 at 16.

³¹ Tr. Vol. 32 at 6640.

³² Tr. Vol. 11 at 2258.

gap” measure, Mr. Moul admitted that it does allow a plant to continue to operate while any necessary transmission upgrades are made.³³

PJM’s oversight of the regional transmission system in its role as the regional transmission organization ensure grid reliability, not Rider RRS.

D. Price signals from the PJM markets are incentivizing new generation in Ohio.

Ohio also has certainty as to the development of new generation in Ohio and within PJM. New natural gas-fired generation is being developed in Ohio, including the 742 megawatt Carroll County Energy Facility (geographically close to Sammis) and the 799 megawatt Oregon Clean Energy Facility (geographically close to Davis-Besse).³⁴ Likewise, other natural gas-fired generation projects have received Ohio Power Siting Board approval.³⁵ The fact that new generation is being developed in Ohio shows that the pricing signals from PJM are working. And with the overall mix of PJM remaining predominantly coal and nuclear, Ohio and PJM will continue to have resource diversity all the while enjoying the benefit of new efficient natural gas-fired generation.³⁶

However, Rider RRS, as noted in Dynegy’s Initial Brief, will result in the Companies’ bidding on output from the plants in a way that has a price-suppressive impact on wholesale markets.³⁷ That, in turn, could have a chilling effect on new generation development and investment, both of which rely on transparent market pricing signals. The Commission can avoid this result by not approving Rider RRS.

³³ Tr. Vol. 11 at 2258-2259.

³⁴ See P3/EPSCA Ex. 1 at Attachment JPK-2.

³⁵ *Id.* at 15-16, fn. 24.

³⁶ See generally, P3/EPSCA Ex. 5 at 18-22 (Dr. Kalt Supplemental Testimony).

³⁷ Dynegy Initial Brief at 12-13.

III. THE PROPOSED OVERSIGHT IS NOT SUFFICIENT TO PROTECT THE WHOLESALE MARKETS

A. The proposed oversight for Rider RRS is different from the oversight imposed on traditional, regulated utilities.

The Companies state in their initial brief that they “welcome rigorous Commission oversight of all costs and revenues included in Rider RRS[.]”³⁸ which will consist of a Staff audit of the annual Rider RRS reconciliation for mathematical errors, a Staff review of the reasonableness of actual costs (excluding the so-called legacy cost components), and confirmation that costs and revenues included in Rider RRS are not unreasonable.³⁹ That review is much different than the oversight the Commission would have over a traditional regulated utility that is operating in a cost-based recovery environment.

Under the Companies’ proposed oversight for Rider RRS, the Commission would only have oversight of the actions of the Companies, and not FES.⁴⁰ The Commission cannot audit legacy costs that will be included in Rider RRS, will not have full access to FES records on how it is distributing costs within its fleet, and will not be able to fully investigate FES’ actions in regards to the incurrence of any capacity performance penalties.⁴¹ Simply put, the Commission’s oversight over both the Companies and FES is significantly limited under the proposed Stipulation.

That state oversight would be much broader if FES was a traditional regulated cost-of-service utility. The Commission has full authority to examine costs, conduct audits and conduct investigations on a regulated public utility’s activities. As R.C. 4905.04 states, “[t]he public

³⁸ Companies Initial Brief at 73.

³⁹ Companies Initial Brief at 73.

⁴⁰ Tr. Vol. 36 at 7702-7703.

⁴¹ *Id. and see* Staff Ex. 9 at 13 (Dr. Choueiki noting lack of full information sharing on other information in fleet and giving example).

utilities commission is hereby vested with the power and jurisdiction to supervise and regulate public utilities ... to require all public utilities to furnish their products and render all services exacted by the commission or by law ...[.]”

The Ohio General Assembly has also empowered the Commission with general supervision over all public utilities within its jurisdiction:⁴²

The public utilities commission has general supervision over all public utilities within its jurisdiction as defined in section 4905.05 of the Revised Code, and **may examine such public utilities** and keep informed as to their general condition, capitalization, and franchises, and as to the manner in which their properties are leased, operated, managed, and conducted with respect to the adequacy or accommodation afforded by their service, the safety and security of the public and their employees, and their compliance with all laws, orders of the commission, franchises, and charter requirements. The commission has general supervision over all other companies referred to in section 4905.05 of the Revised Code to the extent of its jurisdiction as defined in that section, and may examine such companies and keep informed as to their general condition and capitalization, and as to the manner in which their properties are leased, operated, managed, and conducted with respect to the adequacy or accommodation afforded by their service, and their compliance with all laws and orders of the commission, insofar as any of such matters may relate to the costs associated with the provision of electric utility service by public utilities in this state which are affiliated or associated with such companies. **The commission, through the public utilities commissioners or inspectors or employees of the commission authorized by it, may enter in or upon, for purposes of inspection, any property, equipment, building, plant, factory, office, apparatus, machinery, device, and lines of any public utility.** The power to inspect includes the power to prescribe any rule or order that the commission finds necessary for protection of the public safety. In order to assist the commission in the performance of its duties under this chapter, authorized employees of the motor carrier enforcement unit, created under section 5503.34 of the Revised Code in the division of state highway patrol, of the department of public safety may enter in or upon, for inspection purposes, any motor vehicle of any motor carrier .

⁴² R.C. 4905.06 (emphasis added).

The great oversight authority that the Commission has over public utilities shows how little oversight the Commission will have over FES (none) and the Companies (very little) as to Rider RRS.

B. The proposed oversight is insufficient.

The Companies do not dispute that a proposed PPA rider must include “rigorous Commission oversight of the rider,” including a proposed process for a periodic substantive review and audit.⁴³ The oversight proposed by the Companies, however, falls well short of “rigorous oversight.” Even though it reversed its position about Rider RRS after the first phase of the hearing closed, Staff’s testimony on this point remains instructive.

Specifically, Staff witness Dr. Choueiki testified that the Companies’ oversight proposal was not sufficient, and did not constitute rigorous Commission oversight.⁴⁴ He called the Companies’ commitment “vague” and stated that it did not satisfy the definition of a rigorous Commission oversight.⁴⁵ Dr. Choueiki recommended that the Companies *and FES* accept that “all future cost components (fixed and variable) will be audited annually by Staff (or by an outside consultant representing Staff) and for the Companies *and FES* to accept a Commission’s finding to the extent there is a disagreement between the Companies *or FES* and Staff and a hearing is conducted.”⁴⁶

Even though Staff made this recommendation, the Stipulation does not provide oversight over FES.⁴⁷ Moreover, under the Stipulation (Section V.B.3.a.) the proposed oversight process

⁴³ *In re Ohio Power Company*, Case No. 13-2385-EL-SSO et al., Opinion and Order at 25 (February 25, 2015) (“AEP ESP III”).

⁴⁴ Staff Ex. 12 at 12.

⁴⁵ *Id.*

⁴⁶ Staff Ex. 12 at 16.

⁴⁷ Tr. Vol. 36 at 7702-7703.

continues to only consist of an initial Staff audit as to calculation verification, and then a Commission review of the reasonableness of only some of the costs included in the rider.⁴⁸ The Companies' sponsoring witness, Eileen Mikkelsen, testified that the Companies can object to any recommendations from Staff to disallow costs through a hearing.⁴⁹ She also said that the Companies can pursue legal challenges for disallowed costs, and while the dispute is ongoing, can continue to recover those costs during the dispute period.⁵⁰

The continued lack of oversight over FES and the limited oversight of the Companies are not sufficient to protect against any negative impacts to the wholesale markets caused by the Rider RRS construct. As Dr. Bowring, the PJM Market Monitor, explained, separating the responsibility for operating plants and the financial consequences of that operation creates incentive issues.⁵¹ He further explained that "[s]hareholders and management do not have the same incentives to manage performance of the units for which customers bear the risk as they do to manage the performance of the units for which shareholders bear the risk."⁵² P3/EPSCA witness Dr. Kalt also highlighted the problem of insulating the decision makers who can control risk from those who bear the risk, which he said would result in inefficient decisions.⁵³

One example of this is FES' ability to divert cash flow to other units in its fleet for which it is fully liable for capacity performance penalties, while not using its cash flow to lessen the risk of incurring capacity performance penalties at the Sammis unit. Under the proposed term

⁴⁸ Company Ex. 7 at 14-15.

⁴⁹ Tr. Vol. 36 at 7739.

⁵⁰ Company Ex. 7 at 15.

⁵¹ IMM Ex. 2 at 4.

⁵² *Id.*

⁵³ Tr. Vol. 28 at 5692.

sheet, FES appears to have no liability for capacity performance penalties.⁵⁴ Mr. Moul believed that under the proposed PPA term sheet, [REDACTED]

[REDACTED]⁵⁵ With limited to no risk for penalties at the Sammis unit, FES would have an incentive to divert the flow of cash to the other FES units that are not involved with the Rider RRS construct and where it has actual risk for capacity performance. The Commission, however, has no oversight over FES and will be unable to ensure that FES is properly allocating its cash flow and making investment decisions that benefit ratepayers, not just FES.

This is one example of why the oversight proposed in the Stipulation is insufficient. Other examples exist, including the lack of Commission review of legacy costs (costs incurred prior to December 31, 2014) and the Commission's lack of oversight over the actions of FES in bidding capacity forward into the auctions through the 2018/2019 planning years.⁵⁶ As noted by Staff, the Companies have not proposed a program that provides "rigorous Commission oversight of the rider, including a proposed process for a periodic substantive review and audit[.]"⁵⁷ For this reason, the Commission should reject Rider RRS.

C. The Companies should be required to bid into the PJM markets no lower than actual cost.

If Rider RRS is approved in some fashion, then the Commission should add to its oversight by imposing a no lower than actual at-cost bid requirement on the Companies. This requirement is supported by PJM⁵⁸ and would minimize harm to the wholesale markets.

⁵⁴ See Company Ex. 156.

⁵⁵ Tr. Vol. 11 at 2463.

⁵⁶ See e.g. Tr. Vol. 36 at 7702-7703.

⁵⁷ *AEP ESP III*, *supra*.

⁵⁸ PJM Amicus Brief at 5.

As noted by the PJM market monitor, the logical offer by the Companies into the capacity market would be zero. As Dr. Bowring testified:⁵⁹

The logical offer price for these resources in the PJM Capacity Market, under these conditions, would be zero. A zero offer would be rational because this would maximize the revenue offset to the customers who would be required to pay 100 percent of the costs of this capacity and bear all of the performance risks. Offers at or near zero would have an anti-competitive, price suppressive effect on the PJM Capacity Market as would any offers at less than the competitive offer level. The proposed Rider RRS would create strong incentives for FirstEnergy to offer this capacity at less than the competitive offer level.

PJM agreed with Dr. Bowring. In its amicus brief, PJM asked the Commission to “make clear that a reasonable offer behavior for FE would be to offer the units covered by the Rider into the PJM markets at a level no lower than their ‘actual costs’ as that term is understood by PJM and applied consistent with its Tariff and Manuals without consideration of the offsetting revenues provided by Ohio retail customers under the Stipulation.”⁶⁰

Expanding the Commission’s oversight to prevent bidding behavior that can artificially suppress market prices designed to send signals for the development of new generation is warranted. At a minimum, the Companies should be under some form of oversight or directive to maximize revenues from the PJM markets.

IV. IF THE COMMISSION APPROVES RIDER RRS, IT SHOULD CONDITION ITS APPROVAL OF RIDER RRS ON A COMPETITIVE BID PROCESS FOR THE UNDERLYING PPA

For all the foregoing reasons stated above and in Dynegy’s Initial Brief, the Commission should reject the Rider RRS proposal. However, even if the Commission accepts the rationale of Rider RRS, the Commission should refuse to include the Companies’ and FES’ term sheet for a

⁵⁹ IMM Ex. 2 at 5.

⁶⁰ PJM Amicus Brief at 5.

proposed PPA in Rider RRS, a term sheet that is the product of a cursory, one-sided “negotiation” between affiliates of the same parent corporation. Instead, the Commission will achieve the best outcome for Ohio ratepayers by conditioning any approval of Rider RRS on a competitively bid PPA.

A. The underlying transaction benefits FES and its balance sheet.

The Companies allege that their PPA term sheet with FES “was the subject of extensive due diligence and negotiations conducted at arm’s length”; that the Companies’ team engaged in “extensive due diligence and analysis process to determine whether the proposal could benefit customers”; and that the Companies’ team achieved “robust protections for consumers.”⁶¹ In fact, the final product was a term sheet that tilts entirely in favor of FES. Under the term sheet, FES is (i) excused from the consequences of its failure to deliver energy, capacity or ancillary services; (ii) not responsible for any capacity performance penalties that result from such failure, and (iii) not subject to the modest proposals recommended by Commission Staff, including required information sharing, and some level of risk sharing with the Companies’ ratepayers. Despite their rhetoric, in light of the concessions granted to FES, the Companies cannot credibly say that the term sheet was the product of any substantive negotiation. Rather, the term sheet benefits the Companies’ affiliate, FES, at the expense of the Companies’ ratepayers.

For example, Section 8 of the term sheet excuses FES from delivering energy, capacity, and ancillary services for up to 180 days. During such outages, the Companies would be obligated to pay for many of the costs associated with the offline unit, including operation and

⁶¹ Companies Initial Brief at 49-53

maintenance costs, taxes, and return on equity, notwithstanding that the unit is offline.⁶² These costs, in turn, would be passed to the Companies' ratepayers through Rider RRS.

The only exception in the term sheet to FES' excused delivery obligations during an outage of up to 180 days is when the outage results from FES failure to exercise "Good Utility Practice."⁶³ But the "Good Utility Practice" exception affords minimal protection to the Companies or their ratepayers. First, the exception only applies in the case of unit outage as set forth above or under circumstances that qualify under Section 16 of the term sheet as "Force Majeure."⁶⁴ Otherwise, nothing in the term sheet requires FES to actually abide by Good Utility Practices, and to the extent that FES' failure to do so results in increased costs to the Companies, as long as no unit outage or force majeure event occurs, those costs are passed through to the Companies' ratepayers through Rider RRS.

Moreover, in those circumstances where the Good Utility Practice exception could potentially apply, it is unclear *who* decides—the Companies or FES—whether FES failed to abide by Good Utility Practices. As Companies' witness Don Moul conceded, the term sheet is silent on determining which party decides whether Good Utility Practices were followed:⁶⁵

Q. And the term sheet does not clearly delineate who determines whether a unit was operating consistent with good utility practice, correct?

A. Similar to our previous discussion about the term sheet, I would expect that that process would be outlined in any

⁶² Company Ex. 156, at 2, 5-6; *see, also*, Tr. Vol. 9 at 1998.

⁶³ "Good Utility Practice" is defined as "any of the practices, methods and acts engaged in or approved by a significant portion of the electric utility industry during the relevant time period, or any of the practices, methods and acts which, in the exercise of reasonable judgment in light of the facts known at the time the decision was made, could have been expected to accomplish the desired result at a reasonable cost consistent with good business practices, reliability, safety and expedition." Company Ex. 156 at 14.

⁶⁴ Company Ex. 156, at 3, 8.

⁶⁵ Tr. Vol. 11 at 2295.

final purchase power agreement documentation where this proposed transaction comes.

Q. But the document we have in front of us today in this proceeding does not delineate that, correct?

A. It's not – the process isn't specifically outlined in this purchase power agreement – or in this term sheet. Sorry.

Given the lopsided benefits FES received in the term sheet, taken as a whole, there is a risk that under a finalized PPA, FES could enjoy considerable discretion in determining whether it followed Good Utility Practices. And this should be of particular concern to the Commission, because the final PPA—which presumably will address this important point—would fall outside the purview of the Commission's review. Moreover, once it is determined that FES followed Good Utility Practices (however that determination is made), the Companies' ratepayers will ultimately be responsible for FES' costs.

Also, under the PJM capacity performance program, if units fail to perform as required, unit owners must pay significant penalties, which—in some circumstances—can exceed the total capacity market revenue for a generating unit.⁶⁶ Today, FES is liable for these capacity performance penalties. Under the term sheet, FES would no longer have any exposure for capacity performance penalties as long as it conformed with “Good Utility Practice.”⁶⁷ Instead, under Rider RRS, those costs would be paid by the Companies, and ultimately, by the Companies' ratepayers through Rider RRS.

Moreover, even if the finalized PPA will address capacity performance penalties, because Section 8 of the term sheet excuses FES for non-performance for up to 180 days (except when such outage is the result of non-conformance with Good Utility Practice), any capacity

⁶⁶ IMM Ex. 2 at 3-4.

⁶⁷ Tr. Vol. 11 at 2463.

performance penalties that are imposed on FES as a result of an outage in the ordinary course (i.e., in conformance with “Good Utility Practice”) are charged to the Companies, who then pass the charges onto the ratepayers through Rider RRS. That the Companies’ ratepayers will be ultimately responsible for this significant risk only serves to demonstrate that the term sheet is not the result of a substantive arms’ length negotiation.

Other evidence in the record further shows the absence of a true arms’ length negotiation between the Companies and FES. When the Companies revised the term sheet in November 2015, the Companies chose to ignore recommendations of Commission Staff that the term sheet be amended to require FES to commit to certain Commission oversight of Rider RRS. For example, Staff recommended that FES commit to sharing information:⁶⁸

Full Information Sharing: The Companies *and* FES should commit to providing access to information on all the generation fleet of FES. As an example, if Staff is assessing the reasonableness of a specific cost item for the Davis-Besse plant and deems it appropriate to compare such a cost item to a cost item of another plant; such as the Perry or Beaver Valley plants, the Companies *and* FES should make such information available to Staff. Staff recognizes that such information may be deemed market sensitive or considered Critical Energy Infrastructure Information (CEII) and will follow state and federal laws to ensure its protection.

Staff also recommended that FES commit to a risk-sharing mechanism whereby FES would be responsible for a portion of the costs associated with Rider RRS in exchange for a portion of the revenues associated with Rider RRS, or alternatively, that the term sheet incorporate a cap on charges and credits under Rider RRS.⁶⁹

The Companies ignored both of these Staff proposals. Given the already-lopsided nature of the term sheet—with FES being excused from its delivery obligations and relieved of capacity-performance penalties—the Companies’ refusal to even incorporate the Staff *modest*

⁶⁸ Staff Ex. 12 at 16-17.

⁶⁹ *Id.* at 16-17.

information and risk-sharing proposals only confirms that the purported negotiation was in no sense arms-length and did not result in an agreement that adequately protects the Companies' ratepayers. Instead, the term sheet amounts to nothing more than a financial windfall for FES—FES receives its costs, a return on equity, enjoys minimal responsibility for ensuring delivery, and no responsibility for capacity performance penalties, while the Companies' ratepayers are left exposed to significant risk.

That the term sheet is so favorable to FES is not surprising in light of the events leading up to the negotiation. As Dynegy noted in its Initial Brief,⁷⁰ the genesis for the Rider RRS proposal originated with FES, which was incentivized to propose the long-term hedge and the proposed PPA to the Companies due to the poor condition of FES' balance sheet.⁷¹ As Companies witness Moul indicated, FES views the Rider RRS proposal as a mechanism to “provide some certainty in return for our plants,”⁷² and the Companies were all too willing to accommodate their corporate affiliate. The term sheet, coupled with Rider RRS, gives certainty to FES, but at great risk and cost to the Companies' ratepayers.

B. The Commission should condition any approval of Rider RRS on competitively bidding the underlying PPA.

Because the term sheet is so grossly lopsided in favor of FES, even if the Commission agrees with the Companies that the Rider RRS mechanism *generally* offers ratepayers a valuable “hedge,” the Commission would most effectively protect the interests of ratepayers if it requires that the output to be included in Rider RRS be the subject of a competitive bid process. Competitive bidding is favored by Ohio's public policy, has a proven track-record of reducing

⁷⁰ Dynegy Initial Brief at 4.

⁷¹ Dynegy Initial Brief at 23.

⁷² Dynegy Initial Brief at 4; Tr. Vol. 11 at 2290.

energy prices in Ohio, and will lead to market-based offers that are significantly more favorable for Ohio's ratepayers than the proposed PPA with FES.

Ohio law favors competitive bidding. For example, competitive bidding is required for county purchases, leases, or contracts to be obtained through competitive bidding.⁷³ Municipalities⁷⁴ and state agencies⁷⁵ are likewise required to procure supplies or services over a certain dollar amount through competitive bidding. Ohio courts too have recognized the many benefits of competitive bidding to both merchants/service providers and the public at large:⁷⁶

Competitive bidding is well recognized in public matters because it gives everyone an equal chance to bid, eliminates collusion, and saves taxpayers money. There has been a strong public policy in favor of competitive bidding to protect the public and eliminate collusion. It fosters honest competition in order to obtain the best work and supplies at the lowest possible price because taxpayers' money is being used. **It is also necessary to guard against favoritism, imprudence, extravagance, fraud and corruption.** Competitive bidding statutes are to be construed for the benefit of taxpayers and not bidders. The guidepost is the public interest.

The same is just as true here—requiring the Companies to engage in a competitive bidding process to obtain a PPA to include in Rider RRS would give other merchant generators an equal chance to participate, provide a safeguard against lopsided terms that inure to one market participant's exclusive benefit, and will yield significant savings for ratepayers.

The benefits of competitive bidding are also demonstrated by the success of the standard service offer ("SSO") auctions held by the Companies and other electric distribution utilities.

⁷³ See, R.C. 307.86.

⁷⁴ See R.C. 735.05.

⁷⁵ See, R.C. 125.05(B).

⁷⁶ *United States Constructors & Consultants, Inc. v. Cuyahoga Metro. Hous. Auth.*, 35 Ohio App.2d 159, 300 (8th Dist.1973). *Accord State v. Bd. of Cnty. Comm'rs*, 8th Dist. Cuyahoga No. 36979, 1978 Ohio App. LEXIS 10306, at *9-10 (Apr. 27, 1978) (emphasis added).

Today, 100% of the SSO loads of three Ohio electric distribution companies⁷⁷ are being procured through competitive retail auctions administered by the Commission.⁷⁸ As Staff witness Dr. Choueiki noted: “[n]ot only are the resulting SSO rates competitive, they also serve as transparent ‘prices to compare to’ or ‘benchmarks’ for customers who are considering whether to take service from a competitive retail electric service (CRES) provider.”⁷⁹ In other words, competitive SSO auctions offer dual benefits for Ohioans.—they guarantee competitive rates for SSO load customers (including the Companies’ customers), and also ensure that rates stay low for shopping customers. Likewise, in this case, the Companies’ customers would stand to benefit significantly over the current Rider RRS proposal if the Commission conditioned its approval of Rider RRS on a competitively bid PPA.

Even more telling is that merchant generators have indicated their willingness to compete with FES for a PPA to include in Rider RRS. Exelon has made an eight-year offer from 100% emissions-free power units,⁸⁰ and would commit to 100% of the capacity performance risk—unlike FES, which shifts that risk to the Companies’ ratepayers—and will provide over \$2 billion in customer savings over the FES offer.⁸¹ Exelon’s offer is indicative of the sort of market-based offer that could be expected to result from a competitive bid process, and shows that competition produces the best results for Ohio. Dynegy agrees and has expressed interest in competing in a competitively bid process or request for proposal if the Commission approves Rider RRS.⁸²

⁷⁷ Ohio Power Company, Duke Energy Ohio, and the Companies.

⁷⁸ Staff Ex. 12 at 7.

⁷⁹ *Id.* at 7, n.14.

⁸⁰ Exelon Ex. 4 at 6.

⁸¹ *Id.*

⁸² Dynegy Initial Brief at 19-20.

V. CONCLUSION

Dynegy opposes Rider RRS for many reasons, including that it will expose ratepayers to significant financial risk and negatively impact wholesale markets, all the while favoring one wholesale and retail market participants (FES). The Commission cannot and should not approve Rider RRS, especially given that the plants are not at risk of closing. FES may need Rider RRS for its balance sheet, but Ohio ratepayers neither need nor want Rider RRS. The Commission should remove Rider RRS from the Companies' proposed ESP IV. In the alternative, if the Commission does not reject Rider RRS, it must at a minimum, condition any approval on a competitive bid process.

Respectfully submitted,

s/ Michael J. Settineri

M. Howard Petricoff (0008287), Counsel of Record

Michael J. Settineri (00073369)

Gretchen L. Petrucci (00046608)

Vorys, Sater, Seymour and Pease LLP

52 East Gay Street

Columbus, OH 43215

614-464-5414

mhpetricoff@vorys.com

mjsettineri@vorys.com

glpetrucci@vorys.com

Counsel for Dynegy Inc.

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 26th day of February 2016 upon all persons/entities listed below:

s/ Michael J. Settineri
Michael J. Settineri

burkj@firstenergycorp.com
cdunn@firstenergycorp.com
jlang@calfee.com
talexander@calfee.com
dakutik@jonesday.com
cmooney@ohiopartners.org
drinebolt@ohiopartners.org
tdougherty@theoec.org
ghull@eckertseamans.com
sam@mwncmh.com
fdarr@mwncmh.com
mpritchard@mwncmh.com
mkurtz@BKLlawfirm.com
kboehm@BKLlawfirm.com
Marilyn@wflawfirm.com
blanghenry@city.cleveland.oh.us
hmadorsky@city.cleveland.oh.us
kryan@city.cleveland.oh.us
bojko@carpenterlipps.com
gkrassen@bricker.com
dstinson@bricker.com
dborchers@bricker.com
stheodore@epsa.org
mdortch@kravitzllc.com
rparsons@kravitzllc.com
dparram@taftlaw.com
callwein@keglerbrown.com
mkimbrough@keglerbrown.com
rkelter@elpc.org

jkylercohn@BKLlawfirm.com
larry.sauer@occ.ohio.gov
Maureen.grady@occ.ohio.gov
joliker@igsenergy.com
schmidt@sppgrp.com
ricks@ohanet.org
tobrien@bricker.com
stnourse@aep.com
mjsatterwhite@aep.com
yalami@aep.com
jfinnigan@edf.org
wtpmlc@aol.com
mkl@smxblaw.com
gas@smxblaw.com
mkimbrough@keglerbrown.com
mfleisher@elpc.org
matt@matthewcoxlaw.com
todonnell@dickinsonwright.com
jeffrey.mayes@monitoringanalytics.com
twilliams@snhsllaw.com
sechler@carpenterlipps.com
gpoulos@enernoc.com
charris@spilmanlaw.com
dwolff@crowell.com
rlehfeldt@crowell.com
dfolk@akronohio.gov
gghiloni@carpenterlipps.com
jennifer.spinosi@directenergy.com

lhawrot@spilmanlaw.com
dwilliamson@spilmanlaw.com
meissnerjoseph@yahoo.com
trhayslaw@gmail.com
lesliekovacik@toledo.oh.gov
cynthia.brady@exeloncorp.com
david.fein@exeloncorp.com
lael.campbell@exeloncorp.com
christopher.miller@icemiller.com
gregory.dunn@icemiller.com
jeremy.grayem@icemiller.com
BarthRoyer@aol.com
athompson@taftlaw.com
mhpetricoff@vorys.com
mjsettineri@vorys.com
glpetrucci@vorys.com
thomas.mcnamee@puc.state.oh.us
thomas.lindgren@puc.state.oh.us
sfisk@earthjustice.org
msoules@earthjustice.org
tony.mendoza@sierraclub.org
laurac@chappelleconsulting.net
gthomas@gtpowergroup.com
Kevin.moore@occ.ohio.gov
William.michael@oc.ohio.gov
rsahli@columbus.rr.com
ajay.kumar@occ.ohio.gov
kristin.henry@sierraclub.org

This foregoing document was electronically filed with the Public Utilities

Commission of Ohio Docketing Information System on

2/26/2016 4:22:57 PM

in

Case No(s). 14-1297-EL-SSO

Summary: Brief Public Version of Reply Brief electronically filed by Mr. Michael J. Settineri on behalf of Dynegy Inc.