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BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of the Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company For Approval of a Competitive Bidding Process for Standard Service Offer Electric Generation Supply, Accounting Modifications Associated With Reconciliation Mechanisms and Phase In, and Tariffs for Generation Service.	)	Case No. 07-796-EL-ATA Case No. 07-797-EL-AAM

INITIAL COMMENTS OF NUCOR STEEL MARION, INC.

John W. Bentine, Esq. (0016388)
Counsel of Record
E-Mail: jbentine@cwslaw.com
Mark S. Yurick, Esq. (0039176)
Direct Dial: (614) 334-7197
Email: myurick@cwslaw.com
Direct Dial: (614) 334-6121
Chester, Willcox & Saxbe LLP
65 East State Street, Suite 1000
Columbus, Ohio 43215-4213
(614) 221-4000 (Main Number)
(614) 221-4012 (facsimile)

Garrett A. Stone*
Michael K. Lavanga*
E-Mail: gas@bbrslaw.com
E-Mail: mkl@bbrslaw.com
Brickfield, Burchette, Ritts & Stone, P.C.
1025 Thomas Jefferson Street, N.W.
8th Floor, West Tower
Washington, D.C. 20007
(202) 342-0800 (Main Number)
(202) 342-0800 (Facsimile)
* Pending admission *pro hac vice*

Attorneys for Nucor Steel Marion, Inc.

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In accordance with the Entry dated August 16, 2007 in this docket, Nucor Steel Marion, Inc. ("Nucor Marion") submits these initial comments in response to the July 10, 2007 application ("Application") submitted by the Ohio Edison Company ("Ohio Edison"), the Cleveland Electric Illuminating Company, and the Toledo Edison Company (collectively "FirstEnergy"). In its Application, FirstEnergy proposes to establish a competitive bidding process to procure supply for the provision of Standard Service Offer ("SSO") electric generation service to retail electric customers who do not purchase electric service from a competitive retail supplier beginning January 1, 2009. FirstEnergy also proposes new retail rate schedules, including a new interruptible tariff. Nucor Marion urges the Commission in this proceeding to: (1) subject FirstEnergy's proposal to detailed scrutiny in order to ensure that FirstEnergy's competitive bidding mechanism will result in reliable service at the lowest possible rates for customers that select the SSO service option; and (2) to adopt Nucor Marion's recommendations for improvements to FirstEnergy's proposal.

I. INTRODUCTION

Nucor Marion is an electric arc furnace steel maker, one of Ohio Edison's largest industrial customers, and a significant employer in the Marion, Ohio area. Nucor Marion uses an electric arc furnace to melt scrap steel, which is then recycled into new steel products. Electric arc furnace steel making is far more efficient than traditional, fully-integrated steel making, but the electric arc furnace steel making process still requires massive amounts of electric energy. Reliable and economic power supply is an absolute necessity for Nucor Marion to compete and remain profitable in highly competitive world-wide steel markets. As a result, Nucor Marion has a strong interest in Ohio's statewide retail electric supply restructuring efforts in general, and FirstEnergy's proposals to implement retail competition and supply SSO service in particular.

Nucor Marion's parent company, Nucor Corporation ("Nucor"), has steel mills in numerous states throughout the country, including some states that have deregulated their retail electric markets and some states that have not deregulated. In Nucor's experience, it is evident that electric rates in states that have not deregulated are generally lower and more stable than in states with retail competition, despite the fact that customers have the choice to choose their suppliers in retail access states. In short, deregulated retail markets, including those in Ohio, have yet to produce their promised benefits. As Governor Strickland correctly observed in his recently-released energy plan, "[t]here is broad consensus that deregulation has failed to deliver and efficient, competitive market that can meet the needs of Ohio's economy in an affordable, reliable, and sustainable manner."

Given this background, it is critically important that FirstEnergy's SSO electric generation service be designed in a way to provide reliable electric service at stable and low prices to those customers who choose not to take generation service from a competitive supplier.

A well-designed SSO service should provide a reasonable and attractive alternative supply option for customers who do not want to shop for a supplier, and for those customers who cannot find a workable supply option in the competitive market. This would provide protection for FirstEnergy's customers, and it would also put pressure on suppliers in the competitive market to develop services that are as attractive or more attractive to customers than the SSO service option.

Nucor Marion believes that a strong SSO service option should incorporate several features. First, the mechanism for procuring power supply (whether a competitive bidding process as proposed by FirstEnergy or some other supply acquisition process) should ensure that FirstEnergy can procure reliable supply at the lowest possible cost over an extended period of time. Second, the cost allocation and rate design must be fair and must recognize the cost causation differences between the various customer classes. Third, SSO rates should be designed with as much reasonable time-differentiation as possible, so that customers will be encouraged to manage their electricity usage in response to price signals, while also permitting customers to choose how much price volatility they are willing to endure. Finally, and particularly important to Nucor Marion, the SSO service option must incorporate a strong interruptible load program.

The following comments identify various issues with FirstEnergy's SSO mechanism as presented in the Application and offer proposals for how the mechanism can be improved. These comments address FirstEnergy's proposed bidding process, cost allocation and rate design, and interruptible program. It should be noted that these comments address the interruptible program in particular detail since, as a current interruptible customer of Ohio Edison (and with numerous interruptible mills located around the United States), Nucor Marion has a unique understanding

of the benefits interruptible loads provide, and a strong interest in ensuring that an appropriate interruptible rate is retained as part of the SSO service option. These comments are also limited due to limited supporting information contained in FirstEnergy's Application and the limited time available under the procedural schedule in this proceeding.

Below is a brief summary of Nucor Marion's comments:

- Proposed Competitive Bidding Process
    - FirstEnergy does not include enough information to support its competitive bidding proposal, or to show that the specific competitive bidding mechanism it proposes is the best option to procure SSO supply. Accordingly, the Commission should establish a process to determine the best approach to acquiring generation supply for FirstEnergy customers and should exercise caution in considering and implementing FirstEnergy's proposals.
    - FirstEnergy should provide more detail on the relative benefits and shortcomings of the load class and slice of system auction approaches so that the Commission and the parties can fully evaluate these alternatives.
- Proposed Rate Design
    - More time-of-day price differentiation should be built into the rate design; specifically, at a minimum, a super/critical peak period should be added.
    - A hedging mechanism should be built into the hourly pricing option, permitting customers the option of hourly pricing for only a portion of their load.
    - Customers in the Optional Load Response Program should be exempt from the Revenue Variance Rider.
    - If the slice of system approach is chosen, the reconciliation mechanism should reflect the class allocation factors used to develop the rates for each customer class.
    - The avoidable charge under the slice of system approach should be the applicable SSO generation charge plus the reconciliation charge.
- Proposed Optional Load Response Program
    - To build more flexibility into the Optional Load Response Program ("OLRP"), FirstEnergy should split the ORLP into reliability/emergency and economic options, provide various options with regard to notice/response time and hours

of interruption, and tailor the Program Credit to reflect different degrees of participation by customers.

- The Commission should set a robust Program Credit in this proceeding, reflecting long-run avoided generation, transmission and energy costs at a level at least equal to or greater than interruptible credits built into current rates.

- The proposed penalties for failure to interrupt are excessive and should be modified.

- The 400 MW aggregate cap on participation in the OLRP should be eliminated.

- There should be no expiration date for the OLRP.

- There should be no restriction on OLRP customers participating in other demand response programs.

- The OLRP (or at least the reliability component of the program) should not be limited to customers taking generation service under Rider GEN from FirstEnergy.

- Monthly peak demand, not average demand, should be used in calculating a customer's curtailable load.

- The demand measurement time period for measuring a customer's performance should be consistent with the demand measurement time period used to calculate the customer's curtailable load.

II. COMMENTS

A. Bidding Process

FirstEnergy proposes a competitive bidding process to procure generation supply for its SSO customers. FirstEnergy also proposes two alternative bidding processes – a load class option and a "slice of system" option – and leaves it to the Commission to decide which option to choose. Under the load class option, generation supply would be procured separately for each load class (*i.e.*, residential, general service-small, and general service-large), and the winning prices for each class determine retail prices for all customers in the class. Application at 15-16. Under the slice of system option, generation is procured on a total load basis, and the generation

charge for each load class is determined by applying allocation factors based on the ratio of each load class' historical average SSO generation and transmission rates to the average of all historical SSO generation and transmission rates. *Id.* at 16-17.

Under both the load class and slice of system options, the total amount of SSO supply is divided into "tranches," which represent a fixed percentage share of FirstEnergy's SSO hourly load. *Id.* at 10. Suppliers bid to provide "full requirements" supply (including energy, capacity, transmission service, and transmission ancillaries) in a descending clock auction. *Id.* at 10-11. The initial competitive bidding process will procure SSO supply for three staggered delivery periods each beginning on January 1, 2009 but ending at different points in time. *Id.* at 11.

1. FirstEnergy Does Not Provide Enough Support for Its Competitive Bidding Proposal.

While the bidding processes FirstEnergy outlines are options the Commission should consider, the Application does not contain enough detail to justify adopting FirstEnergy's competitive bidding proposal without obtaining considerably more information. A competitive bidding process (with the specific auction proposed by FirstEnergy) is certainly not the only option available to FirstEnergy to procure generation supply for its SSO customers. As FirstEnergy notes, other options include a request for proposal process. Application at 8. Moreover, even if a competitive bidding process is best, that is no reason to believe the particular features selected by FirstEnergy for this process are the best.

According to the Application, a competitive bidding process is the best option because it "incorporates benefits from suppliers' varying approaches to managing their supply sources and to timing and maintaining diversity in their purchases." Application at 8. FirstEnergy concludes that its competitive bidding process will result in an SSO supply portfolio that "will balance out

wholesale market price fluctuations and provide SSO customers with a stable price for a specified period of time." *Id.*

This all may very well be true. The problem is the Application does not explain why and how its specific competitive bidding proposal will have the results FirstEnergy promises[1], or why the proposed mechanism is superior to alternative mechanisms. The Application contains no detailed discussion of other alternatives, and therefore no comparison of the competitive bidding proposal with other alternatives. The Application contains no expert testimony explaining why FirstEnergy's competitive bidding proposal is the best option and the procedural schedule does not appear to allow the parties the opportunity to explore these issues fully through discovery and a hearing. The August 16, 2007 technical conference in this proceeding was useful to get certain details of the proposal explained, but the issue of why the competitive bidding process is the best option was not (and could not have been) addressed in detail in a single day. Finally, although the Commission has invited parties to submit "alternative proposals" on the same date comments are due in this proceeding, the short procedural schedule in this proceeding does not give the parties enough time to fully evaluate FirstEnergy's proposal, fully research other options, and fully develop their own alternative proposals.

For these reasons, the Commission should exercise considerable caution in reviewing and possibly approving FirstEnergy's competitive bidding proposal. The mechanism approved by the Commission will be used to procure billions of dollars worth of SSO energy for a large portion of the retail customers in the state of Ohio. Given what is at stake, the Commission should not approve (or reject) FirstEnergy's proposal in haste and certainly not without thorough review and analysis.

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[1] Relying on FirstEnergy's opinion is particularly problematic when FirstEnergy's regulated utilities have no stake in the outcome and its affiliates with generation would likely benefit from higher prices.

Accordingly, the Commission should consider extending the schedule in this proceeding and instituting hearing and discovery procedures. The schedule currently allows only for a set of initial comments and a set of reply comments. Hearing and discovery procedures would allow for a more thorough investigation of FirstEnergy's proposal and other options to procure SSO supply, as well as the development of a detailed record. The Commission would be far better positioned after such a proceeding to rule on FirstEnergy's proposal than it would be after just a round of comments and reply comments.

Nucor Marion acknowledges FirstEnergy's position that a decision in this proceeding must come quickly, so that FirstEnergy has time to conduct the auction process and be ready to begin providing SSO service on January 1, 2009. However, FirstEnergy should not be allowed to hold the January 1, 2009 target date over the head of the Commission and insist on a truncated proceeding in order to meet that deadline. After all, FirstEnergy had control over when it filed its case. FirstEnergy, moreover, has asserted that it needs a Commission ruling on the competitive bidding process by no later than November 1, 2007 in order to "accommodate the necessary lead times and to ensure the uninterrupted provision of SSO Generation Service" (Application at 9), but there is no evidence that FirstEnergy could not be prepared by January 1, 2009 if the schedule in this proceeding is extended for several months. The Commission should ask FirstEnergy to state and justify the date by which it needs a Commission determination in order for it to conduct a reasonable auction process in time for the start of SSO service on January 1, 2009.

Next, the Commission should not treat FirstEnergy's proposal as an all or nothing proposition. The Commission must ensure that whatever SSO procurement mechanism is selected is the right mechanism before putting it in place permanently. In addition to instituting

a more extensive proceeding to examine FirstEnergy's competitive bidding proposal, the Commission should consider phasing-in the bidding process, or granting conditional approval of the mechanism. For example, the Commission could grant FirstEnergy approval to do one phase of the auction (rather than all three) and keep this docket open so that the results of the first phase can be analyzed, and modifications or improvements can be made before the second two phases of the auction are conducted or before some alternative approach is utilized to obtain the rest of FirstEnergy's supply. For example, if the auction does not provide the best results, the remainder of the supply could be acquired through an RFP or some other approach. Similarly, the Commission could shorten the period of any procurement (for example, 12 or 17 months, instead of three different terms of 17, 29 and 41 months) so that lessons learned can be incorporated more quickly into future supply solicitations. Approving the competitive bidding proposal in incremental steps, rather that all at once, would allow the Commission and parties to analyze how the competitive bidding process is working and make necessary changes before final approval is granted.

Another fundamental concern that goes unaddressed by FirstEnergy's Application is the likely affect of market power exercised by FirstEnergy affiliates over electricity that is available and can be reasonably delivered into the FirstEnergy system. Under FirstEnergy's proposal, a single supplier can provide up to 75% of the SSO supply for any class in the load class alternative for each solicitation, and up to 75% of the system load under the slice of system alternative. Application at 14. The Commission should address whether 75% is the appropriate cap, and explore whether such a high cap signals an insufficient number of competitive suppliers, and the lack of a competitive market. The Commission should carefully evaluate whether

market power exists and, if so, how it should be mitigated in order to ensure a reasonably competitive supply.

2. FirstEnergy Provides No Evidence or Analysis of the Comparative Benefits of the Customer Class and Slice of System Auction Approaches.

Even assuming that a competitive bidding mechanism as proposed by FirstEnergy is the best option to procure SSO supply, there is no way of telling whether the customer class or slice of system approach would be the optimal approach. FirstEnergy describes both options, but provides no explanation of the comparative benefits and shortcomings of each approach. Given the lack of information in FirstEnergy's filing, Nucor cannot take a position on which is the better option. This is another reason supporting extending this proceeding and instituting hearing and discovery procedures. The Commission should not be forced to make a choice between the customer class and slice of system options based on a record devoid of any analysis comparing the two options.

B. Cost Allocation and Rate Design

1. More Price Differentiation Should Be Built Into the Rate Design.

Under FirstEnergy's rate design proposal, rates would be seasonally differentiated (summer and winter) and would also be differentiated based on time of day (on-peak and off-peak) under a time of day option. FirstEnergy also proposes an hourly pricing program for customers with the ability to manage their load and who have the required metering. FirstEnergy explains that these rate design elements will send more appropriate price signals to customers, thereby encouraging customers to reduce energy usage and demand during higher priced periods. Application at 5.

Nucor Marion agrees that price differentiation can lead to better price signals and more demand response by retail customers. In this regard, Nucor Marion supports FirstEnergy's proposal to time-differentiate its rates, although the proposal does not go far enough. FirstEnergy's rate design can and should be refined further in order to provide even more price differentiation, thereby providing more accurate price signals and giving customers better incentives to manage their energy consumption. As currently proposed, there will be prices corresponding to only two seasonal periods and two daily periods. For customers with the ability and willingness to respond to price, this is not enough price variation. Although FirstEnergy is also offering an hourly pricing option, the hourly pricing option incorporates too much price volatility and probably will not be an attractive option for most customers. FirstEnergy's rate design, therefore, would be significantly improved if it incorporates more price differentiation into its time of day rates.

More price variation can and should be built into FirstEnergy's time of day rates by breaking the on-peak and, possibly, off-peak periods down further. The on-peak period can be split into on-peak and super/critical peak periods. For example, rather than having the on-peak period run for 16 hours a day, the super/critical peak period could run for 4 hours and the on-peak period the remaining 12 hours. Setting a super/critical-peak price would send a strong price signal for customers to curtail their usage at times of maximum system usage, which is when demand response can provide the greatest benefit. This approach would also reduce supplier risk of high demands during peak conditions and potentially result in lower bids. If desirable, additional periods, such as a shoulder period could be established, as well.

In summary, more price variation can and should be built into FirstEnergy's SSO option so that customers will have better price signals and a stronger incentive to tailor their usage

patterns to correspond to those price signals. At a minimum, this would include establishing a super/critical peak time period.

2. The Hourly Pricing Option Should Include a Hedging Mechanism.

Under FirstEnergy's proposal, a customer on the hourly pricing option (proposed Rider HPS) is subject to hourly prices for its entire load. As noted above, many customers will probably be reluctant to subject themselves to the volatility of hourly prices reflecting Midwest ISO LMPs. But if a hedging mechanism is built into the hourly pricing program, customers would be more willing to take hourly service for at least part of their loads. Accordingly, the Commission should direct FirstEnergy to build a hedging mechanism into the hourly program, whereby a customer may take hourly service for a portion of its load, but take service under the seasonal/time of day rate for the rest of its load. The amount of load under each type of rate would be specified in advance, either as a percentage or based on a particular amount of electricity usage per hour. This would provide an SSO customer with more flexibility to structure its service in the way that best serves the customer's needs. As noted below, FirstEnergy's interruptible (ORLP) program should be revised so that hourly priced customers under Rider HPS would also have the option to participate.

3. ORLP Customers Should be Exempt from the Revenue Variance Rider.

FirstEnergy explains that customers on rate schedules STL (street lighting service), TRP (traffic lighting service) and OLRP (interruptible), and special contract customers, will be billed for generation service at a rate different than the SSO generation charge for their load class, which results in SSO revenue being less than FirstEnergy's SSO revenue requirements. FirstEnergy proposes to recover the difference between revenue and expenses through a revenue

variance rider ("Rider RVR"). All customers, except STL, TRP, and special contract customers, will be subject to Rider RVR. Application, Exhibit C1 at 6; Exhibit C2 at 8.

Making OLRP customers subject to Rider RVR creates the impression that what FirstEnergy is giving with the right hand, FirstEnergy is taking away with the left. In other words, OLRP customers may not receive the full measure of the cost savings they are due in return for agreeing to be interruptible. To make matters worse, an OLRP customer will not only be responsible for the effects of its own participation in the ORLP, but for the effects of participation by all other OLRP customers as well. In short, making OLRP customers subject to Rider RVR could be a disincentive against participation in the OLRP.

The Commission should require FirstEnergy to make OLRP customers exempt from Rider RVR. FirstEnergy already exempts STL, TRP, and special contract customers from Rider RVR, and FirstEnergy provides no explanation why it is appropriate to exempt those customers, but not ORLP customers. Exempting OLRP customers from Rider RVR will ensure that those customers receive the full measure of compensation they are due, and will eliminate the disincentive against participation in the OLRP. At minimum, OLRP customers should be exempt from the OLRP component of Rider RVR.

4. If the Slice of System Option is Chosen, the Proposed Reconciliation Mechanism Should Reflect the Class Allocation Factors Used to Develop the Rates for Each Customer Class.

FirstEnergy proposes a reconciliation mechanism to recover, among other things, the difference between amounts paid to suppliers and amounts actually billed to customers over the course of a quarter. Application at 19. FirstEnergy explains that if the slice of system competitive bidding process is implemented, there will be a single Reconciliation Charge for all

load classes. *Id.* The Commission should reject this proposal, because it is inconsistent with how the rates for each customer class are set under the slice of system approach.

Under the slice of system option, the SSO generation charge for each load class is calculated by taking the Blended CBP Price and multiplying it by a factor based on the ratio of each load class's historical average SSO generation and transmission rate to the average of all historical SSO generation and transmission rates. Application at 16-17. The rate for each class is then adjusted by the load class seasonal factor and a Time-of-Day Application Factor for those customers on time-of-day rates. Calculating the rates in this manner recognizes that usage patterns vary by customer class and establishes rates that are intended to reflect the costs associated with serving each customer class.

FirstEnergy's proposal to apply a single Reconciliation Charge to all customer classes under the slice of system approach creates an asymmetry between the SSO generation charge and the Reconciliation Charge that would result in certain customer classes bearing disproportionate cost responsibility for reconciliation charges as compared to other customer classes. For example, FirstEnergy proposes Class Allocation Factors of 0.900 for customer class GP and 0.800 for customer class GSU. Application, Exhibit C2 at 1. If a single Reconciliation Charge is applied across all customer classes, class GSU will pay a greater percentage of FirstEnergy's quarterly reconciliation costs as compared to its SSO Load Class Charge class GP. This approach is inconsistent and not reflective of cost causation.

The Commission should direct FirstEnergy to apply the same class allocation factors in determining the Reconciliation Charge for each customer class as FirstEnergy applies in calculating the SSO generation charge for each class. This will ensure that each customer class' Reconciliation Charge is in correct proportion to its SSO Load Class Charge, which will ensure

that customer classes with lower Class Allocation Factors do not pay greater than their fair share of FirstEnergy's quarterly reconciliation costs.

5. The Avoidable Charge Under the Slice of System Option Should Be the Customer's SSO Generation Charge Plus the Reconciliation Charge.

Under the load class option, the avoidable charge for a customer that takes generation service from a supplier other than FirstEnergy is the SSO Generation Charge plus the Reconciliation Charge. Application at 20. Under the slice of system approach, however, FirstEnergy proposes that the avoidable charge for each load class will be equal to the lower of: (i) the blended competitive bid price multiplied by the supplier seasonal billing factor adjusted for average distribution line losses and applicable taxes, or (ii) the customer's SSO Generation Charge. *Id.* at 21. This proposed treatment under the slice of system approach is unreasonable.

The SSO Generation Charge and the Reconciliation Charge are the charges a customer would pay for generation if it takes generation service from FirstEnergy, and therefore are the charges that the customer should avoid if it elects to take generation service from a competitive supplier, even if the Commission chooses the slice of system option. Setting the avoidable charge at the lower of the blended competitive bid price or the SSO Generation Charge could mean that a customer taking generation service from a competitive supplier ends up paying FirstEnergy for some service that is not actually provided by FirstEnergy. Not only would this provide a windfall to FirstEnergy, but it would also be a disincentive for customers to switch to competitive suppliers. Accordingly, the Commission should require FirstEnergy to modify its proposal so that the SSO Generation Charge plus the Reconciliation Charge are the avoidable charges regardless of whether the customer class or slice of system option is selected.

C. Load Response/Interruptible Program

It is vital that the SSO incorporate a strong load response program. By now, the benefits of interruptible load and other demand response programs are undisputed in Ohio and nationwide. Interruptible load provides a unique blend of reliability and economic benefits. According to the United States Department of Energy, demand response programs, such as interruptible load, that reduce peak demand growth "directly avert[] the need for utilities to build more power plants, power lines and other capacity-driven infrastructure or to buy new capacity and energy from other suppliers." U.S. Department of Energy, *Benefits of Demand Response in Electricity Markets and Recommendations for Achieving Them* at 77 (2006) ("*DOE Demand Response Report*"). Interruptible load can also reduce strain on a utility's transmission and distribution system at times of peak demand or during system emergencies, and can be used to provide ancillary services such as spinning reserves and operating reserves. In fact, large industrial "batch processes" such as electric arc furnaces have "traditionally been viewed as ideal substitutes for a generator, as they are large, dispatchable, and can be easily configured with SCADA systems for control and telemetry." Ernest Orlando Lawrence Berkeley National Laboratory, *Loads Providing Ancillary Services: Review of International Experience* at 41 (2007). With respect to the wholesale markets, interruptible load can help reduce prices and price volatility, flatten a region's load profile, and help reduce rates for all customers in the region. *See* Federal Energy Regulatory Commission, Docket Nos. RM07-19-000 and AD07-7-000, *Advance Notice of Proposed Rulemaking on Wholesale Competition in Regions with Organized Wholesale Markets* at 25-26 (2007). Finally, demand response programs such as interruptible load could have direct environmental benefits by reducing emissions from fossil fuel generators at times of peak demand (usually the hottest summer days), thereby reducing the

level of green house gas emissions from such generators and improving air quality. *See* Federal Energy Regulatory Commission, Docket No. AD06-2-000, *Assessment of Demand Response and Advanced Metering* at 12 (2006).

Interruptible programs also provide important benefits to the interruptible customers themselves by lowering their rates. As Nucor Marion and most of Nucor's mills in other states can attest, an interruptible credit is a critical element of their electric rate. Indeed, some industrial customers could not achieve an electric rate low enough to keep their businesses profitable without an interruptible credit. In most cases, interruptible customers would prefer to be firm customers so that they do not have to worry about curtailing their operations at the request of their utility, but they accept the burden of being interruptible (including lost production when they are required to interrupt) so they can qualify for a rate low enough to allow them to remain in business.

Interruptible programs, therefore, provide important benefits to the utility, the interruptible customers themselves, and the utility's other customers. Unfortunately, interruptible programs often have not fared well in deregulated retail environments. Some utilities in deregulated states have washed their hands of interruptible rates since those utilities no longer carry an obligation to serve and are not required to provide generation service to their retail customers, while competitive suppliers in these states may have insufficient incentive to offer a reasonable interruptible rate. As a result, traditional interruptible rates have often atrophied in several retail choice states, sometimes with disastrous consequences. Last spring, for example, Texas experienced rolling blackouts despite the fact that the state had a 17% reserve margin. The blackouts were attributed to unusually hot weather and the fact that many generators were down for maintenance. The Electric Reliability Council of Texas ("ERCOT")

curtailed approximately 1,150 MW of industrial load participating in ERCOT's Load Acting as a Resource Program, but this level of interruptible load was far below the level of interruptible load in ERCOT before the introduction of competition in Texas. If there were more traditional interruptible load available in ERCOT last spring, the rolling blackouts might have been mitigated or avoided. *See* Public Utility Commission of Texas, Docket No. 31972, Rulemaking Concerning Resource Adequacy and Market Power in the Electric Reliability Council of Texas Power Region, Comments of Various Parties Interested in Demand Side Issues at 2 (April 10, 2006) (noting that utilities reported over 3,100 MW of interruptible load in ERCOT prior to restructuring, more than double the amount of interruptible load participating in the Load Acting as a Resource Program). In response to this problem, the Public Utility Commission of Texas ordered ERCOT to establish an emergency interruptible load service to acquire an additional 500 - 1000 MW of emergency interruptible load. *See* Public Utility Commission of Texas, Substantive Rule 25.507[2].

Given the importance of interruptible rates, FirstEnergy's OLRP is a key element of FirstEnergy's SSO proposal.[3] Under FirstEnergy's proposed Rider LRP, the OLRP will be restricted to customers on Rate Schedule GT taking SSO generation service from FirstEnergy under Rider GEN. Application, Exhibit E at 6. The program provides for two types of curtailment events: an Emergency Curtailment Event and an Economic Buy Through Event. *Id.* at 1. An OLRP customer will be required to curtail its electrical consumption in excess of its contract firm load when an Emergency Curtailment Event is called. *Id.* For up to 1,000 hours per calendar year, FirstEnergy may also call an Economic Buy Through Event. *Id.* When such an event is called, the customer will have the option of curtailing, or paying the day-ahead hourly

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2 The Texas citations are available online on the Public Utilities Commission of Texas website, www.puc.state.tx.us, but copies will be made available upon request.

3 See generally Application, Exhibit E for FirstEnergy's description of its ORLP proposal.

Midwest ISO LMP for the customer's consumption in excess of its firm load. *Id.* In return for participating in the OLRP, a customer will receive a Program Credit, based on the amount of the customer's curtailable load. *Id.*

While FirstEnergy's plan to offer the OLRP is welcome, the Application does not provide enough information for the Commission and interested parties to determine whether the program is reasonable. Further, several elements of the OLRP could be improved in ways to make the program more attractive to customers and more useful to FirstEnergy. In evaluating FirstEnergy's OLRP proposal and considering ways it could be improved, Nucor Marion urges the Commission to ensure that the program meets two broad goals. First, as much flexibility and variability should be built into the OLRP as possible, so that customers can tailor their participation in the program to their specific business plans and operations. Second, the compensation (Program Credit) that customers receive for participating in the program should be adequate enough to ensure at least the level of participation in FirstEnergy's current interruptible rates and such compensation should, at a minimum, reflect the benefits and cost savings created by such load. These goals can be met if the recommendations discussed below are incorporated into the ORLP.

1. More Flexibility Should Be Built Into the OLRP.

As currently proposed, the ORLP provides customers with few options. All OLRP customers are subject to both Emergency Curtailment Events and Economic Buy Through Events; all OLRP customers are subject to the same notice periods (*i.e.*, 10 minutes for an Emergency Curtailment Event and no less than 90 minutes for an Economic Buy Through Event); all OLRP customers receive the same Program Credit; and all OLRP customers are exposed to up to 1000 hours worth of Economic Buy Through Events.

The rigidity of these requirements will turn away some customers who might otherwise be willing to participate in the ORLP. For example, a customer might be willing to interrupt for reliability reasons, but unwilling to curtail for economic reasons. The requirement that customers respond to both Emergency Curtailment Events and Economic Buy Through Events would preclude such a customer from participating in the ORLP. Similarly, a customer might be unable to curtail on 10 minutes notice, but might be willing and able to curtail on 30 minutes notice. This customer also could not participate in the ORLP as currently proposed.

a. The ORLP should establish separate reliability and economic interruption programs

More flexibility and variability should be built into the OLRP because every customer's circumstance is different. If there are more options for how customers can participate, customers will be able to tailor their participation in the OLRP to their own business plans and operations, which will result in a higher overall level of participation in the OLRP. To begin with, the OLRP should be broken into two separate programs – a reliability program and an economic program – and customers should be allowed to participate in one or both programs. The necessary requirements for economic interruptions and reliability interruptions differ and the value of such interruptions differ. For example, shorter notice periods are necessary for reliability interruptions. Such interruptions are typically limited, but customers must actually interrupt service during such interruptions. By contrast, economic interruptions are likely more numerous (First Energy proposes up to 1000 hours), but the customer has greater advance notice and may exercise buy-through rights.

There is no reason to require a customer to provide both reliability and economic interruptions. Separate programs are a better approach.

b. The ORLP should establish different notice periods for reliability interruptions with larger credits for less notice

In the reliability program, FirstEnergy should establish at least three notice options. The first option should be instantaneous interruption. Under this approach, customers that sign up would give FirstEnergy the right to directly interrupt service (FirstEnergy would control the switch) with no notice in the event of reliability issues. This would be the most valuable to the utility since it gives the most flexibility and should carry the highest credit. A second option would be a 10 minute notice service such as proposed by FirstEnergy in its ORLP. This would allow FirstEnergy to use the load as spinning reserves. A third option for a longer notice period, 30 minutes or an hour, should also be offered. This option would allow customers that cannot respond to 10 minutes notice the ability to also participate in the program and at least provide long-run capacity cost avoidance.

c. The ORLP should establish different levels of potential hours of economic interruptions as customer options

In the economic interruption program, a customer should have the option to be subject to Economic Buy Through Events for fewer than 1000 hours. 1000 hours is 11% of the total available hours in a year and about 25% of on peak hours. While some customers might be willing to expose themselves to this level of interruption, many industrial customers will be unwilling to participate in the program knowing that they could be required to curtail their operations or be subject to Midwest ISO LMPs during 25% of the on peak hours in the year. FirstEnergy could offer several different levels of participation in the economic program – for example, customers could be given the option to sign up for 1000, 750, 500, or 250 hours of possible Economic Buy Through Events. At a minimum, the value of the credit should reflect

for each level the estimated avoided energy cost (e.g., the estimated LMPs) for the number of hours of permitted interruptions.

d. Improved program options and flexibility will enhance customer participation in and both customer and system benefits from the ORLP

An OLRP with the level of flexibility and variability built in as recommended above might be more complicated to manage than the OLRP as currently proposed, but the benefits would outweigh the costs. Giving customers more options will allow them to choose an option that will work for their businesses, which in turn should increase the level of participation in the OLRP and make it more likely that customers will stay in the program over the long term. Finally, a program with more variability, instead of "one size fits all," would provide FirstEnergy with a more diverse portfolio of interruptible resources, which in turn would allow FirstEnergy and suppliers to use those resources more efficiently. Rather than asking all customers in the OLRP to interrupt any time load response is needed, FirstEnergy could call on only those customers participating in the program options that match up with FirstEnergy's actual needs at the time. For example, if FirstEnergy needs to utilize its spinning reserve, it could interrupt only the customers in the reliability program on the 10-minute-notice option, rather than having to curtail everyone in the program.

2. The Commission Should Set A Robust Interruptible Program Credit in This Proceeding to Reflect Long-term Avoided Generation and Transmission Capacity Cost, as well as Avoided Energy Costs.

Whether a single Program Credit or multiple credits are included in the OLRP, the credits should be established in this proceeding at the same time the Commission is considering other proposed program parameters. Without knowing what the credit will be, it is impossible to assess the reasonableness of the remaining proposed components of the program. Customers

must know what the credit will be before deciding whether to participate in the program, notwithstanding any other elements of the program that are at issue in this proceeding. A customer may be satisfied with all the parameters of the program as described in FirstEnergy's application, but its decision on whether to participate in the program will hinge on whether the credit makes it worth the customer's while to commit to interrupt its operations. Given all of the uncertainties faced by manufacturers as to future electric supply in Ohio, and the effect of these uncertainties on both planning and operations decisions, it is critical that uncertainty be removed wherever possible. The uncertainty regarding the long-term availability of an adequate interruptible program can and should be addressed now.

By the same token, suppliers that wish to participate in the auctions also must have some idea of what the credit will be because they must have a reasonable estimate of how much load will participate in the program before they structure their bids. For example, if the Program Credit is approximately the same as the credit customers on interruptible tariffs currently receive, suppliers could reasonably count on a similar level of participation in the load response program as there currently is in the existing interruptible programs. But if no one knows what the credit will be, it will be impossible for suppliers to calculate reasonable estimates of expected participation in the load response program.

FirstEnergy states that it must wait until 2008 to establish the Program Credit, due to the "continuing evolution of the electric industry in general and the MISO market in particular." Application, Exhibit E at 1. This is not a valid reason to wait to establish the credit. The evolution of the electric industry and the Midwest ISO market will not grind to a halt in 2008, and there will be just as much uncertainty with regard to the markets then as there is now. FirstEnergy can certainly calculate a Program Credit based on what it knows about the markets

now and what FirstEnergy anticipates will happen in the markets in the coming years, in addition to taking into account the same factors used to calculate the credit in FirstEnergy's existing interruptible rates. Once the Program Credit is established, FirstEnergy can request the Commission to adjust the credit over time on a going forward basis if changes in the markets, such as the addition of a capacity market in Midwest ISO, substantially affect the long-term value of interruptibility. Moreover, the principal value of interruptible load is the avoidance of long-run capacity costs. Those costs generally do not vary so significantly as to justify waiting for more market information.

As noted, any credit for reliability interruptions should reflect at least long run avoided generation and transmission costs, along with any operating reserve savings, since reliability interruptions can be called to respond to any threat to system reliability, whether it is the unavailability of generation or transmission. Generation and transmission capacity costs should be avoided for these customers since they will be interruptible whenever capacity is short and such capacity should not be acquired for them. As Professor James C. Bonbright, perhaps the most recognized authority on utility rate design, has observed:

> Interruptible service has been used by both gas and electric companies for peak shaving. The costs cannot be accurately determined because it is a byproduct resulting from generating and bulk transmission facilities built and operated for firm service. As a result, only the customer cost (e.g., customer-connected spur lines and substations) and energy costs (e.g, fuel and incremental maintenance cost) actually incurred and ***no capacity pricing cost should be included in pricing interruptible service***.

James C. Bonbright, Albert L. Danielsen, and David R. Kamerschen, *Principles of Public Utility Rates* at 502, Arlington, Virginia: Public Utilities Reports, Inc. (1988) (citations omitted; emphasis added). For purposes of comparison, the U.S. Department of Energy has estimated typical avoided generation costs alone for interruptible load to be on the order of $75/kilowatt-

year or more than $6/kW per month. *DOE Demand Response Report* at 74. The Department of Energy further observed that "[t]ransmission and distribution system capacity investments are also capital-intensive, and demand response that reduces local maximum demand in areas nearing infrastructure capacity can provide significant avoided cost savings." *Id.* at 75.

Any interruptible/curtailable program that permits economic interruptions should offer a credit that also reflects a reasonable estimate of avoided energy costs. If the Commission decides to establish only a single Program Credit, with both capacity and economic interruptions, then the credit should reflect all of these elements, including capacity and energy cost savings.

At minimum, the Program Credit should be no lower than the current interruptible credit levels included in FirstEnergy rates. This would have several benefits. First, it will provide a level of certainty and continuity for current interruptible customers, which makes it more likely that existing interruptible customers will participate in the OLRP. Second, as noted above, suppliers may assume that if the Program Credit is at least as large as the current interruptible credit, the level of participation in the load response program will be somewhat comparable to the current level of interruptible load. Finally, setting the Program Credit at least as high as the present level will demonstrate FirstEnergy's commitment to retaining some level of demand response in the region.

3. The Proposed Penalties for Failure to Interrupt are Excessive.

FirstEnergy proposes that if a customer fails to curtail when directed under an Emergency Curtailment Event, the customer will: (i) be subject to disconnection during the interruption; (ii) have to pay an economic penalty; and (iii) be subject to removal from the OLRP. Application, Exhibit E at 8. Although it is important that customers curtail when they are required to do so,

the multiple penalties FirstEnergy proposes are unnecessary and would deter customers from participation in the program.

A better approach would be to require customers, when they sign up for the program, to select one of two alternative penalties applicable for customers if they fail to curtail service in an emergency: (i) an economic penalty or (ii) a disconnection of the customer's load during the interruption. Customers would be required to select one of these penalties for failure to interrupt and that would be the penalty applied as long as the customer is in the program. If the disconnection option is selected, the customer should be required to pay for the new equipment, if necessary, for the utility to monitor the load and disconnect it during an interruption in the event of non-compliance. Removing a customer from the program should be an extraordinary penalty, to be applied only if a customer demonstrates a pattern of failure to interrupt when instructed or failure to otherwise comply with the requirements of the OLRP.

4. The Commission Should Reject Unnecessary OLRP Restrictions Proposed by FirstEnergy.

a. The 400 MW cap on OLRP participation should be eliminated.

FirstEnergy proposes to limit participation in the OLRP to an aggregate 400 MW for all three operating companies. FirstEnergy provides no explanation for why this cap is necessary. At first glance, it appears that the entire cap could be used up by just a handful of large industrial customers. Even if all current interruptible load will fit under this cap, the cap would unnecessarily limit the potential growth of the program.

Given the unquestioned benefits demand response provides, the Commission should not approve any cap on participation in the load response program unless there is a compelling reason for such a limit. Even if the Commission determines that a cap is necessary, the cap should be raised significantly above the proposed 400 MW level. FirstEnergy's total load in

Ohio is approximately 11,400 MWs, so if the cap was raised to 800 MW, this would represent only 7% of FirstEnergy's Ohio load. Finally, if the Commission agrees that a cap is appropriate, all existing interruptible customers should be grandfathered into the program at their option to ensure that customers that have been providing demand response benefits will not be shut out of the program.

b. There should be no expiration date on the OLRP.

Proposed Rider LRP provides that the OLRP will expire on December 31, 2010. FirstEnergy offers no justification for an expiration date. The benefits of demand response in general and specifically interruptible load are uncontroverted – why establish any termination date for such a necessary program? Having the program expire after two years is unnecessary and unwise and again creates great uncertainty for large manufacturing operations in Ohio. Customers that wish to participate in the OLRP might have to add new equipment or make major changes to their production processes. Additionally, these customers will have to build OLRP participation into their business plans for the coming years. These customers might very well be unwilling to make these efforts to participate in a program that terminates after just two years. In short, customers need to know that the OLRP will be permanent and stable before they commit to participate in the program. By contrast, it should be noted that FirstEnergy proposes supply bids extending for up to 41 months – this is inconsistent with limiting the interruptible program to 24 months and virtually assures higher bids from suppliers. Accordingly, the expiration date should be removed. If FirstEnergy wishes to terminate or modify the program at some point in the future, FirstEnergy can make a filing at the Commission seeking to do so and allow all affected customers to address the issues at that time.

c. There should be no restriction on OLRP customers participating in other demand response programs.

Rider LRP prohibits a customer in the OLRP from participating in other load response programs, including the Midwest ISO demand response programs. FirstEnergy provides no justification for this prohibition. Customers should be allowed to participate in any other demand response program so long as that participation does not preclude the customer from meeting its responsibilities under the FirstEnergy OLRP. Accordingly, this prohibition should be removed.

d. The OLRP should not be limited to customers taking SSO generation service under Rider GEN from FirstEnergy.

Rider LRP is limited to customers taking generation service from FirstEnergy under Rider GEN. This restriction should be removed, because the OLRP can provide benefits even if the customer takes generation service from someone other than FirstEnergy or if the customer takes service under the Hourly Priced Generation Service Program (Rider HPS). As noted above, competitive suppliers in states with retail competition have little incentive to offer an interruptible rate. Opening the OLRP to all customers, therefore, may be the only way a customer taking service from a competitive supplier will have access to an interruptible rate. Similarly, a customer that chooses FirstEnergy's hourly priced program should also have the option to become interruptible.

At minimum, the Commission should recognize that the reliability benefit interruptible load provides is the same regardless of who the generation supplier is or which supply is being utilized. FirstEnergy notes that an Emergency Curtailment Event occurs when "an electrical system emergency that exists may jeopardize either the transmission or distribution systems in the area." Application, Exhibit E at 1. A customer taking generation supply from someone other

than FirstEnergy (or under the Hourly Priced Generation Service Program) still uses the FirstEnergy transmission and distribution system, and will provide the same reliability benefit by curtailing its load during emergency events as a customer taking generation service from FirstEnergy.

All customers, regardless of how they take generation service, therefore, should at least be eligible to participate in the OLRP for Emergency Curtailment Events. This is another example of why offering separate reliability and economic programs, as proposed above, makes sense. A customer taking generation supply from a competitive supplier might be an ideal candidate for participation in the reliability program only.

5. All Demand and Performance Measurements Under the OLRP Should be Determined Consistently.

a. Monthly peak demand, not average demand from summer on-peak times, should be used in calculating a customer's curtailable load.

FirstEnergy proposes to calculate curtailable load by subtracting the customer's contractual firm load from its Average Hourly Demand. Application, Exhibit E at 2. Average Hourly Demand is calculated by calculating the customer's average load during certain on-peak hours from June through August, excluding July 4. *Id.* The Average Hourly Demand also includes hours of economic curtailment (although it excludes hours of emergency curtailment), thereby making the situation worse by lowering the curtailable load subject to the credit even further if the customer responds to the economic curtailment rather than buying through the curtailment. *Id.* at 7.

Calculating a customer's curtailable load by looking at the customer's <u>average</u> demand is not the best approach to calculate curtailable load, and could significantly under-compensate customers participating in the OLRP. Similarly, limiting curtailable demand measurements to

certain hours during the period June through August, ignores the fact that the customer is curtailable all 8760 hours of the year. Finally, including economic curtailment hours in the calculation further dilutes the credit and sends the incorrect signal that customers should buy-through rather than curtail when possible. Curtailable load should be calculated by subtracting the customer's firm load from its peak demand each month.

An interruptible customer provides a benefit to the system by removing the customer's peak demand, not average demand, from the system. For example, while a customer could have a peak demand during a particular month of 50 MW, its average hourly demand for the months June through August could be a lot less (say 35 MW). Under FirstEnergy's current proposal, if the customer had 15 MW of firm demand, the customer would be compensated for only 20 MW of load reduction (35 MW – 15 MW). But in actuality, the customer is providing 35 MW worth of benefit (50 MW – 15 MW) because FirstEnergy is avoiding having to serve the customer's peak demand, not just the customer's average demand.

The proper way to measure a customer's curtailable load, therefore, is to subtract the customer's firm load from its monthly peak demand.

b. The demand measurement period for measuring a customer's performance should be consistent with the measurement period used to calculate the customer's curtailable load.

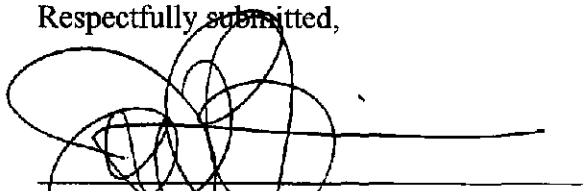
FirstEnergy proposes to calculate curtailable load for purposes of the Program Credit on an hourly basis. However, FirstEnergy proposes to measure a customer's performance in an Emergency Curtailment Event on a half-hour basis. Measuring a customer's curtailable load on an hourly basis, but measuring the customer's performance on a half-hour basis creates a mismatch. This mismatch results in under-compensating customers for their interruptibility. FirstEnergy should use consistent time periods to measure a customer's curtailable load and the

customer's performance in an Emergency Curtailment Event. The demand to which a customer's load is reduced should be the same hourly demand measurement used for determining the curtailable demand. In the alternative, FirstEnergy could use 30-minute peak demands for determining both the curtailable period and the customer's performance.

III. CONCLUSION

In summary, Nucor Marion urges the Commission to consider the comments and recommendations set forth above in evaluating FirstEnergy's SSO proposal.

Respectfully submitted,



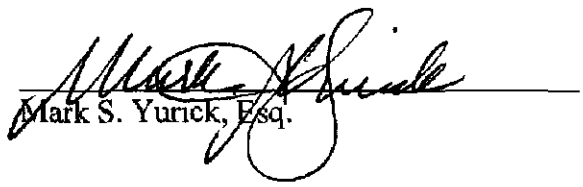
John W. Bentine, Esq. (0016388)
Counsel of Record
E-Mail: jbentine@cwslaw.com
Mark S. Yurick, Esq. (0039176)
Direct Dial: (614) 334-7197
Email: myurick@cwslaw.com
Direct Dial: (614) 334-6121
Chester, Willcox & Saxbe LLP
65 East State Street, Suite 1000
Columbus, Ohio 43215-4213
(614) 221-4000 (Main Number)
(614) 221-4012 (facsimile)

Garrett A. Stone*
Michael K. Lavanga*
E-Mail: gas@bbrslaw.com
E-Mail: mkl@bbrslaw.com
Brickfield, Burchette, Ritts & Stone, P.C.
1025 Thomas Jefferson Street, N.W.
8th Floor, West Tower
Washington, D.C. 20007
(202) 342-0800 (Main Number)
(202) 342-0800 (Facsimile)
* Pending admission *pro hac vice*

Attorneys for Nucor Steel Marion, Inc.

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing pleading was served upon the following parties of record or as a courtesy, via U.S. Mail postage prepaid, express mail, hand delivery, or electronic transmission on September 5, 2007.



Mark S. Yurick, Esq.

SERVICE LIST

Joseph Allotta
Allotta and Fraley Co., LPA
2222 Centennial Rd.
Toledo, OH 43617

David Applebaum
FPL Energy Power Marketing, Inc.
21 Pardee Place
Ewing, NJ 08628

David Boehm
Boehm, Kurtz & Lowry
36 E. Seventh St., Suite 1510
Cincinnati, OH 45202-4454

Carl Boyd
Strategic Energy LLC
Two Gateway Center
Pittsburgh, PA 15222

Sean Boyle
FPL Energy Power Marketing, Inc.
700 Universe Boulevard
Juno Beach, FL 33408

Peter Brickfield
Vallourec & Mannesmann Tubes Corp.
1025 Thomas Jefferson St. NW, Suite 800
Washington, DC 20007

Kerry Bruce
City of Toledo
420 Madison Ave., 4th Fl.
Toledo, OH 43604

James Burk
FirstEnergy Service Co.
76 S. Main St.
Akron, OH 44308

Eric Burkland
Ohio Manufacturers Assn.
33 N. High St.
Columbus, OH 43215

Mayor Bill Cervenik
City of Euclid
585 East 22nd St.
Euclid, OH 44123

Dave Childers
IBEW 1194
17 W. Church St.
P.O. Box 145
Milan, OH 44846

Joseph Clark
McNees Wallace & Nurick, LLC
21 E. State St., 17th Fl.
Columbus, OH 43215

John Comoll
Direct Energy Services LLC
1111 W. 22nd St., Suite 810
Oakbrook, IL 60523

Joseph Condo
Calpine Corp.
250 Parkway Dr., Suite 380
Lincolnshire, IL 60069

Kevin Corcoran
Bob Schmitt Homes, Inc.
8501 Woodbridge Ct.
North Ridgeville, OH 44039

Dolores Davis
42 Orchard St.
Newton Falls, OH 44444

Trent Dougherty
Ohio Environmental Council
1207 Grandview Ave.
Columbus, OH 43212-3449

Henry Eckhart
50 W. Broad St., #2117
Columbus, OH 43215

Stephen Feld
FirstEnergy Corp.
76 S. Main St.
Akron, OH 44308

John Foreman
FPL Energy Power Marketing, Inc.
2 Ashleaf Court
Hockessin, DE 19707

Rev. Mike Frank
Neighborhood Environmental Coalition
5920 Engle Ave.
Cleveland, OH 44127

Mark Frye
City of Perrysburg
300 Sycamore Ln.
Perrysburg, OH 43551

Mark Frye
Palmer Energy
2455 N. Reynolds Rd.
Toledo, OH 43615

Todd Geletka
Ohio Home Builders Assn.
17 S. High St., Suite 700
Columbus, OH 43215

Denis George
The Kroger Co.
1014 Vine St., G07
Cincinnati, OH 45202

Rick Giannantonio
FirstEnergy Service Co.
76 S. Main St.
Akron, OH 4308

John Gibbon
City of Cleveland Heights
1301 E. 9th St., Suite 3500
Cleveland, OH 44114

Paul Goldberg
Counsel for City of Oregon
5300 Seaman Rd.
Oregon, OH 43616

Craig Goodman
National Energy Marketers Assn.
3333 K. St. NW, Suite 110
Washington, DC

Freddi Greenberg
1603 Orrington Ave., Suite 1050
Evanston, IL 60201

William Gruber
2714 Leighton Rd.
Shaker Heights, OH 44120

Peter Gwyn
City of Perrysburg
300 Sycamore Ln.
Perrysburg, OH 43551

Stephen Hadick
76 S. Main St., 8th Fl.
Akron, OH 44308

Joseph Haefner
City of Stow
3760 Darrow Rd.
Stow, OH 44224

Barbara Hawbaker
MidAmerican Energy Co.
4299 NW Urbandale Dr.
Urbandale, IA 50322

Mark Hayden
FirstEnergy Service Co.
76 S. Main St.
Akron, OH 44308

Thomas Hays
Lake Township Trustees
3315 Centennial Rd., Suite A2
Sylvania, OH 43560

Robert Heydorn
Hoover, Heydorn & Herrnstein
527 Portage Trail
Cuyahoga Falls, OH 44221

Ann Hotz
Office of Consumers Counsel
10 W. Broad St., Suite 1800
Columbus, OH 43215

Stephen Howard
Vorys Sater Seymour and Pease LLP
52 E. Gay St.
P.O. Box 1008
Columbus, OH 43216

David Hughes
4037 Ludwick
Pittsburgh, PA 15217

Stephen Huntoon
FPL Energy Power Marketing, Inc
801 Pennsylvania Avenue, NW, Suite 220
Washington, DC 20004

Gary Jeffiries
Dominion Retail, Inc.
501 Martindale St. Suite 400
Pittsburgh, PA 15212

Patrick Kealy
Calpine Corp.
717 Texas St.
Houston, TX 77002

Lance Keiffer
711 Adams St., 2nd Fl.
Toledo, OH 43624

Dano Koehler
City of Stow
3760 Darrow Rd.
Stow, OH 44224

Kathy Kolich
FirstEnergy Corp.
76 S. Main St.
Akron, OH 44308

Leslie Kovacik
City of Toledo
420 Madison Ave., 4th Fl.
Toledo, OH 43604

Glenn Krassen
Northeast Ohio Public Energy Council
Bricker & Eckler LLP
1375 E. Ninth St., Suite 1500
Cleveland, OH 44114-1718

Michael Kurtz
Boehm, Kurtz & Lowry
36 E. Seventh St., Suite 1510
Cincinnati, OH 45202

Chantale LaCasse
NERA Economic Consulting
1166 Avenue of the Americas
New York, NY 10036

Franklin Lewis
City of Cleveland
601 Lakeside Ave., Room 106
Cleveland, OH 44114

Helen Liebman
Jones Day
P.O. Box 165017
Columbus, OH 43216-5017

Sheilah McAdams
City of Maumee
400 Conant St.
Maumee, OH 43537

Joseph Meissner
Citizens Coalition
1223 W. Sixth St.
Cleveland, OH 44113

Kent Meyers
St. Charles Hospital
2600 Navarre Ave.
Oregon, OH 43616

Steven Millard
200 Tower City Center
50 Public Square
Cleveland, OH 44113

James Moan
City of Sylvania
4930 Holland-Sylvania Rd.
Sylvania, OH 43560

Colleen Mooney
Ohio Partners for Affordable Energy
231 W. Lima St.
P.O. Box 1793
Findlay, OH 45839

Nolan Moser
Ohio Environmental Council
1207 Grandview Ave.
Columbus, OH 43212-3449

William Newcomb
Reliant Resources, Inc.
Vorys Sater Seymour and Pease LLP
52 E. Gay St.
Columbus, OH 43216

Steven Nourse
American Electric Power
1 Riverside Plaza, 29th Floor
Columbus, OH 43215

Thomas O'Brien
Bricker & Eckler, LLP
100 South Third St.
Columbus, OH 43215

M. Howard Petricoff
Vorys Sater Seymour and Pease LLP
52 E. Gay St.
P.O. Box 1008
Columbus, OH 43216

Samuel Randazzo
Industrial Energy Users - Ohio
McNees Wallace & Nurick
21 E. State St., 17th Fl.
Columbus, OH 43215

Marvin Resnik
American Electric Power
1 Riverside Plaza, 29th Floor
Columbus, OH 43215

David Rinebolt
Ohio Partners for Affordable Energy
231 W. Lima St.
P.O. Box 1793
Findlay, OH 45839

Teresa Ringenhach
Integrys Energy Services
600 Superior Ave., Suite 1300
Cleveland, OH 44114

Evelyn Robinson
Green Mountain Energy Co.
1721 Leighton Dr.
Reynoldsburg, OH 43068

Barth Royer
Bell, Royer & Sanders Co., LPA
33 S. Grant Ave.
Columbus, OH 43215

Paul Ruxin
Jones Day Reavis & Pogue
901 Lakeside Ave.
Cleveland, OH 44114

Judith Sanders
Bell, Royer & Sanders Co., LPA
33 S. Grant Ave.
Columbus, OH 43215

Thomas Scully
3430 Randall Dr.
Cleveland, OH 44120

Richard Sites
Ohio Hospital Association
155 E. Broad St., 15th Fl.
Columbus, OH 43215

Paul Skaff
Village of Holland
353 Elm St.
Perrysburg, OH 43551

Jeffrey Small
Ohio Consumer's Counsel
10 W. Broad St., Suite 1800
Columbus, OH 43215

Michael Smalz
Ohio State Legal Services Assn.
555 Buttles Ave.
Columbus, OH 43215

Craig Smith
2824 Coventry Rd.
Cleveland, OH 44120

Dane Stinson
Bailey Cavalieri LLC
10 W. Broad St., Suite 2100
Columbus, OH 43215

Robert Triozzi
City Hall
601 Lakeside Ave., Room 106
Cleveland, OH 44114

Larry Tscherne
IBEW 245
705 Lime City Rd.
Rossford, OH 43460

Daniel Verbanac
Integrys Energy Services
1716 Lawrence Dr.
De Pere, WI 54115

Harvey Wagner
Cleveland Electric Illuminating Co.
76 S. Main St.
Akron, OH 44308

Harvey Wagner
Toledo Edison Co.
76 S. Main St.
Akron, OH 44308

Shari Weir
One Citizen Action
614 W. Superior Ave., Suite 1200
Cleveland, OH 44113

William Zigli
City of Cleveland
601 Lakeside Ave., Room 106
Cleveland, OH 44114

Empowerment Center of Greater
3030 Euclid Ave., Unit 100
Cleveland, OH 44115

Northeast Ohio Public Energy Council
583 East Aurora Rd.
Macedonia, OH 44056

Northwest Ohio Aggregation Coalition
One Government Center, Suite 2250
Toledo, OH 43604

PSEG Energy Resources & Trade LLC
80 Park Plaza, 19th Fl.
Newark, NJ 07102

Phyllis Vento
City of Euclid
585 E. 222nd St.
Euclid, OH 44123

Leila Vespoli
FirstEnergy Corp.
76 S. Main St.
Akron, OH 44308

Harvey Wagner
Ohio Edison Co.
76 S. Main St.
Akron, OH 44308

Tim Walters
Consumers for Fair Utility Rates
4115 Bridge Ave.
Cleveland, OH 44113

Sandra Williams
Columbus Southern Power
1 Riverside Plaza, 29th Floor
Columbus, OH 43215

Cleveland Housing Network
2999 Payne Ave.
Cleveland, OH 44114

Ohio Manufactured Housing Assn.
201 Bradenton Ave., Suite 100
Dublin, OH 43017

Cargill, Inc.
P.O. Box 336
Mentone, IN 46539

Ohio Power Co.
1 Riverside Plaza, 29th Floor
Columbus, OH 43215