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BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

IN THE MATTER OF THE APPLICATION)
OF THE CLEVELAND BOARD OF)
EDUCATION FOR THE CLEVELAND)
MUNICIPAL SCHOOL DISTRICT TO) CASE NO. 08-1238-EL-AEC
ESTABLISH A REASONABLE)
ARRANGEMENT WITH THE)
CLEVELAND ELECTRIC ILLUMINATING) PUBLIC VERSION
COMPANY FOR ELECTRICAL SERVICE)
)

DIRECT TESTIMONY OF
MARK R. FRYE OF PALMER ENERGY

ON BEHALF OF
THE CLEVELAND MUNICIPAL SCHOOL DISTRICT

April 30, 2009

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1 DIRECT TESTIMONY OF MARK R. FRYE

2
3 I. INTRODUCTION AND QUALIFICATIONS

4 **Q. Please state your name and business address.**

5 A. My name is Mark Frye. My business address is 241 N. Superior Street,
6 Toledo, Ohio 43604.

7 **Q. What is your occupation?**

8 A. I am an energy consultant and the President of Palmer Energy Company in
9 Toledo, Ohio.

10 **Q. Please describe your educational background and work experience.**

11 A. I have worked in the energy field for 22 years and for clients in 18 states. I
12 earned a Bachelors of Science degree in Energy Technology from
13 Pennsylvania State University's Capitol College. I currently consult on
14 energy procurement and utilization matters for a number of industrial,
15 commercial, educational, institutional and governmental clients.

16 **Q. Have you ever testified before the Public Utilities Commission of Ohio?**

17 A. Yes. I have previously submitted direct testimony in several cases before the
18 Public Utilities Commission of Ohio ("Commission" or "PUCO"), including
19 FirstEnergy's Electric Security Plan ("ESP") Application [Case No. 08-935-
20 EL-SSO], FirstEnergy's Rate Stabilization Plan ("RSP") Application [Case
21 No.03-2144-EL-ATA], American Electric Power's ESP Application [Case
22 No. 08-917-EL-SSO], American Electric Power's IGCC Application [Case
23 No.05-376-EL-ATA], and Dayton Power & Light's ESP Application [Case
24 No. 08-1094-EL-SSO].

1 **Q. On whose behalf are you testifying in this proceeding?**

2 **A. I am testifying on behalf of the Cleveland Municipal School District**
3 **("CMSD") in support of the Second Amended Reasonable Arrangement**
4 **Application filed by CMSD in this case.**

5 **II. ELECTRIC SERVICE AGREEMENT HISTORY**

6 **Q. Are you familiar with the 2002 Electric Service Agreement ("2002 ESA")**
7 **agreed to between the CMSD and Cleveland Electric Illuminating**
8 **Company ("CEI")?**

9 **A. Yes, I am. The 2002 ESA was a negotiated electric pricing agreement**
10 **between CEI and CMSD that provided pricing outside the typical tariff rates.**
11 **The average price paid by CMSD was about ** [REDACTED] ** per kWh and**
12 **included generation, transmission, distribution charges, and taxes. A copy of**
13 **the 2002 ESA was filed under seal in conjunction with CMSD's original**
14 **application in this case.**

15 **Q. When was the 2002 ESA set to expire?**

16 **A. The agreement, which had been extended in 2005, was set to expire December**
17 **31, 2008.**

18 **Q. Prior to December 31, 2008, did you attempt to reach out to CEI on**
19 **behalf of the CMSD to negotiate a new electric service agreement?**

20 **A. Yes. Beginning in the autumn of 2007 I tried to engage CEI in contract**
21 **negotiations, but was unsuccessful.**

22 **Q. Were you present at a meeting in Akron, Ohio on January 23, 2009,**
23 **wherein representatives of CMSD and CEI negotiated a new Electric**
24 **Service Agreement ("New ESA")?**

1 A. Yes. I was present and participated in the discussions at that meeting.

2 **Q. What happened at that meeting?**

3 A. It was agreed that CMSD and CEI would extend the basic rate structure of the
4 2002 ESA with gradual increases over the ensuing three-year period.

5 Specifically, the basic rate structure would be increased by ****[REDACTED]****

6 effective May 1, 2009, ****[REDACTED]**** effective January 1, 2010, and ****[REDACTED]****

7 effective January 1, 2011. It was unequivocally expressed to CEI that the

8 CMSD's overall electricity costs needed to increase gradually so they could

9 be absorbed within CMSD's budget. A copy of the New ESA was filed under

10 seal as a part of CMSD's amended application in this case seeking approval of

11 the New ESA as a reasonable arrangement.

12 **Q. Is CMSD requesting PUCO approval of the New ESA?**

13 A. No. Subsequent to the filing of Amended Reasonable Arrangement

14 Application, the PUCO issued its Second Opinion and Order in FirstEnergy's

15 ESP case. That order approved a pricing structure different from that assumed

16 by CMSD and CEI in negotiating the New ESA. In addition, the PUCO Staff

17 ("Staff") filed comments in this docket raising concerns about the proposed

18 arrangement. In an effort to address Staff objections and create a pricing

19 mechanism more consistent with the mechanism applicable to other school

20 districts, CEI and CMSD negotiated a reasonable arrangement containing a

21 different pricing structure. The resulting arrangement is the arrangement

22 CMSD is now asking the PUCO to approve.

1 III. PRICING STRUCTURE

2 **Q. How is the pricing structured under this arrangement?**

3 A. Rather than providing for increases above CMSD's old rates, the proposed
4 reasonable arrangement has declining percentage reductions from CEI's base
5 rates over a 29-month term. The reduction from the distribution, generation,
6 and transmission rates for January through June 2009 is **[REDACTED]** from
7 July 2009 through June 2010, and **[REDACTED]** from July 2010 through May 31,
8 2011.

9 **Q. What is the expected cost CMSD will pay during the term of the proposed**
10 **arrangement and how does it compare to the costs incurred by CMSD in**
11 **2008 under the 2002 ESA?**

12 A. During the first five months of 2009, based upon the FirstEnergy ("FE")
13 distribution case (Case No. 07-551-EL-ATA), the recent Second Opinion and
14 Order in the FE ESP case, and the FE Rider FUEL case (Case No. 09-0021-
15 EL-ATA), I estimate CMSD costs would be in excess of **[REDACTED]** per
16 month higher than under the reasonable arrangement CMSD is now
17 proposing. The proposed arrangement will still increase CMSD electric costs
18 in excess of **[REDACTED]**, or approximately **[REDACTED]**, in 2009 compared to
19 2008. That is similar to the increase that other districts will experience in
20 2009 compared to 2008. Starting in June, CMSD prices will be driven by the
21 result of the auction and any decision by the Commission regarding phase-in
22 of those prices. However, if the auction price is 6.0 cents per kWh, and the
23 Commission does not authorize phase-in of the price, CMSD's 2009 cost
24 would be approximately \$2.1 million higher than its 2008 cost if the proposed

1 arrangement is rejected and CMSD is served under the school rate approved
2 as a part of FE's ESP. Over the entire 29-month term of the proposed
3 arrangement, CMSD's estimated power cost would be **[REDACTED]**, or
4 **[REDACTED]** cents per kWh. This is approximately **[REDACTED]** cent per kWh higher
5 than CMSD paid in 2008.

6 IV. CMSD IS UNIQUE

7 **Q. In its comments, Staff expressed the view that CMSD is not in a unique**
8 **situation. Do you agree?**

9 **A.** No. CMSD is unique among the school districts served by the FE operating
10 companies. According to the Ohio Department of Education website, in FY08,
11 CMSD's enrollment exceeded 50,000 students. It operates approximately 120
12 schools and ancillary buildings and spends approximately \$6 million on its
13 electric bills. The next two largest school districts in FE's territory, Toledo
14 and Akron, have student populations that are approximately 50% the size of
15 CMSD. Parma, which appears to be have the next largest student population,
16 has only about 25% of the number of students of CMSD. Numerous other
17 districts have student populations below 9,000. Thus, it is likely that one
18 would have to combine at least the next three largest school districts, and
19 perhaps as many as the next 10 largest, to reach the annual increase of \$2.4
20 million CMSD would experience if its proposed arrangement is not approved.

21 **Q. Does the 2002 ESA contribute to the unique situation in which CMSD**
22 **now finds itself?**

23 **A.** Yes. It is my understanding that, from the period of 2002 to 2008, CMSD was
24 the only FE-served school district served under such an agreement. Virtually

1 all other school districts served by FE were served under the "Energy for
2 Education II" ("E4E2") program through the Ohio Schools Council ("OSC").

3 **Q. Please describe your understanding of the OSC E4E2 program.**

4 A. E4E2 was a follow-up program to the initial Energy for Education program
5 that expired at the end of 2005. The original program provided a 10%
6 discount on non-fuel revenue or between 8.5% and 9% below the tariff
7 schedules. E4E2 continued the previous discount for another three years, but
8 also added a prepayment discount of approximately 5%.

9 **Q. How many school districts participate in the E4E2 program?**

10 A. According to the OSC's motion to intervene in FE's distribution case, the
11 E4E2 program served 238 public school districts and 11 MR/DD Boards.
12 Only four Ohio public school districts served by FE are not participating in
13 E4E2 program. While I do not know the identity of the other three districts
14 not participating in E4E2, OSC personnel indicated to me during past
15 conversations that all the major urban public school districts served by FE
16 participated in the program except CMSD.

17 **Q. Are school districts that participated in E4E2 program seeing increases in**
18 **their electric costs?**

19 A. School districts participating in E4E2 were paying 13.5% less than tariff in
20 FY07 according to the OSC website. Since the E4E2 program continued
21 through 2008 it is logical to conclude that despite the Commission-ordered
22 8.693% distribution discount for schools, most districts have likely seen
23 increases since the expiration of the E4E2 program.

1 **Q. How does that compare to the cost increase CMSD will experience if this**
2 **arrangement is not approved?**

3 **A. Had CMSD paid tariff pricing in 2008, it would have paid approximately 49%**
4 **or \$2.8 million above its actual charges. Through May 2009, if the**
5 **arrangement is not approved, the increase would be the difference between the**
6 **school discount and the CMSD proposed arrangement, or approximately 40%.**
7 **Despite the increases for other schools, the total monetary impact on CMSD is**
8 **certainly greater than the dollar impact on other schools, and the percentage**
9 **impact is would also be greater, unless the other district had exclusively**
10 **electrically-heated facilities.**

11 **Q. Please summarize why you consider CMSD unique compared to other**
12 **school districts.**

13 **A. In the FE's Ohio service territory, CMSD serves more children and consumes**
14 **more electricity than any other FE public school district. It has historically**
15 **paid less for electricity than other school districts and, thus, would be forced**
16 **to accept a much greater burden than other schools, both in terms of the total**
17 **cost increase and on a percentage basis, if the proposed arrangement is not**
18 **approved by the Commission. The proposed CMSD arrangement also**
19 **provides for substantial cost increases during 2010 and 2011, moving it much**
20 **closer to the costs paid by other schools.**

21 **V. REASONABLE ARRANGEMENT PROVISIONS**

22 **Q. In its comments, Staff also asserted that the reasonable arrangement**
23 **proposed in the Amended Application filed by CMSD on January 27,**
24 **2009 fell short of the requirements of R.C. 4905.31. Do you agree?**

1 A. No. I believe that arrangement qualified as a reasonable arrangement under a
2 number of paragraphs in R.C. 4905.31 and, contrary to Staff's assertions,
3 created value for CEI, other ratepayers, and the state. Although the
4 arrangement now being proposed contains a different pricing structure, the
5 terms that I will identify as providing a benefit to CEI, other ratepayers, and
6 the state have not changed.

7 **Q. Why should the Commission find that the arrangement now being**
8 **proposed meets the requirements of R.C. 4905.31?**

9 A. Although I am not an attorney, based on my reading of the statute, the
10 proposed arrangement would clearly qualify under paragraphs D and E of
11 R.C. 4905.31.

12 **Q. How would the proposed reasonable arrangement qualify under**
13 **paragraph D of R.C. 4905.31?**

14 A. Paragraph D of R.C. 4905.31 states "A classification of services based upon
15 the quantity used, the time when used, the purpose for which used, the
16 duration of use, and any other reasonable consideration." Although I believe
17 the sheer quantity of electricity used by CMSD, which is larger than that used
18 by any other public school district FE territory, brings the arrangement under
19 this paragraph, the arrangement also qualifies under the "any other reasonable
20 consideration" provision as well. CMSD had an electric service agreement
21 that governed the price it paid for electric service for the seven years that
22 ended December 31, 2008. It is my understanding that CMSD was the only
23 public school district FE had such an arrangement with during this term.
24 CMSD's contract was unique. The fact that that coming off this arrangement

1 will subject CMSD to a substantially greater increase than other school
2 districts will experience is a "reasonable consideration" in my judgment.

3 **Q. How does CMSD's reasonable arrangement qualify under paragraph E**
4 **of R.C. 4905.31?**

5 A. The arrangement also qualifies under Section E as "As any other financial
6 device that may be practicable or advantageous to the parties interested." The
7 Staff focused on determining if the arrangement was advantageous to the
8 parties interested. Although, as I will explain, the arrangement is
9 advantageous to the parties interested, it also qualifies in that it is
10 "practicable." For an arrangement to be practicable it should be workable,
11 feasible, or capable of being put into practice. FE is clearly capable of
12 invoicing a pricing structure of this type. Indeed, FE is required to so for
13 other school districts by Commission order. Thus, invoicing CMSD under a
14 similar pricing mechanism is practicable. Furthermore, FE has the ability to
15 collect the delta revenue of the type created under this agreement from other
16 customers under the PUCO's Second Opinion and Order in the FE ESP case.

17 **Q. Does the proposed arrangement satisfy Staff's interpretation that**
18 **reasonable arrangements under R.C. 4905.31 should provide value to all**
19 **affected parties and the state?**

20 A. Yes. CEI benefits from CMSD's agreement to make CEI its exclusive
21 supplier for the facilities listed during the term of this arrangement. CMSD,
22 while certainly not CEI's largest customer, is clearly a very large consumer of
23 electricity. Many CMSD facilities could be served by Cleveland Public
24 Power ("CPP"). This arrangement avoids the potential loss of CMSD

1 facilities' load to CPP. CMSD also has agreed to work towards reducing its
2 demand and energy consumption over the term of this arrangement, and to
3 cooperate fully with CEI by providing such data and other information as CEI
4 may require so as to utilize CMSD's energy savings in achieving compliance
5 with statutory energy savings benchmarks set forth in R.C. 4928.(A)(1)(a). In
6 my judgment, that also provides significant value to CEI.

7 **Q. How does the proposed arrangement have value for ratepayers?**

8 A. To evaluate the value of this arrangement to the ratepayers it is important to
9 consider the cost. This arrangement will provide CMSD power at a cost
10 approximately ** [REDACTED] ** below that which it would pay under the
11 school rate. If spread across CEI's consumption projection in the long term
12 forecast, the delta revenue created by the arrangement would cost a residential
13 consumer using 750 kWh per month less than six cents per month. CEI
14 ratepayers, many of whom live and/or work in Cleveland, help pay the \$196
15 million in property tax collected each year for CMSD. These payments
16 recognize the value CMSD creates through its efforts to fulfill its mission of
17 educating children. In addition, ratepayers also benefit from the value of the
18 arrangement to the community as a whole.

19 **Q. How will the state of Ohio benefit from the proposed arrangement?**

20 A. Obviously, the state of Ohio is not paying for the delta revenue created by the
21 arrangement. However, in FY09, CMSD expects approximately \$430 million
22 in funding from the state. The state legislature and the Governor saw fit to
23 help fund CMSD. Given the financial challenges facing CMSD in the next
24 few years, any reduction in costs helps CMSD in fulfilling its mission of

1 educating children without seeking additional financial assistance from the
2 state to pay the for power costs that it would incur in the absence of the
3 proposed arrangement.

4 **Q. Do you believe this provides long term value?**

5 A. Yes. Helping CMSD fulfill its mission in this fashion serves to reduce the
6 future tax burden on the general public. US Census Bureau income data
7 shows nearly a \$15,000 annual earnings difference between someone who
8 earned a bachelor's degree compared to a high school graduate. Over a 45-
9 year career, that income differential would equate to nearly \$675,000 more. A
10 student who earns a high school diploma compared to dropping out makes
11 nearly \$7,000 more per year, or \$315,000 over their working years. If one
12 additional child loses its way and is incarcerated, it costs Ohio \$35,000
13 annually [Department of Rehabilitation and Correction FY08 expense vs.
14 number of inmates]. Over 45 years, that equals \$1.6 million per child.

15 **Q. Does the proposed arrangement have potential long-term value in terms**
16 **of the impact on future utility rates?**

17 A. It is logical to expect that a reduction in earnings potential not only impacts
18 payment of income and sales tax potential, but also increases the likelihood
19 that consumers will seek other forms of assistance. One form that impacts
20 ratepayers is the Percentage of Income Payment Plan (PIPP). According to
21 the Ohio Department of Development website, CEI consumers currently have
22 a total PIPP arrearage in excess of \$150 million, and Universal Service Fund
23 (USF) collections from CEI consumers will be \$15.4 million in 2009. The

1 PIPP program is also available for eligible consumers who have natural gas
2 heating.

3 **Q. Please summarize your thoughts with respect to the value created for**
4 **affected parties by the proposed arrangement?**

5 A. In my opinion, this arrangement appears to qualify under at least two different
6 paragraphs of R.C. 4905.31 and is reasonable given CMSD's unique position.
7 The arrangement is practicable. FE can bill it under a collection mechanism
8 approved by the PUCO. It provides value for CEI by providing exclusive
9 supplier status and supporting its efforts to meet the statutory energy savings
10 benchmarks. It provides value to ratepayers and the State by helping CMSD
11 fulfill its mission of educating children.

12 **Q. Does this conclude your testimony?**

13 A. Yes. However, I reserve the right to file rebuttal testimony if Staff or any
14 other party files testimony in this case.

CERTIFICATE OF SERVICE

I hereby certify that a true and accurate copy of the foregoing Direct Testimony of Mark R. Frye was served by regular U.S. mail, postage prepaid, and/or delivered via electronic mail, upon the following parties of record, this 30th day of April 2009.

David A. Kutik
Jones Day
North Point, 901 Lakeside Avenue
Cleveland, OH 44114

Ebony Miller
FirstEnergy Service Company
76 South Main Street
Akron, OH 44308

Anne L. Hammerstein
Assistant Attorney General
Public Utilities Section
180 East Broad Street, 9th Floor
Columbus, OH 43215-3793

Respectfully submitted,



Barth E. Royer (016999)
(Counsel of Record)
Bell & Royer Co., LPA
33 South Grant Avenue
Columbus, Ohio 43215-3900
(614) 228-0704 – Phone
(614) 228-0201 – Fax
Email: BarthRoyer@aol.com

Mark J. Valponi (0009527)
Adrian D. Thompson (0036742)
Taft Stettinius & Hollister LLP
200 Public Square, Suite 3500
Cleveland, OH 44114-2302
(216) 706-3873 – Phone
(216) 241-3707 – Fax
E-mail: mvalponi@taftlaw.com
E-mail: athompson@taftlaw.com

Attorneys for the Applicant