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BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Commission's Investigation into the Value of Continued Participation in Regional Transmission Organizations	))))	**Case No. 09-90-EL-COI**

REPLY COMMENTS OF FIRSTENERGY SERVICE COMPANY

Pursuant to the Commission's entry dated June 15, 2009, FirstEnergy Service Company, on behalf of the operating company subsidiaries of FirstEnergy Corp., submits these Reply Comments.[1] FirstEnergy has reviewed the comments submitted by other parties to this proceeding and, after such review, stands by all of the facts, analysis and arguments presented in FirstEnergy's initial Comments in this proceeding. FirstEnergy takes opportunity in these Reply Comments to address comments submitted by the Ohio Consumers Counsel and by IEU-Ohio.

REPLY TO COMMENTS OF THE OHIO CONSUMERS' COUNSEL

The OCC's sole position in this case is that while RTOs serve an important role, they are less focused on ensuring customer value in electricity services.[2] The OCC supports its position by providing a copy of a report written by its consultant, "Synapse Energy Economics, Inc." (Synapse). But the OCC does not adopt any or even parts of the report as an "official" position. As such, it would be reasonable to infer that while the OCC may agree with some of the concepts in the Synapse report, the OCC stops short of full commitment to its consultant's arguments. Since, as demonstrated below, much of the analysis and argument presented in the Synapse

[1] The operating company subsidiaries are: Ohio Edison Company, The Cleveland Electric Illuminating Company, The Toledo Edison Company, Pennsylvania Power Company, American Transmission Systems, Inc., FirstEnergy Solutions Corp. (FirstEnergy Solutions), Pennsylvania Electric Company, Metropolitan Edison Company, and Jersey Central Power & Light Company (collectively, "FirstEnergy").

[2] PUCO Case No. 09-90-EL-COI, *supra*, Comments by the Office of the Ohio Consumers' Counsel, p. 4 (May 26, 2009), *hereinafter* "OCC."

report is flawed, the OCC's conduct is understandable. In any event, the OCC has yet to establish that RTOs lack focus on ensuring customer value, and the Commission should not accept any such assertion in the absence of further factual support.

The OCC's sole recommendation is that certain unspecified changes to RTO structures may be needed to protect Ohio's electric consumers from unjust and unreasonable electric service costs.[3] Since, however, the OCC has not identified any "unjust and unreasonable" RTO practices or costs, this recommendation is in the nature of good common sense; Ohio and its consumers should avoid bad circumstances.[4] Again, the OCC's non-committal suggestion is understandable. The Federal Power Act – which endows FERC with exclusive jurisdiction over RTO rates and terms of service – prohibits "unjust and unreasonable" rates and charges.[5] Consequently, if the record in this proceeding demonstrated that unjust or unreasonable rates or practices exist in one or both of the RTOs that serve Ohio, then there would be legal basis for change. Inasmuch, however, as no one in this proceeding has demonstrated that any existing RTO practice, rate or charge is "unjust and unreasonable" – the OCC's recommendation should be taken as an acknowledgement that the Commission and all other stakeholders should continue to pursue prevention of the same – but that no changes are needed at this time.

ANALYSIS OF THE SYNAPSE REPORT

As noted above, the OCC provides a copy of a report that was prepared by its consultant, Synapse Energy Economics, Inc. This report is flawed in many respects, and the Commission would be well advised to avoid relying on any facts, analysis or argument presented therein. Instead, to the extent that the Commission seeks facts about or analysis of FERC's RTO policies, or about specific RTOs, the Commission should utilize information provided by governmental agencies with recognized competency, or from utilities and independent third parties that are recognized experts in the matter under review.

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[3] OCC, p. 4.

[4] *Compare* Polonius's counsel upon parting with his son Laertes. Shax, *Hamlet*, ll. 544 -566.

[5] *See* 16 U.S.C. § 824d(a).

The next section of these comments provides an analysis of the flaws in the Synapse report. The analysis is presented in the order or sequence that mirrors the sequence in which each issue is presented in the Synapse report.

I.A. The Synapse argument – that the benefits of [the RTOs] efficient dispatch in the day-ahead market may have been achieved at the expense of long-term bilateral transactions[6] – is fatally flawed.

These flaws include at least the following: Synapse presents no specific facts (specific to one or more of Ohio's electric distribution utilities or to one or more of the RTOs that operate within Ohio) to support its argument. Synapse also fails to account for the fact that many electric distribution utilities, including Ohio electric distribution utilities, have procured and continue to procure electric power supply requirements through long-term bilateral contracts, and that such sourcing often occurs within the context of retail rate proceedings that are regulated by state public utilities agencies.[7] In fact, Synapse fails to present *any* facts or analysis regarding the current levels of long-term bilateral transactions as compared to day-ahead RTO energy market transactions, or the *desired* levels for the same. As such, Synapse's argument consists of nothing more than unsupported allegation, and can be rejected in its entirety.

I.B. Synapse's suggestion – that transmission enhancement costs are allocated only to load[8] – is false.

Again, Synapse presents no specific facts to support its argument. And the tariffs for the RTOs that operate in Ohio do not support Synapse's theory. Rather, each tariff provides that the costs are passed through to transmission customers, a group that includes both loads and generation.[9] And, review of the PJM and Midwest ISO tariffs demonstrates that numbers of generators are in fact transmission customers that purchase electric transmission services

[6] Synapse, p. 2.

[7] Recent examples include: PUCO Case No. 08-935-EL-SSO, *Ohio Edison Co., et al.*, Finding and Order (approving long-term bilateral contracts between electric utility companies and energy suppliers) (May 27, 2009); PUCO Case No. 05-1125-EL-ATA, *Ohio Edison, et al.*, Opinion and Order (authorizing, subject to conditions, electric utility companies to execute long-term bilateral electric supply contracts) (January 4, 2006).

[8] Synapse, p. 3.

[9] PJM OATT (PJM FERC Electric Tariff, Vol. No. 1), Schedule 12, ¶(a)(1-3); .Midwest ISO ASM Tariff (Midwest ISO FERC Electric Tariff, Vol. No.1), Attachment FF, ¶ III.

(network service and point-to-point transmission service) and, as a result, that pay for transmission enhancement costs that are part of transmission rates.[10]

I.C. Synapse's arguments regarding resource adequacy can be rejected because the arguments are based on a fundamental misunderstanding of RTO capacity programs.[11]

RTO capacity programs are intended to ensure that sufficient supply of capacity resources is available during periods of peak demand. The simple fact is that sufficient supply is required to ensure that energy is available to Ohio's consumers at all times. And, in today's environment of open-access transmission policies, another simple fact is that if supply is not contractually committed to cover Ohio's requirements during peak load periods, on a peak day uncommitted suppliers may choose to send energy to consumers outside of Ohio.

Federal policy, and the PJM and Midwest ISO tariffs that implement this policy within Ohio, is to foster market-based approaches that afford opportunity for *all* classes of supply to compete solely on the basis of cost, preferably in open and transparent processes, for the right to receive payment in exchange for committing to supply Ohio's requirements on the peak day. PJM implements this policy through its RPM program; which at its core consists of supply contracts that commit suppliers to provide energy to Ohio's consumers in amounts sufficient to meet reasonable planning requirements during system peaks.[12] The Midwest ISO addresses this policy through its Resource Adequacy program, which calls for electric distribution utilities to lock-in supply by means of bilateral contracts with suppliers.[13]

Synapse artfully characterizes the issue as nothing more than a "subsidy" for generation.[14] However, this characterization ignores the fact that, when properly implemented, RTO resource adequacy programs allow all classes of suppliers to compete for the supply opportunity, including at least the following supplier classes: existing generators, new

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[10] *E.g.*, PJM OATT, Attachments E and I (generators and their agents listed as fPTP and NITS transmission customers); Midwest ISO ASM Tariff, Attachments E and H (generators and their agents listed as NITS and fPTP transmission customers).

[11] Synapse, pp. 3-4.

[12] *E.g.*, PJM OATT, § 8.1.

[13] *E.g*, Midwest ASM Tariff, Module E, § 68.1.3.

[14] Synapse, p. 4.

generators, financial traders, demand response, energy efficiency, and potentially others. The broad spectrum of suppliers suggests that marketplace ingenuity is the only limit on development of new classes and types of suppliers. And there is no "subsidy." Rather, contracts are formulated that reflect the price that consumers must pay to retain the supply commitments that are necessary for reliability. The fact that consumers have to pay for reliability does not mean that the payment is a subsidy.

Ohio's consumers cannot have it both ways. If they are unwilling to accept outages, then they need to lock-in supply to provide energy to Ohio on the peak day. If they are willing to accept the risk of outages, then there is no need to pay for contracts that commit suppliers to Ohio on the peak day, and consumers therefore accept the risk – and eventual reality – of outages.

Interestingly, Synapse criticizes existing resource adequacy policy, but fails to identify any meaningful alternative. And meaningful alternatives do exist. For example, Ohio could adopt an alternative state regulatory approach that, if implemented, could bring new generating capacity into Ohio on a competitive basis. Specifically, the Commission could authorize its electric distribution utilities to implement a "Request-for-Proposal" process whereby generation developers would compete for a long-term contract to provide electricity supply from a new generating station to the affected utility. Other states have seen some success with this approach,[15] so there is basis for further Commission investigation if such is desired.

I.D. Synapse's assertion – that RTOs perform poorly with respect to support of economic demand side resources[16] – is false.

PJM, an RTO that serves many of Ohio's consumers, has seen spectacular growth in demand response providers. Specifically, more than 6,000 commercial and industrial facilities, and more than *45,000* small commercial and residential customers currently participate in PJM's demand response programs.[17] This probably is attributable to the fact that PJM pays both an

[15] *E.g.*, NYSPSC Case No. 02-E-1656, *Consolidated Edison Company of New York*, Declaratory Ruling on Cost Recovery (January 24, 2003).

[16] Synapse, p. 4.

[17] PJM Real Time Economic Demand Response Program, *available*, http://www.pjm.com/markets-and-operations/demand-response/~/media/markets-ops/dsr/dsr-brochure.ashx (emphasis added).

energy price and a capacity price to demand response providers. In fact, this evidence supports a Commission finding that establishing the proper market signal, consisting in PJM of both an energy and a capacity value, encourages participation by demand response resources, both directly on a demand resource's own behalf, and also indirectly through aggregators and energy supply companies.

Against this track record, Synapse offers some analysis of conditions in New England and some academic theories about the basis for alleged flaws in New England's program. Fortunately, Ohio is not in New England, so the Commission can disregard Synapse's theorizing about why New England's programs are not working and, instead, focus on coordinating its new demand response regulations[18] with the PJM program.

There may be room, however, to improve the Midwest ISO's demand response programs. As such, it may be worthwhile for the Commission and other interested stakeholders to encourage the Midwest ISO to adopt demand response programs that mirror PJM's successful programs.

I.E. Synapse's concern – that RTOs place little emphasis on retail electric customer value[19] – is unfounded.

Both of the RTOs that serve Ohio's ratepayers periodically publish reports that demonstrate that value that their respective operations brings to their respective ratepayers.[20] Synapse presents no credible challenge to the facts or analysis presented in these documents. Rather, Synapse grounds its arguments in criticisms of RTO philosophies that encourage "keeping the lights on" (that is, ensuring reliability) and in complaints about RTO governance, specifically, allegations that the generators "pack" the RTO stakeholder process.[21]

[18] O.A.C. Chapter 4901:1-39 Energy Efficiency and Demand Response Benchmarks.

[19] Synapse, pp. 7-8.

[20] *E.g.*, PJM, *Analysis of the Impact of Coordinated Electricity Markets on Consumer Electricity Charges* (2006), *available* http://www.pjm.com/documents/~/media/documents/reports/20061121-analysis-coordinated-elec-mkts.ashx; Midwest ISO, *Midwest ISO Value Proposition* (2007), *available* http://mktweb.midwestiso.org/publish/Document/6871db_117a25bcaa6_-7a200a48324a/ValuePropStudy.pdf?action=download&_property=Attachment.

[21] Synapse, p. 7.

Synapse's concerns lack merit. First of all, FERC's dockets that deal with RTO matters are filled with effective advocacy by consumer groups and representatives – a fact that gives the lie to Synapse's theory that consumers are unable to advocate for themselves in RTO stakeholder processes.[22] Next, even assuming *arguendo* that consumers currently are unable to make themselves heard in RTO stakeholder processes (an assumption that is not valid), the fact that consumers are unwilling to advocate for their own interests does not create an affirmative obligation for compensatory action by all other stakeholders. In any event, given that the OCC and other consumer representatives have been and apparently will continue to be involved in RTO stakeholder processes and related FERC dockets, good reason exists for the Commission to find that Ohio's consumers will continue to be represented effectively in RTO stakeholder processes and in FERC dockets that deal with RTO tariff issues.

II.A. Synapse's recommendation – that the RTOs that serve Ohio need to reflect "independence" – fails to account for the fact that the RTOs that serve Ohio's consumers already reflect the very "independence" recommended by Synapse.[23]

The RTOs that serve Ohio's consumers – PJM and the Midwest ISO – are not-for-profit entities whose organic documents prohibit Board members from having any financial interest in any market participant.[24] As such, it is difficult to see that Synapse is recommending anything in this part of its report.

II.B. Synapse fails to explain or justify its recommendation that RTOs should include at least two slots on their Boards for members who represent retail consumers.[25]

RTO governance is described in contracts that have been approved by the FERC. Such agreements represent settled practice and should not be disturbed lightly. Synapse presents no

[22] *E.g.*, FERC Docket No. ER09-1063, *PJM Interconnection*, Protest of the Office of the Ohio Consumers' Counsel, *et al.* (June 26, 2009); FERC Docket No. ER09-1049, *Midwest ISO*, Comments of the Office of the Ohio Consumers' Counsel (May 26, 2009); *etc.*

[23] Synapse, p. 8.

[24] PJM Operating Agreement (PJM Rate Schedule FERC No. 24), Article 2 (powers and purposes), § 7.2 (Board member qualifications); Midwest ISO Transmission Facility Owners Agreement (Midwest ISO FERC Electric Rate Tariff Schedule No. 1), Article 2.

[25] Synapse, p. 9.

facts, arguments, policy or law that compel or justify its recommendation that the documents be amended to require the changes to the composition of RTO Boards. Consequently, there is no basis to change existing governance documents, and the Commission can disregard this recommendation.

II.C. Contrary to Synapse's characterizations, the language in Order 719 regarding an RTO "commitment to responsiveness to customers" is an aspirational objective, not a rigid mandate.[26]

In Order 719, the FERC "encourages" RTO mission statements to include a commitment to responsiveness to customers and other stakeholders, and ultimately to the consumers who benefit from and pay for electric services.[27] Importantly, FERC goes on to explain its expectation that this "responsiveness *objective*" would not conflict with existing elements of the RTO's mission.[28] In other words, RTOs are to be responsive to customers in a manner that does not conflict with other recognized (and apparently different, but not conflicting) RTO objectives.

In any event, PJM and the Midwest ISO have filed Order 719 compliance filings that satisfy the FERC's Order 719 requirements.[29]

II.D. Synapse's recommendation that RTO stakeholder processes and FERC regulatory proceedings be changed to afford more opportunity for consumer input lacks merit because the RTOs that serve Ohio's consumers already have stakeholder processes that allow market participants – including consumers and consumer representatives – to propose changes and advise regarding RTO-proposed changes. And FERC's procedures likewise allow stakeholders, including consumers and consumer representatives, to bring differences with RTO-proposals to FERC's attention.[30]

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[26] Synapse, p. 9.

[27] Order 719, PP 478, 556.

[28] Order 719, P. 556 (emphasis added).

[29] FERC Docket No. ER09-1063, *PJM Interconnection*, compliance filing dated April 29, 2009; FERC Docket No. ER09-1049, *Midwest ISO*, compliance filing dated April 28, 2009.

[30] Synapse, p. 9.

PJM is organized and structured to permit any willing stakeholder to participate fully in all stakeholder processes, including equal opportunity to raise new issues or ideas, to advocate for positions, and to vote for a given member's interests.[31] The Midwest ISO likewise is structured to include stakeholder processes that afford opportunities for stakeholders to raise new issues, advocate for positions, and vote to support their respective interests.[32] And FERC's regulations and processes afford ample opportunity for interested stakeholders to intervene and participate on an equal basis in FERC's dockets, and advocate for any given point of view.[33] As such, it is difficult to see what, if any, point is being made by Synapse.

It is true that participating in RTO stakeholder processes and FERC proceedings requires resources. However, numerous state agencies, non-governmental groups, and consumer organizations seem equal to the challenge. So there is no reason to assume that Ohio's consumers somehow are burdened or systematically limited or excluded from these processes, and the Commission can disregard any suggestion to the contrary.

II.E. Synapse's recommendation that current levels of market monitoring and mitigation be maintained fails to account for the fact that relevant FERC policies trend toward *strengthening* the RTO market monitoring function.[34]

The current PJM and Midwest ISO tariffs and agreements describe the market monitoring requirements that apply to each RTO. The language in these documents cannot be changed without FERC's prior written authorization,[35] so there is no need for concern that changes can occur outside of an open and transparent regulatory process. Moreover, in the Order 719 proceedings, the FERC recently has had opportunity to revisit to generic policies that control for market monitoring and mitigation, as well as the

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[31] *See* PJM Operating Agreement, Article 11; *and* PJM Manual No. 33, *Administrative Services for the PJM Interconnection Operating Agreement.*

[32] Midwest ISO Transmission Facility Owners Agreement, Article 2, Sections 5, 6, 7.

[33] *See* 18 C.F.R. Part 385, FERC Rules of Practice and Procedure.

[34] *Compare* Synapse, pp. 9-10 (advocating to maintain existing RTO market monitoring and mitigation).

[35] *E.g.*, 16 U.S.C. 824d(d).

specifics of the PJM and Midwest ISO market monitoring programs.[36] In other words, FERC continues to evaluate RTO market monitoring and mitigation, and is actively seeking to improve the same. It therefore is difficult to determine what, if anything, is being "recommended" in this part of the Synapse report.

II.F. Synapse fails to recommend anything specific with regard to system planning by RTOs.[37]

Synapse articulates generalities and criticisms about RTOs and (apparently) system planning, but makes no concrete recommendations in this part of its report. In fact, the only language that can be construed as a "recommendation" in this part of the report is the language to the effect that there needs to be "a better delineation of roles" and "better coordination" "between the RTOs, the state commissions, the state consumer advocates and other stakeholders." Unfortunately, no specifics are provided – although the caption supports an inference that Synapse intends that such delineation and coordination should go (only) to system planning. Since, however, Synapse does not identify a specific existing problem or present a specific "improvement," the Commission need not address Synapse's apparent theory that system planning for Ohio's RTOs needs to be improved.

III. Synapse admits that its description of perceived problems with the PJM RTO is not founded on fact or credible analysis.[38]

Synapse asserts that it does not have an opinion as to whether PJM or Midwest ISO provides better value for Ohio's consumers.[39] The Commission therefore should not rely on the Synapse report for any conclusion regarding the comparative value for Ohio's consumers as between the PJM and Midwest ISO RTOs.

The pitfalls of relying on any comparisons in the Synapse report is illustrated in the language used in the report. For example, Synapse asserts that membership in PJM *probably*

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[36] Order 719, PP 310-476; FERC Docket No. ER09-1063, *supra*, PJM compliance filing dated April 29, 2009; FERC Docket No. ER09-1049, *supra*, Midwest ISO compliance filing dated April 28, 2009

[37] Synapse, p. 10.

[38] Synapse, pp. 11-13.

[39] *Id.*, p. 11.

increases wholesale electric prices in Ohio.[40] However, Synapse goes on to explain that it is not aware of any facts or studies that prove this point, that it has not performed any study that establishes this fact, and suggests that the only way to establish this fact would be to perform a cost-benefit study.[41]

Notwithstanding its admission that it really doesn't know if membership in PJM increases costs to Ohio consumers, Synapse rushes forward to recommend fundamental changes in PJM's programs (and governing documents) -- here, to shift PJM membership charges off of consumers and onto suppliers. Synapse further suggests that generation affiliates be compelled to "share the benefits" of PJM membership with their Ohio electric distribution utility affiliates. Unfortunately for Synapse, this suggestion runs completely contrary to state and federal law (not to mention Article V of the U.S. Constitution). In any event, since Synapse offers no facts that establish that membership in PJM increases wholesale electric prices in Ohio, and since Synapse's proposals to address such an eventuality are unlawful, the Commission can and should reject Synapse's theories about how to "improve" PJM.

ANALYSIS OF APPENDICES A AND B OF THE SYNAPSE REPORT

In Appendices A and B of its report, Synapse provides its answers to the questions propounded by the Commission in this proceeding. In the interests of keeping these reply comments short, FirstEnergy notes here that Synapse presents no credible facts or valid analysis or arguments that are responsive to the questions, or that compel findings or conclusions that are different than those provided in FirstEnergy's initial Comments in this proceeding. Accordingly, FirstEnergy incorporates by reference its answer to the Commission's questions as such answers are provided in FirstEnergy's initial Comments. To the extent that any fact or argument presented by Synapse is different that a fact or argument provided in FirstEnergy's initial Comments, FirstEnergy submits that the FirstEnergy facts and arguments are valid and correct, and that conflicting or contrary facts and analysis presented by Synapse can be ignored.

[40] Synapse, p. 11 (emphasis added).

[41] Synapse, pp. 11-12.

REPLY TO COMMENTS OF THE INDUSTRIAL ENERGY USERS – OHIO (IEU-OHIO)

The IEU-Ohio's position in this case is that without major reforms it is not in the public's or customers' interest to continue to permit: (1) Participation in RTOs as such participation may relate to "Day 2" market structures; and, (2) Electric distribution utilities ("EDUs") to pass on the cost of RTO participation to Ohio retail customers until they make an affirmative demonstration that the direct customer benefits of the RTO selections (made by the EDUs or their affiliates) exceed the costs.[42] In addition, IEU-Ohio states that RTOs are presently incapable of serving the public interest in "just and reasonable rates"[43] and claims that FERC's regulatory choices are substantially similar to the *laissez faire* approach to our Nation's regulation of financial institutions over the last decade, an approach that has pushed us into a global financial crisis.[44] FirstEnergy respectfully disagrees, and believes that RTOs have provided many benefits and have served the public well, that RTO rates are regulated for the purpose of achieving "just and reasonable" levels, and that alleged parallels between electricity regulation and the financial markets are clearly unfounded.

The IEU-Ohio attempts to support its position by providing a RTO History and a discussion of FERC and market-based rates in its initial comments. IEU-Ohio bootstraps its arguments about market-based rates by excerpting various pieces of testimony from various unrelated proceedings and jurisdictions. But – other than the testimony from other jurisdictions that does not discuss or directly apply to RTO policy – IEU-Ohio offers little in the way of empirical evidence to support its core position that RTO policy is flawed and that drastic changes are necessary. Nor do they suggest metrics or offer other hard evidence regarding how their position might be supported. The fact that IEU-Ohio is unable to offer evidence that is directly on point, or even identify processes or methodologies for developing such evidence, supports an inference that the Commission can disregard the IEU-Ohio position.

Turning to specifics, IEU-Ohio complains that there have not been empirical studies that show that RTOs provide the benefits as promised. This complaint about the purported lack of

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[42] Case No. 09-90-EL-COI, *Comments of IEU-Ohio*, p. 3 (hereinafter, "IEU-Ohio").

[43] IEU-Ohio p. 2.

[44] IEU-Ohio p. 6.

empirical studies showing RTO benefits ignores the multiple studies conducted by or on behalf of the RTOs and others that quantify the value RTOs have proven to provide.[45] The point here is that, contrary to what has been suggested by IEU-Ohio, there are accepted and acknowledged studies regarding the value that RTOs provide to end-use customers, and the Commission can consult such studies if and as needed.

IEU-Ohio offers recommendations of two alternatives: 1) that RTOs return to Day-1 operations, where RTOs assume limited responsibility for reliability and scheduling functions; or 2) the creation of an "Ohio-only RTO" with limited responsibility for reliability and scheduling functions, in effect, a Day-1 Ohio-only RTO. IEU-Ohio asserts that RTOs are presently incapable of serving the public interest in "just and reasonable rates."[46] However, IEU-Ohio has not presented detailed facts or law that compel these changes.

Since neither IEU-Ohio nor any other party to this proceeding has demonstrated that any existing RTO practice, rate or charge is "unjust and unreasonable" – the IEU-Ohio recommendation should be taken as an acknowledgement that current practices – while perhaps resulting in rates that are deemed to be too high by IEU-Ohio's members – are "just and reasonable." As such, IEU-Ohio is advocating for radical change in existing RTO models, and is seeking to enlist the Commission's help. The Commission will have to judge the merits of this position – but any such effort doubtless would be long and costly; and the eventual end state would be of uncertain value.

ANALYSIS OF IEU – OHIO COMMENTS

By way of introduction, and as noted above, to the extent that the Commission seeks facts about or analysis of FERC's RTO policies, or about specific RTOs, the Commission should utilize information provided by governmental agencies with recognized competency, or from utilities and independent third parties that are recognized experts in the matter under review. Since IEU-Ohio fails to present any new information, the Commission can be confident that existing sources capture the most up-to-date consensus about RTO policy.

[45] *See, e.g.*, studies referenced or cited in FirstEnergy's initial Comments in this proceeding. Case No. 09-90-EL-COI, *Comments of FirstEnergy*, at pp. 7,10,11, and 13.

[46] IEU-Ohio, p 2.

The remainder of these comments provides an analysis of the flaws in the IEU-Ohio's comments. The analysis is presented in the order or sequence that mirrors the sequence in which each issue is presented in the Comments of the IEU-Ohio.

- The IEU-Ohio argument – that PJM's introduction of RPM in 2005 was universally criticized by consumers, state regulators and public power authorities as unnecessary and likely to lead to higher electricity prices[47] – fails to articulate a compelling reason for change.

RTO capacity programs are intended to ensure that sufficient supply of capacity resources is available during periods of peak demand. Sufficient supply is required to ensure that energy is available to Ohio's consumers at all times. And, in today's environment of open-access transmission policies, another fact is that if supply is not contractually committed to cover Ohio's requirements during peak load periods, uncommitted suppliers may choose to send energy to consumers outside of Ohio that are willing to pay more on the peak day.

IEU-Ohio characterizes the issue as leading to higher prices for consumers.[48] However, this characterization ignores two facts. First, consumers must pay for capacity – and such payments exist whether or not the customer is in an RTO. Second, when properly implemented, RTO resource adequacy programs allow all classes of suppliers to compete for the supply opportunity – meaning that competitive forces within RTO markets for capacity should result in the lowest possible costs for consumers.

Resources that clear in PJM's RPM auctions take on specific obligations: to offer energy into daily energy markets, and to provide energy when called upon by PJM, which is necessary to ensure reliability and keep the lights on during system peaks. So while it is true that customers have to pay for reliability, it is equally true that PJM's RPM has a successful record of procuring the capacity necessary to provide for reliable electric service, and for doing so by means of a market process that is designed to result in the lowest possible price.

- The IEU-Ohio argument – that FERC's faith-based regulatory approach has not served the public well and that FERC's regulatory choices are substantially similar to

[47] IEU-Ohio, p. 30.

[48] IEU-Ohio, p. 30.

the *laissez faire* approach to our Nation's regulation of financial institutions over the last decade, which has pushed us to a global financial crisis.[49] – is not valid.

IEU-Ohio's attempt to draw a parallel between regulation in the nation's financial markets to electricity is the classic "straw man" argument. IEU-Ohio describes an open and acknowledged problem in the financial markets. They include excerpts of impressive testimony, and wax eloquent about the situation – which everyone deplores.

But they utter fail to establish a direct cause-and-effect relationship between the problems and proposed solutions in the nation's financial markets and the purpose of this proceeding, which is to ascertain the value that RTOs provide to Ohio's electric consumers.

Since IEU-Ohio's description of and arguments about the financial markets lack direct relevance or applicability to the matters under consideration in this docket, the Commission can ignore them.

- IEU-Ohio's argument – that FERC has not conducted any empirical analysis to identify if RTO markets were producing benefits[50] – is unfounded.

IEU-Ohio's argument regarding the lack of empirical studies showing RTO benefits ignores multiple studies conducted by or on behalf of the RTOs and others that quantify the value RTOs have proven to provide. A Midwest ISO study estimates consumers served by the Midwest ISO see saving of between $555 and $850 million per year. In another assessment furnished by PJM, it is estimated that consumers served by PJM RTO see $2.3 billion in annual savings. In addition, many other analysis and reports have quantified the benefits of RTOs and of competitive markets.[51]

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[49] IEU-Ohio, p. 31

[50] IEU-Ohio, p. 35.

[51] *See, e.g.*, studies referenced or cited in FirstEnergy's initial Comments in this proceeding. Case No. 09-90-EL-COI, *Comments of FirstEnergy*, at pp. 7,10,11, and 13.

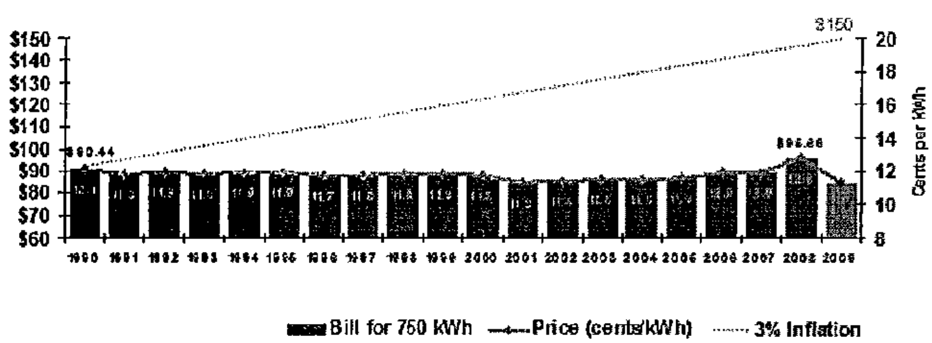
- IEU-Ohio's claims – that FERC's faith-based approach on RTO markets has come at the expense of consumers[52] and that experience since the early 1990's consistently shows that the actual results of the changes federal regulators and RTOs have implemented have been diametrically different than FERC's projections[53] - are not backed by hard evidence.

While IEU-Ohio claims rate shock for consumers within RTOs and adverse results for consumers, they do not provide any hard evidence of such a claim. And, the record as developed in this proceeding to date, runs in the opposite direction.

Additional evidence, at least for customers of FirstEnergy's Ohio electric distribution utilities, demonstrates that there has been no rate shock. For example, the following tables demonstrate that prices largely have declined for retail customers of Ohio's electric distribution utilities during recent years.

- **Ohio Edison**

Bill for 750 kWh and Residential Price (cents per kWh)



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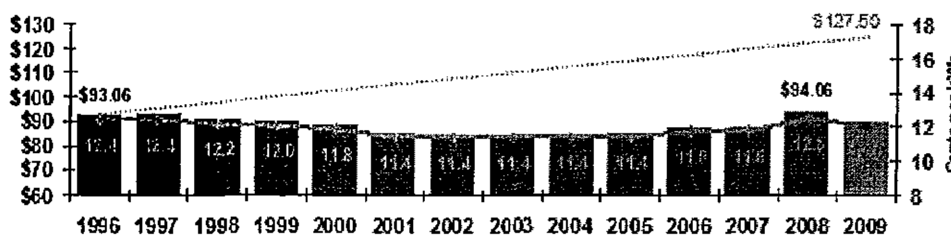
[52] IEU-Ohio, p. 47.

[53] IEU-Ohio, p. 49.

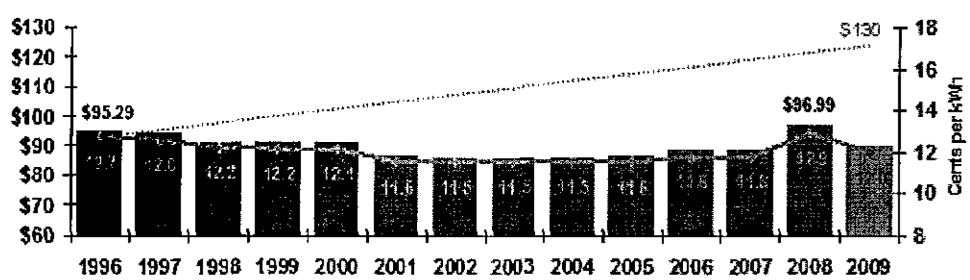
- **The Illuminating Company**

Bill for 750 kWh and Residential Price (cents per kWh)



– Toledo Edison

Bill for 750 kWh and Residential Price (cents per kWh)



Interestingly, the tables also demonstrate that electricity prices for FirstEnergy's Ohio utilities have significantly lagged inflation for more than ten years.

DISCUSSION OF INDUSTRIAL ENERGY USERS-OHIO RECOMMENDATIONS

- Recommendation 1 - A return to "Day 1" RTO operation where RTOs assume limited responsibility for reliability and scheduling functions.

Transparent RTO markets are a necessity to facilitate national energy policy initiatives such as renewable portfolio standards, increased demand response, and the "Smart Grid". FirstEnergy supports RTOs because they administer markets that have many attributes that benefit customers and that support national and state energy policies and initiatives, particularly state policies promoting retail competition. RTO markets provide market transparency, improved forward market liquidity and hedging capability. RTO markets also provide hourly scheduling and settlement services. RTO markets, because of their open access and non-discriminatory market rules provide a level playing field for all market participants.

RTO markets provide for least cost security constrained dispatch over larger regions than other markets. This facilitates more efficient reserve sharing, reduces transmission loading relief (TLR), improving overall reliability, economics and cost effectiveness of the RTO region. RTO markets enable implementation of new technologies better than other bilateral markets because of their transparency, as well the fair, equal, and open access to the transmission system they provide. New technologies include Demand Response Resources, Renewable Generation Resources, Distributed Generation Resource and other Smart Grid technologies. Because RTO markets level the playing field for diverse types of generation and demand resources to compete to bring the lowest cost electricity to consumers, RTOs are seeing robust investment in environmentally-friendly generation.

FirstEnergy believes that RTOs are a necessity for regions, including Ohio, that have adopted retail choice. The RTO-administered energy and ancillary markets provide the mechanism that enables retail providers to balance loads and resources from hour to hour without having to rely on illiquid bi-lateral markets. These markets also provide the mechanisms by which retailers can settle their wholesale commitments without over burdening the electric distribution companies. Therefore, FirstEnergy believes it would not be in the best interest of Ohio's consumers to return to a "Day 1" RTO.

- Recommendation 2 - The creation of an "Ohio-only RTO" with limited responsibility for reliability and scheduling functions... in effect, a "Day 1" Ohio-only RTO.

For all the reasons stated above (in the previous section) it would not be in the best interest of Ohio's consumers to have an Ohio-only "Day 1" RTO.

Furthermore, FirstEnergy does not believe it would be viable or cost-effective for the Ohio Commission to pursue an "Ohio-only" RTO. The vast majority of Ohio customers are served by three large multistate utilities who offer open access transmission service over their integrated transmission systems at a single transmission rate. In some instances, Ohio customers are served over these transmission systems by generation plants located in other states; in other instances, generation in Ohio is transmitted over these transmission systems to customers in other states. An Ohio only RTO construct ignores the historical reality that Ohio has never been a single market for the multistate electric utilities that serve customers within its borders, and there does not appear to be any compelling reason to make it one. An Ohio only RTO approach would create market inefficiencies as well as regulatory and practical issues that may be incapable of resolution.

Power flows do not recognize State boundaries. Neither does wholesale energy or transmission markets. And Ohio's major electric utilities all are interconnected to a greater or lesser degree with utilities in other states. These considerations are such that it is challenging to see how an Ohio-only RTO would function.

It is doubtful whether an Ohio-only RTO could satisfy the FERC's requirements for RTO status. For example, the FERC requires RTOs to exhibit four different characteristics: (i) independence; (ii) size and scope of footprint; (iii) operational authority; and (iv) short-term reliability.[54] Speaking to independence, how would an Ohio-only RTO demonstrate the required independence from transmission owners and market participants? Speaking to size and scope, it would seem difficult to reconcile an Ohio-only RTO with FERC's repeated emphasis that proposed RTOs should be "regional" in size and large in scope.[55] Several years ago, FERC rejected formation of the Alliance RTO because its scope and configuration was inadequate, even though the Alliance RTO – which included AEP, DPL, and FirstEnergy - was far larger than a theoretical Ohio-only RTO.[56] It is difficult to imagine that an Ohio only RTO would ever meet these criteria, especially given the fact that it represents an inferior alternative to RTO configurations accepted by the FERC.

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[54] FERC Docket No. RM99-2, *Regional Transmission Organizations*, Order 2000, p 152.

[55] E.g., FERC Docket No. ER08-637, *Midwest ISO*, Order on Market Service Proposal, 126 FERC ¶ 61,139, P 61 (2009).

Speaking to operational authority, the FERC has identified eight functions that must be present before RTO status can be approved. Many of these functions – including the congestion management, planning and expansion, and interregional coordination functions, suggest a preference for a regional, as opposed to a statewide approach to a given issue. Moreover, it is difficult to visualize an Ohio-only RTO as performing all of these functions to the same levels as such functions are performed currently by the incumbent RTOs. The last characteristic, short-term reliability probably comes down to an implementation issue: conceivably, with enough money and time an Ohio-only RTO could be constructed to satisfy this requirement. And perhaps the same is true for all four characteristics: it is possible – although by no means easy or likely – that Ohio's electric consumers could pay out enough money to construct an Ohio-only RTO that satisfies the Order 2000 characteristics. But would the costs exceed the benefits? Yes, almost certainly. Moreover, given the other issues described herein, even if the benefits were to exceed the costs, could the other regulatory hurdles be cleared? Most likely not.

Therefore, it would be better for Ohio and its RTO participants to continue to work within the existing RTOs to improve their performance and continue to add value to Ohio's consumers.

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[56] FERC Docket No. RT01-88, *Alliance Companies, et al.*, Order on Requests for Rehearing, 97 FERC 61,327 (2001).

CONCLUSION

FirstEnergy Service Company appreciates this opportunity to respond to comments submitted by other parties in this proceeding.

Dated: Akron, Ohio
July 24, 2009

Respectfully submitted,

Morgan E. Parke / JTS per authorization

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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing *Reply Comments of FirstEnergy Service Company* was served upon the parties on the attached Service List this 24th day of July, 2009 by first class mail, postage prepaid.

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