

**BEFORE THE  
THE PUBLIC UTILITIES COMMISSION OF OHIO**

In the Matter of the Commission Review of	)	
the Capacity Charges of Ohio Power	)	Case No. 10-2929-EL-UNC
Company and Columbus Southern Power	)	
Company.	)	

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**FIRSTENERGY SOLUTIONS CORP.'S MEMORANDUM CONTRA OHIO POWER  
COMPANY'S MOTION FOR RELIEF AND REQUEST FOR EXPEDITED RULING**

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**I. Introduction**

The Commission should deny the Motion for Relief (“Motion”) filed by Ohio Power Company (“AEP Ohio”) because it is legally and procedurally deficient. The Commission rejected the September 7, 2011 Stipulation and Recommendation (the “Stipulation”) *en toto* in its February 23, 2012 Entry on Rehearing (the “Feb. 23, 2012 Entry”). Yet AEP Ohio now seeks permission from the Commission to continue to impose on CRES providers and retail customers one of the most anti-competitive and discriminatory aspects of that Stipulation – bifurcated pricing for capacity used by non-SSO customers that will, in effect, result in burdensome shopping caps that will stymie the competitive markets in AEP Ohio’s service territory. What AEP Ohio proposes is to continue to price capacity for a minority of non-SSO customers based on the PJM Reliability Pricing Model (“RPM”) market price while more than doubling the price all other non-SSO customers pay.<sup>1</sup> Yet AEP Ohio’s bifurcated capacity pricing scheme existed only as a creation of the Stipulation and, with the Stipulation now having been properly rejected by the Commission, it has ceased to exist along with the Stipulation. There is no mechanism to “revive” only the most anti-competitive and discriminatory aspects of that now-rejected

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<sup>1</sup> As discussed below, AEP Ohio’s favored \$255/MW-day capacity price is more than double the current RPM-based capacity price. It is more than ten times higher than the RPM-based capacity price that will become effective June 1, 2012.

Stipulation. AEP Ohio has a right to seek rehearing of the Feb. 23, 2012 Entry, but it does not have a right to cherry-pick one element from a defunct Stipulation and claim that that element alone should be retained in order to maintain the “status quo.”

Under any objective reading of the February 23, 2012 Entry, the intent of the Commission is unmistakable: to “reset” the process in this case to the point just before the filing of the now-rejected Stipulation and Recommendation. Prior to the filing of the Stipulation, the Commission, by its Entry of December 8, 2010 (the “Dec. 8, 2010 Entry”), required AEP Ohio to charge RPM-based capacity prices.<sup>2</sup> As the Commission observed in the Dec. 8, 2010 Entry, and as the Commission represented and warranted to FERC in comments submitted there, it simply made explicit what had already been implicit given AEP Ohio’s long-time use of RPM-based pricing.<sup>3</sup> Thus, by its “reset” of this proceeding, the Commission meant nothing other than to require AEP Ohio to charge RPM-based capacity prices unless and until the Commission determines otherwise.

Therefore, the Commission should direct AEP Ohio to comply with the Feb. 23, 2012 Entry, which obligates AEP Ohio to charge CRES providers for capacity based on the current RPM capacity prices for the 2011/2012 delivery year and continue to adjust those charges consistent with the results of the RPM auctions in the PJM unconstrained region. AEP Ohio has always priced capacity based on this unconstrained-region RPM market price except for the last

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<sup>2</sup> Dec. 8, 2010 Entry at ¶ 4 (citing to Case No. 08-917-EL-SSO *et al.*).

<sup>3</sup> *Id.* See Comments Submitted On Behalf Of The Public Utilities Commission of Ohio at p. 3, FERC Docket No. ER11-2183-000 (filed Dec. 10, 2010) (“Although the state compensation mechanism has implicitly been in place since the inception of AEP-Ohio’s current Standard Serve Offer, the Ohio Commission expressly adopted as its state compensation mechanism the AEP Ohio Companies’ charges established by the reliability pricing model’s three-year capacity auction conducted by PJM.”); *id.*, p. 3 fn. 3 (“The 2010/2011 rate is effective through May 31, 2011. The 2011/2012 rate, which becomes effective on June 1, 2011, is equal to \$110.00 per MW-day (without the adders)”). See also Testimony of Michael M. Schnitzer (“Schnitzer Direct”), FES Exh. 4, p. 23; Testimony of Philip J. Nelson (“Nelson Direct”), AEP Ohio Exh. 7, p. 7; Direct Testimony of Roy J. Shanker (“Shanker Direct”), FES Exh. 14, pp. 11, 14.

two months under the Stipulation, so a return to RPM-based pricing is a return to the status quo. Customers have known and have lived with RPM-based prices for years. The reinstitution of those prices only brings customers back to the pricing model that they are used to.

AEP Ohio's claimed confusion about what it should be required to do is belied by the statements of its management. AEP Ohio witness Nelson acknowledged that, for as long as CRES providers have been purchasing capacity from AEP Ohio, AEP Ohio has priced that capacity using the then-current RPM market price.<sup>4</sup> At the time of hearing, AEP Ohio witness Hamrock admitted that AEP Ohio currently priced capacity based on RPM prices and that the Commission had never authorized AEP Ohio to charge anything other than a rate based on the RPM price.<sup>5</sup> Moreover, he agreed that, **if the Commission rejected the proposed ESP, the existing RPM-based pricing would remain in effect** and that "the state compensation mechanism as of today is the RPM price."<sup>6</sup> The Commission should take Mr. Hamrock at his word and reject this ill-advised Motion.

Similarly, it's hard to fathom how AEP Ohio can claim that RPM-based rates are confiscatory. AEP Ohio claims that adoption of its discriminatory pricing scheme is necessary to protect its double-digit earnings (*see* Motion, pp. 4-6), but AEP Ohio fails to identify or request any of the other less anti-competitive alternatives that may be appropriate had it established any need for relief or requested it through a lawful mechanism.<sup>7</sup> Indeed, if RPM-based pricing is "confiscatory" as claimed by AEP Ohio in its Motion, why did AEP Ohio voluntarily use RPM pricing as the basis for its capacity rate prior to the Dec. 8, 2010 Entry?

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<sup>4</sup> Tr. Vol. V, p. 735.

<sup>5</sup> Tr. Vol. V, pp. 842-843.

<sup>6</sup> Tr. Vol. V, pp. 811, 843.

<sup>7</sup> In contrast to the relief sought in the Motion, AEP Ohio could have pursued distribution-related relief that was not discriminatory and anti-competitive.

Regardless, AEP Ohio has offered no valid justification for discriminating against some shopping customers by charging an arbitrary capacity price for them that is a multiple of market pricing. Indeed, both CRES providers and customers are reliant upon AEP Ohio's continued provision of capacity based on the RPM market price through May 31, 2015.<sup>8</sup> As AEP Ohio has stated, CRES providers "act as a middle-man on capacity flowing from AEP Ohio" to shopping customers.<sup>9</sup> AEP Ohio's compliance with the Feb. 23, 2012 Entry is necessary to protect those customers from harm.

Nor does AEP Ohio fare any better by claiming that a "reset" to RPM-based capacity prices somehow prejudices the outcome in this case. The Commission simply seeks to reinstate what it ordered in December 2010 and what was in place for all shopping customers until this past December. In fact, it is AEP Ohio's Motion that seeks to have the Commission prejudge the issues in this case. Why, for example, would AEP Ohio attempt to have the Commission review evidence now to support alleged full-embedded cost-based rates if not to have the Commission determine the merits of that proposal before a hearing? Further, AEP Ohio ignores the weight of the evidence against its proposal – evidence that includes the testimony of witnesses who supported the Stipulation. The Commission should deny AEP Ohio's Motion.

## **II. AEP Ohio's Motion Is Procedurally Defective.**

AEP Ohio has options available to it under Ohio law to seek relief from the harm it claims will result from the Commission's rejection of the Stipulation. This Motion is not one of them.

As authorized by R.C. § 4905.10, it may seek rehearing of the Feb. 23, 2012 Entry. If it pursues this course, it must demonstrate how the Feb. 23, 2012 Entry is unreasonable or

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<sup>8</sup> See Shanker Direct, p. 7.

<sup>9</sup> Nelson Direct, p. 7.

unlawful. However, because the Feb. 23, 2012 Entry was immediately effective upon filing, AEP Ohio's making of such an application will not excuse it from complying with the entry or operate to stay or postpone its enforcement during the rehearing process.<sup>10</sup>

AEP Ohio also could seek emergency relief as authorized by R.C. § 4909.16. However, the Commission's "power to grant emergency relief is extraordinary in nature" and may only be granted after a utility sustains its burden of proving that, absent emergency relief, it will be financially imperiled or its ability to render service will be impaired.<sup>11</sup> A utility's evidence of financial impairment must "clearly and convincingly demonstrate the presence of extraordinary circumstances which constitute a genuine emergency situation."<sup>12</sup> If an emergency is shown, the Commission is limited to granting temporary relief "only at the minimum level necessary to avert or relieve the emergency."<sup>13</sup> The Commission in the past has directed the utility seeking emergency relief to provide expert testimony supporting its application and has conducted hearings on the application.<sup>14</sup> Obviously, none of the criteria for obtaining emergency relief is satisfied by AEP Ohio's Motion.

In addition, if AEP Ohio's complaint is with the state compensation mechanism process set out in the PJM Reliability Assurance Agreement ("RAA"),<sup>15</sup> AEP Ohio may direct its claim to PJM and the Federal Energy Regulatory Commission ("FERC"). Indeed, given that AEP

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<sup>10</sup> R.C. § 4903.10.

<sup>11</sup> *In re Akron Thermal, Ltd. Partnership*, Case No. 00-2260-HT-AEM, Opinion and Order at p. 3 (Jan. 25, 2001).

<sup>12</sup> *Id.*

<sup>13</sup> *Id.*

<sup>14</sup> *Id.*, p. 2.

<sup>15</sup> The RAA is available from the PJM website at [pjm.com/~media/documents/agreements/raa.ashx](http://pjm.com/~media/documents/agreements/raa.ashx).

Ohio is a party to the PJM RAA,<sup>16</sup> any claim arising out of the allegedly confiscatory impact of the state compensation mechanism established pursuant to the RAA is more properly directed to PJM and the FERC. Notably, after the FERC rejected AEP Ohio's attempt to establish a cost-based rate in early 2011, AEP Ohio filed a complaint at the FERC, Docket No. EL11-32-000, seeking to change the terms of the RAA.<sup>17</sup> If AEP Ohio believes that the RAA is imposing confiscatory rates, it can pursue that argument in Docket No. EL11-32-000.

In contrast to the options outlined above, this Motion disregards the rehearing process and is not authorized by statute. The Commission should deny it as procedurally defective.

### **III. AEP Ohio's Claim that RPM Pricing Will Cause It Immediate and Irreparable Harm Is Untimely, Unfounded and Disingenuous.**

In the Dec. 8, 2010 Entry, the Commission ordered AEP Ohio to continue to base its capacity pricing on RPM auction results as it had always done. AEP Ohio sought rehearing of the Dec. 8, 2010 Entry, but it did not claim at that time that RPM market-based capacity pricing would cause it immediate and irreparable harm.<sup>18</sup> At the time, Columbus Southern Power Company's earnings were approximately 18-20%, and Ohio Power Company's earnings were approximately 10-11%, even without counting the hundreds of millions of dollars received for off-system sales.<sup>19</sup> In fact, while charging RPM-based pricing for capacity, AEP Ohio was able

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<sup>16</sup> See *In re American Electric Power Service Corporation*, FERC Docket No. ER11-2183-000, Entry ¶ 12 (Jan. 20, 2011).

<sup>17</sup> See Nelson Direct, p. 9.

<sup>18</sup> See Ohio Power Company's and Columbus Southern Power Company's Application for Rehearing filed Jan. 7, 2011.

<sup>19</sup> *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Administration of the Significantly Excessive Earnings Test under Section 4928.143(F), Revised Code, and Rule 4901:1-35-10, Ohio Administrative Code*, Case No. 10-1261-EL-UNC, Opinion and Order at pp. 22, 35 (hereinafter, "2009 SEET Order"); *In the Matter of the 2010 Annual Filing of Columbus Southern Power Company and Ohio Power Company Required by Rule 4901:1-35-10, Ohio Administrative Code*, Case No. 11-4571-EL-UNC et al., Direct Testimony of Joseph Hamrock filed July 29, 2011, at p. 6.

to earn amounts that were so significantly excessive that the Commission ordered the company to refund amounts to customers.<sup>20</sup> Regardless, by not raising this argument in a timely manner when challenging the Dec. 8, 2010 Entry, AEP Ohio waived the argument.

The Commission's restoration of RPM-based capacity pricing for all non-SSO customers is not a stunning "flash cut" to a radically new pricing regime. To the contrary, it is nothing more than a return to what AEP Ohio has always done and, prior to December 8, 2010, did voluntarily, and what AEP Ohio fully expected to charge if the Stipulation was not approved.

AEP Ohio cannot credibly claim that a Commission order requiring a capacity charge based on a final RPM zonal price of approximately \$116/MW-day for delivery year 2011/2012 is confiscatory when AEP Ohio voluntarily charged for capacity as recently as the 2009/2010 delivery year using the final RPM zonal price of approximately \$105/MW-day.<sup>21</sup> AEP Ohio voluntarily used RPM pricing in its 2009-2011 ESP without suffering (much less complaining about) "confiscation". In fact, it charged all shopping customers for capacity based on the RPM auction results for 2011/2012 as recently as December 2011.<sup>22</sup> Indeed, AEP Ohio's earnings estimates for 2012 and 2013, if they can be trusted,<sup>23</sup> show significant earnings even though those projections include an unsupported and unrealistic assumption that the "vast majority" of its customers will switch to CRES providers during this time period.<sup>24</sup> Of course, these projected positive earnings appear to be Ohio jurisdictional only, which means they ignore the

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<sup>20</sup> 2009 SEET Order, p. 35.

<sup>21</sup> See Exh. KDP-5 to Testimony of Kelly D. Pearce filed Sept. 13, 2011, AEP Exh. 3; Nelson Direct, p. 7.

<sup>22</sup> See Schnitzer Direct, pp. 22-23.

<sup>23</sup> AEP Ohio's estimates of its 2012 and 2013 earnings, which are attached to the Motion without verification, explanation or support, are not record evidence and should not be relied upon by the Commission in considering AEP Ohio's Motion.

<sup>24</sup> Motion, pp. 5, 9.

hundreds of millions of dollars AEP Ohio will earn in off-system sales and through its retail arm if shopping does increase.<sup>25</sup>

Moreover, there is no reason to believe that AEP Ohio's earnings estimates are any more reliable than the misleading projections AEP Ohio submitted to the Commission in the ESP II proceeding. For example, although AEP Ohio now projects the impact of RPM-based capacity pricing as driving down its estimated ROE from 10.4% to 7.6% in 2012, a level it now claims is somehow confiscatory, AEP Ohio witness Allen forecast an ROE for AEP Ohio of 7.71% in 2012 with all provisions of the Stipulation in place, including, presumably, the anti-competitive bifurcated capacity pricing.<sup>26</sup> Thus, after AEP Ohio's property is "confiscated", AEP Ohio will be earning almost exactly what it forecast it would earn under the proposed ESP. Further, while a decline in market capitalization of \$1 billion sounds impressive,<sup>27</sup> it merely returned AEP's stock price to where it had been in late November 2011.

Continuing the state compensation mechanism as required by the Dec. 8, 2010 Entry will not create uncertainty and instability for customers. Indeed, what AEP Ohio proposes inures only to the benefit of AEP Ohio and does not provide stability to customers. To the contrary, it was the Stipulation's anti-competitive and discriminatory bifurcated pricing scheme that, for a short time, created uncertainty and instability for customers. Of course, that discriminatory scheme retained RPM pricing for shopping customers as of September 7, 2011, so it effectively burdened only new shopping customers. Now that the status quo has been restored by the

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<sup>25</sup> See Testimony of Tony C. Banks in Opposition to the Partial Stipulation filed Sept. 27, 2011, FES Exh. 1 ("Banks Direct"), Exh. TCB-11 attached thereto (AEP Ohio explaining that "We have the shopping exposure, that we have just losing that retail margin, but then of course Todd is making up a significant component, once he's able to get in terms of off-system sales.")

<sup>26</sup> Testimony of William A. Allen in Support of the Stipulation and Recommendation, AEP Exh. 4, p. 20 and Exh. WAA-5.

<sup>27</sup> Motion, p. 5.



Commission's rejection of the Stipulation, AEP Ohio's capacity pricing returns to non-discriminatory market-based pricing for all customers, which is what all customers expect, what all shopping customers have been paying, and what Ohio policy requires.<sup>28</sup>

#### **IV. AEP Ohio Should Do What the Commission Has Ordered It To Do: Charge RPM-Based Pricing For Capacity.**

The Feb. 23, 2012 Entry does not require clarification regarding the requirement to continue the capacity charges approved under the Dec. 8, 2010 Entry. AEP Ohio is well aware that continuance of those charges requires only notice to PJM, not the filing of a retail tariff with the Commission.

The Feb. 23, 2012 Entry rejected the Stipulation and directed AEP Ohio to file, no later than February 28, 2012, new proposed tariffs to continue the provisions, terms and conditions of its previous Electric Security Plan, including, *inter alia*, "an appropriate application of capacity charges under the approved state compensation mechanism established in the Capacity Charge Case."<sup>29</sup> As Chairman Snitchler explained, the Feb. 23, 2012 Entry "effectively hits the reset button on AEP's electric security plan, [and] allows us to start over from the beginning. . . ."<sup>30</sup> Thus, the Feb. 23, 2012 Entry "reset" all parties to the position they were in prior to AEP Ohio's filing of the Partial Stipulation on September 7, 2011. With respect to the rate charged by AEP Ohio to CRES providers for capacity, the Commission restored the state compensation mechanism established by the Dec. 8, 2010 Entry. In that Entry, the Commission defined the state compensation mechanism as "the current capacity charges established by the three-year

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<sup>28</sup> See R.C. § 4928.02.

<sup>29</sup> The Capacity Charge Case is Case No. 10-2929-EL-UNC.

<sup>30</sup> February 23, 2012 Media Release, "PUCO revokes AEP-Ohio electric security plan settlement agreement", available at <http://www.puco.state.oh.us/puco/index.cfm/media-room/media-releases/puco-revokes-aep-ohio-electric-security-plan-settlement-agreement/>.

capacity auction conducted by PJM, Inc. during the pendency of this review.”<sup>31</sup> Currently, the state compensation mechanism is based on the applicable PJM RPM auction price for the 2011/2012 delivery year.<sup>32</sup> And consistent with the Commission’s Dec. 8, 2010 Entry and AEP Ohio’s historic implementation of capacity charges, that charge will adjust consistently with the results of auctions for future periods.<sup>33</sup>

The state compensation mechanism was established by the Commission pursuant to authority bestowed under Schedule 8.1, Section D.8, of the PJM RAA, to which AEP Ohio is a contracting party.<sup>34</sup> As the FERC explained early last year, AEP Ohio voluntarily consented to the Commission’s establishment of the state compensation mechanism by becoming a party to the PJM RAA.<sup>35</sup> Once the Commission has established the state compensation mechanism, it

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<sup>31</sup> *In the Matter of the Commission Review of the Capacity Charges of Ohio Power Company and Columbus Southern Power Company*, Case No. 10-2929-EL-UNC, Entry at p. 2.

<sup>32</sup> Direct Testimony in Support of September 7, 2011 Stipulation of David Fein on Behalf of Constellation NewEnergy, Inc. and Constellation Energy Commodities Group, Inc. dated Sept. 13, 2011, p. 7; Direct Testimony of Teresa L. Ringenbach In Support of September 7, 2011 Stipulation On Behalf of the Retail Energy Supply Association dated Sept. 13, 2011, p. 7.

<sup>33</sup> The final capacity price is based on the clearing price of the Base Residual Auction, plus incremental auctions, and is adjusted for a scaling factor, loss factor and pool requirement. Shanker Direct, p. 7 fn. 4 and p. 11 fn. 7.

<sup>34</sup> Schedule 8.1, Section D.8, of the RAA provides in relevant part:

In the case of load reflected in the FRR Capacity Plan that switches to an alternative retail LSE, where the state regulatory jurisdiction requires switching customers or the LSE to compensate the FRR Entity for its FRR capacity obligations, such state compensation mechanism will prevail. In the absence of a state compensation mechanism, the applicable alternative retail LSE shall compensate the FRR Entity at the capacity price in the unconstrained portions of the PJM Region, as determined in accordance with Attachment DD to the PJM Tariff [rest-of-pool or “RTO” RPM clearing prices], provided that the FRR Entity may, at any time, make a filing with FERC under Sections 205 of the Federal Power Act proposing to change the basis for compensation to a method based on the FRR Entity’s costs or such other basis shown to be just and reasonable.

See Shanker Direct, pp. 10-11.

<sup>35</sup> *In re American Electric Power Service Corporation*, FERC Docket No. ER11-2183-000, Entry ¶ 12 (Jan. 20, 2011). The fact that FERC already has rejected AEP Ohio’s complaint that the Commission lacked authority to set the state compensation mechanism makes obvious how empty AEP Ohio’s threats

fixes the charge that AEP Ohio and PJM must assess under the RAA for AEP Ohio's capacity utilized by CRES providers.

"Resetting" capacity charges to RPM-based prices is neither complicated nor extraordinary. AEP Ohio has made clear in prior filings in this docket that restoration of RPM-based capacity pricing is a simple matter of notifying PJM of the applicable state compensation mechanism.<sup>36</sup> According to AEP Ohio, no state tariff filing is necessary because "Section D.8 of Schedule 8.1 of PJM's RAA is the basis for a State commission such as the PUCO to adopt a SCM. . . . There has been no PUCO-approved tariff required in order to implement the SCM that has been in place for more than a year. There is no reason to conclude now that a State tariff is required."<sup>37</sup> According to AEP Ohio, once PJM is notified of the applicable state compensation mechanism, "PJM has advised AEP Ohio that under RAA Schedule 8.1, Schedule D.8 [sic], no additional filing with [the FERC] is necessary to incorporate the Ohio state compensation mechanism as an appendix to the RAA. PJM further stated that it will put CRES Providers and other market participants on notice of the AEP Ohio capacity rate via a posting of the rate on PJM's web site."<sup>38</sup>

Thus, in order to comply with the Feb. 23, 2012 Entry, AEP Ohio need only notify PJM that the applicable state compensation mechanism is again based on the RPM market price for the 2011/2012 delivery year, as previously mandated by the Dec. 8, 2010 Entry, and as has been in place throughout AEP Ohio's previous ESP. The applicable rate, based on a final RPM zonal

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are to "pursue all possible remedies at law before any available federal and state court or administrative body, including the FERC, federal courts, and state courts." Motion, p. 5.

<sup>36</sup> See Memorandum of Ohio Power Company in Opposition to Industrial Energy Users-Ohio's Motion and FirstEnergy Solutions' Objections/Request for Relief, filed Jan. 4, 2012, at p. 15.

<sup>37</sup> *Id.*

<sup>38</sup> *Id.*, Attachment at p. 2 (Dec. 22, 2011 Letter from Steven J. Ross, counsel for AEP to Kimberly D. Bose, FERC). See also Motion, pp. 18-19.

price of \$116.15/MW-day for the 2011/2012 delivery year, has been charged by PJM as recently as December 2011 to all shopping customers and to most shopping customers in January and February 2012. If AEP Ohio is unwilling to provide this notice, then this Commission should provide the required notice directly to PJM.

**V. AEP Ohio Is Not Entitled to Recover Its Full Embedded Costs Under the PJM RAA.**

AEP Ohio devotes a substantial portion of its Motion to arguing that it is entitled to recover the full embedded costs of its generating facilities through the state compensation mechanism.<sup>39</sup> However, the Commission sets the state compensation mechanism pursuant to the PJM RAA, and nothing in the RAA authorizes AEP Ohio or any other Load Serving Entity (“LSE”) to recover its full embedded cost of capacity.<sup>40</sup> The state compensation mechanism must reflect market pricing and, if cost-based, cannot reflect more than short-run marginal costs, as explained in further detail below.

**A. Fixing the state compensation mechanism at any price other than an RPM market-based price is anticompetitive and unreasonable.**

Under PJM’s RAA and the Fixed Resource Requirement (“FRR”), AEP Ohio is obligated to procure its share of a regional capacity requirement within PJM.<sup>41</sup> The FRR election allows eligible LSEs, such as AEP Ohio, the option to submit an FRR capacity plan to meet a fixed capacity requirement as an alternative to participating in the RPM auction for

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<sup>39</sup> Motion, pp. 9-14.

<sup>40</sup> Shanker Direct, p. 9.

<sup>41</sup> See Shanker Direct, p. 5.

capacity.<sup>42</sup> AEP Ohio has voluntarily made the FRR election since the inception of RPM and has continued this election through the 2014/15 delivery year.<sup>43</sup>

The FRR alternative accommodates retail switching.<sup>44</sup> In accordance with the PJM RAA, AEP Ohio's capacity charges have been established by the Commission at a level equal to the current respective delivery year (i.e., June 1, 2011-May 31, 2012) clearing price for the Regional Transmission Organization ("RTO") as established in PJM's RPM.<sup>45</sup> The RAA also allows any eligible LSE (such as CRES providers) within an FRR designated area that has retail access to establish its own FRR plan.<sup>46</sup> However, such an election can only occur after the existing FRR plan for the region (e.g., AEP Ohio's FRR plan) ends.<sup>47</sup> As a result, LSEs, such as FES and other suppliers, are "locked in" to purchasing capacity from AEP Ohio through May 31, 2015.<sup>48</sup>

Capacity rates in PJM normally are set via the RPM auction process that constitutes PJM's capacity market.<sup>49</sup> All supply offers are subject to price caps.<sup>50</sup> These price caps mean that offers must be based on a resource's short run marginal costs, or "avoidable" costs.<sup>51</sup> Specifically, suppliers' caps are established at the avoided cost rate (the "ACR"), as specified in

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<sup>42</sup> See PJM Reliability Assurance Agreement, Schedule 8.1, Sec. D ("FRR Capacity Plan").

<sup>43</sup> Shanker Direct, p. 6.

<sup>44</sup> Shanker Direct, p. 6.

<sup>45</sup> See Dec. 8, 2010 Entry.

<sup>46</sup> Shanker Direct, p. 7. A CRES provider must meet certain requirements, including both the identification of adequate reliability resources and notice. Shanker Direct, p. 6.

<sup>47</sup> Shanker Direct, p. 7.

<sup>48</sup> Shanker Direct, p. 7.

<sup>49</sup> Shanker Direct, p. 7.

<sup>50</sup> Shanker Direct, p. 8.

<sup>51</sup> Shanker Direct, p. 8.

section 6.8 of Attachment DD of the PJM tariff.<sup>52</sup> Suppliers cannot make offers at their full embedded costs.<sup>53</sup>

The purpose of the price caps is to replicate the offer and bid behavior that would be expected in a competitive environment.<sup>54</sup> In the absence of market power, individual suppliers would be expected to offer supplies at their short-term “to go” costs.<sup>55</sup> This would represent the costs that could be avoided by either retiring or “mothballing” an existing unit for a year.<sup>56</sup> The ACR values used in the PJM auction process reflect an attempt to administratively set the determination of such “to go” costs, allowing not only for typical marginal short-term costs, but also allowing for the types of incremental investment that would be expected with maintaining large, capital intensive projects.<sup>57</sup>

The RAA does not authorize AEP Ohio or any supplier participating under the FRR alternative to recover its full embedded cost of capacity.<sup>58</sup> The RAA does address default pricing options in FRR regions for LSEs operating under retail access programs to receive some capacity payments from migrating load.<sup>59</sup> In the absence of a specific state designation, this capacity payment for migrating load defaults to the PJM RPM auction results for the unconstrained RTO area.<sup>60</sup> As provided in Schedule 8.1, Section D.8, of the RAA:

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<sup>52</sup> Shanker Direct, p. 8.

<sup>53</sup> Shanker Direct, p. 8.

<sup>54</sup> Shanker Direct, p. 8.

<sup>55</sup> Shanker Direct, pp. 8-9.

<sup>56</sup> Shanker Direct, p. 9.

<sup>57</sup> Shanker Direct, p. 9.

<sup>58</sup> Shanker Direct, p. 9.

<sup>59</sup> Shanker Direct, p. 9.

<sup>60</sup> Shanker Direct, p. 9.

In the case of load reflected in the FRR Capacity Plan that switches to an alternative retail LSE, where the state regulatory jurisdiction requires switching customers or the LSE to compensate the FRR Entity for its FRR capacity obligations, such state compensation mechanism will prevail. In the absence of a state compensation mechanism, the applicable alternative retail LSE shall compensate the FRR Entity at [rest-of-pool or “RTO” RPM clearing prices], provided that the FRR Entity may, at any time, make a filing with FERC under Sections 205 of the Federal Power Act proposing to change the basis for compensation to a method based on the FRR Entity’s costs or such other basis shown to be just and reasonable.<sup>61</sup>

Thus, the default compensation is the RTO capacity clearing price, which itself is based on mitigated avoided cost or “to go” offers.<sup>62</sup> There is no mention in the RAA of full embedded costs.<sup>63</sup> In the absence of a state compensation mechanism, the alternatives to this default rate are to have a cost basis (but certainly not full embedded costs) or other just and reasonable compensation.<sup>64</sup> AEP Ohio has recognized that the default price under the RAA is the RPM price.<sup>65</sup> Thus, restoring the default price while this docket remains open is not “pre-judging the outcome” but simply complying with the RAA and restoring all parties to the circumstances in place throughout all of AEP Ohio’s first ESP.

Therefore, the most appropriate state compensation mechanism under the RAA is to continue RPM pricing, which the Commission has adopted through the Dec. 8, 2010 Entry. If any cost basis were to be considered, it would have to be linked to marginal or “to go” cost concepts and clearing prices similar to the RPM default provision and not be based on full

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<sup>61</sup> See Shanker Direct, pp. 10-11.

<sup>62</sup> Shanker Direct, p. 11.

<sup>63</sup> Shanker Direct, p. 11.

<sup>64</sup> Shanker Direct, p. 11.

<sup>65</sup> Tr. Vol. V, pp. 746-747.

embedded cost recovery.<sup>66</sup> However, AEP Ohio's entire case, as reflected in the testimony of AEP Ohio witness Pearce and others, assumes that it is entitled to recover its full embedded costs through the state compensation mechanism. This simply is not true and, even if it were, AEP Ohio's calculations are erroneous as discussed below. Thus, the Commission lacks any legal justification to adopt AEP Ohio's claimed cost basis for the state compensation mechanism.

**B. The record does not support a capacity cost of \$255/MW-day.**

The Stipulation's capacity price of \$255/MW-day is not a cost-based or market-based figure; rather, it is a negotiated number agreed to by some, but not all, parties as part of a global settlement intended to resolve all of the inter-related issues in a complicated case.<sup>67</sup> \$255/MW-day exists solely as a product of the Stipulation negotiations and lacks any record basis. In fact, *at no time since RPM came into effect through May 2015 has the RPM price been at or above \$255/MW-day in the PJM unconstrained region.*<sup>68</sup> Thus, now that the Stipulation has been rejected, the Commission lacks a record basis to approve \$255/MW-day as an element of the state compensation mechanism.

The record evidence demonstrated that AEP Ohio's claim to have capacity costs at a level more than six times above the average market level for the term of the proposed ESP is anything but credible. Even assuming *arguendo*, that AEP Ohio is entitled to receive compensation based on its full embedded costs, which it is not, the evidence established that AEP Ohio's calculation of its purported capacity costs was significantly overstated and incorrect for at least three reasons: (1) S.B. 3 requires that all generation plant investment after January 1, 2001, be

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<sup>66</sup> Shanker Direct, p. 11.

<sup>67</sup> Tr. Vol. V, p. 740 (AEP Ohio witness Nelson admitting that \$255/MW-day is not a cost-based rate but a negotiated rate).

<sup>68</sup> Tr. Vol. XII, p. 2183.



recovered solely in the market, and AEP Ohio inappropriately seeks to recover post-2000 costs through its capacity price;<sup>69</sup> (2) AEP witness Pearce inappropriately included pre-2001 stranded costs in his capacity cost calculation;<sup>70</sup> and (3) AEP Ohio's formula rate failed to include an offset for energy revenue.<sup>71</sup> When the appropriate adjustments are made, AEP Ohio's actual capacity cost is \$57.35/MW-day.<sup>72</sup>

AEP Ohio cites to the Commission's reliance upon FES witness Schnitzer's maximum above-market price, which it adjusted upward for deferred fuel to a rate of more than \$200/MW-day.<sup>73</sup> This testimony, however, does not support adoption of a bifurcated discriminatory rate scheme with an upper rate of \$255/MW-day. First, Mr. Schnitzer's calculation of a maximum above-market rate was done solely to show a maximum level that could be economically justified, not to show what a cost-based rate would be.<sup>74</sup> It is not record evidence of a cost-based rate. **Mr. Schnitzer made clear that "there is no valid economic basis for supporting either the Stipulation capacity price of \$255 per MW-day or the \$347.97 per MW-day capacity price that AEP Ohio proposed in Case No. 10-2929-EL-UNC."**<sup>75</sup> He also explained that he was not recommending that the Commission adopt his maximum above-market rate as the capacity price.<sup>76</sup> He recommended that the Commission adopt the RPM price.<sup>77</sup>

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<sup>69</sup> Post-Hearing Brief of FirstEnergy Solutions Corp. filed Nov. 10, 2011 ("FES Brief"), pp. 61-64, 67-68.

<sup>70</sup> FES Brief, pp. 66-67.

<sup>71</sup> FES Brief, pp. 68-70.

<sup>72</sup> FES Brief, pp. 69-73.

<sup>73</sup> Motion, p. 14.

<sup>74</sup> Schnitzer Direct, p. 31.

<sup>75</sup> Schnitzer Direct, p. 30.

<sup>76</sup> Schnitzer Direct, p. 31.

<sup>77</sup> Schnitzer Direct, p. 31.

Second, an adjustment to Mr. Schnitzer's calculation for fuel costs is inappropriate. To be sure, in response to a hypothetical question posed by AEP Ohio's counsel, Mr. Schnitzer stated that such an adjustment would increase his maximum above-market capacity price to approximately \$204/MW-day – still well below AEP Ohio's proposed \$255/MW-day price.<sup>78</sup> However, Mr. Schnitzer never agreed that such an adjustment was necessary or proper. He did not agree because the fuel deferral costs claimed by AEP Ohio would be recovered elsewhere. Thus, inclusion of those fuel costs in the capacity calculation would result in double recovery.<sup>79</sup> In fact, AEP Ohio witness Nelson admitted that the fuel deferrals on which AEP Ohio based its proposed adjustments to the maximum above-market price were already going to be recovered elsewhere on a nonbyassable basis.<sup>80</sup> Accordingly, no adjustment to Mr. Schnitzer's calculation was necessary or appropriate. Mr. Schnitzer's estimate of a maximum above-market capacity price is not record evidence to support maintenance of a bifurcated, discriminatory pricing scheme.

**VI. AEP Ohio Cannot Rely On the Stipulation's \$255/MW-day Compromise or Its Claimed \$355/MW-day Full Embedded Costs.**

Although AEP Ohio pretends that the hearing record in the consolidated cases can be used to support its full embedded cost claims in this docket, that consolidated hearing was for the limited purpose of considering the Stipulation.<sup>81</sup> The Stipulation did not include the capacity cost of \$355/MW-day claimed in AEP Ohio witness Pearce's testimony. Thus, Pearce's claimed full embedded costs were not directly at issue in the hearing, and the Commission cannot rely upon that testimony to grant AEP Ohio the relief it seeks now in the Motion.

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<sup>78</sup> Tr. Vol. VII, pp. 1457-59.

<sup>79</sup> See FES Brief, p. 72.

<sup>80</sup> Tr. Vol. XII, p. 2205.

<sup>81</sup> See Sept. 16, 2011 Entry at p. 4.

Additionally, several Signatory Parties agreed that setting the capacity price based on anything other than RPM was unreasonable. These parties agreed to the Stipulation only because other purported benefits of the Stipulation made it acceptable. AEP Ohio cannot in good faith retain the one section of the Stipulation that will harm competitive markets and create a windfall for AEP Ohio, yet ignore all other “benefits of the bargain” that other parties negotiated. This simply is not fair or reasonable to customers and the other Stipulating Parties and is prohibited by the Stipulation itself, which makes clear that the Stipulation was submitted to the Commission as an indivisible whole.<sup>82</sup>

RESA witness Ringenbach testified that capacity charges to CRES providers should be RPM based.<sup>83</sup> Ms. Ringenbach also agreed that, absent the Stipulation, AEP Ohio was not entitled to charge CRES providers a capacity price of \$355/MW-day.<sup>84</sup> OEG, Constellation, and Exelon offered similar testimony.<sup>85</sup> Staff witness Choueiki testified that AEP Ohio’s proposal to use cost-based rates was “not reasonable.”<sup>86</sup> Staff also found that “to the extent there is a transparent forward capacity price available in the market, such a price should be used . . .”<sup>87</sup> Staff witness Fortney agreed with this analysis, and agreed that Staff supported pricing at RPM.<sup>88</sup> Absent the Stipulation, using anything other than RPM market-based pricing is unreasonable.

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<sup>82</sup> Stipulation, pp. 28-30.

<sup>83</sup> Tr. Vol. IV, pp. 539-540.

<sup>84</sup> Tr. Vol. IV, p. 540.

<sup>85</sup> See Tr. Vol. III, p. 236 (OEG); Tr. Vol. VI, pp. 970-971, 982-983 (Constellation); Tr. Vol. VI, pp. 1043-1044 (Exelon).

<sup>86</sup> Direct Testimony of Hisham M. Choueiki on behalf of the Staff of the Public Utilities Commission of Ohio, Staff Ex. 2 (“Choueiki Direct”), p. 4.

<sup>87</sup> Choueiki Direct, pp. 4, 7-8.

<sup>88</sup> Tr. Vol. X, p. 1707.

**VII. AEP Ohio's Proposal Is Unlawful, Discriminatory And Adverse To The Promotion Of Governmental Aggregation.**

**A. AEP Ohio's proposal is discriminatory.**

The Commission cannot adopt a bifurcated pricing scheme that is clearly discriminatory. AEP Ohio's request to maintain bifurcated capacity pricing discriminates not only amongst shopping customers, but also between shopping and non-shopping customers. SSO customers pay a wholly separate, unknown price for the same AEP Ohio capacity. AEP Ohio witness Hamrock acknowledged that there will be three different capacity prices: (1) the arbitrary \$255/MW-day price; (2) the RPM price; and, (3) the SSO price.<sup>89</sup> AEP Ohio has been unable to identify the capacity price paid by SSO customers – and, in fact, could not identify the price for capacity being charged today through the SSO or that would be charged at any time during the proposed ESP.<sup>90</sup> AEP Ohio witness Pearce, the Companies' witness on capacity cost, did not know what capacity cost would be included in the SSO's base generation rate.<sup>91</sup> Mr. Hamrock did not even know how the SSO capacity price compares to the other two prices.<sup>92</sup>

The Commission initially determined in December that this discriminatory pricing scheme was justified by other perceived benefits of the Stipulation. Yet now that the Stipulation has been rejected, there are no such benefits that outweigh the harm caused to competitive markets by AEP Ohio's pricing scheme. Thus, the Commission must reject AEP Ohio's attempt to retain one of the most anti-competitive and discriminatory components of the Stipulation.

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<sup>89</sup> Tr. Vol. VI, p. 844.

<sup>90</sup> See Tr. Vol. I, pp. 85-86 (AEP Ohio witness Roush); Tr. Vol. V, pp. 730-731 (AEP Ohio witness Nelson).

<sup>91</sup> Tr. Vol. II, p. 179.

<sup>92</sup> Tr. Vol. VI, p. 844.

**B. AEP Ohio’s “reasonable alternative” would harm governmental aggregation.**

Remarkably, although AEP Ohio wants to continue to discriminate against and among shopping customers by continuing the bifurcated capacity pricing scheme from the Stipulation, it also makes clear in its Motion that it wants to ignore the Commission’s modifications to that pricing scheme made in the December 14, 2011 Opinion and Order, as clarified by the Commission in its January 23, 2012 Entry.<sup>93</sup> AEP Ohio apparently wants the discrimination to continue at least until this proceeding is finally decided, which means customers could be harmed for several more years. AEP Ohio has no interest in accommodating governmental aggregation and again asks the Commission to reverse its earlier decisions regarding what AEP Ohio calls the “five new and enhanced obligations.”<sup>94</sup> Yet AEP Ohio signals that it is willing to bargain here: it will accept four of the five obligations but only if it can exclude mercantile customers from governmental aggregations.<sup>95</sup>

There is no procedural basis for using a motion to bargain over what terms of a Commission order, since preempted, a utility is willing to implement. Moreover, AEP Ohio lacks any reasonable basis for discriminating against mercantile customers who participate in governmental aggregation programs.<sup>96</sup> The proper course for AEP Ohio to pursue is an application for rehearing of the Feb. 23, 2012 Entry and, if that is unavailing, an appeal to the Ohio Supreme Court. In the meantime, AEP Ohio’s one obligation is to inform PJM that the

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<sup>93</sup> See Motion, p. 7. See also Motion, p. 15.

<sup>94</sup> Motion, p. 7.

<sup>95</sup> *Id.* Since AEP Ohio refers only to offering RPM-priced capacity for the first 21% of load, it is unclear whether AEP Ohio intends to withdraw RPM-priced capacity from all those commercial customers who switched on or before September 7, 2011, but exceeded the 21% queue limit.

<sup>96</sup> See R.C. § 4928.20. See also FES’s Memo. in Opp. to Ohio Power Company’s Application for Rehearing, filed Feb. 17, 2012, pp. 10-12.

state compensation mechanism for all capacity is once again derived from the current unconstrained PJM auction price.

AEP Ohio's alternative to its Revised Detailed Implementation Plan is to charge RPM-based pricing to all customers who submitted a switch request through February 23, 2012, and \$255/MW-day to all other shopping customers, including all additional governmental aggregation load.<sup>97</sup> This proposal directly conflicts with state law and policy<sup>98</sup> and with the Commission's intent expressed in the December 14, 2011 Order to accommodate governmental aggregation at least through the end of 2012. Under AEP Ohio's proposal, all governmental aggregation load from the November 2011 ballot initiatives would be denied RPM-based capacity pricing. Because those communities have not completed enrollments, using the arbitrary February 23, 2012 date is a back-door attempt to violate state policy. The commercial and industrial customers who have switched would benefit from RPM-based capacity pricing, but the bulk of residential customers would not. One expects that the protests would be as widespread and emotional as those that prompted the Feb. 23, 2012 Entry. This proposal directly conflicts with the Commission's intent, expressed in the December 14, 2011 Order, to accommodate governmental aggregation. Good sense suggests that the Commission should reject AEP Ohio's alternative proposals, all of which are designed to harm shopping and governmental aggregation.

### **VIII. AEP Ohio's Goal Is to Restrict Shopping**

Given that the \$255/MW-day capacity price that AEP Ohio seeks to charge lacks any record basis, it is obvious that the singular goal of AEP Ohio's Motion is to limit shopping. AEP Ohio has not hidden this fact. On September 7, 2011 – the very day the Stipulation was signed

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<sup>97</sup> Motion, p. 15.

<sup>98</sup> See R.C. § 4928.20

and filed – AEP Ohio’s Senior VP for Regulatory Services, Richard Munczinski, proudly announced to AEP Ohio investors and market analysts that the shopping caps resulting from the \$255/MW-day capacity price would allow AEP Ohio to continue to limit shopping: “Over those [shopping cap] percentages, if you want to shop, you pay the full cost of \$255 per megawatt day.

**So the thought and the theory is that the shopping will be constrained to the discounted RPM price.**”<sup>99</sup> AEP Ohio’s executive further clarified that **AEP Ohio “should see no more shopping than the 20%, 30%, 40% levels that are included in the stipulation.”**<sup>100</sup>

Mr. Munczinski’s admissions are well-supported. Any increase in capacity price would limit CRES providers’ ability to make competitive offers to customers, as FES witness Banks established and as even Signatory Party witnesses admitted. For example, RESA witness Ringenbach agreed that increases in capacity costs charged to CRES providers would have the effect of reducing the amount of headroom for CRES providers, which would take savings away and deter CRES providers from offering service.<sup>101</sup> She further admitted that the \$255/MW-day price arbitrarily set in the Partial Stipulation, which is four times higher than market for the term of the proposed ESP, would limit or constrain shopping.<sup>102</sup> Staff witness Fortney also testified that “if the CRES provider had to pay a higher capacity price, he would not be able to make as good an offer to the ultimate customer and so it would discourage shopping in that sense.”<sup>103</sup> Similarly, Constellation witness Fein testified that a 200% increase in capacity prices over RPM prices “would adversely affect shopping.”<sup>104</sup>

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<sup>99</sup> Banks Direct, p. 36, Ex. TCB-8 (emphasis added).

<sup>100</sup> Banks Direct, p. 36, Exh. TCB-9 (emphasis added).

<sup>101</sup> Tr. Vol. IV, p. 543, 544.

<sup>102</sup> Tr. Vol. IV, p. 544.

<sup>103</sup> Tr. Vol. X, pp. 1693-1694.

<sup>104</sup> Tr. Vol. VI, pp. 970-971.

If the Commission approves above-market capacity pricing of \$255/MW-day, this will force customers to stay with AEP Ohio's generation service – a result that mirrors Mr. Munczinski's conclusions and AEP Ohio's executives' stated goals to inhibit shopping and favor their own generation,<sup>105</sup> and a result that is in violation of state law and policy, and one that cannot be supported by the record evidence. AEP Ohio's anticompetitive proposal is unlawful and improper. It should be rejected.

## **IX. Conclusion**

For the foregoing reasons, the Commission should deny AEP Ohio's Motion for Relief.

Respectfully submitted,

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<sup>105</sup> Banks Direct, pp. 20, 35-36.



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I hereby certify that a copy of the foregoing *Memorandum Contra* was served this 29th day of February, 2012, via e-mail upon the parties below.

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