COMPANY EXHIBIT _____

BEFORE THE
PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Review of the Alternative Energy Rider Contained in the Tariffs of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company	)	Case No. 11-5201-EL-RDR

DIRECT TESTIMONY OF

DEAN W. STATHIS

ON BEHALF OF

OHIO EDISON COMPANY
THE CLEVELAND ELECTRIC ILLUMINATING COMPANY
THE TOLEDO EDISON COMPANY

DIRECT TESTIMONY OF DEAN W. STATHIS

I. Introduction and Purpose

Q. Please state your name, business address and position.

A. My name is Dean W. Stathis and my business address is 2800 Pottsville Pike, Reading, Pennsylvania 19612. I am employed by FirstEnergy Service Company as Director, Regulated Commodity Sourcing ("RCS").

Q. Describe your background and professional qualifications.

A. I have a Master's Degree in Economics from Youngstown State University. I have over 30 years of experience in the electric utility industry and have extensive experience in procurements for both physical and financial power supply, renewable products and natural gas. I have been in my current position as Director, Regulated Commodity Sourcing since June 2006. My qualifications and professional experience are more fully described in Attachment DWS-1.

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

A. I am testifying on behalf of the FirstEnergy Ohio Utilities ("FEOUs") - Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company.

Q. Please describe the purpose of your testimony.

A. The purpose of my testimony is to describe: (i) the strategic approach that RCS employs for all regulated procurements – both for power and renewable products;

(ii) the implementation process that RCS employed for the six regulated renewable procurements for the FEOUs for the period 2009-2011; (iii) the decision making/evaluation of the 2009-2011 FEOUs renewable procurement results with specific focus on the In-State All Renewable product; and (iv) the response to audit findings and recommendations of Exeter Associates ("Exeter") and Goldenberg Schneider ("Goldenberg").

In summary, I demonstrate that the actions taken by the FEOUs in purchasing Renewable Energy Credits ("RECs") were reasonable for several reasons. First, at all times the Companies followed the dictates of Ohio law; specifically, Ohio Revised Code Section 4928.64 and this Commission's orders approving the rules promulgated to implement the statute. Second, at all times the Companies' procurement actions complied with the then current terms of the Electric Security Plans that were broadly supported by many parties and approved by the Commission. Third, consistent with the statute and the Commission's orders, and as indicated in Exeter's findings, the process used by the FEOUs was open, transparent and produced a competitive price. Fourth, given the recent nature of the Ohio renewables market – and especially, the relative constraints on supply and the uncertainty about the likelihood and timing of new entrants into the market – the FEOUs' decisions to purchase RECs at the prices and dates that they were purchased were reasonable. Indeed, these decisions were all first recommended by an independent third party, Navigant Consulting, Inc. ("Navigant"), a nationally recognized consulting firm with expertise in managing renewable procurements. Further, the notion that the REC prices that the FEOUs paid should be compared to RECs prices in other states is demonstrably wrong. Any data regarding other states available at the time of the Companies' procurement decisions was limited. Further, Ohio's In-State All Renewables market had unique features which made comparisons to other states' REC prices, even to this meager data, useless.

Fifth, possible alternative courses of action, now suggested by Exeter after the fact, would not have been reasonable. For example, delaying purchase decisions would have jeopardized the Companies' ability to meet their compliance obligations. Similarly, Exeter's suggestion merely not to purchase available RECs and instead to pay a compliance payment was not an option. The Companies must comply with the law and did so. Given the undisputed fact that RECs were available for purchase, there was no basis upon which the Companies would have been unquestionably able to obtain relief from their purchase obligations. Exeter's apparent suggestion that the Companies should have violated the law must be rejected.

Other comments by Exeter should similarly be rejected. For example, the suggestion that the FEOUs should have discussed their decisions with Staff ignores that Staff, in fact, had information regarding the Companies' process and decisions available to it. Further, the idea put forward by Exeter that the FEOUs should have included better contingency planning – including planning for "high" prices or setting a maximum or limit price – was unworkable. This suggestion overlooks that there was simply insufficient market information to set such limits.

II. Strategic Approach to Regulated Procurements

Q. What does RCS do?

A. RCS is responsible for procuring power and renewable products for all of FirstEnergy's utilities.[1] A primary function of RCS is to provide oversight in the implementation of these power procurement processes, including, but not limited to: (a) supporting the procurement plans of the utilities in regulatory proceedings; (b) developing both solicitation and contract materials; (c) interacting with independent evaluators; (d) executing contracts; and (e) handling many of the operational aspects of these solicitations which require interface with Regional Transmission Operator ("RTO") personnel. Most importantly, the regulated procurement activities of RCS must conform to the provisions of the FirstEnergy Utilities Commodity Risk Management Policy ("RMP") which governs the structure and authority for managing regulated procurement risks.

Because employees of RCS represent the marketing arm of the regulated utilities, they are considered regulated marketing function employees by the Federal Energy Regulatory Commission ("FERC"). This classification requires two organizational separations from the rest of FirstEnergy Corp. and its affiliates. First, from an affiliate restrictions standpoint, RCS must be independent of, and separate from, FirstEnergy Corp.'s unregulated power supply subsidiary, FirstEnergy Solutions ("FES"). This is accomplished through separate

[1] Jersey Central Power & Light Company, Metropolitan Edison Company, Monongahela Power Company, Ohio Edison Company, Pennsylvania Electric Company, Pennsylvania Power Company, The Potomac Edison Company, The Cleveland Electric Illuminating Company, The Toledo Edison Company and West Penn Power Company.

physical work locations, separate corporate identification credentials, separate IT Systems and mandatory affiliate restrictions training administered by the Corporate Compliance Department within FirstEnergy Service Company. Secondly, RCS must be separated from the regulated transmission function of the FirstEnergy regulated affiliates to ensure that RCS does not receive non-public transmission information. This separation is similarly accomplished by separate physical work locations, separate corporate identification credentials, separate IT Systems and mandatory FERC standards of conduct training for employees across the FirstEnergy organization as administered by the Corporate Compliance Department.

Q. Describe your responsibilities as Director, RCS.

A. My primary responsibility is to oversee the power supply and renewable procurement processes and associated activities for each of the FirstEnergy utilities including compliance with all applicable policies and procedures. Under my direction and oversight, FirstEnergy utilities in Ohio, Pennsylvania, New Jersey and Maryland have conducted over seventy competitive power procurements utilizing both auction and request for proposal ("RFP") formats. As such, I am very familiar with these procurement processes, which are tailored for the specific markets in which the solicitations are conducted. For example, our procurements in the PJM Interconnection, L.L.C. ("PJM") regional transmission organization ("RTO") are tailored to be consistent with PJM rules and business practices.

Q. What are the key provisions of the RMP that RCS adheres to in conducting regulated procurements for either power supply or renewable products?

A. The key provisions of the RMP are as follows: (a) ensuring proper organizational review of regulated commodity risk exposures; (b) targeting the regulated procurement objective of minimizing the utilities' and their customers' exposure to volume and price risk; (c) ensuring regulated procurements are competitive and do not give preferential treatment to any bidder; (d) properly recording and executing transactions; and (e) ensuring that regulated procurement activities are conducted ethically and in accordance with all laws, affiliate restrictions and standards of conduct. I will expand on each of these points below.

Q. What are "regulated commodity risk exposures"?

A. Regulated commodity risk exposures are primarily: 1) the volume and price risk associated with managing the power supply and renewable requirements for non-shopping customers of the FirstEnergy utilities; and 2) the prudent management of certain regulated non-utility generation contracts on behalf of ratepayers. RCS has the primary responsibility for managing these risks on behalf of the FirstEnergy utilities.

Q. What is "volume and price risk"?

A. Volume risk includes the uncertainty around the ability of the FirstEnergy utilities to fulfill the volume requirements necessary to satisfy both their hourly power supply and renewable obligations for non-shopping customers. Price risk includes the uncertainty around the ability of the FirstEnergy utilities to obtain competitive prices to fulfill power and renewable obligations as well as managing associated commodity price volatility.

Q. How does RCS ensure that regulated commodity risk exposures receive proper organizational review?

A. As reflected in the RMP, various FirstEnergy departments assist RCS in managing regulated commodity risk exposure. For example, the Enterprise Risk Group ("ERG") within FirstEnergy Service Company ensures compliance with applicable policies and reviews the credit qualifications of potential bidders. The Legal Department within the FirstEnergy Service Company ensures supplier agreements have the necessary safeguards to protect utility interests. The Rates Department within the FirstEnergy Service Company ensures incurred commodity costs are properly reflected in rate calculations as one of its various contributions to the overall RFP process. Finally, the Business Services/Accounting groups within the FirstEnergy Service Company ensure that these commodity and commodity procurement costs are properly booked to the appropriate regulated account. This team approach of managing regulated commodity risk is followed for all of the FirstEnergy utilities.

Q. How does RCS manage exposure to volume and price risk?

A. A primary vehicle to manage volume and price risk is through well-structured power and renewable product competitive solicitations that contain contingency plans or allow for contingency actions in the event of unforeseen market conditions. All regulated procurements seek to obtain the lowest cost supply at the time of the solicitation and achieve the targeted volume of power or renewable products. However, it may not be possible to always achieve these twin goals. In instances where winning suppliers default or if solicitation targets are not achieved, contingency actions may need to be implemented. Contingency plans also may need to address procurements where supply conditions in a particular market are thin or limited either in the near term or for the foreseeable future.

Q. Are contingency plans always written documents?

A. No. The plans are normally a set of shared expectations of the internal review group. These are discussed and agreed to ahead of the implementation of the solicitation process, but can be augmented as more information becomes available throughout the solicitation process. Contingency plans are not always reduced to writing for each RFP.

In the case of the RFPs at issue, while a contingency plan was not incorporated into the RFP documents or separately reduced to writing, a plan was established prior to the initial RFP and acted upon during the 2009 through 2011 compliance period. RCS and the internal review group determined that, if necessary, the FEOUs would implement contingencies consistent with previous competitive procurement solicitation contingency plans. Most notable among these planned contingencies was that the FEOUs would address potential product volume shortfalls by issuing additional RFPs for unfilled volumes and by attempting to access the market through brokers or otherwise. Consistent with plans in other procurements, the plan with regard to the RFPs acknowledged that there may be some contingencies that might not be specifically contemplated beforehand. As was the case with other FirstEnergy competitive procurement contingency plans, the RFPs contemplated that if an unforeseen contingency arose, RCS and other FirstEnergy departments would consider next steps in light of the conditions in the market and the results of the solicitation to arrive at a course of action that would achieve an outcome that would be in the best interests of the FEOUs and their customers.

Q. How does RCS ensure that any bidder will not receive undue preference in any regulated competitive solicitation?

A. The RMP states that "no affiliate or non-affiliate will receive undue preference during any stage of the process." Consequently, RCS incorporates the following four principles into each procurement process:

- **transparency**: ensuring the competitive solicitation is open to all qualified bidders and is fair;
- **definition:** ensuring the product to be procured is well understood by bidders and precisely defined;
- **evaluation**: ensuring evaluation criteria--both price-based and non-price-based--are standardized and applied equally to all bids and bidders; and
- **oversight**: using an independent third party to design, administer and evaluate the solicitation prior to the Company's selection.

RCS has consistently applied these principles in its power and renewable solicitation since RCS was formed in June 2006.

Q. What key provisions of the RMP does RCS follow with respect to transactional execution and recording?

A. The RMP specifies which commodities RCS personnel can purchase and sell. The RMP also requires that contracts only be executed after the ERG approves counterparty creditworthiness and requires that contracts be executed by personnel with the appropriate level of signature authority. Moreover, the RMP requires that RCS maintain accurate logs and records of all commodity risk management transactions and prepare and maintain proper documentation of transactions.

Q. How does RCS ensure its employees behave ethically and observe all laws, codes and standards of conduct?

A. RCS is required to ensure that all appropriate employees receive the necessary information and training in the application of the RMP and that those employees annually confirm by signature that they are in compliance with its provisions. Moreover, all RCS employees are subject to the Ethical Business Practices section of the RMP, which address, among other things, fraud, market manipulation, deception, and improper business conduct. In addition and separate from the RMP, the employees of RCS are required to participate in the FirstEnergy Corporate Compliance Department annual mandatory anti-market manipulation training, affiliate restrictions training, and FERC standards of conduct training.

Should employees have any concerns as to illegal or unethical conduct of any kind, the employee may contact the Employee Concerns Line 24-hours a day, 7 days a week to report a violation or suspected violation or any other illegal or unethical conduct.

Q. Did RCS adhere to the key provisions of the FEOUs RMP in conducting the six regulated renewable procurements in the 2009-2011 timeframe?

A. Yes. With respect to the five key provisions of the RMP, RCS complied as follows:

- Involved Rates, Legal, ERG, and Business Services/Accounting in determining rate calculations and adherence to regulatory obligations, supplier agreement structure, credit qualifications and accounting treatment, respectively.
- Developed competitive solicitation objectives of least cost pricing of available supply designed to satisfy the Ohio Renewable Energy Standards and invoked contingency plans for In-State Solar, All States Solar and In-State All Renewable categories (details of which are more fully described in Section IV).
- Ensured that no affiliate or non-affiliate received any undue preference, hired an independent evaluator (Navigant), and had Navigant design and oversee open and transparent solicitations, each with well defined renewable product definitions and standardized evaluation criteria.

- Executed transactions with creditworthy suppliers according to RMP limits of authority and recorded transactions.
- Observed that RCS personnel met all ethical standards of RMP and were up to date on all mandatory compliance training requirements.

Q. Did RCS make the RMP available to Exeter?

A. Yes, the appropriate RMPs (each year the ERG updates the RMP for certain changes to reflect organizational/policy changes) were forwarded to Exeter.

Q. Did Exeter find any inconsistencies between the RMP and the way RCS conducted any six of their renewable procurements?

A. The Exeter Report did not find any issues or inconsistencies with RCS' procurement activity and the RMP.

III. Renewable Procurement Implementation Process

Q. What procurements appear to be at issue in this case?

A. Over the 2009 through 2011 audit review period, FEOU conducted six RFP procurements which were reviewed by Exeter. The RFPs and products sought were as follows:

RFP #	**RFP Issuance**	**In-State Solar**			**In-State All Renewable**			**All States Solar**			**All States All Renewable**		
		2009	**2010**	**2011**	**2009**	**2010**	**2011**	**2009**	**2010**	**2011**	**2009**	**2010**	**2011**
1	July 2009	X	X	X	X	X	X	X	X	X	X	X	X
2	September 2009	X	X	X	X	X	X	X	X	X			
3	July 2010		X	X		X	X		X	X			X
4	March 2011		X										
5	August 2011			X						X			
6	September 2011*[2]			X			X						

Per the Exeter report, Exeter takes exception with RFP1, RFP2 and RFP3 for the In-State All Renewable product.

Q. **What steps were involved in implementing the six renewable procurements and how did RCS and Navigant allocate responsibility for these steps?**

A. There were sixteen major process steps in implementing each of the six renewable procurements. These steps are listed below. The lead entity for that process step is shown in parenthesis.

- Introduce Navigant to procurement background and objectives (RCS)
- Identify web address to be used in procurement (RCS)
- Website design and layout (Navigant/RCS)
- Develop Master Supplier Agreement (RCS/FE Legal)
- Identify RCS staff to be Subject Matter Expert for Navigant (RCS)
- Develop Bid Rules, Communication Protocols and Application Forms (Navigant)
- Conduct Market Research and Develop Distribution List (Navigant)
- Finalize Procurement Calendar and announce RFP (Joint Navigant/RCS)

[2] The agreement term was for the ten year period from 2011 through 2020.

- Administer FAQ process (Navigant)
- Hold Webinar (Navigant)
- Administration of Phase I Evaluation of Qualifying Applications (Navigant)
- Administration of Phase II Ranking of Bid Proposals (Navigant)
- Selection Recommendations of Phase II Bid Proposals (Navigant)
- Procurement decision (RCS)
- Contract Executions and/or Contingency event (RCS)
- Document Process and Results (Navigant)

Company witness Daniel Bradley of Navigant will elaborate on the steps that Navigant was responsible for in these renewable procurements. I will discuss the steps that RCS led or co-led with Navigant in more detail below.

Q. What steps did RCS follow in implementing the six renewable procurements from 2009-2011?

A. There were essentially eight steps RCS followed to implement these six regulated procurements. First, once Navigant was selected as the independent evaluator, RCS arranged a series of meetings with Navigant to discuss the procurement parameters, proposed timing, introduce RCS support staff, discuss regulatory requirements underlying the procurement and other pertinent information that Navigant needed to prepare for the solicitations. Second, a unique regulated FirstEnergy website was created to be used to interface with potential suppliers and the public. Third, Navigant and the FEOUs jointly designed the RFP website and layout. Fourth, the FEOUs' supplier agreement was reviewed with Navigant.

Fifth, RCS identified specific individuals that would be used as subject matter experts to assist Navigant in responding to Frequently Asked Questions ("FAQs"). Sixth, RCS and Navigant agreed to a specific calendar of procurement event dates that were subsequently posted on the web page that identified when certain procurement actions would occur. Seventh, once RFP results were known, RCS led a discussion with an internal review team (as described in Section IV below) to review Navigant's recommendations and make procurement decisions. Lastly, procurement decisions were implemented resulting in either approved and executed contracts, a contingency event, or both.

Q. Did RCS follow these steps in implementing the six regulated renewable procurements from 2009-2011?

A. Yes. I will address each of the RCS controlled implementation steps separately including the selection of the independent evaluator.

Q. How was Navigant selected to be the independent evaluator?

A. Navigant was selected from competitive vendor selection processes that were overseen by the Supply Chain ("SC") Department within FirstEnergy Service Company. This department is responsible for ensuring vendor products and services purchased by all of the FirstEnergy Companies are done so in a fair and competitive manner. SC solicited input from RCS on service scope and identities of firms that could provide independent evaluator services to the FEOUs and the overall renewable market. With input from RCS, SC prepared a solicitation package for interested bidders and held solicitations in May 2009 and again in

November 2010, and, based upon those solicitations, SC selected Navigant as the independent evaluator.

Q. How did RCS complete the first step – briefing Navigant on the renewable solicitation background and procurement objectives – in the implementation process?

A. Once Navigant was under contract, and for each of the subsequent six RFPs held from 2009-2011, a series of meetings – via conference calls – was held with representatives of Navigant to discuss the Ohio renewable energy requirements under SB 221 and the status of the FEOUs' annual 2009-2011 compliance obligations with respect to the mandated four procurement products: (a) All States Solar; (b) In-State Solar; (c) All States All Renewable; and (d) In-State All Renewable. Besides discussing Solar Renewable Energy Credit/Renewable Credit ("SREC/REC") compliance obligations for each product, RCS and Navigant discussed a number of other issues that were important to implementing the RFP. These included: (a) website design; (b) bidder presentation material; (c) webinar logistics; and (d) time reasonably needed to complete Phase I (pre-bidder qualification), Phase II (bid proposal evaluation) components of the first RFP and to determine any lessons learned from the prior solicitation, if applicable.

Q. How did RCS complete step two – website identification?

A. Since it was both cost effective and more efficient for Navigant to use a FEOU-sponsored internet web address, the FEOUs established a separate internet web address for each of the six FEOUs' renewable procurements. These links were accessible either in the announcements concerning these procurements or potential suppliers could access the procurement website via the FirstEnergy Corporate portal.

Q. How did RCS complete step three, website design and layout – with Navigant?

A. RCS and Navigant reviewed various key design components of a renewable website. These included features such as home page formatting, web page location of links to procurement topics, and links to external renewable websites. Navigant then selected a final website design for all the renewable procurements that were used for all six solicitations from 2009-2011.

Q. How did RCS complete step four – reviewing and posting of the Supplier Master Agreement ("SMA")?

A. The SMA used in all agreements was developed by the FEOUs. The SMA was a non-negotiable agreement with uniform terms and conditions for all bidders that enabled the comparison of bids to be based solely on price within each RFP. Before posting to the procurement website and before each bidder webinar, the SMA was reviewed with Navigant to clarify the main provisions and highlight any changes made to the SMA for any of the six procurements held during the 2009-2011 timeframe.

Q. How did RCS complete step five – identifying subject matter experts for use by Navigant in answering FAQs by suppliers?

A. RCS held conference calls with Navigant prior to each solicitation. One purpose of these calls was to identify a subject matter expert for topics that could be the subject of an FAQ, and specifically: (a) general; (b) SMA; (c) rates; (d) credit; (e) PJM Generator Attribute Tracking System ("GATS"); and (f) billing and invoicing. All other categories – bid rules, communication protocols, web design oversight, FAQ process - were under Navigant's control and therefore were addressed by Navigant when FAQs were submitted.

Q. How did RCS and Navigant complete step six – finalizing procurement calendar and announcing the RFP?

A. Both RCS and Navigant laid out time requirements for completing process steps under their respective control. Both entities exchanged information on other known procurements in the renewable and commodity markets to ensure dates chosen did not overlap with other major procurements and allowed enough time for thoughtful evaluation of procurement information – particularly Phase I and Phase II process steps. Once approved, the calendar was posted to the website and Navigant managed the procurement accordingly.

Each RFP was announced to the market by a press release from the FEOUs and by email communication from Navigant through an extensive e-mail list developed specifically for the FEOU's RFPs as is more fully detailed in witness Bradley's testimony.

Q. How did RCS complete steps seven – procurement decisions – and eight – contract execution and / or contingency event implementation?

A. Section IV below describes the procurement decisions for the renewable procurements discussed herein for the 2009-2011 period along with contract execution and where applicable contingency event implementation steps were taken.

Q. Did Exeter review the RFP process employed by the FEOUs?

A. Yes.

Q. What did Exeter conclude?

A. As outlined in Findings 1-6 on page 12 of its report, Exeter concluded that " The RFPs issued by the FirstEnergy Ohio utilities are reasonably developed and do not appear to incorporate any provisions or terms that could be assessed to be anti-competitive."

IV. Evaluation and Decision Making of Phase II Results

Q. Please describe the general regulatory backdrop that served as the basis for the FEOUs renewable procurement decision making.

A. The FEOUs' Electric Security Plan ("ESP1"), which was the result of a broad based stipulation among interested parties and approved by the Commission in March of 2009, contained provisions that addressed renewable energy resource requirements. Specifically, ESP1 required that renewable energy resource requirements for the period January 1, 2009 through May 31, 2011 would be met using an RFP process. That process would be separate from the process used to procure standard service offer ("SSO") load. Additionally, at the request of other parties, the Companies agreed that any waiver of the alternative energy resource requirement would be limited to those waivers identified in Ohio Revised Code Section 4928.64. As a result of the ESP1 negotiations, the Companies were expected to comply with the mandates and not rely on waivers, other than those included in that statute, as a means to avoid compliance.[3]

Q. What were the primary renewable procurement components agreed to by the parties in ESP1?

A. The primary renewable components were 1) a Request for Proposal ("RFP") format separate from the FEOUs auction for SSO load, 2) a performance period from January 1, 2009 through May 31, 2011, to satisfy renewable energy resource requirements, 3) a by-passable rider for the collection and subsequent recovery of prudently incurred costs for renewable products during the three year term and 4) any waiver of the alternative energy resource requirements shall be limited to those waivers identified in Section 4928.64 Revised Code.

Q. Did the FEOUs consider beginning their renewable procurements before the ESP1 renewable plan was approved in March 2009?

A. No. It was not viewed as reasonable to either commence a procurement process when a stipulation addressing the issue was pending before the Commission or to

[3] The ESP1 Stipulation also required the Companies to work with certain parties to implement a residential REC purchase program.

begin incurring procurement costs without some understanding about the specific approval mechanism for the recovery of such costs. Stepping out into the market ahead of having a Commission approved plan that included a cost recovery mechanism may have exposed the FEOUs to the risk of stranded procurement costs and/or renewable procurement provisions inconsistent with those ultimately approved in ESP1.

Q. What were RCS' baseline procurement expectations and contingency plan prior to the issuance of RFP1?

A. Because the regional renewable markets were still in the early stages of development, RCS expected that it would hold 3 RFPs for all 4 renewable products – one per year. RCS believed that the 2009 RFP would seek 100% of 2009 compliance obligations, and some percentage of 2010 and 2011; the 2010 RFP would seek the remaining percentages needed for 2010 compliance and some additional percentage of 2011; and the 2011 RFP would seek the residual percentages, per product, needed for 2011 compliance. Initially, RCS believed that this purchasing strategy (assuming renewable supply was adequate) would bring some diversity to procurement pricing. In the event the supply and demand dynamics proved inadequate, RCS would employ a contingency plan that it had previously used in past power procurements: namely, to issue an additional RFP in the event of insufficient supplier interest or to pursue spot supplies (broker market supply in this case) if enough time was not available to conduct an additional RFP.

Q. Please describe the general framework used for the FEOUs' procurement decisions, including the distinction between Phase I and Phase II RFP results.

A. Many regulated renewable and power supply procurements are conducted by independent evaluators using a two-phased process. Such a process was employed for the FEOUs' RFPs. In Phase I, the independent evaluator collects certain financial and credit information from prospective bidders to ensure that these bidders meet the credit and financial standards set forth in the bidding rules. The independent evaluator controls Phase I and may use regulated utility personnel in an advisory capacity on an as needed basis. Results from Phase I, – *i.e.,* the number and identity of the bidders – are shared with regulated utility personnel. In Phase II, the independent evaluator collects and tabulates the bid results of the bidders qualified in Phase I. The independent evaluator then shares with the regulated utility personnel those bid results and sets forth its recommendations in spreadsheet format.

Here, once Phase II results and recommendations are received from the independent evaluator, the FEOUs used a two-step approach to arrive at specific procurement decisions. First, RCS and an internal regulated review team (comprised of members from ERG, the Rates Department, and the Legal Department) met with Navigant to review this information and understand, among other things, the bid rankings, number of qualified bids and recommendations from Navigant. Secondly, RCS then convened a separate internal meeting with the same regulated internal review team to review: (a) independent broker market price and liquidity information (if available); (b) its alignment, or lack thereof, with Navigant's recommendations; and (c) any need for contingency event actions in light of Navigant's recommendations. A consensus decision was then reached. From time to time, I reviewed the procurement decision(s) with my direct supervisor before contract execution and/or contingency event implementation.

Q. Did all of the FEOUs' first six RFPs solicit In-State All Renewable RECs?

A. No. As noted, only RFPs 1, 2, 3 and 6 sought those types of RECs for 2009, 2010 and 2011, as applicable.

Q. Please summarize the results of RFP1 as it relates to the In-State All Renewable product.

A. Phase II results for RFP1 were received from Navigant on August 12, 2009. Information from Navigant and feedback RCS telephonically received from brokers indicated that the In-State All Renewable market was extremely thin and still developing and that no supplier certification applications had been approved by the PUCO – one of the necessary conditions to deliver RECs under the Alternative Energy Portfolio Standard ("AEPS"). Bids received for the In-State All Renewable category made up only 35%, and 45% of the 2009 and 2010 RFP desired amounts, respectively. No bids were received for 2011 In-State All Renewable supply. RFP1 results are shown below.

Table 2009 RFP 1 Results (July 2009)

REC Category	2009 REC Compliance Obligations (1)	2009 RFP Desired RECs (1)	RECs Bid	Navigant Recommended RECs	Actual REC Purchased	Cumulative % of Obligations Purchased	Market Liquidity
In-State Solar	943	1,040	0	0	0	0.0%	C
In-State All Renewable	57,965	63,960	20,000	20,000	20,000	35%	C
All States Solar	943	1,040	0	0	0	0.0%	C
All States All Renewable	57,964	63,960	87,360	87,360	87,360	151%	A

REC Category	2010 REC Compliance Obligations (1) (2)	2010RFP Desired RECs (1)	RECs Bid	Navigant Recommended RECs	Actual REC Purchased	Cumulative % of Obligations Purchased	Market Liquidity
In-State Solar	3,206	2,600	0	0	0	0.0%	C
In-State All Renewable	111,477	127,400	50,000	50,000	50,000	45%	C
All States Solar	3,169	2,600	0	0	0	0.0%	C
All States All Renewable	111,476	127,400	104,000	104,000	104,000	93%	A

REC Category	2011 REC Compliance Obligations (1) (2)	2011 RFP Desired RECs (1)	RECs Bid	Navigant Recommended RECs	Actual REC Purchased	Cumulative % of Obligations Purchased	Market Liquidity
In-State Solar	7,026	3,250	0	0	0	0.0%	C
In-State All Renewable	176,156	105,083	0	0	0	0.0%	C
All States Solar	5,447	3,250	0	0	0	0.0%	C
All States All Renewable	176,155	105,084	105,084	105,084	105,084	60%	A

Market Liquidity
C = Constrained (Less than desired number of bids or no significant broker market offers / recorded transactions)
A = Readily Available (Adequate bids or significant broker market offers / recorded transactions)

Notes:

(1) REC compliance obligations do not match RFP desired RECs due to timing differences between the RFP date and the final obligation requirements, which were based on actual sales volumes. RFP desired RECS were based on forecasted sales volumes.
(2) 2010 and 2011 Compliance Obligations include the PUCO ordered REC Shortfall carryover from the prior year.

Q. How many bidders qualified and submitted offers for In-State All Renewable supply in RFP1?

A. Only 1 bidder qualified and submitted offers for this product in RFP1.

Q. During the RFP1 process, and in light of the number of bidders for In-State All Renewable supply, did RCS have concerns regarding the availability of resources to fulfill the FEOUs In-State All Renewable obligations?

A. Yes. Since this was the FEOUs' first RFP for these products, there were concerns about how slowly the market was developing for the In-State All Renewable product (as well as the two solar products). As described above, prior to the issuance of RFP1, RCS expected that it might need to conduct one RFP each year for all four products given the uncertainty that existed on market supply. RFP1 confirmed that very little certified supply was available in 2009 for the In-State All Renewable category.

Q, In light of these results, did RCS deploy its contingency plan as part of its decision making process?

A. Yes. Given these results, the FEOUs decided that implementing a contingency event to re-enter the market with a second RFP within 2009 for the three products with supply concerns would be appropriate. This would allow RCS to learn more about these individual markets and to uncover any available supply potentially missed from RFP1. Because the 2009 target for All States All Renewable resources was over-subscribed and the excess could be banked and applied to 2010 compliance obligations, there was no need to include that product in RFP2. With regard to the three other products, however, the FEOUs recognized that they might need to consider filing a force majeure application if the RFPs proved insufficient to obtain the necessary number of RECs.

Q. In addition to the contingency event, what decisions were made with respect to the In-State All Renewable bids received from RFP1?

A. Consistent with both of Navigant's recommendations and FEOUs' internal review, a contract was executed with the winning supplier for this product on August 20, 2009.

Q. Please summarize the results of RFP2 as it relates to the In-State All Renewable product.

A. Phase II results for RFP2 were received from Navigant on October 15, 2009. This solicitation sought only the supply-constrained products from RFP1 – In-State Solar, In-State All Renewable, and All States Solar for the 2009-2011 timeframe. For the In-State All Renewable product, the FEOUs purchased 37,965 RECs, and when combined with the RECs from RFP1, held enough supply to satisfy 100% of their 2009 compliance obligation. Additionally, the FEOUs procured 31,800 and 26,084 of 2010 and 2011 In-State All Renewable supply, respectively. These purchases, when combined with RFP1 procurements, resulted in the FEOUs achieving 73% and 15% of their respective 2010 and 2011 compliance target for this product. Results for RFP2 are shown below.

Table 2009 RFP 2 Results (September 2009)

REC Category	2009 REC Compliance Obligations (1)	2009 RFP Desired RECs (1)	RECs Bid	Navigant Recommended RECs	Actual REC Purchased (2)	Cumulative % of Obligations Purchased	Market Liquidity
In-State Solar	943	1,040	0	0	0	0.0%	C
In-State All Renewable	57,965	43,960	43,960	43,960	37,965	100%	C
All States Solar	943	1,040	49	49	49	5.2%	C
All States All Renewable	57,964	0	0	0	0	151%	N/A

REC Category	2010 REC Compliance Obligations (1) (3)	2010 RFP Desired RECs (1) (4)	RECs Bid	Navigant Recommended RECs	Actual REC Purchased	Cumulative % of Obligations Purchased	Market Liquidity
In-State Solar	3,206	2,600	6	6	6	0.2%	C
In-State All Renewable	111,477	77,400	77,400	77,400	31,800	73%	C
All States Solar	3,169	2,600	208	208	208	6.6%	C
All States All Renewable	111,476	0	0	0	0	93%	N/A

REC Category	2011 REC Compliance Obligations (1) (3)	2011 RFP Desired RECs (1) (4)	RECs Bid	Navigant Recommended RECs	Actual REC Purchased	Cumulative % of Obligations Purchased	Market Liquidity
In-State Solar	7,026	3,250	1,345	1,345	1,345	19%	C
In-State All Renewable	176,156	105,084	105,084	105,084	26,084	15%	C
All States Solar	5,447	3,250	4	4	4	0.1%	C
All States All Renewable	176,155	0	0	0	0	60%	N/A

Market Liquidity
C = Constrained (Less than desired number of bids or no significant broker market offers / recorded transactions)
A = Readily Available (Adequate bids or significant broker market offers / recorded transactions)

Notes:

(1) REC compliance obligations do not match RFP desired RECs due to timing differences between the RFP date and the final obligation requirements, which were based on actual sales volumes.

(2) 2009 In-State All Renewable purchases were less than the RFP desired and Navigant recommended amount because an adjusted obligation was available during the time period the RFP was in progress. This resulted in a lower obligation requirement, and the Ohio Utilities actual purchases were reduced to meet the new lower requirment.

(3) 2010 and 2011 Compliance Obligations include the PUCO ordered REC Shortfall carryover from the prior year.

(4) 2010 & 2011 All States All Renewables were not included in RFP II due to banked RECs purchased in 2009 which were expected to be sufficient to meet the obligation requirements.

Q. How many bidders qualified and submitted offers for In-State All Renewable supply in RFP2?

A. Only 1 bidder qualified and submitted offers for this product in RFP2.

Q. During the RFP2 process, did RCS continue to have concerns about the availability of In-State All Renewable supply to fulfill the FEOUs' compliance obligation?

A. Yes. Information from Navigant and RCS' information from brokers continued to show that the supply for the In-State All Renewable product remained extremely thin and that the market was still developing. Few suppliers had certified with the PUCO – one of the necessary conditions to deliver renewable products under the newly enacted Ohio law and Commission rules and the RFP. This requirement proved to be a significant barrier to participation by suppliers.

Q. Was the fact that only one bidder qualified for In-State All Renewables in RFP1 and RFP2 inconsistent with the information available to RCS?

A. No. As Attachment DWS-2 shows, and confirmed in discussions with Navigant, the amount of available supply from qualifying facilities receiving certifications from the PUCO and therefore able to supply In-State All Renewable products was extremely limited during the time frame of RFP1 and RFP2. This was also consistent with the feedback that the FEOUs were receiving contemporaneously from brokers.

Q. Was the In-State All Renewable product the only product that the FEOUs had availability concerns about?

A. No. Both Solar products were exhibiting little bidder interest and market intelligence from Navigant and the broker market indicated that the situation was not likely to improve in time for the FEOUs' 2009 compliance filings. RCS recommended that, as a contingency, the FEOUs anticipate filing a force majeure application in early 2010 for both Solar categories for the 2009 Compliance Year. Such an application was subsequently filed on December 7, 2009 and approved by the PUCO on March 10, 2010.

Q. Why did RCS procure less than the Navigant recommended amount for the In-State All Renewable category for all three compliance years as part of RFP2?

A. During the RFP2 process, the non-shopping load was lowered and therefore the FEOUs' future renewable obligations were lowered from RFP1 levels. For example, the 2009 In-State All Renewable compliance target went from 63,960 RECs to a new and lower compliance target of 57,965 RECs – approximately 10% lower. More significant reductions were correspondingly experienced for the 2010 and 2011 In-State All Renewable compliance targets. Consistent with these lowered compliance obligations, RCS targeted purchase amounts were lower than the RFP2 Navigant recommended amounts for In-State All Renewable RECs.

Q. What actions did RCS take following RFP2 for the FEOUs In-State All Renewable compliance obligations?

A. Consistent with Navigant's supply outlook for this category and the concern over the uncertainties regarding in-state renewable development and risks, RCS commissioned Navigant to undertake an additional review of the In-State All Renewable market to ascertain how long supply constraints were likely to continue.

Q. When was this review delivered to the FEOUs and what did it conclude?

A. Navigant issued a report reviewing market conditions of the In-State All Renewable market to the FEOUs on October 18, 2009. The report concluded that the supply of In-State All Renewable RECs would likely remain constrained for at least another year.

Q. Following receipt of this report, what procurement actions did the FEOUs take?

A. The FEOUs took two actions. First, as discussed above, the FEOUs executed contracts for the amount of In-State All Renewable supply consistent with the revised (lower) expected compliance obligations for the 2009-2011 timeframe. On October 23, 2009, contracts were executed with the lone supplier for In-State All Renewable (as well as the successful suppliers for both solar categories). Second, it was decided to hold a third RFP in the summer of 2010 for the 2010 and 2011 requirements for In-State All Renewable, as well as both solar products.

Q. What were the prices for the bids accepted for the In-State All Renewable product in RFP1 and contingency RFP2?

A. Average prices received for the 2009 In-State All Renewable product were [redacted]/REC for RFP1 and [redacted]/REC for RFP2. Average prices received for the 2010 In-State All Renewable product were [redacted]/REC for RFP1 and [redacted]/REC for RFP2.

Q. Did the prices seem unreasonable based on what you knew at the time?

A. No. They were the result of a fair and reasonably designed process, as noted above and as described by Company witness Bradley. Further, these prices did not seem unreasonable given that 1) no In-State All Renewable REC price benchmark existed to compare procurement results, and 2) the high price spreads observed between renewable REC products having a geographic restriction and those that do not have a geographic restriction.

Q. Did you consider rejecting these bids?

A. Yes, but given the undisputed fact that RECs were available for purchase, there was no basis for the Companies to simply reject the bids. There were, in addition, a number of factors which gave rise to considerable uncertainty that the FEOUs could get additional bidders, much less bidders willing to come in at a lower price. As shown in DWS-2, the In-State All Renewable market was not exhibiting timely or significant growth in certified supply. When RFP1 bids were being considered, there were no MW of In-State All Renewable resources certified. By the time that bids were considered for RFP2, there were only

47.8MW of such facilities certified. Thus the FEOUs expected that there would be very few bidders or projects.

This was especially so given the significant economic downturn that was occurring at that time and accompanying credit constraints and other uncertainties for new projects. As discussed by Company witnesses Daniel Bradley and Robert Earle, the availability for financing projects had tightened and Ohio's share of grants under the American Restoration and Reinvestment Act of 2009 was relatively small. In short, there was virtually no evidence that supply conditions were going to significantly improve over the near term or certainly in time to meet the FEOUs obligations for 2009 and 2010. Given these uncertainties and the potential that the RECs that had been bid might be sold elsewhere if the FEOUs rejected the bids, the course of action recommended by Navigant and approved by the Companies was to accept the bids.

Q. Did the FEOUs commission Navigant to undertake a second market report before RFP3?

A. Yes. The FEOUs, seeking to maximize bidder participation for RFP3, commissioned Navigant to canvass potential suppliers of in-state RECs in an effort to solicit feedback that may lead to an improved procurement process and higher bidder participation levels.

Q. What did the Navigant report conclude and what changes were made in RFP3 based on this report?

A. Navigant delivered the report entitled "Market Research Report Regarding Supplier Views on REC RFPs" on June 3, 2010. The report concluded that bidders showed a strong preference for (a) shortening the evaluation period between bid submittal and bid selection, (b) reasonable security levels for winning bidders, and (c) a longer term contract. None of these changes could be implemented for RFP3 but the FEOUs would give these points more consideration in future renewable RFPs.

Q. Please summarize the results of RFP3 as it relates to In-State All Renewable supply.

A. Phase II results for RFP3 were received from Navigant on August 3, 2010. The 2010 and 2011 In-State All Renewable product results achieved the RFP3 desired amounts and when combined with RFP1 and RFP2 previous procurements, were enough to satisfy the FEOUs' compliance obligations for these years. Results of RFP3 are shown below.

Table 2010 RFP 3 Results (July 2010)

REC Category	2010 REC Compliance Obligations (1)	2010 RFP Desired RECs (2)	RECs Bid	Navigant Recommended RECs	Actual REC Purchased (3)	Cumulative % of Obligations Purchased	Market Liquidity
In-State Solar	3,206	3,200	175	175	175	5.6%	C
In-State All Renewable	111,477	29,676	29,676	29,676	29,676	100%	C
All States Solar	3,169	2,961	550	550	550	24%	C
All States All Renewable	111,476	0	0	0	0	93%	N/A

REC Category	2011 REC Compliance Obligations (1)	2011 RFP Desired RECs	RECs Bid	Navigant Recommended RECs	Actual REC Purchased	Cumulative % of Obligations Purchased	Market Liquidity
In-State Solar	7,026	4,109	946	946	946	32.6%	C
In-State All Renewable	176,156	150,269	155,269	150,269	150,269	100%	C
All States Solar	5,447	5,450	3,331	3,331	3,331	61%	C
All States All Renewable	176,155	49,351	242,202	49,351	49,351	88%	A

Market Liquidity
C = Constrained (Less than desired number of bids or no significant broker market offers / recorded transactions)
A = Readily Available (Adequate bids or significant broker market offers / recorded transactions)

Notes:
(1) 2010 and 2011 Compliance Obligations include the PUCO ordered REC Shortfall carryover from the prior year.
(2) 2010 All States All Renewables were not included in RFP III due to banked RECs purchased in 2009 which were expected to be sufficient to meet the obligation requirements.

(3) For the "actual REC purchased" in 2010 All States Solar category, 550 SREC were purchased however 7 of the SRECs delivered for this category were actually In-State Solar and were used for In-State Solar for the 2010 compliance period.

Q. How many bidders qualified and submitted offers for In-State All Renewable supply in RFP3?

A. Only 2 bidders qualified and submitted offers for this product in RFP3.

Q. What were the initial prices received for the In-State All Renewable products in RFP3?

A. RFP3 sought 29,676 In-State All Renewable RECs to complete 2010 compliance and 150,269 RECs to complete 2011 compliance. The 29,676 2010 RECs were priced at [redacted]/REC while the 150,269 2011 RECs were offered in two slices: 5,000 RECs offered at [redacted]/REC and the remaining 145,269 RECs at [redacted]/REC.

Q. Did the FEOUs have a concern about the supply offer for the quantity of 145,269 2011 In-State All Renewable RECs priced at [redacted]/REC? If so, was a contingency event deployed?

A. Yes. With the results of RFP3, the FEOUs now had more information about the development of the In-State All Renewable RECs market. For the first time, a second bidder submitted an offer to supply RECs. This new supplier observation was also consistent with the upcoming expiration of the 12 month constrained supply time frame that the October 2009 Navigant market report had identified almost a year earlier. Moreover, the FEOUs had information that other Ohio utilities were meeting their in-state benchmarks – an indication that the market was quite possibly beginning to expand.

Given these new in-state market developments, the FEOUs suggested the possibility of declining Navigant's purchase recommendation for the 2011 In-State All Renewable RECs at [redacted]/REC and pursuing a counter-offer in this category with the high volume supplier in hopes of reducing total cost. Navigant was instructed to examine the bid rules of the RFP to determine whether such a counter-offer on the basis of price alone was an acceptable option. Navigant reviewed the bid rules and concluded that a counter-offer of this type with a supplier was not precluded under the RFP bid rules, would not be unfair to the other bidder (because all of that bidder's RECs were going to be purchased), and would be appropriate. The FEOUs then instructed Navigant to make a counter-offer with the high volume supplier to see if the FEOUs could reach an agreement for a lower price for this product in 2011. This effort was successful, resulting in a lower price for the 2011 In-State All Renewable product. The lower price for 2011 In-State All Renewable supply saved the FEOUs and their customers approximately $24 million.

Q. Did the FEOUs seek any In-State All Renewable Supply as part of either RFP4 or RFP5?

A. No. RFP4 and RFP 5 were contingency events designed to seek additional In-State Solar and All State Solar supplies. When taken together, these RFPs, along with additional quantities of SRECs purchased in the broker market, were successful in achieving 100% compliance for 2010 and 2011 All States Solar. Significant progress was also made with the 2010 and 2011 In-State Solar category, but not enough to prevent the filing of a second force majeure application for 2010 In-State Solar. The FEOUs filed a force majeure application which was subsequently approved by the PUCO on August 15, 2011.

Q. Please summarize the results of RFP6 as it relates to the In-State All Renewable product.

A. Phase II results for RFP6 were received from Navigant on October 25, 2011. It was beginning to appear from the results of both RFP5 and RFP6 that as the overall U.S. economy was starting to improve, the Ohio In-State REC market was showing improvement in participation and pricing and therefore was beginning to mature. The results of RFP6 satisfied the volume target for In-State All Renewable RECs by multiple suppliers with pricing falling from prior solicitations for both products procured. Results of RFP6 are shown below.

Table 2011 RFP 6 Results (September 2011)

REC Category	2011 REC Compliance Obligations (1)	2011 RFP Desired RECs (1)	RECs Bid	Navigant Recommended RECs	Actual REC Purchased	Cumulative % of Obligations Purchased	Market Liquidity
In-State Solar	7,026	5,000	14,805	5,000	5,000	178%	A
In-State All Renewable	176,156	20,000	98,680	20,000	20,000	113%	A

Market Liquidity
C = Constrained (Less than desired number of bids or no significant broker market offers / recorded transactions)
A = Readily Available (Adequate bids or significant broker market offers / recorded transactions)

Notes:
(1) 2011 Compliance Obligations include the PUCO ordered REC Shortfall carryover from the prior year.

Q. How many bidders qualified and submitted offers for In-State All Renewable RECs in RFP6?

A. Six bidders qualified and submitted offers for this product in RFP6.

Q. What was RCS' assessment of the market and what decisions were made as a result of RFP6?

A. By the end of 2011, a greater supply of In-State All Renewable RECs was becoming available and this market was becoming more transparent and liquid thus creating greater competition resulting in lower prices for the FEOUs.

Q. You have mentioned contingency actions taken as part of the renewable procurement process during the 2009-2011 timeframe. Please summarize the contingency implementation of RFP1 through RFP6.

A. The contingencies planned and implemented by the FEOUs for the six RFPs held during the 2009-2011 timeframe were grounded in both the FirstEnergy Utilities Commodity Portfolio Risk Policy and RCS' past experience running regulated power and renewable procurements. RCS responded to the lack of sufficient market supply in three out of four renewable product categories through a series of contingency actions, initially beginning with a previously successful approach – *i.e.*, issuing additional RFPs and, in the case of SRECs, purchasing from the spot or broker market. When limited results were achieved through its traditional contingency methods, RCS modified its contingency approach in light of constrained supply market conditions and expanded its contingency actions to include supply counter-offer, early deliveries from suppliers (in-state solar) and, as a last resort, force majeure filings. These contingency actions provided benefits by: (a) uncovering additional supply and meeting compliance obligations for both the In-State Renewable and All States Solar categories; and (b) lowering costs for the In-State All Renewable category.

V. Response to Audit Findings and Recommendations

1. Audit Findings

Q. The Exeter Report found that the FEOUs did not establish a maximum (or limit) price that they were willing to pay for In-State All Renewable RECs prior to the issuance of RFPs. Why didn't the FEOUs do that?

A. The FEOUs had a statutory mandate to meet with respect to renewable energy procurement goals and a regulatory commitment not to seek waivers, especially if competitively priced supply was available. Thus, as long as the FEOUs were not to exceed the three percent test set out in Ohio Revised Code Section 4928.64, the FEOUs believed that they were obligated to purchase RECs so long as the price was competitively determined.[4]

Moreover, in the experience of RCS, particularly in its power procurement activities, maximum or limit prices can be reasonably established only where markets are mature and where there is sufficient and transparent historical price information. In such markets, limit prices may be derived using statistical analysis of past pricing trends. In products where such history exists (such as PJM power delivered to the FirstEnergy Utilities zone), it is possible to apply statistical techniques to derive such a limit or reservation price. Since there was

[4] The only reference in Ohio Revised Code Section 4928.64 to anything related to cost is the three percent test set forth in Section 4928.64(C)(3). Even then, under the Commission's rules, a failure of the three percent test does not automatically allow a utility to avoid its statutory procurement obligation. At most, "failing" the test would provide a utility with the option to file an application which, if granted, would only delay (rather than totally relieve) the compliance obligation.

no reliable price history available for the In-State All Renewable category, no statistical analysis could be legitimately applied to develop such a limit price.

Further, exceeding a maximum price established by the independent evaluator or FEOUs, by itself, would not be a sufficient basis to constitute a force majeure event or have eliminated the statutory obligation to purchase the RECs when available.

Q. The Exeter Report found that the FEOUs paid unreasonably high prices for In-State All Renewable RECs and should have been aware that the prices paid were not in line with prices paid for non-Solar RECs elsewhere in the country nor in line with available market price information for In-State All Renewable RECs. How do you respond?

A. According to the Navigant Market Assessment Report, dated October 18, 2009,[5] the market supply conditions for the In-State All Renewable product were marked by few willing and certified suppliers. Further, there were major uncertainties with respect to economic conditions that could support new renewable project development. Specifically, credit conditions concerning financing for new projects were a significant limiting factor as discussed by witnesses Bradley and Earle.

Moreover, the out-of-state pricing for RECs, pointed to by Exeter as representative is clearly not comparable. Each state market has specific local

[5] Much of the information found in the report had been conveyed to the RCS as part of the RFP1 and RFP2 processes.

supply and demand factors and different rules (such as certification requirements and the ability or lack thereof to pay a compliance payment recoverable from customers), all of which impact pricing. Company witnesses Bradley and Earle discuss this in more detail.

Similarly, the pricing trends that Exeter points to as evidence that pricing for In-State All Renewable products were trending down are not instructive. That data came from one broker that, as it turns out, RCS talked to in an attempt to gain market information for Ohio (in fact, it was a major independent source that RCS relied upon to compare information obtained from Navigant). Through these discussions as to the development of the Ohio REC market (available suppliers, available RECs and transparency of pricing), it was confirmed that no meaningful price discovery existed for In-State All Renewable RECs until the fall of 2010.

Price discovery for certifiable In-State All Renewable products in 2008 and early 2009 would have been problematic because the PUCO had not certified any renewable in-state suppliers until mid 2009. Thus, there was no information, other than the bids that were ultimately received, on prices for In-State All Renewables throughout 2009. Both information that was available and that was provided to RCS by Navigant, along with broker discussions, consistently pointed to highly constrained supply conditions for this category throughout 2009 and 2010. Indeed, monthly PUCO-certified MW information extracted from the PUCO's website by RCS post-RFP6 showed that supply conditions for the In-

State All Renewable product were constrained for much, if not all, of the 2009-2011 timeframe. This data is shown in Attachment DWS-2.

Q. The Exeter Report found that the contingency planning employed by the FEOUs during the first three RFPs was inadequate. Do you agree with this finding?

A. No. As evidenced by Section III of the FEOUs' RMP, contingency events are contemplated in regulated procurements as part of a well-structured competitive solicitation process. With the results of each solicitation and market information the FEOUs had available throughout 2009 and 2010 from both broker discussions and from Navigant, RCS implemented a contingency event following each solicitation. As explained in Section IV above, RCS employed a number of contingency events over the first three RFPs due to the constrained supply conditions for three of the four renewable products. These included: (a) issuing an additional RFP; (b) entering into broker market transactions when available; (c) counter-offer with a supplier when appropriate; (d) obtaining early deliveries from suppliers; and (e) filing a force majeure application as a last resort to reconcile the lack of supply. Once the "traditional" types of contingency actions – additional RFP issuance and broker (spot) market purchases– were found to be of limited effectiveness given limited supply, the FEOUs implemented other contingency actions – counter-offers, accelerated purchasing actions (in-state solar) and force majeure filings. These latter actions resulted in more product supply, lower cost of supply or more information on market conditions which on two occasions were used to successfully receive a force majeure designation.

As noted, RCS did not plan – and due to the paucity of market data, could not have planned – for a contingency if lowest priced bids exceeded a certain maximum or limit price that is not defined by SB221 or by the Commission's regulations. Moreover, as also noted, the prices received for In-State All Renewable RECs in RFP1 and RFP2 were reasonable given: (a) they were the product of a competitive, market-based solicitation and procurement process; and (b) the constrained nature of the market which, in similar conditions in other states, had produced significant price spreads between products with geographic restrictions and those same products that could be sourced with no restriction on sourcing location.

Q. The Exeter Report also found that the FEOUs had several alternatives available to the purchase of high-priced In-State Renewable RECs. These included the following: (a) approaching the Commission to explain the results of the RFPs; (b) paying the statutory compliance payments in lieu of purchasing the In-State Renewable RECs; and (c) delaying the purchase of these RECs until some time in the future when presumably prices would be lower. How do you respond to each of these alternatives?

A. None of these alternatives would have likely yielded a different result or would have been feasible. Representatives of the FEOUs and Navigant met with the Staff of the PUCO in 2009 to discuss the strategic approach of the renewable RFP process. Moreover, the PUCO Staff had the ability to access Navigant at any time in the process to discuss results, or to attend webinars or RFP bid events to obtain the status of the RFP process or the market. Moreover, as the FEOUs retired

RECs in the GATS system, the PUCO Staff could view the pricing associated with each REC purchased and subsequently retired. For the 2009 compliance year, RECs were retired on March 31, 2010. Thus, the PUCO Staff had access to pricing at this time and could view, among other things, prices for the In-State All Renewable products procured from the first two RFPs. Given that the FEOUs had briefed the PUCO Staff on process steps and given that the PUCO Staff had access to Navigant and FEOU representatives and given that the PUCO had access to REC pricing in GATS, the FEOUs believed sufficient process and price transparency existed relative to the PUCO Staff.

With respect to paying the "Alternative Compliance Payment," there is no such thing as an "Alternative Compliance Payment" in Ohio. Although the Ohio Revised Code discusses a "compliance payment," the renewable energy compliance payment, unlike alternative compliance payments in other states, would be imposed on the utility by the Commission if it determined there was avoidable under compliance or noncompliance after review, notice and opportunity for hearings. The compliance payment is not to be recovered from customers. Thus, the compliance payment is a penalty for noncompliance. In this regard, Ohio's renewable energy requirements are unlike the market design established in several states where utilities may make alternative compliance payments *<u>in lieu of purchasing renewable resources</u>*. Indeed, the Companies' belief that paying compliance payments would not excuse the FEOUs' purchase obligations appeared consistent with the Commission's treatment of the force majeure applications that the FEOUs filed. In each case, the Commission did not excuse the Companies from their purchase obligation; the Companies were ordered to purchase the shortfall ultimately. Because the FEOUs had found competitively priced supply to meet their obligations, the FEOUs were not in a situation where a penalty was called for. The Companies must comply with the law and did so.

With respect to delaying purchasing decisions, despite exercising due diligence, the FEOUs could not have reasonably known: (a) when markets would become fully developed; (b) when additional qualified suppliers would become certified; or (c) when those qualified, certified suppliers would elect to participate in a solicitation held by the FEOUs. As confirmed by Navigant's market study, by RCS broker communications and by PUCO supply data (as shown in Attachment DWS-2), the In-State All Renewable markets in 2009 and 2010 were neither well developed nor liquid. Rather than conclude that supply conditions would improve by a certain point in time, the FEOUs properly and reasonably moved to secure the limited supply that was available. Indeed, as of the conclusion of RFP2 there was no evidence, and as of the conclusion of RFP3 there was no overwhelming evidence that supply conditions would dramatically improve in time for 2009, 2010 or 2011 compliance for this renewable product category.

Q. The Exeter Report found that the FEOUs should have been aware that the prices paid for In-State All Renewable products reflected significant economic rents and were excessive. How do you respond?

A. I do not agree. The competitive process employed for the RFPs was designed to yield competitively priced renewable products that reflect demand and supply at a point in time. In fact, Exeter reviewed the design of the RFPs and found "the RFPs….reasonably developed" and did not contain anti-competitive provisions or processes. Further, all of the RFPs were managed by an independent evaluator, Navigant. Having an independent evaluator helps to ensure that the prices paid by FEOUs were reflective of an arms' length transaction between a willing buyer and a willing seller and that there was no bias given to any participant at any stage of the procurement process. Moreover, when winning bids were accepted, neither Navigant nor the FEOUs knew (or had any way of knowing) the margin the winning supplier would be making on the award. For example, if the winning supplier has obtained supply from a third party and attached a premium that is not discoverable by Navigant or the FEOUs. Further, as far as RCS is aware, there was no published information on development costs in Ohio in 2009 and 2010. Thus, in or around the time of the RFPs at issue only the suppliers could know, with any degree of certainty, the cost structure underlying its bid and only the suppliers could know their margin, or if there was an economic rent.

2. Audit Recommendations

Q. The Exeter Report recommended that the PUCO should consider requiring Commission approval of REC purchases for retail suppliers of SSO prior to contracts being signed. Please respond.

A. If the PUCO ordered that REC purchase contracts be approved by the Commission, that provision would be inserted into the bid rules for renewable solicitation and the FEOUs would develop a time line to seek approval and then execute approved contracts with suppliers.

Q. The Exeter Report recommended that the FEOUs should implement a more robust contingency planning process for the procurement of RECs, with this plan subject to review from the PUCO staff prior to implementation. Please respond.

A. The FEOUs believe that the contingency language in its RMP provides the flexibility and direction that protects against volume and price risk. The FEOUs conduct an annual review of the RMP and will consider during this review to revise sections addressing contingency events or planning. If the Commission suggests, the FEOUs will review contingency plans with the PUCO or its Staff prior to implementation.

Q. The Exeter Report recommended that a thorough market analysis should precede the issuance of any future RFPs. Please respond.

A. As demonstrated above, and also in the testimony of Company witness Bradley, the FEOUs – through their independent evaluator and through their broker contacts -- conducted thorough market analyses prior to each of the RFPs at issue. All of Navigant's market analyses performed prior to the award of bids in the RFP process was provided to the FEOUs prior to any award decision. The FEOUs will continue to use broker information, renewable pricing information from subscription services and other information that may be garnered by the independent evaluator or RFP managers. However, in order to document more formally the conditions of the market at the time of a solicitation, the FEOUs agree to have a more formal written market analysis completed prior to the issuance of any future RFPs and, in fact, implemented such a process for the October 2012 Ohio Renewable RFP.

Q. The Goldenberg Report recommended that RCS should provide an estimate of REC expense for the calculation of Rider AER. Do the FEOUs agree?

A. Yes. The FEOUs agree with this recommendation and implemented this process in the development of the Rider AER rates effective October 1, 2012.

Q. The Goldenberg report recommended that the Companies should continue its 2011 REC retirement policy but change the third tier to retire the highest cost RECs first. Do the FEOUs agree?

A. Yes. The FEOUs agree to change the third tier to retire the highest cost REC first.

Q. The Goldenberg report recommended that the FEOUs should review their procedures for retirement of RECs to ensure the right quantity of RECs is moved to the reserve account each year. Do the FEOUs agree?

A. Yes. The FEOUs agree with this recommendation and have previously implemented a retirement process procedure to ensure the correct retirement quantities are identified and moved to the reserve account prior to the 2011 Compliance Year filings for Ohio.

Q. The Goldenberg report recommended that the FEOU's REC retirement policy should remain consistent to provide for a consistent, logical and orderly means to value inventory and reflect the expense of compliance. Do the FEOUs agree?

A. Yes. The FEOUs agree with this recommendation and have created a set of procedures within RCS to document all pertinent process steps, timing and expected outcomes of the REC retirement process. These procedures will be reviewed annually for any revisions.

Q. Does this conclude your testimony?

A. Yes. I reserve the right to supplement my testimony.

EDUCATIONAL AND PROFESSIONAL BACKGROUND

My name is Dean W. Stathis and my business address is 2800 Pottsville Pike, Reading Pennsylvania 19605. I am employed by FirstEnergy Service Company as Director of the Regulated Commodity Sourcing Department. This position is responsible for overseeing the power supply procurement activities associated with FirstEnergy Corp.'s utility subsidiaries, including compliance with all AEPS requirements.

I received a Bachelor of Arts degree in Economics from Youngstown State University in May 1979 and a Master of Arts degree in Economics from Youngstown State University in August 1981.

In September 1981, I was employed by the Middle South Utilities (currently doing business as Entergy) as a forecasting analyst. From September 1981 through April 1989, I was responsible for the development and maintenance of the Company's sales, peak load and economic forecasting models as well as various load research activities.

In May 1989, I became a staff analyst for GPU Service Inc. ("GPUS") and held various forecasting-related positions in the Load Forecasting Department. In August 1996, I became Manager, Natural Gas Transactions in the GPUS Power Supply Department. My responsibilities included procurement of natural gas for both Company-owned generating units and certain gas-fired Non-Utility Generators ("NUGs") and the development of fuel forecasts for budget purposes.

In January 2001, I became a Financial Trader for the Power Supply group of both the Jersey Central Power & Light Company ("JCP&L") and GPU's Pennsylvania affiliates. My responsibilities in this capacity included identification of power supply related risks and the deployment of financial hedge instruments to offset these associated risks.

In January 2002, I became Manager of JCP&L's Commodity Sourcing Department with primary responsibilities including oversight of the Company's participation in the BGS Auction process and management of JCP&L's 900 MWs of non-utility generation.

In June 2006, I assumed my current position.

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing was delivered to the following persons by e-mail this 23d day of January, 2013:

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