

**BEFORE  
THE PUBLIC UTILITIES COMMISSION OF OHIO**

In the Matter of the Application of )  
Duke Energy Ohio for Authority to )  
Establish a Standard Service Offer )  
Pursuant to Section 4928.143, )  
Revised Code, in the Form of an ) Case No. 14-841-EL-SSO  
Electric Security Plan, Accounting )  
Modifications and Tariffs for )  
Generation Service. )

)  
)  
)  
In the Matter of the Application of )  
Duke Energy Ohio for Authority to ) Case No. 14-842-EL-ATA  
Amend its Certified Supplier Tariff, )  
P.U.C.O. No. 20. )  
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**REPLY BRIEF OF INDUSTRIAL ENERGY USERS-OHIO**

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## TABLE OF CONTENTS

	<b>Page</b>
I. INTRODUCTION .....	1
II. THE COMMISSION SHOULD NOT AUTHORIZE THE PSR .....	2
A. The PSR is not related to an item listed in R.C. 4928.143(B)(2)(d) and therefore cannot be a term of an ESP.....	3
B. The PSR would not provide “certainty” or “stability” regarding retail electric service .....	6
1. The PSR would inject additional volatility into customer bills .....	7
2. The PSR will impose a cost on customers .....	7
3. Duke’s digression on problems of the wholesale energy and capacity markets is incomplete and irrelevant.....	8
4. The PSR will adversely affect competitive markets in Ohio .....	12
C. The Commission should reject the PSR because it violates state energy policy.....	13
D. Authorization of the PSR is preempted by the FPA .....	15
E. Duke has failed to comply with the requirement of R.C. 4928.20(K) to demonstrate the effect of the PSR on large-scale governmental aggregation.....	18
F. The Commission should not authorize the modified PSR proposed by OEG .....	19
III. THE PROPOSED ESP IS NOT MORE FAVORABLE IN THE AGGREGATE THAN AN MRO .....	22
A. Duke fails to account for the costs of the PSR in its analysis.....	23
B. The Commission cannot approve the ESP based on alleged non-quantitative benefits.....	24
IV. CONCLUSION.....	26

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**I. INTRODUCTION**

In this proceeding, Duke Energy Ohio, Inc. (“Duke”) seeks authorization of an Electric Security Plan (“ESP” or “proposed ESP” as appropriate) for the period of June 1, 2015 to May 31, 2018.<sup>1</sup> As the initial briefs of the parties demonstrate, the most significant contested issue in this proceeding is Duke’s request that the Public Utilities Commission of Ohio (“Commission”) authorize the proposed and misnamed Price Stability Rider (“PSR”).

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<sup>1</sup> Duke Ex. 1.

In its initial brief, Duke argues the PSR as proposed is lawful and reasonable. No other party supports authorization of the PSR as proposed, and all but one recommend that the Commission refuse to authorize it in any form because authorization of the PSR would violate Ohio and federal law. Because the PSR is unlawful and unreasonable, the Commission should not authorize it.

Duke also claims that the proposed ESP, including its pricing and all other terms and conditions, including any deferrals and any future recovery of deferrals, is more favorable in the aggregate as compared to the expected results that would otherwise apply under R.C. 4928.142 (“ESP v. MRO Test”). Duke, however, fails to account for the cost of the PSR in its application of the ESP v. MRO Test and unreasonably argues that non-quantitative benefits tip the benefits of the ESP in favor of approval. When the costs of the PSR are properly assigned, the proposed ESP fails the ESP v. MRO Test. Accordingly, the Commission must reject or modify the proposed ESP.

## **II. THE COMMISSION SHOULD NOT AUTHORIZE THE PSR**

Through the PSR, Duke seeks to guarantee that it will recover the cost of its contractual obligations to the Ohio Valley Electric Corporation (“OVEC”) under the Inter-Company Purchase Agreement (“ICPA”).<sup>2</sup> Many pages of the initial briefs of Duke and the intervenors are devoted to the expected cost of the PSR, but the Commission need not place itself in the intractable position of guessing whether the PSR would result in a charge or credit to retail customers because Ohio law precludes the Commission from authorizing the proposed rider. Even if the Commission could authorize a nonbypassable wholesale generation-related service rider, Duke has failed to

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<sup>2</sup> Duke’s contractual rights to obtain power from OVEC are referred to herein as the OVEC Entitlement.

demonstrate that authorization of its PSR would be reasonable. Further, a Commission order approving the PSR would be preempted by the Federal Power Act (“FPA”). Additionally, Duke has not complied with the requirement of R.C. 4928.20(K) to show the effect of the PSR on large-scale governmental aggregation. Therefore, the Commission should not authorize the PSR.

**A. The PSR is not related to an item listed in R.C. 4928.143(B)(2)(d) and therefore cannot be a term of an ESP**

An ESP may include only those provisions authorized by R.C. 4928.143(B).<sup>3</sup> Division (B)(2)(d) of that section provides that an ESP may include terms, conditions, or charges “relating to limitations on customer shopping for retail electric generation service, bypassability, standby, back-up, or supplemental power service, default service, carrying costs, amortization periods, and accounting or deferrals, including future recovery of such deferrals, as would have the effect of stabilizing or providing certainty regarding retail electric service.” In support of its claim that the Commission may authorize the PSR under that division, Duke argues that the division’s reference to “bypassability” is a sufficient basis.<sup>4</sup> Duke’s interpretation of this division, however, would lead to an absurd result and conflict with other provisions of Ohio law.

If Duke is correct, there is no limit on the charges that could be authorized under R.C. 4928.143(B)(2)(d). Any bypassable or nonbypassable charge could be authorized. That result is absurd, and the Commission must reject it because “[i]t is a cardinal rule of statutory interpretation that a statute should not be interpreted to yield an absurd result.”<sup>5</sup>

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<sup>3</sup> *In re Columbus S. Power Co.*, 128 Ohio St.3d 512 (2011).

<sup>4</sup> Duke Initial Brief at 18.

<sup>5</sup> *Mishr v. Poland Bd of Zoning Appeals*, 76 Ohio St.3d 238, 240 (1996).

Further, “[i]n enacting a statute, it is presumed that ... [t]he entire statute is intended to be effective.”<sup>6</sup> Additionally, “[i]f a general provision conflicts with a special or local provision, they shall be construed, if possible, so effect is given to both.”<sup>7</sup> Authorization of the PSR under R.C. 4928.143(B)(2)(d), however, would result in violations of several other provisions of Ohio law restricting the Commission’s authority to authorize generation-related nonbypassable charges. For example, R.C. 4928.02(H) precludes the authorization of a nonbypassable charge for existing generation-related resources. R.C. 4928.39 also prohibits the Commission from authorizing an electric utility from receiving transition revenue or its equivalent except as authorized by R.C. 4928.31 to R.C. 4928.40. Thus, Duke’s interpretation of R.C. 4928.143(B)(2)(d) would render other sections ineffective, a result the Commission should reject.

Moreover, the Commission already has rejected an interpretation of R.C. 4928.143(B)(2)(d) similar to that urged by Duke. In support of a claim to recover closure costs through a nonbypassable charge, Ohio Power Company (“AEP-Ohio”) advanced multiple claims, including one that relied on R.C. 4928.143(B)(2)(d)’s reference to “carrying costs” and “deferrals.”<sup>8</sup> After noting that Section 4928.143(B)(2)(c) did not authorize the recovery of costs of plants placed in service prior to 2009, the Commission went on to state:

We cannot agree ... that any provision of Section 4928.143, Revised Code, authorizes recovery of the closure costs for Sporn Unit 5, or that the only determination for the Commission to make with respect to

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<sup>6</sup> R.C. 1.47. Additionally, “[i]f amendments to the same statute are enacted at the same or different sessions of the legislature, one amendment without reference to another, the amendments are to be harmonized, if possible, so that effect may be given to each.” R.C. 1.52.

<sup>7</sup> R.C. 1.51.

<sup>8</sup> *In the Matter of the Application of Ohio Power Company for Approval of the Shutdown of Unit 5 of the Philip Sporn Generating Station and to Establish a Plant Shutdown Rider*, Case No. 10-1454-EL-RDR, Reply Comments of Ohio Power Company at 7 (Apr. 21, 2011) (“*Sporn*”).

a proposed ESP is whether it is more favorable in the aggregate than the expected results of a market rate offer. The Commission must also determine whether the costs to be recovered under the ESP are authorized by statute. *With respect to the closure costs for Sporn Unit 5, we find no statutory basis within Section 4928.143, Revised Code, or anywhere else in the Revised Code.*<sup>9</sup>

The Commission went on to note that the authorization would also violate the prohibition of the recovery of generation-related costs through a distribution or transmission rate contained in R.C. 4928.02(H).<sup>10</sup> Thus, the Commission in *Sporn* determined that the provisions of R.C. 4928.143(B)(2)(d) cannot be interpreted to override the prohibition of the recovery of generation-related costs through a nonbypassable rider set out in R.C. 4928.02(H).

Further, R.C. 4928.143(B)(2)(d) must be read in light of the fact that the division specifies the generation-related costs that are covered.<sup>11</sup> R.C. 4928.143(B)(2)(d) permits the Commission to approve a provision that relates to restrictions on shopping, or standby, back-up, supplemental power, or default service. As the record demonstrates, the PSR has no relationship to the provision of retail electric generation services provided to customers (other than it would likely increase their bills for electricity).<sup>12</sup> In particular, Duke states that it will not affect default service since the power will be offered into PJM Interconnection, LLC (“PJM”) markets and will not be bid into the Competitive Bidding Process (“CBP”).<sup>13</sup> Because the PSR is unrelated to any

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<sup>9</sup> *Id.*, Finding and Order at 18-19 (emphasis added).

<sup>10</sup> *Id.* at 19.

<sup>11</sup> *In re Columbus S. Power Co.*, 128 Ohio St.3d 512 (2011) (the Commission may not authorize any term not expressly included in the list of items that may be included in an ESP).

<sup>12</sup> Tr. Vol. II at 465-66.

<sup>13</sup> Duke Ex. 6 at 12.

of the generation-related items listed in the division, R.C. 4928.143(B)(2)(d) does not provide authorization for the rider.

**B. The PSR would not provide “certainty” or “stability” regarding retail electric service**

Even if the Commission wrongly concluded that the PSR related to a listed item in R.C. 4928.143(B)(2)(d), that division also requires Duke to demonstrate that the charge has the effect of providing certainty or stability in the provision of retail electric service. Rather than providing evidence supporting a finding that the rider will have the effect of providing certainty or stability in the provision of electric service, however, Duke chose to offer an opinion that the PSR would operate in that way because OVEC’s operational costs were relatively stable.<sup>14</sup> It offered nothing in the way of cost or revenue information in its Application, and its responses to discovery demonstrated that the PSR would be a cost to customers throughout the term of the ESP. Thus, Duke’s “proof” that the PSR would have the effect of stabilizing or providing certainty is instead a demonstration that Duke’s wholesale price risk associated with the OVEC Entitlement would be shifted to Duke’s retail customers.<sup>15</sup>

Duke’s initial brief adds nothing to demonstrate that the PSR will have the effect of stabilizing or providing certainty regarding retail electric service. After a digression in which Duke provides its view of the state of PJM’s wholesale generation resources with references to coal plant retirements and PJM’s actions in response to the January 2014 weather events,<sup>16</sup> the likelihood of wholesale price spikes, and a plea to the

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<sup>14</sup> *Id.* at 14.

<sup>15</sup> For detailed discussion of Duke’s failure to support a finding that the PSR will provide stability or certainty in the provision of retail electric service, see, e.g., IEU-Ohio Initial Brief at 26-30 (Dec. 15, 2014).

<sup>16</sup> Duke Initial Brief at 21-22.



Commission's "stewardship" of retail customers,<sup>17</sup> Duke at last offers that the PSR "will function as a counter-cyclical hedge," but fails to address the substantial record showing that the PSR would inject added volatility into customers' bills.<sup>18</sup> Accordingly, Duke fails to demonstrate that the PSR will have the effect of providing stability or certainty in the provision of retail electric service.

### **1. The PSR would inject additional volatility into customer bills**

According to Duke, the PSR will "mitigate retail rate volatility."<sup>19</sup> That claim is not correct.

Regardless of whether the PSR results in a charge or credit, it would increase the volatility of customer bills of both shopping and nonshopping customers. Shopping customers, including residential customers, can secure long-term contracts of up to three years at a fixed rate.<sup>20</sup> Nonshopping customers would benefit from the stability provided by the laddering and staggering of the CBP.<sup>21</sup> Authorization of the nonbypassable PSR, however, would increase price risk for both shopping and nonshopping customers by adding Duke's wholesale price risk associated with the OVEC Entitlement to customers' bills. Regardless of whether the PSR results in a charge or credit, the rider will increase the volatility of customers' bills because it shifts the risk of the OVEC Entitlement to customers, a risk they would not otherwise incur.

### **2. The PSR will impose a cost on customers**

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<sup>17</sup> *Id.* at 20.

<sup>18</sup> *Id.*

<sup>19</sup> *Id.* at 22.

<sup>20</sup> Tr. Vol. II at 472-73; Tr. Vol. X at 2697. See the Commission's Apples to Apples Chart applicable to Duke, viewed at <http://energychoice.ohio.gov/ApplesToApplesCategory.aspx?Category=Electric>.

<sup>21</sup> Staff Ex. 3, *passim*.

Further, the PSR will be detrimental to customers because it will increase their cost of service through a nonbypassable charge. Although Duke chose to ignore the costs associated with the PSR in both its description of the rider<sup>22</sup> and its analysis of cost impacts,<sup>23</sup> estimates of the cost of the PSR offered by customers demonstrated that the rider will impose a \$22 million cost (at least) during the term of the ESP.<sup>24</sup> Thus, the so-called benefits of the hedge run exclusively to Duke during the term of the ESP.

### **3. Duke's digression on problems of the wholesale energy and capacity markets is incomplete and irrelevant**

In support of its proposed rider, Duke also constructs an argument that the Commission should act as a steward for Duke's ratepayers because of changes in the PJM wholesale capacity and energy markets.<sup>25</sup> Duke's digression, however, does not provide a full picture of the changes that are occurring and is irrelevant because it rests on a false assumption that the Commission can expand its authority to approve the PSR.

Even if the factual claims Duke makes about the state of PJM's generation resources were relevant to the findings that the Commission must make to authorize the PSR, the claims are so incomplete as to be misleading. For example, Duke points out that a substantial amount of generation is scheduled to retire by 2019.<sup>26</sup> Duke, however, ignores that (1) PJM is responsible for maintaining reliability of the PJM region and has adopted procedures such as the capacity and energy markets to accomplish

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<sup>22</sup> Duke Ex. 6 at 10-16.

<sup>23</sup> Duke Ex. 18 at Ex. JEZ-3.

<sup>24</sup> See, e.g., OEG 1.

<sup>25</sup> Duke Initial Brief at 20.

<sup>26</sup> *Id.* at 21.

that result; (2) net additions to generation resources in the PJM construction queue exceed retirements;<sup>27</sup> (3) the reliability needs of PJM have already been satisfied by the capacity auctions which now extend for the full term of the proposed ESP;<sup>28</sup> and (4) the OVEC units will continue operation with or without the PSR. By leaving out these key facts, Duke seeks to create the false impression that reliability of electric generation to serve its customers is at risk if the PSR is not authorized. The Commission would be misguided if it accepted Duke's incomplete view of wholesale markets as a reason to authorize the PSR.

Duke's reliance on an incomplete picture of the wholesale generation markets, however, does not end with its description of the generation resources that are and will be available to maintain reliability. Duke also points to "price spikes" that may occur due to decreased fuel diversity and changes in PJM and FERC regulations.<sup>29</sup> These spikes, however, are largely irrelevant to retail customers.<sup>30</sup> End users, *i.e.* the retail customers of Duke, purchase power either through the standard service offer ("SSO") or a competitive retail electric service ("CRES") contract. Generation rates of SSO customers would be hedged through the laddering and staggering built into the auction process used to secure power for the SSO.<sup>31</sup> Customers that shop may elect long-term fixed contracts.<sup>32</sup> Thus, Duke's reliance on wholesale price volatility is misleading since

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<sup>27</sup> IEU-Ohio Ex. 3 & 4.

<sup>28</sup> The PJM auctions are for the delivery of capacity service three years forward. The base residual auction for the 2017-2018 planning year was conducted in May 2014. Staff Initial Brief at 9-10.

<sup>29</sup> Duke Initial Brief at 21.

<sup>30</sup> *Id.* at 21-23.

<sup>31</sup> Duke Ex. 3 at 8.

<sup>32</sup> Tr. Vol. II at 472-75.

customers are not directly exposed to the volatile wholesale markets and can hedge their exposure through retail choices guaranteed by Ohio law.

Although Duke's incomplete rendition of the wholesale market does not provide a justification for authorizing the PSR, Duke apparently offers its faulty account to encourage the Commission to authorize the rider because the Commission is a "steward for ratepayers."<sup>33</sup> The notion that ordering customers to pay Duke a subsidy of at least \$22 million is an act of "stewardship" is itself an absurdity. Moreover, even if the Commission were inclined to "help" customers by approving the PSR, the Commission is without authority to do so.

"It is axiomatic that the PUCO, as a creature of statute, may exercise only that jurisdiction conferred upon it by the General Assembly."<sup>34</sup> Retail generation service has been declared a competitive service in Ohio as a matter of law.<sup>35</sup> As to generation-related charges, the Commission is authorized to approve an SSO in the form of either an MRO or an ESP.<sup>36</sup> With regard to an ESP, the Commission's authority to authorize a price for the generation-related services is limited to those provisions listed in R.C. 4928.143(B).<sup>37</sup> Under that section, there is no lawful basis for approval of the PSR as a provision of an ESP because it is not related to one of the listed items.<sup>38</sup> An appeal to the Commission's "stewardship" of customers will not change that authority.

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<sup>33</sup> Duke Initial Brief at 20.

<sup>34</sup> *Columbus S. Power Co. v. Pub. Util. Comm'n of Ohio*, 67 Ohio St.3d 535, 537 (1993).

<sup>35</sup> R.C. 4928.03.

<sup>36</sup> R.C. 4928.141 to R.C. 4928.143.

<sup>37</sup> *In re Columbus S. Power Co.*, 128 Ohio St.3d 512 (2014).

<sup>38</sup> For a detailed discussion of the requirements of R.C. 4928.143(B)(1) and (2), see IEU-Ohio Initial Brief at 6-12.

The limitations on the Commission's authority to authorize the PSR, however, are not restricted to R.C. 4928.143(B). As demonstrated in IEU-Ohio's initial brief, the Commission also must ensure that the ESP complies with R.C. 4928.02(H), which provides that it is the policy of the State to ensure effective competition in the provision of retail electric service by avoiding anticompetitive subsidies flowing from a noncompetitive retail electric service to a competitive retail electric service or a product or service other than retail electric service or vice versa. Additionally, R.C. 4928.02(H) prohibits the recovery of any generation-related costs through distribution or transmission rates.<sup>39</sup> Authorization of the PSR would result in an anticompetitive subsidy to or from a noncompetitive retail electric service from or to a service other than retail electric service.<sup>40</sup> Authorization also would violate the prohibition of the recovery of generation-related costs through a nonbypassable rider.<sup>41</sup>

Additionally, the jurisdiction of the Commission does not permit the Commission to increase the compensation of Duke for wholesale generation-related services. If approved, the PSR would authorize Duke to increase its wholesale compensation for its OVEC Entitlement in an amount up to the costs it pays OVEC for the related power and capacity. The Commission's jurisdiction, however, is limited to transactions between an electric light company and consumers, *i.e.*, retail transactions.<sup>42</sup> Because the Commission is without authority to adjust the wholesale compensation of Duke, authorization of the PSR would exceed the Commission's jurisdiction and be illegal.

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<sup>39</sup> IEU-Ohio Initial Brief at 12.

<sup>40</sup> *Id.*

<sup>41</sup> *Id.* at 12-14. See, *Sporn*, Finding and Order at 19.

<sup>42</sup> R.C. 4905.02, R.C. 4905.03, & R.C. 4928.01(A)(6) & (7). For the detailed discussion of the Commission jurisdiction to establish retail prices, see IEU-Ohio Initial Brief at 19-20.

The Commission also cannot authorize Duke to recover transition revenue or its equivalent. Under the requirements of R.C. 4928.32 to 4928.40, an EDU had a single opportunity for a limited time to collect transition revenue from customers if it could demonstrate it had transition costs.<sup>43</sup> In 2000, Duke sought but gave up any claims it may have had to secure generation-related transition revenue through its settlement of its Electric Transition Plan (“ETP”). Although Duke again is seeking transition revenue or its equivalent through the authorization of the PSR, Duke has not presented a claim for transition revenue that complies with the statutory requirements, the time for such a claim has expired, and Duke has stipulated that it will not seek generation-related transition revenue.<sup>44</sup> Accordingly, the Commission cannot lawfully authorize the PSR.

#### **4. The PSR will adversely affect competitive markets in Ohio**

Duke also asserts that the PSR will mitigate price volatility “without causing any impact on wholesale markets” because “[t]he existence of the PSR has no impact on Duke Energy Ohio’s obligation under the ICPA to pay OVEC for its entitlement. Thus the capacity and energy will persist, with or without Rider PSR.”<sup>45</sup>

While Duke is correct that the Commission’s refusal to authorize the PSR would not affect the operation of OVEC, Duke’s claim that the authorization of the PSR will not affect wholesale markets is without merit. Because the PSR would guarantee that Duke would never be at risk for the costs it is charged by OVEC, Duke would be immune from wholesale price risk.<sup>46</sup> In contrast, competitors cannot resort to the protection Duke is

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<sup>43</sup> R.C. 4928.31 to R.C. 4928.40.

<sup>44</sup> For a detailed discussion on the bar on the recovery of transition revenue or its equivalent, see IEU-Ohio Initial Brief at 15-19.

<sup>45</sup> Duke Initial Brief at 24 n.79.

<sup>46</sup> RESA Ex. 3 at 13.

seeking.<sup>47</sup> Thus, the PSR would place unregulated generation providers at a competitive disadvantage.

Further, the PSR would alter the decision of an owner to operate the plant. According to a Duke witness, if the economically rational owner does not expect to recover the facility's costs of production in the wholesale market, it will close or mothball the facility (or in Duke's case, transfer or sell its interest to an affiliate or third party).<sup>48</sup> If the owner is guaranteed fixed and variable cost recovery through a mechanism such as the PSR, however, the owner will retain and bid the unit into the PJM auction with a zero bid so that it clears the PJM wholesale market.<sup>49</sup> Accordingly, assertion that the authorization of the PSR will not have an adverse effect on the market fails to address its own testimony that the PSR's subsidizing effect would alter an owner's decision to mothball a plant and is a benefit to Duke that is not available to CRES providers.

**C. The Commission should reject the PSR because it violates state energy policy**

Duke does not address the state energy policy in its discussion of the PSR, but instead argues that the PSR advances state policies in its general discussion of the compliance of the ESP with those policies.<sup>50</sup> It makes three claims. None is valid.

First, Duke claims that the PSR is structured to increase benefits to customers during periods of high or rising market prices, thereby mitigating the overall rates paid by customers.<sup>51</sup> Duke, however, did not provide any evidence to support that claim

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<sup>47</sup> Tr. Vol. II at 428-29.

<sup>48</sup> Tr. Vol. XVI at 4365.

<sup>49</sup> Tr. Vol. XVI at 4365-66.

<sup>50</sup> Duke Initial Brief at 41-49.

<sup>51</sup> *Id.* at 42.

other than its theoretical description of the rider.<sup>52</sup> Duke also chose to ignore the rider's bill impacts<sup>53</sup> and left out the PSR's cost to customers when it asserted that the proposed ESP passed the ESP v. MRO Test.<sup>54</sup> As the intervenors showed, moreover, Duke's claims regarding the stability of OVEC's costs (which in turn drive the alleged counter-cyclical effect of the rider) were unsupported, the "stabilizing" effect of the rider was minimal if any, and the rider would likely increase customers' bills through the term of the ESP.<sup>55</sup> Thus, Duke's claim that the rider will mitigate the overall rates paid by customers is unsupported by the record.

Second, Duke claims its ESP will be in compliance with R.C. 4928.02(H) because it would not recover generation-related costs through distribution or transmission rates.<sup>56</sup> That claim is wrong in two respects.

The first respect in which this claim is in error is that Duke will recover generation-related costs through the PSR. As proposed by Duke, it will secure wholesale capacity and energy resources from OVEC under the terms of the ICPA and offer those resources into the PJM wholesale markets. The unrecovered costs Duke pays OVEC are the generation demand and energy-related costs to operate the OVEC generating facilities.<sup>57</sup> That difference will be collected through the PSR. Thus, the amounts recovered under the PSR are generation-related costs.

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<sup>52</sup> Duke Ex. 6 at 10-16.

<sup>53</sup> See discussion above.

<sup>54</sup> Duke Ex. 6 at 24-26

<sup>55</sup> For the references to the extensive record demonstrating that the PSR does not operate as an effective hedge, see IEU-Ohio Brief at 26-30; OCC Initial Brief at 28-42; IGS Initial Brief at 26-31; and Sierra Club Initial Brief at 5-20.

<sup>56</sup> Duke Initial Brief at 45.

<sup>57</sup> IEU-Ohio Ex. 5.



The second respect in which this claim is in error is that the recovery will be through a rider that is the equivalent of a distribution rider.<sup>58</sup> As the Commission found in the *Sporn* case, a generation-related nonbypassable rider is the equivalent of a distribution rider since it is billed and collected from all customers.<sup>59</sup> If the Commission authorized a nonbypassable PSR, therefore, the rider would violate the prohibition of the recovery of generation-related costs through a nonbypassable rider contained in R.C. 4928.02(H).

Third, Duke claims that the ESP would facilitate the State's effectiveness in global markets because "in reliance upon Ohio-based generating facilities" it would mitigate customers' exposure to "uncertainty and volatility in market-based prices."<sup>60</sup> Subsidizing Duke by increasing customers' cost of electricity, however, will not advance the effectiveness of the energy-intensive customers that currently operate in Duke's service territory or encourage new entrants. Thus, the claim that Duke can increase the cost of electricity and thereby increase the State's effectiveness in global markets is unwarranted.

In summary, the PSR does not comply with the state energy policy in any of the ways asserted by Duke. Accordingly, if the Commission approved an ESP that included a PSR, the Commission would not comply with the requirement of R.C. 4928.06 that it effectuate state energy policy.

#### **D. Authorization of the PSR is preempted by the FPA**

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<sup>58</sup> Duke Ex. 6 at 16.

<sup>59</sup> *Sporn*, Finding and Order at 19.

<sup>60</sup> Duke Initial Brief at 49.

As IEU-Ohio demonstrated in its initial brief, the Third and Fourth Circuit Courts of Appeals have already affirmed district court decisions finding that attempts by states to increase the compensation of a generation owner for wholesale capacity and energy services are preempted because they invade a field of regulation within the exclusive authority of FERC and stand as an obstacle to the accomplishment of Congressional objectives.<sup>61</sup> Although Duke fails to address the preemptive effect of the FPA on the PSR in its initial brief, Ohio Energy Group (“OEG”) claims that approval of the PSR would not violate the FPA.<sup>62</sup> That claim is not correct.

According to OEG, the PSR avoids preemption because it “is not remotely similar to the Maryland and New Jersey approaches.”<sup>63</sup> In support of this argument, OEG claims that the Maryland and New Jersey commissions attempted to establish a supplemental wholesale rate and that the PSR would operate solely at the retail level pursuant to state law.<sup>64</sup> Additionally, OEG attempts to draw a distinction based on the purpose of the rider, claiming that the Maryland and New Jersey price recovery mechanisms are different because they sought to encourage new generation.<sup>65</sup>

OEG’s first claim, that the PSR would not establish a supplement to Duke’s wholesale recovery, is plainly inconsistent with the proposed operation of the rider. As described by Duke, the PSR would authorize it to recover the difference between what it recovers in the wholesale market and its costs incurred from OVEC. Thus, the rider

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<sup>61</sup> IEU-Ohio Initial Brief at 20-25, discussing *PPL EnergyPlus, LLC v. Hanna*, 977 F. Supp.2d 372, 393, (D. N.J. 2013), *aff’d sub nom.*, *PPL EnergyPlus LLC v. Solomon*, 766 F.3d, 241, 253 (3d Cir. 2014) and *PPL EnergyPlus, LLC v. Nazarian*, 974 F. Supp.2d 790 (D. Md. 2013), *aff’d*, 753 F.3d 467 (4th Cir. 2014).

<sup>62</sup> OEG Initial Brief at 11-14.

<sup>63</sup> *Id.* at 11.

<sup>64</sup> *Id.* at 12

<sup>65</sup> *Id.* at 12-13.

would operate exactly in the same manner as that rejected by the courts in New Jersey and Maryland; it would increase the compensation of the generation owner, in this case Duke, by the amount of generation-related costs not recovered through sales in the PJM market.

The second claim that the rider is different than that rejected by the New Jersey and Maryland federal courts because it would operate at the retail level is also inaccurate. As decisions in both federal cases explain, retail customers would have covered the above-market portions of the charges the state commissions ordered the local utilities to pay the generation owners under the challenged contracts.<sup>66</sup> Thus, there is no distinction in regard to retail cost recovery between the PSR and the mechanisms found unconstitutional by the New Jersey and Maryland federal courts.

OEG's third claim, that the authorization of the PSR would not be preempted because it serves a different purpose than the mechanisms rejected by the courts in New Jersey and Maryland, has no basis in the well-understood doctrine of federal preemption. Under preemption doctrine, the state's purpose is irrelevant if the state regulation conflicts with or invades a field of federal regulation. As the District Court of New Jersey explained:

Where a state law conflicts with a federal law, the Court does not balance the competing federal and state interests. In fact, the Supreme Court held that “[u]nder the Supremacy Clause of the Federal Constitution, ‘[t]he relative importance to the State of its own law is not material when there is a conflict with a valid federal law’ for ‘any state law, however clearly within a State’s acknowledged power, which interferes with or is contrary to federal law, must yield.’”<sup>67</sup>

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<sup>66</sup> *PPL EnergyPlus, LLC v. Nazarian*, 974 F. Supp.2d at 822; *PPL EnergyPlus, LLC v. Solomon*, 766 F.3d at 246.

<sup>67</sup> *PPL EnergyPlus, LLC v. Hanna*, 977 F. Supp.2d at 410.

The PSR would invade a field of exclusive federal authority and frustrate the price signals in the FERC-authorized PJM capacity market by permitting an uneconomic facility to bid into the market when the rational economic response would be to close or mothball the unit. Accordingly, authorization of the PSR is preempted by the FPA, regardless of the local purpose the Commission might find that the PSR advances.

**E. Duke has failed to comply with the requirement of R.C. 4928.20(K) to demonstrate the effect of the PSR on large-scale governmental aggregation**

R.C. 4928.20(K) requires the Commission to consider the effect on large-scale governmental aggregation of any nonbypassable generation charge. As explained in Commission rules, the application for an ESP must include “[a] description of how the electric utility proposes to address governmental aggregation programs and implementation of division[] ... (K) of section 4928.20 of the Revised Code.”<sup>68</sup>

Duke presents conflicting statements regarding its compliance with the requirements of R.C. 4928.20(K). Duke’s Application states that Duke’s “proposed ESP does include non-bypassable charges,” but then asserts that those charges will not adversely affect governmental aggregation.<sup>69</sup> In its testimony supporting its Application, however, Duke’s witness stated that compliance with R.C. 4928.20(K) “requires conduct by the Commission but, importantly, there are no non-bypassable generation charges being proposed in the proposed ESP.”<sup>70</sup> Then in its initial brief, Duke asserts that the

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<sup>68</sup> Rule 4901:1-35-03(C)(6), Ohio Administrative Code (“OAC”). After an EDU files an application for a standard service offer, the Commission must set the application for hearing, and “[a]t such hearing, the burden of proof to show that the proposals in the application are just and reasonable and are consistent with the policy of the state as delineated in divisions (A) to (N) of section 4928.02 of the Revised Code shall be upon the electric utility.” Rule 4901:1-35-06, OAC.

<sup>69</sup> Duke Ex. 1 at 19.

<sup>70</sup> Duke Ex. 6 at 31.

proposed ESP will not hinder the continued existence of governmental aggregations “and does not include any non-bypassable generation charge.”<sup>71</sup>

Duke’s most recent claim that the ESP does not contain a generation-related nonbypassable charge is not correct since the PSR is such a charge. According to Commission rules, therefore, Duke was required to provide a “description of how the electric utility proposes to address governmental aggregation programs and implementation of divisions (I), (J), and (K) of section 4928.20 of the Revised Code.”

Duke, however, chose to ignore that requirement, claiming that R.C. 4928.20(K) requires conduct of the Commission. Because Duke provides no other information regarding the effect of the PSR on large-scale aggregation, Duke has failed to carry its burden of proof, and the Commission cannot determine what the effect of the PSR is on large-scale governmental aggregation. Since Duke has failed to comply with both R.C. 4928.20 and Commission rules, the Commission may dismiss the Application.<sup>72</sup>

Because Duke has applied for an ESP, however, the Commission also may modify the application for an ESP under R.C. 4928.143(C)(1) to remove the unlawful rider. If the PSR is removed from the proposed ESP, the Commission would not be required to perform the review mandated by R.C. 4928.20(K). Accordingly, the Commission could “fix” the problem Duke has created by removing the PSR and proceed on the Application as modified.

**F. The Commission should not authorize the modified PSR proposed by OEG**

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<sup>71</sup> Duke Initial Brief at 40.

<sup>72</sup> *In the Matter of Application of Duke Energy Ohio, Inc. for Approval of a Market Rate Offer to Conduct a Competitive Bidding Process for a Standard Service Offer Electric Generation Supply, Accounting Modifications, and Tariffs for Generation Service*, Case No. 10-2586-EL-SSO, Opinion and Order at 26 (Feb. 23, 2011).

In contrast to every other intervenor and Commission Staff (“Staff”), OEG supports authorization of a PSR, presenting many of the same arguments in support of a nonbypassable generation-related rider as Duke. OEG’s proposed rider, however, is substantially different from Duke’s version. First, OEG recommends that the PSR be limited to a term of 9.5 years. Second, it recommends that energy-intensive commercial and industrial customers have the option of opting out of the rider.<sup>73</sup>

Like Duke, OEG claims that R.C. 4928.143(B)(2)(d) authorizes the rider, but OEG argues that the rider can be authorized under that division because the PSR is a limitation on shopping.<sup>74</sup> OEG, however, does not explain how the rider would operate as a limitation on shopping, and Duke stated that the PSR would not affect shopping.<sup>75</sup> Accordingly, OEG, like Duke, has failed to demonstrate that its version of the rider could be approved as a term of an ESP under R.C. 4928.143(B)(2)(d).

OEG also argues that the rider will provide stability to customers that would otherwise be exposed to wholesale price volatility.<sup>76</sup> According to OEG, the PSR will diversify the energy resources available to customers and protect them from future price increases.<sup>77</sup> This argument and the supporting claims, however, ignore that SSO customers are not exposed to wholesale prices due to the laddering and staggering of auction results and that the auction results themselves are not based on daily wholesale prices but rather forward prices.<sup>78</sup> Further, OEG notes and then ignores that customers can manage price risk through competitively secured retail contracts with fixed prices

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<sup>73</sup> OEG Initial Brief at 14-15

<sup>74</sup> *Id.* at 5.

<sup>75</sup> Duke Ex. 6 at 12.

<sup>76</sup> OEG Initial Brief at 6-8.

<sup>77</sup> *Id.* at 7.

<sup>78</sup> See discussion above.

and fixed terms. Thus, there is no practical reason to impose the price risk of Duke's ownership interest in OVEC on customers when they can hedge price risk through means authorized by Ohio law.

OEG also claims that the PSR would be consistent with the policies embedded in Ohio law.<sup>79</sup> As discussed above, however, the PSR is inconsistent with state energy policy regarding customer choice and the encouragement of retail electric competition and is prohibited by R.C. 4928.02(H).

As part of its attempt to secure approval of its version of a PSR, OEG also criticizes the Staff for opposing the PSR and "ceding complete control of energy and capacity pricing to PJM."<sup>80</sup> The Commission's authority, however, is limited to the pricing of retail electric services, not wholesale services.<sup>81</sup> By approving the PSR, moreover, the Commission would be exposing customers to additional wholesale price volatility.<sup>82</sup> Thus, OEG's appeal to the Commission to assert jurisdiction it does not have is both pointless and likely harmful to the customers.

OEG also complains that the Staff's opposition to a PSR on legal and policy grounds is not based on a cost-benefit analysis.<sup>83</sup> A cost-benefit analysis, however, is not warranted because the Commission is legally prohibited from authorizing the rider. Moreover, OEG's suggestion that the PSR might provide a benefit to customers is not credible in light of its evidence of the rate effects of the rider and its recommendations to modify Duke's version. OEG itself demonstrated that the rider will be a cost to

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<sup>79</sup> OEG Initial Brief at 2-4.

<sup>80</sup> *Id.* at 10-13.

<sup>81</sup> R.C. 4905.02, R.C. 4905.03, & R.C. 4928.01.

<sup>82</sup> Staff Ex. 1 at 14-15; IGS Ex. 12 at 9.

<sup>83</sup> OEG Initial Brief at 9.

customers through the term of the ESP,<sup>84</sup> and OEG recommends that the PSR be a nonbypassable charge for all customers other than those with more than a ten megawatt load at a single site; the energy intensive customers could elect to opt out of the PSR.<sup>85</sup> Because OEG's own evidence shows that retail customers will not likely see a benefit and OEG seeks an escape hatch, the Commission should place little weight on a claim by OEG, or anyone else, that there is any benefit associated with permitting Duke to transfer its above-market costs of the OVEC Entitlement to retail customers.

### **III. THE PROPOSED ESP IS NOT MORE FAVORABLE IN THE AGGREGATE THAN AN MRO**

The Commission may approve an ESP "if it finds that the [ESP] so approved, including its pricing and all other terms and conditions, including any deferrals and any future recovery of deferrals, is more favorable in the aggregate as compared to the expected results that would otherwise apply under section 4928.142 of the Revised Code."<sup>86</sup> This test requires an objective comparison of the proposed ESP to a MRO.<sup>87</sup> As demonstrated in IEU-Ohio's initial brief, Duke's proposed ESP is at least \$22 million less favorable than an MRO when the cost of the PSR is properly included on the ESP side of the test.<sup>88</sup> IEU-Ohio further demonstrated that the Commission could not rely on the four alleged non-quantitative benefits identified by Duke to find that the proposed

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<sup>84</sup> OEG Ex. 1, *passim*.

<sup>85</sup> OEG Initial Brief at 15.

<sup>86</sup> R.C. 4928.143(C)(1).

<sup>87</sup> IEU-Ohio Initial Brief at 35-36 (*citing Consumers' Counsel v. Pub. Util. Comm'n of Ohio*, 61 Ohio St.3d 396, 406 (1991)).

<sup>88</sup> IEU-Ohio Initial Brief at 33-34. As discussed below, OCC witness Wilson demonstrated that Duke's OVEC analysis, which produced the \$22 million figure, likely understates the cost that would ultimately flow to customers because the \$22 million was based on the flawed assumptions and modeling. OCC Initial Brief at 28-42.



ESP is more favorable than an MRO.<sup>89</sup> Accordingly, the proposed ESP fails the ESP v. MRO Test.

In its initial brief, Duke repeats the arguments raised in its testimony, which were addressed in IEU-Ohio's initial brief. According to Duke, its proposed ESP is quantitatively equivalent to an MRO because there is no difference between the cost of generation service procured under its proposed ESP and an MRO.<sup>90</sup> Duke then argues that four non-quantitative benefits to its proposed ESP render the proposed ESP more favorable in the aggregate than an MRO.<sup>91</sup> Both of Duke's arguments are incorrect.

**A. Duke fails to account for the costs of the PSR in its analysis**

As it did in its testimony, Duke's initial brief argues that its proposed ESP is quantitatively equivalent in cost to an MRO because "[a]ll of the SSO generation service under an MRO would have to be procured through a competitive process, just as is proposed for the Company's next ESP."<sup>92</sup> Duke concludes that "[t]he resultant cost of the service must therefore be the same."<sup>93</sup>

In its analysis, however, Duke again fails to include the cost of the PSR as a cost of the proposed ESP. The record demonstrates that the PSR is projected to add at least \$22 million in costs to the ESP.<sup>94</sup> Because there is no provision of R.C. 4928.142 that would allow for the inclusion of a rider like the PSR under an MRO, the \$22 million must be accounted for as a cost of the ESP for purposes of the ESP v. MRO Test.<sup>95</sup>

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<sup>89</sup> IEU-Ohio Initial Brief at 34-40.

<sup>90</sup> Duke Initial Brief at 27.

<sup>91</sup> *Id.* at 27-32.

<sup>92</sup> *Id.* at 27.

<sup>93</sup> *Id.*

<sup>94</sup> OEG Ex. 1.

<sup>95</sup> R.C. 4928.142.

Accordingly, on a quantitative basis, Duke's proposed ESP is \$22 million less favorable than an MRO.

**B. The Commission cannot approve the ESP based on alleged non-quantitative benefits**

In its initial brief, Duke also argues, as it did in its testimony, that there are four non-quantitative factors that create a "substantial advantage to the ESP" when compared to an MRO.<sup>96</sup> According to Duke, these four non-quantitative benefits consist of: (1) rate design modifications and the elimination of non-market-based influences on customer behavior; (2) promotion of competition through further leveling the playing field between SSO auction winners and CRES providers; (3) improvements to the safety and reliability of the distribution system; and (4) stabilization of competitive generation prices for shopping and non-shopping customers.<sup>97</sup>

Although Duke relies exclusively on these non-quantitative benefits to support its claim that the proposed ESP satisfies the ESP v. MRO Test, Duke has not provided any metric by which the Commission can "weigh" these non-quantitative "benefits" against the quantitative harm caused by the ESP relative to an MRO.<sup>98</sup> R.C. 4903.09, however, requires the Commission to base its decisions upon record evidence, and conversely, the Commission cannot base its decisions on "subjective belief, wishful thinking, or folk wisdom."<sup>99</sup> It is now too late for Duke to fill that gap in the record.

Moreover, changes in rate design and the leveling of the playing field, through additional rate design changes, between SSO auction winners and CRES providers do

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<sup>96</sup> Duke Initial Brief at 28-32.

<sup>97</sup> *Id.*

<sup>98</sup> IEU-Ohio Initial Brief at 35-36.

<sup>99</sup> *Consumers' Counsel v. Pub. Util. Comm'n of Ohio*, 61 Ohio St.3d 396, 406 (1991) (quoting *Columbus v. Pub. Util. Comm'n of Ohio*, 58 Ohio St.2d 103, 104 (1979) (Brown, J., dissenting)).

not provide benefits unique to an ESP. As IEU-Ohio showed in its initial brief, the rate design changes identified by Duke in its first two alleged non-quantitative benefits also are available to Duke under an MRO and therefore are not a non-quantitative benefit of the proposed ESP when compared to an MRO.<sup>100</sup>

Likewise, any safety and reliability improvements that result from investments in Duke's distribution system could be achieved under a base distribution rate case.<sup>101</sup> The accelerated cost recovery that Duke is seeking through the distribution rider, moreover, would result in actual quantitative costs for customers.<sup>102</sup> Rather than being a benefit of the ESP, accelerated cost recovery under Rider DCI should be considered as an additional cost of the ESP.

Finally, Duke's claim that the PSR will provide stable prices to customers is not supported by the record. The rider will inject an additional level of price instability in bills of both SSO and shopping customers. The rider also will result in an objective cost to customers; the record shows that the PSR is likely to result in an additional charge to customers of at least \$22 million.<sup>103</sup> As an Office of the Consumers' Counsel ("OCC") witness indicated, however, the analysis producing the \$22 million in projected costs understates the costs that customers would ultimately bear if the rider is approved.<sup>104</sup> Thus, the PSR should be considered as at least a \$22 million quantitative cost of the

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<sup>100</sup> IEU-Ohio Initial Brief at 36-37.

<sup>101</sup> *Id.* at 38.

<sup>102</sup> OCC Ex. 48 at 12.

<sup>103</sup> OCC Ex. 43 at 7 & 17.

<sup>104</sup> *Id.* at 24 (Duke's OVEC analysis is "an unreliable estimate of the potential future net costs to customers of the OVEC entitlement through the proposed PSR, due to the uncertain and speculative nature of the assumptions used in the analysis, and also apparent shortcomings or simplifications that were adopted in performing the analysis"); *see, also*, OCC Initial Brief at 28-43.

proposed ESP and a further non-quantitative harm to customers in the form of additional price instability and uncertainty.

In summary, Duke does not offer a method for the Commission to weigh the alleged non-quantitative benefits against the known costs of the ESP, and the four alleged non-quantitative benefits cited by Duke are either more appropriately classified as additional costs of the ESP or are not unique to Duke's ESP. Because Duke's proposed ESP is less favorable than an MRO, the Commission must either reject the ESP or modify it. If the Commission does modify the ESP, a necessary first step would be to remove the illegal and unreasonable PSR.

#### **IV. CONCLUSION**

The Commission should not authorize the PSR because Duke has not demonstrated that the PSR is lawful or that authorization of the rider is reasonable. Additionally, the Commission should not approve the proposed ESP without modifications because it fails an objective, cost-based application of the ESP v. MRO Test.

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## CERTIFICATE OF SERVICE

In accordance with Rule 4901-1-05, Ohio Administrative Code, the Commission's e-filing system will electronically serve notice of the filing of this document upon the following parties. In addition, I hereby certify that a service copy of the foregoing *Reply Brief of Industrial Energy Users-Ohio* was sent by, or on behalf of, the undersigned counsel for IEU-Ohio to the following parties of record this 29th day of December 2014, via electronic transmission.

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**ON BEHALF OF NON-PARTY OHIO VALLEY  
ELECTRIC CORPORATION**

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