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

***** UNREDACTED VERSION *****

REPLY BRIEF
BY
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May 6, 2013

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I. INTRODUCTION

FirstEnergy[1] filed its Initial Brief ("Brief"), consisting of 80 pages, on April 15, 2013. Nowhere in FirstEnergy's Brief is there a single mention of the grossly excessive prices, ranging from $300 to $700,[2] paid by FirstEnergy for In-State All Renewable Energy Credits ("RECs") and charged to its customers. Likewise, there is no mention that the transactions in question, the overpriced RECs, were purchased from its affiliate FirstEnergy Solutions. Finally, FirstEnergy fails to mention that its affiliate, FirstEnergy Solutions, exhibited market power.[3] FirstEnergy does appear to imply however, that charging these incredible prices to its customers and having its affiliate collect economic rents is "healthy."[4]

[1] In this Reply Brief, the word "FirstEnergy" means the FirstEnergy Ohio electric distribution utilities and is also referred to as "Utility."

[2] Exeter Audit Report at 28.

[3] OCC Initial Brief at 22-26.

[4] *See* Initial Brief of FirstEnergy at 65.

For some reason, FirstEnergy Solutions thought that if it offered In-State All Renewable Energy Credits at prices as high as $700/REC to its affiliate, then FirstEnergy would purchase them. FirstEnergy Solutions was right.

FirstEnergy can pay whatever it wants to its affiliate for Renewable Energy Credits. But FirstEnergy cannot collect any imprudent costs from its customers. FirstEnergy knows this. This restriction is included in the Stipulation that it signed to establish Rider AER.[5]

FirstEnergy states that "The issue presented by this case is largely this: whether the Companies *paid the proper price* for certain renewable resources originating in Ohio during 2009-2011 ("In-State All Renewables")."[6] That is not the issue. "Proper" is not a standard for anything in this case.

FirstEnergy can only collect prudently incurred costs from its customers.[7] FirstEnergy bears the burden of proof and failed to meet it. FirstEnergy failed to show that the costs incurred for the purchase of In-State All Renewable Energy Credits from FirstEnergy Solutions were prudent. Indeed, there is no evidence in the record that any buyer in Ohio (or the United States) purchased non-solar renewable energy at a price of more than more than $56/REC, excepting the prices FirstEnergy paid to FirstEnergy Solutions.

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[5] *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company and The Toledo Edison Company for Authority to Establish a Standard Service Offer Pursuant to R.C. 4928.143 in the Form of an Electric Security Plan*, Case No. 08-935-EL-SSO, Stipulation and Recommendation, at 10-11 (Feb. 19, 2009).

[6] Initial Brief of FirstEnergy at 1. (Emphasis added.)

[7] *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company and The Toledo Edison Company for Authority to Establish a Standard Service Offer Pursuant to R.C. 4928.143 in the Form of an Electric Security Plan*, Case No. 08-935-EL-SSO, Stipulation and Recommendation, at 10-11 (Feb. 19, 2009).

In its introduction, FirstEnergy states that "The unrebutted evidence demonstrates that all In-State All Renewables purchased by the Companies *** reflected the market at the time."[8] But FirstEnergy does not offer any evidence of a market where anyone purchasing non-solar renewable energy credits was paying anywhere near the prices it paid to its affiliate. However, FirstEnergy's introductory statement above would be correct if all affiliate transactions were removed from the equation. Specifically, OCC would agree that the bid price of $26.50/REC that FirstEnergy paid in 2010 to Sterling Planet, a non-affiliate, was more reflective of "the market at the time."[9]

FirstEnergy states that "The Exeter Report, however, did not recommend that any such disallowance be ordered or provide any specific amount that should be considered for a disallowance."[10] But FirstEnergy knows more than that. FirstEnergy was given the Exeter Auditor's report in draft form, for review, before the report's public issuance.[11] And FirstEnergy knows there was something in the draft audit report that it questioned—being the very recommendation that it can now say is lacking. Indeed, the Exeter Auditor's draft report contained an Auditor recommendation for a disallowance of all costs for In-State All Renewable Credits that FirstEnergy purchased above $50/REC.[12] That draft recommendation to protect customers was missing from the Exeter Auditor's Report that ultimately was filed at the PUCO.

The record contains the recommendations of the Exeter Auditor, including what

[8] Initial Brief of FirstEnergy at 1.

[9] Transcript Volume I-confidential, page 202.

[10] Initial Brief of FirstEnergy at 8.

[11] Transcript Volume III-public, page 512, line 24 through page 513, line 4; s*ee also* Initial Brief of OCC at 49-50.

[12] Transcript Volume III-public, page 512, line 24 through page 513, line 4; s*ee also* Initial Brief of OCC at 49-50.

appeared in the Draft Audit Report.[13] And the record contains the recommendations of OCC witness Wilson Gonzalez.[14] This and other evidence are detailed in OCC's Initial Brief. And the evidence is overwhelming that customers were greatly overcharged by FirstEnergy. The Commission should exercise its authority and protect customers from paying for FirstEnergy's imprudence.

II. BURDEN OF PROOF

FirstEnergy bears the burden of demonstrating that its costs for procurement of Renewable Energy Credits were prudently incurred.[15] But FirstEnergy claims that the other parties must overcome a presumption that FirstEnergy purchased the RECs prudently.[16] Neither the language of Rider AER nor case law support FirstEnergy's argument about a presumption in its favor.

According to the Stipulation that established Rider AER, FirstEnergy could only recover the "prudently incurred cost[s] of" renewable energy resource requirements "pursuant to R.C. § 4928.64."[17] That Stipulation, however, granted no presumption that FirstEnergy's expenditures for RECs were prudently incurred. To the contrary, the utility seeking reimbursement has the burden of proof.[18] The Stipulation that OCC, FirstEnergy and others signed does not provide for a presumption favoring FirstEnergy. The PUCO

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[13] Transcript Volume III-public, page 512, line 24 through page 513, line 4.; s*ee also* Initial Brief of OCC at 49-50.

[14] Direct Testimony of Wilson Gonzalez at 5.

[15] *See In Re Duke Energy Ohio, Inc.*, 131 Ohio St.3d 487, 2012-Ohio-1509, 967 N.E.2d 201, at ¶9.

[16] Initial Brief of FirstEnergy at 27; *See also id*. at 69.

[17] *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company and The Toledo Edison Company for Authority to Establish a Standard Service Offer Pursuant to R.C. 4928.143 in the Form of an Electric Security Plan*, Case No. 08-935-EL-SSO, Stipulation and Recommendation, at 10-11 (Feb. 19, 2009).

[18] *In Re Duke Energy Ohio, Inc.*, 131 Ohio St.3d 487, 2012-Ohio-1509, 967 N.E.2d 201, at ¶9; *See also*, R.C. 4909.19; R.C. 4928.142(D)(4); R.C. 4928.1473(E) and (F).

should enforce the Stipulation and not allow customers to be harmed by a presumption favoring their utility company, FirstEnergy.

At multiple points throughout its Initial Brief, however, FirstEnergy attempts to turn the burden of proof on its head by arguing that "the Commission adopts a presumption that the utility's decisions are prudent."[19] Thus, FirstEnergy argues that, based upon Commission precedent, it is the PUCO Staff, OCC and other parties challenging the reasonableness of FirstEnergy's purchases that have the obligation of proving imprudence.[20] FirstEnergy is wrong. FirstEnergy's incorrect claim that prudence is presumed relies on a number of Commission decisions[21] that have been effectively superseded by the Supreme Court of Ohio's decision in a recent Duke Energy case.[22]

In the Supreme Court's decision in *Duke Energy*, Duke sought reimbursement for roughly $30.7 million in costs associated with damages caused by Hurricane Ike.[23] The Commission limited Duke's recovery to only $14.1 million (based in part on OCC's evidence).[24] Duke then appealed the decision to the Supreme Court of Ohio and argued, much like FirstEnergy, that "other parties did not conclusively prove that the claimed

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[19] Initial Brief of FirstEnergy at 27; *See also id*. at 69.

[20] *See* Initial Brief of FirstEnergy at 27.

[21] *In the Matter of the Regulation of Purchased Gas Adjustment Clause Contained within the Rate Schedules of Syracuse Home Utilities Company, Inc. and Related Matters*, Case No. 86-12-*GA-GCR, 1986 Ohio PUC LEXIS 1, at 21-23 (Dec. 30, 1986); *In the Matter of the Investigation into the Perry Nuclear Power Station*, Case No. 85-521-

EL-COI, 1988 Ohio PUC LEXIS 1269, at 21 (Jan. 12, 1988).

[22] *See In Re Duke Energy Ohio, Inc.*, 131 Ohio St.3d 487, 2012-Ohio-1509, 967 N.E.2d 201.

[23] *In Re Duke Energy Ohio, Inc.*, 131 Ohio St.3d 487, 2012-Ohio-1509, 967 N.E.2d 201, at ¶2.

[24] *In Re Duke Energy Ohio, Inc.*, 131 Ohio St.3d 487, 2012-Ohio-1509, 967 N.E.2d 201, at ¶6.

expenses were unreasonable or imprudent."[25] But, as the Supreme Court held, "that [argument] is irrelevant because those parties did not bear the burden of proof."[26] The Court explained that it is the Utility that has to "prove a positive point: that its expenses had been prudently incurred *** [t]he commission did not have to find the negative: that the expenses were imprudent."[27] As a result, the Supreme Court upheld the Commission's decision to disallow much of the $30 million that Duke sought to recover from customers for storm damage, flatly rejecting any presumption of prudence.

Similarly, FirstEnergy failed to prove that its decision was prudent to purchase In-State All Renewable RECs at prices that exceeded $45. Indeed, the evidence introduced by the other parties indicated that RECs should not have been purchased at prices anywhere near the prices paid by FirstEnergy to its affiliate—FirstEnergy Solutions. FirstEnergy, therefore, failed to meet its burden of proof. That means the PUCO should disallow FirstEnergy from overcharging its customers for its unreasonable REC purchases.

III. LAW AND ARGUMENT

A. The Exeter Auditor's Draft Report Contained A Recommendation That FirstEnergy's Customers Not Pay For The Costs Of Procuring In-State All Renewable Credits Above $50 Per REC.

FirstEnergy addressed the recommendations of the Exeter Auditor that the PUCO hired to independently audit the prudence of FirstEnergy's purchases. FirstEnergy states that "The Exeter Report, however, did not recommend that any such disallowance be

[25] *In Re Duke Energy Ohio, Inc.*, 131 Ohio St.3d 487, 2012-Ohio-1509, 967 N.E.2d 201, at ¶9.

[26] *In Re Duke Energy Ohio, Inc.*, 131 Ohio St.3d 487, 2012-Ohio-1509, 967 N.E.2d 201, at ¶9.

[27] *In Re Duke Energy Ohio, Inc.*, 131 Ohio St.3d 487, 2012-Ohio-1509, 967 N.E.2d 201, at ¶8.

ordered or provide any specific amount that should be considered for a disallowance."[28]

But FirstEnergy knows more than that. FirstEnergy knows that it engaged in a private process where it was given the Exeter Auditor's report in draft form before the report's public issuance.[29] And FirstEnergy knows that something was removed from the Exeter Auditor's draft report—the Auditor's draft recommendation for the PUCO to disallow all costs for In-State All Renewable Credits that it purchased above $50/REC.[30] Indeed, the Exeter Auditor's recommendation in the draft Audit Report, for a disallowance to protect customers from overcharges, was eliminated from the final report filed at the PUCO.[31]

The Exeter Auditor's draft recommendation is similar to OCC's testimony that all REC costs above $45 should not be paid by FirstEnergy's customers.[32] The evidence is overwhelming that FirstEnergy greatly overcharged its customers. The PUCO should protect customers from paying exorbitant charges for renewable energy.

B. Customers Should Not Have To Pay For FirstEnergy's Imprudent Purchases of Exorbitantly Priced In-State All Renewable Energy Credits From A Bidder FirstEnergy Knew Had Significant Market Power —FirstEnergy Solutions.

FirstEnergy states that the potential bidders did not know the identities or number of the other bidders. And FirstEnergy claims that the competitive outcome was not affected by the lack of bidders.[33] FirstEnergy is wrong. The fact that the bidders may not

[28] Initial Brief of FirstEnergy at 8.

[29] Transcript Volume III-public, page 512, line 24 through page 513, line 4.; s*ee also* Initial Brief of OCC at 49-50.

[30] Transcript Volume III-public, page 512, line 24 through page 513, line 4.; s*ee also* Initial Brief of OCC at 49-50.

[31] Initial Brief of OCC at 49-50.

[32] Revised Confidential Exhibit WG-3, OCC Ex. 17A.

[33] FirstEnergy Initial Brief at 32-33.

have known who else was bidding or at what prices is only one component of many in determining whether there was an effective competitive bidding process for producing reasonable prices for consumers.

A more determinative factor (regarding the bidding process) is that FirstEnergy knew the identities of the bidder(s) when it decided whether to purchase the RECs at the prices bid.[34] One can hardly think of anything that would have jeopardized the independence and neutrality of FirstEnergy's decision-making process more than the Utility knowing that its affiliate (in this case—FirstEnergy Solutions) was a qualified bidder, and in 2 of the 3 RFPs, the only qualified bidder for In-State All Renewable RECs.

Realizing that a utility's independence and neutrality in making REC purchasing decisions could be significantly influenced by its affiliate's participation, at least one other Ohio utility (AEP-Ohio) included a provision in its RFP that prohibited affiliates from submitting bids.[35] FirstEnergy did not provide its customers with any such protection.[36]

Moreover, the Exeter Auditor was not aware that FirstEnergy knew its affiliate was a bidder in advance of its decision to purchase RECs at prices as high as $700 per REC from FirstEnergy Solutions.[37] Had FirstEnergy disclosed this fact to the Exeter Auditor, it may have impacted the Auditor's findings.

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[34] Transcript Volume I-confidential, pages 314-316.

[35] Transcript Volume III-public, page 565.

[36] *See* Exeter Audit Report at iv.

[37] Transcript Volume I-confidential, page 67.

Although FirstEnergy may have employed a competitive process, it did not achieve a competitive result.[38] Throughout its Initial Brief, FirstEnergy insinuates that a competitively designed RFP process necessarily results in a competitive outcome.[39] This is not the case, however, where bids were submitted by a single bidder that holds market power. FirstEnergy's affiliate, FirstEnergy Solutions, was the sole bidder for RFPs 1 and 2,[40] and was one of only two bidders representing 96.7% of the In-State All Renewable RECs bid in response to RFP 3.[41] In fact, FirstEnergy's consultant, Navigant, recognized that FirstEnergy Solutions' bids "represent[ed] over 75% of the total estimated Ohio-REC production for 2010" and "over 90% of the total certified Ohio REC production for 2010."[42]

Contrary to FirstEnergy's argument that "[t]he number of bidders thus did not affect whether the outcome would be competitive,"[43] the lack of bidders created a position of market power for FirstEnergy Solutions.[44] FirstEnergy Solutions, therefore, had the ability to affect the total quantity and/or price for In-State All Renewable RECs

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[38] Transcript Volume III-public, page 567.

[39] FirstEnergy Initial Brief at 31-35 ("Navigant worked with the Companies to develop a series of competitive RFPs to meet the Companies' renewable energy benchmarks required by Section 4928.64 for the 2009 through 2011 compliance years" and "Exeter found that the Companies' RFPs were open and competitive and designed to attract suppliers in the industry" and "OCC witness Gonzalez similarly testified that the RFP process that the Companies used was competitive, transparent, offered a clear product and generally designed to obtain a competitive outcome").

[40] Direct Testimony of Daniel R. Bradley at 28-30, 33-35; Direct Testimony of Wilson Gonzalez (confidential) at 19.

[41] Direct Testimony of Daniel R. Bradley at 40-41; Exeter Audit Report at 4, 23-25.

[42] OCC Exhibit 9, EA Set 3-INT – 3 Attachment 2-confidential, at p. 4 of 10. Navigant also goes on to say that "Based on a review of available information, NCI has not been able to determine whether the remaining 25% of 2010 Ohio-REC production is already under contract to other parties."

[43] FirstEnergy Initial Brief at 32.

[44] Initial Brief of OCC at 23-26. *See also* the Exeter Auditor's conclusion that "RECs prices of that magnitude indicate that some degree of **market power** is being exercised by a segment of the market given offered prices well above the cost of production." Exeter Audit Report at 31. (Emphasis added.)

for the time period at issue.[45] As a result, FES bid prices (as much as $700/REC)[46] that were exorbitantly higher than anywhere else in the country.[47]

In-State All Renewable RECs were not "reasonably available" where such market power existed.[48] Thus, while FirstEnergy is correct when it argued that it is uncontested that the RFP process was designed to be competitive,[49] the competitive process did not produce a competitive result because of the limited number of bidders that was, at most times, limited to FirstEnergy's affiliate - FES.[50]

FirstEnergy further argues that it "lacked sufficient information to create a maximum or limit price for In-State All Renewables."[51] FirstEnergy appears to use this as an excuse to justify purchasing RECs at any price because the prices bid arguably reflected the market price in a nascent market. But the Alternative Compliance Payment ("ACP") is the maximum price that should have been paid for RECs, especially in a nascent market. The illogic of FirstEnergy's position was evidenced and supported not only by OCC, but was supported by The Environmental Law & Policy Center, The Ohio Environmental Council, and Sierra Club, all of which maintained that the ACP is the maximum amount that FirstEnergy should have paid for RECs.[52]

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[45] *See* OCC Exhibit 9, EA Set 3-INT – 3 Attachment 2-confidential, at p. 4 of 10.

[46] Direct Testimony of Daniel R. Bradley at 28-30, 33-35, 40-41; *see also* Exeter Audit Report at 23.

[47] Exeter Audit Report at 26.

[48] *See* Direct Testimony of Wilson Gonzalez at 19, 34.

[49] FirstEnergy Initial Brief at 34-35.

[50] Transcript Volume III-public, page 639.

[51] FirstEnergy Initial Brief at 37.

[52] Initial Brief of OCC at 3, 48-50; *see* Initial Brief of Environmental Law& Policy Center, The Ohio Environmental Council, and Sierra Club at 18, 21.

Furthermore, simply because a price was bid, does not mean it reflects a competitive market price, much less that accepting the offer would be a prudent decision. This is why the Exeter Auditor explained that an absence of market information should not have led to a conclusion that prices in the Ohio market for In-State All Renewable RECs would have differed "so markedly from the cost of renewable development elsewhere in the country," where "underlying economic factors *** are the same."[53] The price indicatives for In-State All Renewables reflected a market price of less than $45.[54]

Because the prices bid were so high[55] and FirstEnergy knew, prior to making the decision to purchase In-State All Renewable RECs, that they were bid by its generation affiliate[56] with market power,[57] it was incumbent upon the Utility to recognize the absence of a competitive market.[58] At a minimum, prudence demanded an additional level of review, if for no other reason than to explore other options (e.g. ACP and/or *force majeure*) prior to purchasing grossly over-priced RECs from its affiliate. Had alternatives been implemented, FirstEnergy would not have collected millions of dollars in imprudent costs from its customers through Rider AER.

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[53] Exeter Audit Report at 30.

[54] Direct Testimony of Wilson Gonzalez at Attachment 2; Direct Testimony of Daniel R. Bradley at Attachment DRB-2; *see infra*, Section F.

[55] *See* Exeter Audit Report at 25-26.

[56] Transcript Volume II-public, p. 316.

[57] *See* OCC Exhibit 9, EA Set 3-INT – 3 Attachment 2-confidential, at p. 4 of 10. Navigant also goes on to say that "Based on a review of available information, NCI has not been able to determine whether the remaining 25% of 2010 Ohio-REC production is already under contract to other parties." *See also* the Exeter Auditor's conclusion that "RECs prices of that magnitude indicate that some degree of **market power** is being exercised by a segment of the market given offered prices well above the cost of production." Exeter Audit Report at 31. (Emphasis added.)

[58] *See* Direct Testimony of Wilson Gonzalez at 18-19.

C. Navigant Was not charged with the Duty of exploring all Options available to FirstEnergy, failed to consider Maximum Prices, and made A Recommendation that was rejected by FirstEnergy.

In May 2009 FirstEnergy retained Navigant Consulting, Inc. to conduct renewable procurements during the period 2009-2011.[59] Now FirstEnergy tries to meet its burden of proving that its decision to purchase over-priced RECS was reasonable and prudent by relying on recommendations made by Navigant. FirstEnergy is mistaken.

Throughout much of its Initial Brief, FirstEnergy relies upon Navigant's recommendations to justify its purchase of In-State All Renewable RECs[60] at outrageous prices and even argues that Navigant's "expertise and independence was unquestionable."[61] Such reliance, however, is misplaced because Navigant was not charged with the duty of exploring all options available to FirstEnergy, failed to consider maximum prices, and made recommendations that were rejected by FirstEnergy.

Navigant was retained by FirstEnergy and charged with the responsibility of determining whether RECs were reasonably available to the Utility.[62] Despite this responsibility, Navigant failed to consider the possibility of making a compliance payment in lieu of purchasing the In-State All Renewable RECs[63] or filing a *force majeure* action.[64] In fact, Navigant's Mr. Bradley explained that weighing the option of

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[59] Direct Testimony of Daniel R. Bradley at 3.

[60] FirstEnergy Initial Brief at 1 (arguing "[t]he Companies' purchase decisions were based on recommendations from Navigant").

[61] FirstEnergy Initial Brief at 30.

[62] FirstEnergy Initial Brief at 31; Transcript Volume I-public, page 250.

[63] Transcript Volume I-public, page 184.

[64] Transcript Volume I-public, page 169.

paying the compliance payment, contained in R.C. 4928.64(C)(2)(b), was not part of Navigant's scope of work.[65]

Moreover, while FirstEnergy argued that Navigant was to provide support for the Utility's *force majeure* application should Navigant find that RECs were not reasonably available,[66] Mr. Bradley testified that the consideration of a *force majeure* action was not within Navigant's scope of work either.[67] Thus, Navigant's recommendations were made in a vacuum, free from considering other options that may have reduced and/or alleviated FirstEnergy's REC purchase requirements. Knowing that Navigant's scope of work was so limited, FirstEnergy cannot rely on Navigant's recommendations to justify purchasing In-State All Renewable Energy Credits priced as high as $700 per REC. FirstEnergy's evidence about Navigant's recommendations is not credible given how FirstEnergy itself limited Navigant's ability to recommend alternatives such as seeking *force majeure* relief or making a compliance payment.

FirstEnergy's reliance on Navigant is further discredited by the fact that Navigant, for all intents and purposes, made recommendations regarding whether RECs were reasonably available irrespective of price. Mr. Bradley testified that prices in the $480 to $700 were reasonable.[68] What does reasonable mean to Navigant? Unfortunately for Ohioans, Navigant's version of reasonableness should be taken with many grains of salt. Mr. Bradley testified that FirstEnergy should be prepared to pay "at least as high as

[65] Transcript Volume I-public, pages 184-185; Transcript Volume I-public, page 169.

[66] FirstEnergy Initial Brief at 31 (citing Transcript Volume I-public, page 250).

[67] Transcript Volume I-public, page 169.

[68] Direct Testimony of Daniel R. Bradley at 36; Transcript Volume I-confidential, page 190-191.

$100/REC or $5,000/S-REC," and it may "need to pay even" multiples of $100 for RECs and even multiples of $5,000 per SREC.[69]

In fact, Mr. Bradley testified that it may have been reasonable, and that he may have even recommended that FirstEnergy pay up to $35,000 per SREC.[70] And it was apparent that Navigant would have recommended upwards of $1,000 per REC, which was Navigant's calculation of the three percent cost cap set forth in R.C. 4928.64(C)(3).[71] Other than the three percent cost cap, price was not a component in Navigant's assessment of whether RECs were reasonably available.

Even FirstEnergy had moments of clarity (that regrettably were too few) about the inadequacy of Navigant's recommendations. For example, RFP 3 sought bids for RECs to meet compliance in years 2010 and 2011. With respect to the bids for the 2011 compliance year, one bidder submitted a bid of 5,000 RECs at $26.50 per REC, while FES submitted a bid of 145,269 RECs at $500.00 per REC.[72] Unfortunately, Navigant recommended purchasing all of the aforementioned RECs at the prices bid.[73] FirstEnergy rejected Navigant's recommendation regarding FES's $500/REC bid for 145,269 RECs. It was only upon FirstEnergy's suggestion that Navigant subsequently made a counter-offer.[74] Ultimately, the amount of $325 per REC was accepted by FES.[75]

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[69] Transcript Volume I-confidential, pages 195-196.

[70] Transcript Volume I-confidential, page 197.

[71] Transcript Volume I-public, page 188.

[72] Direct Testimony of Dean W. Stathis at 35; Direct Testimony of Daniel R. Bradley at 41; *See also*, Exeter Audit Report at 23-25.

[73] Direct Testimony of Daniel R. Bradley at 41.

[74] Direct Testimony of Daniel R. Bradley at 41.

[75] Direct Testimony of Daniel R. Bradley at 42.

FirstEnergy claims that Navigant reviewed all bids for reasonableness. But these events indicate that Navigant was merely tasked with recommending the purchase of any available RECs, regardless of the reasonableness or prudence of such decisions. Moreover, it is somewhat disingenuous for FirstEnergy to argue that it "purchased In-State All Renewables in RFPs 1, 2, and 3 at or below prices recommended by Navigant,"[76] after specifically rejecting one of Navigant's recommendations.

FirstEnergy was well aware that Navigant's recommendations were made without consideration of alternatives. But FirstEnergy continued to rely upon Navigant's perfunctory recommendations, to the detriment of its Ohio customers. And now—despite what FirstEnergy knew of Navigant's sky-high recommendations and despite how FirstEnergy limited the ability of Navigant to provide reasonable advice—FirstEnergy holds out Navigant to the PUCO as its excuse for its own bad decisions. This Commission regulates FirstEnergy, not Navigant. And that regulation should now spare nearly two million consumers from paying the overcharges that were the result of their utilities' bad decisions.

D. The PUCO Should Reject FirstEnergy's Position That *Force Majeure* Requests, Compliance Payment Filings, And Consultations With The PUCO Staff Were Not Steps It Should Have Taken Prior To Purchasing (And Charging Customers for) All-Renewable Energy Credits At Prices As High As $700 Per Credit.

As expected, FirstEnergy argues that it was "statutorily mandated to purchase" the grossly excessive-priced RECs that it purchased from 2009-2011[77] because it was "able to procure In-State All Renewables through competitive solicitations, [and] such

[76] FirstEnergy Initial Brief at 40.

[77] Initial Brief of FirstEnergy at 3.

resources were [reasonably] available."[78] The In-State All Renewable RECs, however, were not "reasonably available" for the reasons set forth in OCC's Initial Brief.[79]

Worse, FirstEnergy did not even try to avoid charging its customers for these costs, through the numerous options that were available. In advance of its spending spree, FirstEnergy did not consult with the PUCO Staff for ways to avoid charging its customers some of the highest fees in the country for renewable energy. Sadly for customers, after the fact—after its high-priced purchases—FirstEnergy did communicate with the PUCO's Auditor to seek prevention of the PUCO Auditor's draft recommendation (that FirstEnergy's overspending should be disallowed) from appearing in the final audit report. [80]

FirstEnergy could have protected its customers by filing for *force majeure* or by making an alternative compliance payment. But FirstEnergy chose to rely on Navigant, its independent consultant that recommended high prices and that was not instructed by its employer (FirstEnergy) to consider all options for saving money for customers.

FirstEnergy is overcharging its customers by $157.7 million.[81] Running up a bill of that magnitude was not a question of FirstEnergy making decisions between choices that were virtually indistinguishable for best serving Ohio customers. No, FirstEnergy made some really bad decisions for its customers—some obviously bad decisions—that OCC now asks the PUCO to remedy by giving customers the protection that their electric

[78] *Id.*

[79] Initial Brief of OCC at 32-40

[80] Transcript Volume III-public, page 512, line 24 through page 513, line 4.; s*ee also* Initial Brief of OCC at 49-50.

[81] Direct Testimony of Wilson Gonzalez at 34.

utilities did not. FirstEnergy calls that Monday morning quarterbacking.[82] FirstEnergy forgets that we've seen its playbook.

1. FirstEnergy Should Have Sought *Force Majeure* Determinations to Protect Customers from Bid Results That Exceeded the Amount of the Applicable Compliance Payment.

When presented with prices that were far beyond even those contemplated by its consultant, Navigant, prudence demanded that FirstEnergy file for a *force majeure* determination.[83] Indeed, Navigant made known its expectation that "three factors" "will necessarily drive price to the high end of the range we have seen, and likely far beyond that."[84] And "FirstEnergy should be prepared to go at least as high as $100/REC or $5,000/S-REC *** " as indicative of the level FirstEnergy might have to pay to purchase RECs in the Ohio market.[85] These were the prices that Navigant, in July 2009, without any consideration of limiting prices in consideration of *force majeure* or compliance payments as alternatives, suggested that FirstEnergy "should be prepared to go."[86] And this assessment was made ***before anybody knew*** that there would only be one bidder, FirstEnergy's affiliate, FES.

Navigant suggested that FirstEnergy should have been prepared to pay up to a certain price. Then, however, Navigant went on to say that FirstEnergy "may reasonably need to pay even a multiple of these numbers." [87] It is difficult to see how these

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[82] Initial Brief of FirstEnergy at 69 (confidential version) at 70 (public version.)

[83] *Id.*

[84] OCC Confidential Exh. 5, page 2-3.

[85] OCC Confidential Exh. 5, page 3. It is interesting to note that although Navigant projected SRECs as high as $5,000, Gonzalez Attachment 1 indicates that the highest SREC price paid from 2009-2011 was $500 (or ten times lower than Navigant's estimate) as recorded in PJM/EIS.

[86] OCC Confidential Exh. 5, page 3.

[87] OCC Confidential Ex. 5, page 3.

recommendations could be consistent. Moreover, Navigant made this recommendation without any consideration of the availability of *force majeure* or compliance payments.[88]

Navigant's guidance certainly lacked consistency. But FirstEnergy's reliance on Navigant's recommendation, when it had *force majeure* and compliance payments as options, simply makes no sense. In the face of Navigant's statement that FirstEnergy "should be prepared to go at least as high as $100/REC" in this market, the burden was on FirstEnergy to justify any price higher than what was deemed to be tolerable by its own "independent" consultant as well as any amount above Ohio's alternative compliance payment.

a. Availability and Price Were Factors, Among Others, to be Considered by a Utility Serving Customers in Determining Whether Renewables Were "Reasonably Available" at the Time.

FirstEnergy was reluctant to make a *force majeure* filing to protect its customers in the face of the high non-solar REC prices with which it was presented. That decision cannot be understood in any way the PUCO could find reasonable. Based on broker and regulatory reports of prices, the prices that FirstEnergy paid for In-State All Renewable RECS were outrageously excessive compared to prices paid for non-solar RECs elsewhere. FirstEnergy argues that it could not obtain relief based upon Ohio law.[89] However, neither the language of the statute nor of the regulation supports FirstEnergy's interpretation.

[88] Transcript Volume I-public, pages 169, 184-185.

[89] Initial Brief of FirstEnergy at 19-24.

First, the word "reasonably," as it is used in R.C. 4928.64(C)(4)(b), must not be treated as mere surplusage.[90] It cannot be limited to mean simply that RECs were available or that the process to procure the RECs was reasonable.[91] Moreover, as discussed in OCC's Initial Brief, the significant market constraints and bid prices from a single supplier would likely have been sufficient to demonstrate that In-State All Renewable RECs were not "reasonably available."[92] Other cases decided by the Commission, and quoted in OCC's Initial Brief, clearly support this conclusion.[93]

In contrast, the case law cited by FirstEnergy did not address the interpretation of "reasonably available" as it is used in R.C. 4928.64(C)(4)(b). Rather, the case law addressed whether there was a "statutory out" from compliance payments if *force majeure* was not granted and the three-percent cap was not exceeded.[94] In this case, FirstEnergy's decision to forego a *force majeure* determination, not once, but three times, was grossly imprudent under any measurable standard.

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[90] R.C. 1.47 ("[t]he entire statute is intended to be effective"); *Excalibur Exploration, Inc. v. Board of Trustees*, Ninth Dist. Case No. 13956, 48 Ohio App. 3d 179, 180, 549 N.E.2d 224 (1989) (citing R.C. 1.47)

[91] Initial Brief of FirstEnergy at 23. For example, in its Application for force majeure in Case No. 09-987-EL-EEC AEP cited inflated REC pricing as one of the reasons supporting their request. Transcript Volume III-public at page 586. The Commission in its 1/7/10 Order in the AEP case had the opportunity but did not reject AEP's price argument when granting the force majeure.

[92] Initial Brief of OCC at 32-40. FirstEnergy argues "that the market in 2009 for In-State All Renewable RECs was nascent and supply was highly constrained." Initial Brief of FirstEnergy at 36. OCC asks, how can the market supply of RECs be "highly constrained" and "reasonably available" at the same time as FirstEnergy alleges? FirstEnergy cannot have it both ways.

[93] Initial Brief of OCC at 35-37, *citing In the Matter of Direct Energy Business LLC for a Waiver from Meeting the 2010 Ohio Sited Solar Energy Resource Benchmarks,* Case No. 11-2447-EL-ACP, 2011 Ohio PUC LEXIS 931, PUCO Finding & Order (Aug. 3, 2011) and [93] *In the Matter of the Application by Noble Americas Energy Solutions LLC for a Waiver from 2010 Ohio Sited Solar Energy Resource Benchmarks,* Case No. 11-2384-EL-ACP, 2011 Ohio PUC LEXIS 944, PUCO Finding & Order (Aug. 3, 2011).

[94] *In the Matter of the Adoption of Rules for Alternative and Renewable Energy Technology, Resources, and Climate Regulations, and Review of Chapters 4901:5-1, 4901:5-3,4901:5-5, and 4901:5-7 of the Ohio Administrative Code, Pursuant to Chapter 4928.66, Revised Code, as Amended by Amended Substitute Senate Bill No. 22,* Case No. 08-888-EL-ORD, Entry on Rehearing, pp. 35-37 (June 17, 2009).

b. FirstEnergy Mischaracterizes the Exeter Auditor's Testimony Regarding When Companies Should Seek *Force Majeure* Relief.

FirstEnergy takes issue with the Exeter Auditor's position on *force majeure*. Specifically, FirstEnergy points out that the Exeter Auditor testified that it would be prudent for a utility to be "confident" in its position before filing for *force majeure* relief and that the utility could not be confident in its position as there were appropriately certified RECs that could be purchased.[95] However, Dr. Estomin was not testifying to "prudence" in the regulatory sense. Furthermore, on redirect, he clarified his position by stating:

> Q. Dr. Estomin, I believe you testified that a company would need to be confident that a force majeure application would likely be granted before making that filing. My question is, can a company ever – ever be absolutely certain that any application they make will be granted by the State Commission?
>
> A. No, with potentially some rare exceptions, but even in the event that a force majeure is applied for and ultimately rejected, at least that provides some guidance to the utility on what the objectives are of the Commission.[96]

Thus, Dr. Estomin was of the opinion that it was prudent to apply for *force majeure* under these circumstances.

2. FirstEnergy Should Have Made Compliance Payments as a Way to Protect Customers if It Was Not Granted *Force Majeure* Relief.

FirstEnergy also argues that the law does not allow it to pay a compliance payment in lieu of actual compliance.[97] In doing so, FirstEnergy contends that the PUCO

[95] Initial Brief of FirstEnergy at 23, (citing Transcript Volume I-public, p. 97).

[96] Transcript Volume I-public at page 127.

[97] Initial Brief of FirstEnergy at 25-26.

Auditor and OCC's position are "at odds with the plain language of Section 4929.64."[98] Specifically, FirstEnergy claims that the absence of the word "alternative" before "compliance payment," as it appears in R.C. 4928.64(C)(3)(b), means that the compliance payment is not a payment that can be made "in lieu of" meeting a compliance obligations.[99] To the contrary, FirstEnergy argues that the compliance payment is a "penalty," which is not recoverable from customers and is only assessed after the Commission makes a finding that the utility failed to comply with its benchmark.[100] As discussed in OCC's Initial Brief, however, FirstEnergy's arguments are inconsistent with the clear statutory intent.[101]

The language of R.C. 4928.64(C)(5) allows the Commission, after a study, to increase the amount of compliance payments to deter utilities from making compliance payments "in lieu of" meeting their compliance obligations.[102] Given this language ("in lieu of actually acquiring or realizing energy derived from renewable energy resources"), a utility's obligation is excused if it makes the compliance payment upon a finding that it failed to meet its benchmarks.

Furthermore, neither the fact that compliance payments are not recoverable nor the fact that the process for assessing compliance payments begins with a PUCO determination of non-compliance or under-compliance in any way contravenes that compliance payments are "in lieu of" meeting compliance obligations. For these reasons, FirstEnergy's positions are not supported by the law and should be rejected.

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[98] Initial Brief of FirstEnergy at 25.

[99] Initial Brief of FirstEnergy at 25.

[100] Initial Brief of FirstEnergy at 25-26.

[101] Initial Brief of OCC at 40-43.

[102] R.C. 4928.64(C)(5).

3. FirstEnergy Should Have Informed The PUCO Regarding The Status of The Bids When Presented With Excessively High Renewable Energy Credit Bids.

FirstEnergy's repeated failure to inform the PUCO Staff or make a filing with the Commission (before purchasing the excessively high RECs) was imprudent. The Exeter Auditor's position is that FirstEnergy should have *considered* informing the Commission prior to purchasing the expensive RECs.[103] FirstEnergy did not.[104]

In response, FirstEnergy questions what the PUCO Staff would have or could have advised FirstEnergy to do under the circumstances.[105] In support of this position, FirstEnergy points to Dr. Estomin's testimony that he doesn't know what Staff would have done had FirstEnergy provided this information to Staff.[106] But FirstEnergy never acknowledges that it could have informed "the Commission of the status of the bids received to obtain Commission input regarding a decision to purchase"[107] by making a public filing. Such a filing would have provided notice to interested stakeholders. And potentially direction from the Commission. Yet FirstEnergy did not even *consider* obtaining input from the Commission upon receipt of the excessively high-priced bids.[108] FirstEnergy's decision was imprudent for several reasons.

First, and perhaps most apparently, it was FirstEnergy's affiliate, FES that was the sole bidder of the high-priced RECs that far exceeded any prices reported in the All-Renewables REC markets across the country. FirstEnergy should have been well aware

[103] Exeter Audit Report at 32.

[104] Exeter Audit Report at 32.

[105] *See* Initial Brief of FirstEnergy at 67.

[106] Initial Brief of FirstEnergy at 67.

[107] Exeter Audit Report at 32.

[108] *Id.*

that, in light of the size of these transactions, serious questions would arise regarding compliance with affiliate codes of conduct in proceeding with these transactions.

Second, tens of millions of customer dollars were at stake for a relatively small number of RECs. Third, the REC market had just opened in Ohio and the PUCO had thus had little opportunity to offer regulatory guidance at the time FirstEnergy was presented with these bids from its affiliate. Both in addressing the practical realities of implementation of the renewable energy standard and in interpreting provisions of the law such as *force majeure* and compliance payments, it would have been prudent to seek PUCO Staff guidance before moving forward with these affiliate transactions. For example, FirstEnergy certainly was not shy about proposing a new or different supply arrangement to the PUCO for approval in its most recent electric security plan case when it thought the market warranted a different approach for procurement.[109]

FirstEnergy argues that since it had met with the PUCO Staff to discuss its "strategic approach to meet their compliance obligations" and because the PUCO Staff had pricing information at its disposal from the PJM GATS system, the burden was on the PUCO Staff to advise FirstEnergy whether it was making imprudent purchasing decisions.[110] To further support this position, FirstEnergy points to the Exeter Auditor's testimony regarding the information that was available to the Staff to step in to guide the Utility in the procurement process.[111]

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[109] In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company and The Toledo Edison Company for Authority to Provide for a Standard Service Offer Pursuant to R.C. § 4928.143 in the Form of an Electric Security Plan, Case No. 12-1230-EL-SSO, Application and Stipulation and Recommendation, of April 13, 2012, proposing new bidding and pricing scheme for SSO load.

[110] Initial Brief of FirstEnergy at 68.

[111] Initial Brief of FirstEnergy at 68.

FirstEnergy attempts to shift to government (the PUCO Staff) the Utility's burden of managing the reasonableness of its procurement decisions. FirstEnergy's position is all the more discredited given that it never brought the issues to the PUCO Staff's attention in advance. The PUCO Staff may provide regulatory guidance on matters not before the Commission in litigation. But it is not the PUCO Staff's responsibility to oversee day-to-day utility management decisions, including purchasing decisions.[112]

The Exeter Auditor is correct. Had FirstEnergy made a filing with the Commission or met with the PUCO Staff, the Utility may have received some money-saving guidance prior to incurring over $150,000,000[113] in imprudent costs that it is charging to its customers.

[112] In the Matter of the Application of Ohio Edison Company for Certification of the West Lorain Combustion Turbine Project in Lorain County, Ohio, Case No. 99-540-EL-BGN, 2000 Ohio PUC LEXIS 416 (PUC Ohio April 17, 2000) at 43-44 ("As we move towards a competitive electric industry, the Board must be mindful to allow the market to dictate certain aspects of electric service and not to micromanage electric companies. We believe that it is clearly the company's responsibility to determine whether to curtail supply to or load of any customer or curtail or shut down the West Lorain project based on operational constraints. These are operational considerations best left to the company."); *see also* In the Matter of the Commission-Ordered Investigation of Ameritech Ohio Relative to Its Compliance with Certain Provisions of the Minimum Telephone Service Standards Set Forth in Chapter 4901:1-5, Ohio Administrative Code, Case No. 99-938-TP-COI, 2000 Ohio PUC LEXIS 678 (PUC Ohio July 20, 2000) at 44 ("This Commission is not required to micromanage Ameritech's record keeping. If Ameritech is not able to understand the meaning of "case-by-case documentation," then we may have a far more serious problem with Ameritech's record keeping than we realize.")

[113] Direct Testimony of Wilson Gonzalez-Confidential at 34 & Exh. WG-3-Confidential.

E. FirstEnergy's Arguments Ignore Price-Indicative Data For Compliance Markets Across The Country That Was Available At The Time of Purchase and That Could Have Been Used to Protect Customers From Over-Charges.

FirstEnergy primarily argues that there was not sufficient market price data for it to have made decisions regarding the purchase of In-State All-Renewables.[114] FirstEnergy contends that, "[d]uring RFPs 1, 2, and 3, no market price information on In-State All Renewables was available to the Companies" and that "no Ohio market pricing information was available that could be used to evaluate the pricing levels of bids,"[115] or develop a maximum limit price.[116]

While Ohio's In-State market, like virtually any nascent market, lacked "reliable, transparent information on market prices," as the Exeter Auditor and Mr. Gonzalez recognized,[117] the lack of transparency in Ohio was not a ticket to buy In-State All Renewables at any price.[118] Rather, during the nascent market period, an assessment of market prices was necessary through analysis of pricing available in other renewable compliance markets in the United States.[119] And there was "no basis for concluding that the cost of renewable energy development in Ohio differs so markedly from the cost of renewable development elsewhere in the country" as to warrant a conclusion that Ohio REC prices would be $300 per REC or more.[120]

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[114] Initial Brief of FirstEnergy at 37-39, 51-54

[115] Initial Brief of FirstEnergy at 37-38 (citing Direct Testimony of Daniel Bradley at 53).

[116] Initial Brief of FirstEnergy at 37-38 (citing Direct Testimony of Daniel Bradley at 53; Direct Testimony of Dean Stathis at 39-40).

[117] Exeter Audit Report at 26-27, 30 Transcript Public-Volume IV at 570. (Gonzalez testimony).

[118] Exeter Audit Report at 30; Direct Testimony of Wilson Gonzalez at 18.

[119] Exeter Audit Report at 30; Direct Testimony of Wilson Gonzalez at 18.

[120] Exeter Audit Report at 30.

Prices elsewhere were not more than "$45 per REC during the relevant period, and many were selling for prices considerably lower."[121] Since other markets had developed earlier, information on prices in other compliance markets ***was*** available at the time FirstEnergy purchased RECs. And it was appropriate and necessary to look at prices in those other markets to evaluate the reasonableness of prices bid in response to RFP1, 2 and 3.

It was FirstEnergy that inscrutably failed to reasonably assess the prices bid by its affiliate, FES, in light of the available information from across the country. That failure prevented it from establishing a reasonable maximum price that it would pay. FirstEnergy also failed to consider that the prices bid by a single bidder, FES, reflected FES's market power, rather than the modest premium to be paid in a nascent market. As a result, FirstEnergy accepted bids "well above the cost of production," which were "composed largely of economic rents."[122]

1. The Exeter Auditor's Figure 3 Provides a Barometer of Prices That Were Much Lower Than What FirstEnergy Paid for All-Renewable Energy Credits in Other Compliance Markets During the Applicable Period.

FirstEnergy asserts that differences in compliance markets between states undermine the usability of compliance market data from other states, as relied upon by the Exeter Auditor in Figure 3.[123] Although there are certainly differences between compliance markets, and prices may vary between compliance markets based on differences in those markets, Figure 3 is a barometer – an approximation – of market

[121] Exeter Audit Report at 30.

[122] Exeter Audit Report at 31. FirstEnergy witness Earle acknowledged that the "price of RECs in the market is determined by many factors. One of the factors is certainly the cost of development." Transcript Vol II-public at 440.

[123] Initial Brief of FirstEnergy at 53-54.

prices for All Renewable RECs. It was not used to suggest that prices in Ohio's In-State All Renewable RECs market would be exactly what they were in other states during this period.

Rather, Exeter used Figure 3 to show that prices in other states' All Renewables markets generally fell within a certain range – $45 or below (and in almost all cases, significantly below that level).[124] In other words, the price levels in other states' compliance markets, as shown on Figure 3, are representative of a range and trend of prices for non-solar (All Renewables) RECs in eight different compliance markets followed by the Department of Energy. Those eight markets include six PJM markets (Delaware, District of Columbia, Illinois, Pennsylvania, Maryland, New Jersey). While the data could not precisely predict prices in the Ohio In-State All Renewables market, it was an appropriate barometer of what prices would be reasonable in the Ohio market.

In fact, Exeter recognized that the data was subject to the effects of differences between compliance markets. Thus, Exeter stated:

> Second, the specifics of the Renewable Portfolio Standard legislation in place in the various states differ from the Ohio AEPS legislation. These differences include the types of renewable resources eligible to meet the requirements and the geographic areas from which the RECs may originate. Particularly with respect to the second factor, the Ohio AEPS legislation is more restrictive than the legislation in other states, including the New Jersey, Maryland, and the Pennsylvania legislation, which, other factors equal, could result in higher REC prices in Ohio than elsewhere.[125]

[124] Exeter Audit Report at 26.

[125] Exeter Audit Report at 27.

Exeter's recommendation, in its draft report, for a disallowance of prices above $50 per REC,[126] recognized that Ohio's more restrictive AEPS might justify prices somewhat – but not significantly – greater than the those prices shown in Figure 3.[127]

Figure 3 is an appropriate basis for approximating prices in the Ohio market. Together with Ohio's alternative compliance payment, it should have been used to assist in establishing a market or limiting price, avoiding the payment of prices "well above the cost of production" and preventing economic rents paid to FirstEnergy's affiliate, FES, that Utility customers would be asked to pay.[128]

2. OCC's Table Provides a Barometer of Prices That Were Much Lower Than What FirstEnergy Paid for All-Renewable Energy Credits During Nascent Market Periods in Compliance Markets.

In the same fashion, FirstEnergy also criticizes the Table shown on page 13 of Mr. Gonzalez's testimony.[129] Mr. Gonzalez utilizes that Table to show that All-Renewable REC prices during other compliance states' nascent market periods were a fraction of what FirstEnergy paid.[130] In its Initial Brief, FirstEnergy refers to this Table as the "Wind Power Table" because it is taken from the Department of Energy's Annual Report on Wind Power Installation Costs Performance Trends 2007.[131] But that Table actually reflects Tier I non-solar REC pricing, not just wind pricing, as described in that report attached to Mr. Gonzalez's testimony.[132]

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[126] Transcript Volume III-public, pages 512, line 24 through page 513, line 4.

[127] Exeter Audit Report at 27.

[128] Exeter Audit Report at 26, 31.

[129] Initial Brief of FirstEnergy at 61-63.

[130] Direct Testimony of Wilson Gonzalez at 13.

[131] Initial Brief of FirstEnergy at 61.

[132] Direct Testimony of Wilson Gonzalez at 13 & Attachment.

FirstEnergy also misrepresents Mr. Gonzalez's use of this Table. Mr. Gonzalez used this Table simply to show that Tier 1 REC prices in other states' nascent compliance markets did not show prices significantly above the prices reflected in Figure 3.[133] This argument was made merely to rebut FirstEnergy's argument that Figure 3, of the Exeter Audit Report, did not reflect nascent period prices.

FirstEnergy, however, criticizes the fact that the Table includes more than the 3-year period that Mr. Gonzalez defined as "nascent" and some of the data precedes the effective date of the states' RPS statutes.[134] The fact is that the data shown ***includes the nascent market compliance period***. Thus, the data, which are used to rebut FirstEnergy's argument that Figure 3 is not reflective of nascent market periods in other compliance markets, does support the point for which it was used. The fact that the Table includes more than just the nascent market period does not undermine its intended use. Nor does the fact that the data shown is for Tier 1 All Renewable RECs affect the use of this information. This is because Tier 1 RECs are typically the higher-priced All Renewable RECs, whereas Tier 2 RECs tend to be lower-priced, as shown in OCC Exhibit 2 for Pennsylvania pricing.[135]

FirstEnergy also contends that the headline from the DOE article, which accompanies the nascent market data relied upon by Mr. Gonzalez, has some significance.[136] This headline -- "REC Markets Remain Fragmented and Prices Volatile" – is a generalization. The headline points out that different states have different prices

[133] Direct Testimony of Wilson Gonzalez at 13.

[134] Initial Brief of FirstEnergy at 62.

[135] OCC Exh. 2 - Pennsylvania Alternative Energy Credit Program.

[136] Initial Brief of FirstEnergy at 62.

because of varying factors in each market. It also points out that, as can be expected in newer REC markets, prices vary significantly. However, the point made by this data is that prices throughout the market have nonetheless been consistently far below the grossly excessive prices paid by First Energy to its affiliate.

Neither the Exeter Auditor nor OCC witness Gonzalez have taken issue with the fact that prices in the REC market vary by state. Nor is there any question that this variability and the nascence of REC markets contribute to volatility relative to other more established markets. However, the fact that there are differences doesn't change the fact that other states' pricing stands as a reasonable barometer or "broad reference" for REC pricing under a wide range of conditions. The prices paid by FirstEnergy for RECs should have been similar to the prices paid in other compliance markets as shown both in Exeter's Figure 3 and in the Table on page 13 of Mr. Gonzalez's testimony. Unfortunately for FirstEnergy's customers, their Utility paid prices far above the prices in other compliance markets.

3. Market Price Data from Other Markets Was Available and Was an Appropriate Tool to Gauge the Reasonable Level of Market Prices in Ohio for In-State All Renewable Energy Credits (and For What Utility Customers Should Have to Pay).

As emphasized in OCC's Initial Brief, market data was available as published in various sources, including DOE reports, reports from individual states, and broker transaction information.[137] It was and is possible to gauge prices in the Ohio In-State All Renewables REC market based on this information.[138] And, as Mr. Gonzalez testified, it was "mind-boggling" for FirstEnergy to assume that the prices in the Ohio In-State All-

[137] Initial Brief of OCC at 16-21.

[138] *See* Direct Testimony of Wilson Gonzalez at 18.

Renewables RECs market were so different from prices in other states All-Renewables RECs markets, including other states' In-State markets.[139] In addition to comparing available data for prices in other states' All-Renewables compliance markets, Mr. Gonzalez also compared prices of In-State markets as compared to All-States markets and found that the prices "generally vary by a factor less than two." [140]

The Spectrometer report, which began to publish prices for Ohio RECs by category in August 2010, at the time bids for RFP 3 were being evaluated, showed that In-State All Renewable RECs were priced between $32.00 per REC to $36.00 per REC.[141] Certainly, rather than paying $325 per REC for 2010 and 2011 RECs, FirstEnergy should have recognized that the market was easing and prices were decreasing. In fact, Navigant had predicted as much in October 2009.[142] Indeed, FirstEnergy received a bid for 5,000 RECs of $26.50 per REC.[143] FirstEnergy knew the market was changing and it should have responded accordingly.

4. Ohio's Nascent Market Period Was No Different Than Other Compliance Market Nascent Market Periods. Like Other Compliance Markets, There Were Factors That Made The Ohio Market Different, but No Factor or Level of Uncertainty Justified FirstEnergy's Payment Of Grossly Excessive Prices to Its Affiliate, FES, For Customers Then to Pay.

FirstEnergy argues that for 2009 and 2010, developers in Ohio "had less competition and more uncertainty due to the nascent state of the Ohio market," which

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[139] Direct Testimony of Wilson Gonzalez at 18.

[140] Direct Testimony of Wilson Gonzalez at 11, fn.11 & Attachment 1.

[141] OCC Initial Brief at 26; OCC Exhibit 15, Set 3-INT-2, Attachment 25 (Confidential); *see also,* Transcript Volume II-confidential, page 493.

[142] OCC Confidential Exh. 9 EA Set 3-INT-3 Attachment 2 Confidential, p. 1. In August 2009, Navigant projected that no "major new supply entrants to the Ohio-REC market over the next 12 months," indicating that the market would be easing in their opinion following that initial period, or at least after 2010.

[143] Direct Testimony of Daniel R. Bradley at 41.

allowed them to seek higher prices than they would have otherwise sought in other states.[144] Ohio's nascent market, however, was not "so markedly different" from other nascent markets to justify the prices that FirstEnergy paid for In-State All Renewable RECs.[145] While prices could be expected to be somewhat higher than those in other states, they could not be expected to be so significantly higher.[146]

In fact, the requirement that RECs be produced in Ohio – reducing the competition for this supply – was an advantage to Ohio developers. It ensured that a specific level of supply would be produced in Ohio, which would reduce uncertainty for Ohio developers.

F. FirstEnergy's Contention That The Exeter Auditor And OCC Would Have Required FirstEnergy To "Time The Market" Or To "Gamble" In A Nascent Market Is A Gross Exaggeration.

FirstEnergy argues that, given what was known at the time, the Exeter Auditor and OCC witness Gonzalez would have required the Utility to "time the market" and "gamble" on the availability of supply and the price for that supply in later periods.[147] The expectation that prices will decline and prices will ease as supply develops in a nascent market, however, is not gambling or timing the market. Rather, it is a normal and natural progression that should be reasonably expected through development of the market, and that should be considered for providing customers with reasonable prices. FirstEnergy's belief that the market would stall or fail to improve was not reasonable or prudent when faced with the evidence that was available at the time.

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[144] Initial Brief of FirstEnergy at 66.

[145] Exeter Audit Report at 30.

[146] Direct Testimony of Wilson Gonzalez at 18. Also, FirstEnergy witness Earle admitted that most REC markets were nascent in the last 10 years. Transcript-Volume II-Public at 445-46

[147] Initial Brief of FirstEnergy at 49-51.

Moreover, while "laddering" may be a sound approach in a developed market, it is not such a prudent decision in a nascent market like Ohio's In-State All Renewable RECs market. The factors that justify laddering in a developed market are simply not present in a nascent market. As OCC emphasized in its Initial Brief, laddering makes no sense in a highly constrained market where a single player exercises significant market power that results in economic rents.[148] Laddering of prices based on such market power is unreasonable and imprudent for serving customers.

1. There Is No Basis to Conclude That Prices in Ohio's In-State All Renewables Market Would Be Very Different from Prices in Other All Renewables Markets, Including the Texas In-State All Renewables Market.

FirstEnergy argues that prices in Ohio's In-State All Renewables market would be very different than prices in other All Renewables markets, including in Texas, which has a substantial In-State All Renewable requirement.[149] OCC submits that there is no basis in available pricing data for such a conclusion.

Prices in Texas's In-State All Renewables REC market, either in its nascent market period or otherwise, have not been shown to be such outliers as the prices paid by FirstEnergy to FES.[150] FirstEnergy contrasts the Texas In-State All Renewable market with the Ohio In-State All Renewable market, suggesting that prices in the Ohio In-State All Renewable market would necessarily be grossly higher.[151] However, there is no basis for such a suggestion.

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[148] Initial Brief of OCC at 29.

[149] Initial Brief of FirstEnergy at 55.

[150] Exeter Audit Report at 26; Direct Testimony of Wilson Gonzalez at 13.

[151] Initial Brief of FirstEnergy at 55-56.

While the Texas market is far more developed than Ohio's,[152] there is no data indicating that Texas In-State All Renewables prices during Texas's nascent compliance period grossly exceeded prices in All-States Renewables markets during the initial compliance period. Indeed, the Table on page 13 of Mr. Gonzalez's testimony, taken from the 2007 Annual Wind Power report and in Exeter Auditor's Figure 3, show that prices in Texas's All Renewable REC market between 2002 through October 2011, consistently remain below $20 per REC.[153] To suggest that Ohio's In-State All Renewable REC market could reasonably see prices between 16 times ($320 per REC) and 35 times ($700 per REC) the highest prices reported in Texas's All Renewables market simply makes no sense.

Furthermore, while FirstEnergy contrasts Texas's retail electricity sales (2.3 times that of Ohio) and renewable generation of 8.1% of the state's retail sales in 2010 with the comparable figure in Ohio of 0.7% in 2010, such comparisons make little sense for a number of reasons.[154] First, Texas is significantly larger than Ohio. FirstEnergy fails to account for the vast differences in size, population, and gross domestic product of each respective state.[155] More importantly, FirstEnergy relies on 2010 data from Texas' market, but Texas opened its renewables market in 1999, with its compliance period

[152] Direct Testimony of Robert Earle, Attachment RE-13, page 2.

[153] Direct Testimony of Wilson Gonzalez at 13 & OCC Exhibit 17; Exeter Audit Report at 26.

[154] Initial Brief of FirstEnergy at 55.

[155] OCC Ex. 14 "U.S. Renewable Energy Technical Potentials: A GIS Based Analysis. This report describes the complexity of reasons for differences in the potential of renewable markets from state-to-state. Also, FirstEnergy witness Earle acknowledged that Texas's technical potential is larger, stating "if you make the same area bigger with all the same characteristics, that increases the technical potential." Transcript-Volume II-Public at 474.

beginning in 2006,[156] and was far more developed in 2010 than the Ohio In-State All Renewables market, which only opened in 2009.

FirstEnergy's argument that there was insufficient comparable In-State All Renewables market data to allow FirstEnergy to reject FES's bids is similar to the "nascent market" argument in that no other market is precisely comparable in terms of market timing or statutory requirements. However, in preparing its Audit Report, the Exeter Auditor plainly considered this factor, stating:

> We would expect, and in fact see, different values of RECs in different states based on a multitude of factors, most importantly including:
>
> - The geographical area from which eligible RECs can be drawn; generally, the larger the geographical area from which RECs can originate, the lower the price of the RECs.[157]

In FirstEnergy witness Earle's Attachment RE-9 to his testimony, Dr. Earle provides data, reported by SNL Energy, showing that prices for Ohio In-State All Renewable RECs (Vintage 2011 and 2012) from January 2012 to November 2012, were as much as $12 per In-State All-Renewable REC, or a number of times the prices for Ohio All-States All Renewables RECs.[158] But while the prices of Ohio In-State All Renewables were converging during this period with the prices for All-States All Renewables, they were, at their highest point, only approximately $12 per REC.[159] Thus, the emphasis on percentage differences misses the point. This $12 per REC Ohio In-State All Renewables price was far below Ohio's compliance payment and far below

[156] Transcript-Volume II-Public at 471-72. *See also* Direct Testimony of Robert Earle, RE-13.

[157] Exeter Audit Report at 30.

[158] Direct Testimony of Robert Earle, Attachment RE-9.

[159] Direct Testimony of Robert Earle, Attachment RE-9.

prices that had been paid in compliance markets across the country for RECs in recent years. These prices were also prices paid in compliance markets for RECs reported in October 2011 (3 months before the data on Dr. Earle's Attachment RE-9), as shown on Figure 3 of the Exeter Audit Report.[160]

The difference between Dr. Earle's position for FirstEnergy and the Exeter/OCC position is that Exeter/OCC recognized that there will be variability in market prices for In-State All Renewable RECs as compared to All-States All Renewable RECs. However, this variability will be limited by the level of compliance payments and reflective of differences in state requirements.

2. It Was and Should Have Been Reasonably Expected that In-State All Renewable Energy Credit Availability Would Increase Over a Reasonable Period of Time.

FirstEnergy's arguments are also disingenuous in their insistence that market price data was not readily available. These arguments ignore the fact that the market itself had just opened, and the rules for certification of renewables were only finally adopted in December 2009.[161] While all three of Ohio's other major electric utilities had begun their efforts to obtain RECs more than a year before FirstEnergy issued its first RFP (in anticipation of the adoption of reasonable rules that would be consistent with the

[160] Exeter Audit Report at 26.

[161] Ohio Adm. Code 4901:1-40-04(F). *See In the Matter of the Adoption of Rules for Alternative and Renewable Energy Technology, Resources, and Climate Regulations, and Review of Chapters 4901:5-1, 4901:5-3,4901:5-5, and 4901:5-7 of the Ohio Administrative Code, Pursuant to Chapter 4928.66, Revised Code, as Amended by Amended Substitute Senate Bill No. 22,* Case No. 08-888-EL-ORD, Opinion and Order (PUCO April 15, 2009); *modified by Entries of June 17, 2009, June 24, 2009, October 15, 2009, and November 12, 2009* . The first Resource Qualification application appears to have been filed on June 25, 2009 by Buckeye Biogas at Case No. 09-0526-EL-REN.

statutory mandates),[162] the first certification applications could not be filed until the PUCO issued draft rules in April 2009.

Thus, it could not have reasonably been expected that In-State REC availability would happen overnight. Rather, FirstEnergy should have reasonably understood that availability would occur over a reasonable period of time. And FirstEnergy should have recognized that the bids put forward by FES in RFPs 1, 2 and 3 demonstrated significant exertion of market power in such an environment.

3. FirstEnergy Asserted that Product Differences Between States May Have Played a Role in Pricing, But Provided No Evidence that Ohio's Product Definitions Are More Restrictive and Costly Than In Other States

FirstEnergy argues that the "product definitions across markets *** make comparison across markets difficult" and that making comparisons without taking "transferability" into account is "inappropriate."[163] In his Direct Testimony, FirstEnergy witness Earle gave, as an example, that "coal mine methane is a qualifying Tier 1 source in Pennsylvania, but it is not in New Jersey, Connecticut or Maryland."[164] Dr. Earle also argued that "transferability of the product from one jurisdiction to another is not always automatic or reciprocal, stating that "there are RECs from Illinois that are eligible for Pennsylvania, but not Ohio, while there are RECs from Pennsylvania that are eligible for Ohio, but not for Illinois."[165]

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[162] Direct Testimony of Daniel R. Bradley at 26-27. AEP Ohio issued an RFP on July 15, 2008. *Id.* Duke Energy Ohio, Inc. issued an RFP on June 19, 2008. *Id.* Dayton Power & Light issued an RFP on July 25, 2008. *Id.*

[163] Initial Brief of First Energy at 57-58 (citing Direct Testimony of Robert Earle at 21-23; citing to Exeter Audit Report at 8).

[164] Direct Testimony of Robert Earle at 23.

[165] Direct Testimony of Robert Earle at 23.

It is clear that there are definitional differences between products. This fact is recognized by both the Exeter Auditor and OCC witness Gonzalez.[166] The Exeter Auditor specifically stated that he would expect to see different values of RECs based on a multitude of factors, including "[t]he types of resources that qualify as "renewable"; those states allowing relatively low-cost resources to qualify as renewable, such as black liquor or waste coal, tend to exhibit lower prices."[167] However, as discussed above, consideration of these factors would not have led the Exeter Auditor, or Mr. Gonzalez, to conclude that prices for Ohio In-State All Renewable RECs would have differed markedly from prices paid for All Renewable RECs elsewhere. Thus, FirstEnergy's brief argument on this issue should be rejected.

4. FirstEnergy's Argument that Renewable Energy Developers in Ohio Faced "Financing Challenges" Not Experienced in Other States is Not Supported by Any Credible Evidence.

FirstEnergy makes a brief argument that "financing challenges" resulting from the global economic crisis "would have had a greater negative impact in Ohio than most other states because the Ohio market was relatively new during this time period."[168] Yet FirstEnergy's Dr. Earle admitted that he had done no systematic analysis of the impact of financing on Ohio's REC market.[169] FirstEnergy's claims in this respect should be rejected.

Furthermore, while FirstEnergy points to the Exeter Report to support this position,[170] Exeter nowhere indicates that the effects of the recession would have

[166] Exeter Audit Report at 30.

[167] Exeter Audit Report at 30.

[168] Initial Brief of FirstEnergy at 57 (citing Direct Testimony of Robert Earl at 21-22).

[169] Transcript-Volume II-Public at 480-481.

[170] Initial Brief of FirstEnergy at 57 (citing Exeter Audit Report at 29).

impacted the Ohio market differently in this regard than any other state.[171] OCC submits that there is no sound evidence that "financing challenges" had any meaningful impact on REC prices in Ohio, and certainly no different impact than in any other market.[172]

G. Compliance Payments Do Act As Price Limits Even Where Compliance Payments, Such As In Ohio and Pennsylvania, Are Not Recoverable From Customers.

FirstEnergy argues that Ohio's statutory provision prohibiting recovery of compliance payments from customers[173] prevents Ohio's compliance payment from acting as a price cap.[174] While this may have justified paying a price slightly higher than the ACP,[175] it does not justify the purchase of RECs at the grossly excessive prices paid by FirstEnergy. In these respects, Ohio's compliance payment clearly acts as a price cap. Nor does this excuse FirstEnergy's failure to apply for *force majeure* consideration or failure to consult with the PUCO Staff.

Additionally, Ohio is not the only state that prohibits recovery of compliance payments from customers. For example, Pennsylvania prohibits recovery of compliance payments from customers.[176] Yet prices for non-solar RECs in Pennsylvania have never approached the levels paid by FirstEnergy for non-solar RECs.[177]

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[171] Exeter Audit Report at 29.

[172] In fact, FirstEnergy's flawed argument that any REC price was acceptable until renewable REC costs reach the three percent cap would have provided much comfort to renewable project developers and the institutions financing their projects.

[173] R.C. 4928.64(C)(2)(c).

[174] Initial Brief of FirstEnergy at 58-59 (citing Direct Testimony of Robert Earle at 22).

[175] Exeter Auditor Steven Estomin acknowledged that "some premium" over REC prices in states with an ACP that allowed for recovery from customers should be accounted for in determining the comparable limit price in Ohio. Transcript-Volume 1-Confidential at 143.

[176] 52 Pa. Code §75.65(b)(3). *See also* Transcript-Volume II-Public at 481 (Dr. Earle).

[177] Exeter Audit Report at 26; OCC Exhibit 2 (PA AEPS Pricing).

OCC submits that there is no reasonable basis to suggest that Ohio's compliance payment does not act as an effective price cap. And such a cap should compel utilities to either make the compliance payment or seek other remedies (such as *force majeure*) to protect customers if available prices exceed the compliance payment amount.

H. To Protect Customers and the Market, the Commission Should Order An Investigation Of The Corporate Separation Between FirstEnergy And FirstEnergy Solutions.

The Environmental Intervenors maintain that "This case presents strong circumstantial evidence of improper and anti-competitive behavior on the part of FirstEnergy or/and its enriched affiliate FirstEnergy Solutions."[178] The Environmental Intervenors urge the Commission to "exercise its powers under Ohio Revised Code §§ 4928.17 and 4928.18 and open an investigation."[179] OCC agrees that, given the significance of the issues involving affiliate transactions and the negative impact on customers, the Commission should order an investigation of the corporate separation between FirstEnergy and FirstEnergy Solutions. The Commission should investigate, among other things, whether there were any inappropriate communications (regarding the purchase of In-State All-Renewable Energy Credits) between FirstEnergy (or its representatives) and FirstEnergy Solutions.

Although the Exeter Auditor raised the issue of "improper conveyance of information to FES by FirstEnergy Ohio utilities,"[180] it is evident that the Exeter Auditor did not go far enough in evaluating this issue.[181] In this regard, the Exeter Auditor perceived certain limitations in the scope of its work. Specifically, Mr. Estomin testified

[178] Initial Brief of Environmental Intervenors at 22.

[179] Initial Brief of Environmental Intervenors at 22.

[180] Exeter Audit Report at 31.

[181] Direct Testimony of Wilson Gonzalez at 19-20.

that it was not within Exeter's scope of work to conduct an investigation into whether FirstEnergy Solutions received any special treatment from FirstEnergy.[182]

Furthermore, the Exeter Auditor was not aware that FirstEnergy was provided the names of the qualified bidder before the decision whether to purchase the RECs was made by FirstEnergy.[183] Had FirstEnergy disclosed this fact to the Exeter Auditor, it may have impacted the Auditor's findings and recommendations.

The Commission should recognize the limited scope of the audit that was conducted by the Exeter Auditor. And, as the Environmental Intervenors urge,[184] the Commission should now exercise its jurisdiction under R.C. 4928.18 "to determine whether an electric utility or its affiliate has violated any provision of section 4928.17 of the Revised Code or an order issued or rule adopted under that section."[185] Accordingly, based on the evidence in this case, the Commission should now order a complementary investigation of the "elephant in the room" issue that remains to be investigated and that is central to assuring FirstEnergy's adherence to its Corporate Separation Plan and Codes of Conduct. And upon finding a violation of the law by FirstEnergy, the Commission should impose a forfeiture on the utility or affiliate of up to $25,000 per day, per violation, under R.C. 4928.18.[186]

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[182] Transcript Volume I-confidential, pages 64-65.

[183] EXAMINER PRICE: And then later they opened the bids and chose on price. When they chose on prices, did Navigant inform the companies that FirstEnergy Solutions was the successful bidder or was applying?

THE WITNESS: I don't believe at that point that the company was informed that FirstEnergy was the successful bidder. I think they were simply provided price information, is my understanding. Transcript Volume I-confidential, page 67.

[184] Initial Brief of Environmental Intervenors at 22.

[185] R.C. 4928.18(B).

[186] Transcript Volume III-public, page 635.

I. The Three Percent Cost Cap Mandated By Ohio Law Should Be Calculated By April 15th Of Each Compliance Year Using The Methodology Advocated By The PUCO Staff.

The Commission should mandate that FirstEnergy employ the six-step analysis discussed in the PUCO Staff's Initial Brief to determine whether the Utility purchased RECs that exceeded the three percent cost cap.[187] The three-percent cost cap is one of the provisions of the law that protects consumers from excessive costs associated with compliance with Ohio's alternative energy standard. Under the law, utilities are not required to comply with alternative energy benchmarks if the "reasonably expected cost of that compliance exceeds its reasonably expected cost of otherwise producing or acquiring the requisite electricity by three percent or more."[188] In making this determination, the statute refers to both historical and future looking components.[189]

The three-percent cost cap issue was first addressed in the financial audit report conducted by Goldenberg Schneider, LPA ("Goldenberg" or "Financial Auditor"), which was filed with the Commission on August 15, 2012. The Goldenberg Audit Report included a discussion of the three-percent provision and analyzed several different methodologies for approaching the calculation.[190] Three witnesses also addressed the three-percent cost cap in their prefiled direct testimony.[191] The methodology for

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[187] R.C. 4928.64(C)(3) "An electric distribution utility or an electric services company need not comply with a benchmark under division (B)(1) or (2) of this section to the extent that its reasonably expected cost of that compliance exceeds its reasonably expected cost of otherwise producing or acquiring the requisite electricity by three per cent or more. The cost of compliance shall be calculated as though any exemption from taxes and assessments had not been granted under section 5727.75 of the Revised Code."

[188] R.C. 2928.64(C)(3).

[189] R.C. 4928.64(C)(3).

[190] Final Report, Financial Audit 1 of the Alternative Energy Resource Rider of the FirstEnergy Ohio Utility Companies, prepared by Goldenberg Schneider, LPA ("Goldenberg Audit Report), filed on August 15, 2012 in PUCO Case No. 11-5201-EL-RDR at 24.

[191] Direct Testimony of Eileen M. Mikkelsen at 8-9; Direct Testimony of Dennis J. Goins at 6-10; Direct Testimony of Bruce Burcat at 5-7.

calculating the three-percent cost cap recommended by PUCO Staff incorporates both historical and future components addressed in the statute through the following 6-step analysis:

> Step 1: Determine the sales baseline in megawatt-hours (MWHs) for the applicable compliance year consisting of an average of the Company's annual Ohio retail electric sales from the three preceding years. Such calculation should be performed individually for each FirstEnergy electric distribution utility.
>
> Step 2: Calculate a "reasonably expected" $/MWH figure for the compliance year. This $/MWH figure should be a weighted average of the SSO supply for delivery during the compliance year, net of distribution system losses.
> Step 3: Staff should annually calculate a $/MWH suppression benefit (if any) and distribute this suppression calculation to all affected Companies. Such calculation and distribution should occur early in the compliance year so that the Companies timely can compute their 3% fund, as detailed below in Step 6.
>
> Step 4: Calculate an adjusted $/MWH figure by adding the Suppression Benefits,[192] if any, to the $/MWH figure from Step 2.
>
> Step 5: Calculate the Total Cost by multiplying the Step 4 adjusted $/MWH figure by the baseline calculated in Step 1.
>
> Step 6: Multiply the Total Cost from Step 5 by 3%, with the result representing the maximum funds available to be applied towards compliance resources for that compliance year.[193]

The Commission should require FirstEnergy to perform the three percent test, using the PUCO Staff's six-step analysis on or before April 15th of each compliance year, to identify FirstEnergy's maximum available compliance funds for the year. OCC agrees with the PUCO Staff that if an operating company reaches its maximum available

[192] Goldenberg Audit Report at 27; Direct Testimony of Bruce Burcat at 6.

[193] Initial Brief of PUCO Staff at 9-10.

compliance spending, it should not spend any additional funds for compliance for that compliance year unless given specific PUCO direction.[194]

J. The Commission Should Adopt The Financial Auditor's Recommendation Concerning The Calculation Of Rider AER.

The Financial Auditor recommended that the "overall Rider AER rate calculated for each Operating Company should be used rather than allocating to rate schedule based on Loss Factors."[195] The current FirstEnergy Loss Factor calculation method increases the cost to residential customers by $1,122,429[196] over the audit period relative to the method recommended by the Financial Auditor.[197] Nucor Steel Marion, Inc. ("Nucor") and Ohio Energy Group ("OEG") challenge the Financial Auditor's recommendation and parrot FirstEnergy's justification for the allocation by stating that it is consistent with the design of the energy portion of its Generation Service Rider and it would violate the current ESP settlement.[198]

The Financial Auditor's reasoning is that since "Rider AER is calculated and billed on delivered kWh and the RECs /S-RECs are purchased to meet a compliance requirement based on billed sales, we recommend using one Operating Company rate (the overall rate) for all of that Operating Companies' rate schedules. OCC concurs. This approach would also eliminate the detriment to the residential, commercial and lighting customers to the benefit of the larger customers."[199] Moreover, paragraph 5 of

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[194] Initial Brief of PUCO Staff at 10.

[195] Goldenberg Audit Report at 31.

[196] *Id.* at 10.

[197] *Id.*

[198] Initial Brief of Nucor Marion Steel, Inc. at 26-27, Initial Brief of Ohio Energy Group at 8, Initial Brief of FirstEnergy at 79-80.

[199] Goldenberg Audit Report at 10.

the latest FirstEnergy Stipulation states, "[t]he rate design currently in effect remains in place other than as modified below. However, the Commission may, with the Companies' concurrence, institute a changed revenue neutral distribution rate design ***."[200] Accordingly, the Commission should adopt the Financial Auditor's recommendation concerning the calculation of Rider AER and reject Nucor, OEG, and FirstEnergy's critique of the Financial Auditor's recommendation.

K. Giving Customers A Credit For The Amount Of A Disallowance, Plus Carrying Costs, Is Lawful And Does Not Constitute Retroactive Ratemaking.

The Commission should find that FirstEnergy unlawfully passed on to customers, through Rider AER, the cost of RECs that were purchased at unreasonably high prices. The Commission should disallow such costs (including any carrying costs).And the Commission should credit Rider AER (and the customers that pay it) for the amount of the disallowance. By crediting Rider AER, customers will receive the benefits of the credit prospectively, beginning with the next quarterly Rider AER filing.

Contrary to FirstEnergy's claims,[201] the application of such a credit to prospective rates is lawful and does not constitute retroactive ratemaking. As explained in OCC's Initial Brief,[202] the Commission, in an analogous rider case, specifically found that *Keco Industries, Inc. v. Cincinnati Suburban Tel. Co.* (1957), 166 Ohio St. 254, 141 N.E.2d 465, was inapplicable, stating:

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[200] *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company and The Toledo Edison Company for Authority to Provide for a Standard Service Offer Pursuant to R.C. § 4928.143 in the Form of an Electric Security Plan*, Case No. 12-1230-EL-SSO, Stipulation at 12 (April 13, 2012).

[201] FirstEnergy Initial Brief at 75-78.

[202] OCC Initial Brief at 52.

> *Keco* does not apply in this situation. The Commission is not considering modifying a previous rate established by a Commission order through the ratemaking process as the Court considered in *Keco*. Rather, the Commission, by ordering [AEP-Ohio] to credit more of the proceeds from the Settlement Agreement to [AEP-Ohio's] deferral balance, is establishing a future rate based upon the real cost of the coal used by [AEP-Ohio] to generate electricity during the 2009 FAC audit period. [203]

Similarly, by crediting the disallowance plus carrying costs to Rider AER, the Commission would not be refunding unlawfully collected rates, but would be establishing a future rate based upon the reasonable price that should have been paid for RECs purchased by FirstEnergy. Accordingly, FirstEnergy's reliance on *Keco i*s misplaced, and should be rejected.

Similarly, *Lucas County* is inapplicable to the case at bar, and any reliance on such decision should be rejected.[204] As the Commission has previously stated in the analogous rider case:

> *Lucas Cty*. does not apply to the present situation. In *Lucas Cty.*, the Court held that the Commission was not statutorily authorized to order a refund of, or credit for, charges previously collected by a public utility where those charges were calculated in accordance with an experimental rate program which has expired. As noted above, the Commission has not made a determination modifying the rate the Companies collected during 2009. Additionally, there is no experimental rate program involved in the current case. Thus, *Lucas Cty.* does not apply in this matter.[205]

In that rider case, the Commission determined that issuing a credit against a rider outside of an experimental rate program did not constitute modifying a previous rate; but, rather, was establishing a new, prospective rate that took into account excessive rates that had

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[203] *In the Matter of Fuel Adjustment Clauses for Columbus Southern Power Company and Ohio Power Company*, Case Nos. 09-872-EL-FAC, 09-873-EL-FAC, Opinion and Order at 13 (January 23, 2012), *reh'g denied*, Entry on Rehearing at 6-7 (April 11, 2012), *appeal pending*, S.Ct. Case No. 2012-1484.

[204] *Lucas County Comm's v. Pub. Util. Comm.*, 80 Ohio St.3d 344, 686 N.E.2d 501 (1997).

[205] *Supra* n.3 at 14.

been charged in prior periods.[206] Similar to the rider case regarding the fuel adjustment clause, the Commission in this case "is engaging in a reconciliation and accounting" of the costs associated with Rider AER,[207] as contemplated by FirstEnergy's ESP through an audit process.[208] Rider AER is not an experimental rate program and, as mentioned above, the credit would be establishing a future rate, not refunding to customers unlawfully collected rates.

Moreover, reasonable costs incurred for compliance with the renewable energy resource benchmark (including any reasonable costs incurred in purchasing RECs), can then be passed on to customers through a rider mechanism that is updated quarterly and reconciled. These varied rates are independent from the formal rate-making process.[209] Without this formal ratemaking process, retroactive ratemaking cannot exist.[210]

Therefore, consistent with Ohio law, the Commission should determine that the cost of the purchased RECs was imprudent, unjust, and unreasonable. The PUCO should direct FirstEnergy to apply the amount of the disallowance plus carrying costs to Rider AER as a credit. That credit will then flow through to customers prospectively through Rider AER rates established in subsequent AER quarterly filings.

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[206] *Id.* at 13-14.

[207] *Id.* at 13.

[208] *See In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Authority to Establish a Standard Service Offer Pursuant to Section 4928.143, Revised Code, in the Form of an Electric Security Plan*, Case No. 08-935-EL-SSO, Stipulation and Recommendation at 10-11 (Feb. 19, 2009).

[209] *See* Ohio Adm. Code 4901:1-40-03(A)(3) and 4901:1-40-04(D).

[210] *River Gas Co. v. Pub. Util. Comm.*, 69 Ohio St.2d 509, 512, 433 N.E.2d 568, 571 (1982).

L. The Supplier-Identity And Supplier-Pricing Information Of Alternative Energy Marketers Should Be Publicly Disclosed.

The Environmental Intervenors maintain that "[t]he public should have the opportunity to fully evaluate FirstEnergy's REC purchases, including the seller identity and prices paid, because ratepayers are ultimately responsible for paying these costs."[211] OCC could not agree more.

The information that FirstEnergy seeks to conceal from the public shows that FirstEnergy made imprudent decisions to purchase In-State All Renewable Energy Credits at excessive prices only from its affiliate—FirstEnergy Solutions. Such information is not trade secret under Ohio law. [212]

Like OCC,[213] the Environmental Intervenors, show in their Initial Brief that some of the information that the Attorney Examiner has ruled to be trade secret information has been in the public domain since the filing of the Exeter Audit Report.[214] As a result of the Attorney Examiner's ruling, the Environmental Intervenors maintain that "[t]he parties and intervenors are thus forced to ceremoniously protect the confidentiality of these alleged trade secrets during Commission proceedings, while the same facts are generally known and openly discussed in the public domain."[215] Such treatment of information is contrary to Ohio's public records law.[216] Accordingly, as urged by the

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[211] Initial Brief of Environmental Intervenors at 31.

[212] Initial Brief of OCC at 58-89.

[213] Initial Brief of OCC at 79.

[214] Initial Brief of Environmental Intervenors at 24-26.

[215] Initial Brief of Environmental Intervenors at 25.

[216] R.C. 149.43. Initial Brief of OCC at 64.

Environmental Intervenors, "the seller identity and pricing information does not qualify as a trade secret and should be publicly disclosed."[217]

IV. CONCLUSION

The record of this proceeding shows the unreasonableness of FirstEnergy's management decisions that should be reasonable and prudent in the interest of customers. The PUCO now must ensure that utilities, such as FirstEnergy, are held to appropriate standards in purchasing power, especially renewables. More importantly, the PUCO must take appropriate actions to ensure that customers are protected from costly purchasing decisions that are imprudent. This is especially the case where, as here, the transaction involves an affiliate.

Respectfully submitted,

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[217] Initial Brief of Environmental Intervenors at 31.

CERTIFICATE OF SERVICE

I hereby certify that a copy of the Reply Brief (CONFIDENTIAL Version) was served on the persons listed below, via electronic service, this 6th day of May 2013.

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Summary: Brief 3 - Reply Brief Unredacted Filed by Office of the Ohio Consumers' Counsel electronically filed by Ms. Deb J. Bingham on behalf of Healey, Christopher Mr.