BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

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. 14-1297-EL-SSO

DIRECT TESTIMONY OF
CHERYL ROBERTO
ON BEHALF OF
ENVIRONMENTAL DEFENSE FUND
AND OHIO ENVIRONMENTAL COUNCIL

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I. INTRODUCTION

Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.

A. My name is Cheryl Roberto. My business address in 1207 Grandview Ave., Suite 201, Columbus, OH 43212.

Q. BY WHOM ARE YOU CURRENTLY EMPLOYED, AND WHAT IS YOUR JOB TITLE?

A. I am employed by Environmental Defense Fund ("EDF") as Associate Vice President, EDF Clean Energy Program.

Q. PLEASE BRIEFLY DESCRIBE YOUR EDUCATIONAL BACKGROUND AND YOUR RELEVANT PROFESSIONAL EXPERIENCE.

A. I earned a B.A. in Political Science from Kent State University, a J.D. from the Ohio State University Moritz College of Law. In my current position at EDF, I lead the national EDF Clean Energy Program. Through regulatory reform and new utility incentives, among other approaches, the EDF Clean Energy Program aims to help modernize our outdated energy infrastructure, accelerate the deployment of cutting-edge, clean technologies into the nation' electric system and break down the regulatory and financial barriers to broad-scale adoption of renewable energy, energy efficiency and other innovative ways to generate, distribute and use energy. Prior to joining EDF, I served as a Commissioner of the Public Utilities Commission of Ohio (PUCO) from 2008 to 2012, where I was the lead commissioner for PUCO's partnership with the United States Department of Energy combined heat and power pilot project. As a member of the National Association of Regulatory Utility Commissioners (NARUC), I served as Co-Chair of the 2012 National Electricity Forum, which centered on envisioning an

intelligent, interactive and resilient electric grid. I also served as a member of the NARUC Task Force on Environmental Regulation and Generation, the Committee on Electricity, as Vice-Chair of the Committee on Critical Infrastructure, and on the board of the National Regulatory Research Institute. During my tenure on the Ohio Commission, I participated in all three prior Electric Security Plan (ESP) cases (12-1230-EL-SSO, 10-388-EL-SSO, and 08-935-EL-SSO) for Ohio Edison Company, The Cleveland Electric Illuminating Company and The Toledo Edison Company ("the Companies"). Prior to joining the Ohio Commission, I served as Director of Public Utilities for the City of Columbus, Ohio. In that capacity, I led a municipal water, wastewater, and electric utility with combined annual operating budget of $400 million dollars, an annual capital budget of $250 million dollars, and a staff of 1300 people serving 15th largest City and 22 Central Ohio political subdivisions. In this role, I oversaw cost of service rate updates for three of the utilities. For the electric distribution utility I structured and negotiated a staggered, load-following power procurement agreement that included pre-existing bilateral contracts and limited owned generation.

Q. ON WHOSE BEHALF ARE YOU TESTIFYING?

A. I am testifying on behalf of EDF and the Ohio Environmental Council ("OEC"), intervenors in this case.

Q. HAVE YOU SUBMITTED TESTIMONY IN ANY PREVIOUS CASES BEFORE THE COMMISSION?

A. I have previously testified in PUCO Case No. 13-2385-EL-SSO concerning the Ohio Power Company's plan to eliminate Time of Use Tariffs; (ii) review the Company's gridSmart Phase 2 Rider; and (iii) review the Company's Economic Development Rider.

WHAT IS THE PURPOSE OF YOUR TESTIMONY?

A. The purpose of my testimony is to review what the Companies have labeled as the Economic Stability Program, but which is more aptly described as a Non-Competitive Purchase Agreement, within their fourth proposed ESP.

II. OVERVIEW OF "NON-COMPETITIVE PURCHASE AGREEMENT" AND OUTLINE OF TESTIMONY

Q. ARE YOU FAMILIAR WITH THE COMPANIES' PROPOSED ECONOMIC STABILITY PROGRAM, OR AS YOU HAVE REFERRED TO IT, THE "NON-COMPETITIVE PURCHASE AGREEMENT"?

A. Yes. The Companies propose to enter into a 15-year commitment to purchase the output from power plants owned by its sister company ("Non-Competitive Purchase Agreement" or "Agreement") FirstEnergy Solutions ("FES"). The Non-Competitive Purchase will be secured or guaranteed by payments made by their customers under a new fee or tariff which they propose to call a "Retail Rate Stabilization Rider" or Rider RRS. Under the Non-Competitive Purchase Agreement, FES would transfer to the Companies the right to sell all output, including energy, capacity and ancillaries, from the FES share of the Ohio Valley Electric Corporation ("OVEC") which includes two sixty-year old, coal-fired power plants (Kyger Creek in Cheshire, Ohio and Clifty Creek in Madison, Indiana) , the fifty-two year old, Sammis coal-fired plant and the Davis-Bessie nuclear plant which is two years from the expiration of its forty-year license. The Companies, pursuant to the guarantee of their customers, would pay their sister company, FES, for the plants' operation and upkeep including but not limited to fuel and environmental compliance obligations and a profit. The customers would assume all risk that the plants will remain

operational. In the case of the Davis-Besse plant, the customers will also assume the risk that the plant will be re-licensed.

The Companies would sell the plants' output into the PJM markets. The Companies would collect from its customers through Rider RRS the difference between the plants' costs (including profits for its sister company) and whatever revenues may be earned in the PJM markets. While the Companies acknowledge that for at least the first years, its customers will be required to subsidize the operation of its sister company's plants, Companies claim that this proposal has a net present value of $800 million for customers over the fifteen year life of the Non-Competitive Purchase Agreement. The Companies stated purpose in proposing this Agreement is to provide electric reliability and price stability to customers.

Q. PLEASE EXPLAIN HOW YOUR TESTIMONY IS ORGANIZED.

A. I have presented my testimony in two sections. First, I explain my recommendation as to why the Commission should reject the Non-Competitive Purchase Agreement Non-Competitive Purchase Agreement. Next, I present recommendations which the Commission should impose on the Companies if the Commission is inclined to approve the Agreement.

III. THE COMMISSION SHOULD REJECT THE NON-COMPETITIVE PURCHASE AGREEMENTNON-COMPETITIVE PURCHASE AGREEMENT

Q. WHAT IS YOUR INITIAL RECOMMENDATION REGARDING THE NON-COMPETITIVE PURCHASE AGREEMENT?

A. I recommend that the Commission should reject the Non-Competitive Purchase Agreement because the Agreement is not necessary to achieve the stated goal of

reliability and it: (1) would harm the market by subsidizing the Companies' uneconomic generation for the near term; (2) would lock the Companies into a risky long-term supply contract; (3) would distort the competitive market; (4) was not developed through an integrated resource process or request for proposal or the Companies' long-term forecast; (5) did not include an evaluation of other types of generation resources, or cost-effective energy efficiency or demand response resources; (6) interferes with wholesale energy and capacity markets; (7) is based on the faulty premise that the Companies are responsible for the reliability of generation and transmission service; (8) could make it more costly for Ohio to comply with the EPA's Clean Power Plan; (9) could provide a windfall for FirstEnergy and the Companies by allowing them to, in effect, receive an improper double recovery of transition costs; (10) involves inconsistent energy and capacity price forecasts than what the Companies have previously submitted to the Commission; and (11) involves an inherent, and unacceptable, conflict of interest among Companies and their affiliates.

Q. HOW WOULD RELIABILY BE ACHIEVED IN THE ABSENCE OF THIS NON-COMPETITIVE PURCHASE AGREEMENTE?

A. Mr. Moul testified that the plants' economic vitality is in doubt because market-based revenues for energy and capacity have been at historic lows and do not cover the costs of making the necessary investments and operating the plants. He testified that this will continue to be the case for the near-term future. As a result, the plants could be retired causing reliability concerns. However, if, in fact, a plant's deactivation would cause reliability concerns, PJM's Open Access Transmission Tariff at Part V - Generation Deactivation provides an avenue for the plant to receive cost of service compensation.

The plant could voluntarily continue operating under a "must run" contract and be compensated in a manner similar to that proposed in the Non-Competitive Agreement. Any costs incurred to provide adequate compensation to the generation owner who would otherwise deactivate a plant would be allocated as an additional transmission charge to those within the area where reliability would be impacted. In other words, there is no reliability reason whatsoever for the Companies to enter any commitment and certainly not a fifteen year commitment to purchase the output from its sister company's plants. If these plants ever become uneconomic to run *and* their deactivation causes a reliability concern, PJM will offer FES a cost-based contract to continue operating – exactly the remedy proposed but without the fifteen year commitment to a Non-Competitive Purchase Agreement.

Q. HOW WOULD THE NON-COMPETITIVE PURCHASE AGREEMENT SUBSIDIZE THE COMPANIES' UNECONOMIC GENERATION?

A. As mentioned above, Mr. Moul testified that the plants' economic vitality is in doubt because market-based revenues for energy and capacity have been at historic lows and do not cover the costs of making the necessary investments and operating the plants. He testified that this will continue to be the case for the near-term future. As a result, the plants could be retired. Only in the later years of the Program are the revenues projected to exceed the costs. To the extent that the costs of the plants exceed revenues, the Companies' customers would subsidize the plants through Rider RRS. This includes customers who have actively chosen to shop for their electricity. For instance, a customer who chooses to use only power that does not contribute to greenhouse gases would still be required to pay -- on top of her own bill for green power -- for the deficit

caused by this Non-Competitive Purchase Agreement for the uneconomic coal-fired plants.

Q. WHY WOULD IT BE RISKY FOR THE COMPANIES TO ENTER INTO THE NON-COMPETITIVE PURCHASE AGREEMENT?

A. The term of the Program is for a 15-year term and it commits the Companies to investing in plants which are already aged and near the end of their useful lives. In fact, in vertically integrated states in which the commissions are still responsible for regulating generation the useful life of a coal-fired plant as assumed for depreciation purposes is between 40 and 60 years. All of the coal units in question will exceed that before the Non-Competitive Purchase Agreement even begins. The Agreement's projected benefits arise from the claim that wholesale market prices for energy and capacity will exceed the plants' costs only in the outer years of the Program, so the benefits are back-end loaded. This is a risky proposition because the longer the term covered by an energy market price forecast, the less reliable it is likely to be. This is due, in part, because the forecast is based on economic conditions and economic conditions are difficult to predict for a 15-year period. Moreover, the legal, regulatory and environmental requirements for the plants are presently unknown. The plants are also more likely to have more operational issues as they near the end of their useful lives. It is entirely possible the plants could be retired during the 15-year period, destroying most or all of the alleged value under the Non-Competitive Purchase Agreement, and could cause the Companies' customers to incur a loss.

Q. HOW WOULD THE NON-COMPETITIVE PURCHASE AGREEMENT DISTORT THE COMPETITIVE MARKET?

A. In recent years, Ohio electric distribution utilities have procured their supply for default customers through a competitive bidding process. This process has been quite successful in procuring supply at a low cost. PJM operates a regional wholesale market which procures energy, capacity and ancillary service through competitive auctions. The PJM markets have also been successful in procuring these services at a reasonable cost. If the Companies' customers would subsidize the plants through the Non-Competitive Purchase Agreement, this would allow the plants to remain in operation even though their actual operating would exceed the revenues earned in the competitive market. This would allow the plants to remain open even though they are non-economic. This would artificially keep wholesale prices lower, and would discourage other market participants from investing in new generation resources. In the long run, the lack of new generation investment would harm the competitive market.

In addition, the Program would interfere with customer choice. The competitive market was designed to provide a level playing such that FirstEnergy could operate its plants in competition with other competitive retail electric suppliers ("CRES"). Under this proposal, the CRES customers would have to pay for generation owned by the Companies, even though the customers do not procure generation service from the Companies. The generation will revert back to FES after the 15-year Program expires. This is an unfair advantage for FES's generation and these subsidies could inhibit other CRES from offering competitive generation service in Ohio over the long term.

Q. HOW DO UTILITIES PRUDENTLY PROCURE GENERATING RESOURCES?

A. For a commission to judge that a utility prudently procured resources, a utility operating under traditional regulation would develop an integrated resource plan ("IRP"). A utility

in a restructured environment should use a competitive process such as issuing a request for proposals ("RFP") or undertaking an auction. In both cases, the utility would consider all types of generating resources and demand side resources including energy efficiency, storage, distributed generation and demand response.

Q. DID THE COMPANIES DEVELOP AN IRP OR ISSUE AN RFP IN THIS CASE?

A. No.

Q. DID THE COMPANIES EVALUATE BUILDING NEW GENERATING RESOURCES OR BUYING THE OUTPUT FROM NEW GENERATING RESOURCES OTHER EXISTING GENERATING RESOURCES?

A. No.

Q. DID THE COMPANIES EVALUATE OR ISSUE RFP FOR ENERGY EFFICIENCY, STORAGE, DISTRIBUTED GENERATION OR DEMAND RESPONSE RESOURCES AS AN ALTERNATIVE TO THE NON-COMPETITIVE PURCHASE AGREEMENT?

A. No.

Q. HOW DOES THE COMPANIES' FAILURE TO USE A COMPETITIVE PROCESS OR EVALUATE ANY ALTERNATIVE TO CENTRAL UTILITY SCALE GENERATION IMPACT THE COMPANIES' CUSTOMERS?

A. The result is that the Companies cannot establish that the Non-Competitive Purchase Agreement is just and reasonable. Assuming higher energy and capacity prices will occur, the Companies did not act in the customers' interests by trying to obtain the most cost-effective solution to mitigate the higher prices. Instead, the Companies simply accepted the only deal they evaluated – from their sister company, FES. Additionally,

Companies are proposing to eliminate time variant pricing, critical peak pricing, and demand response programs that could be used to optimize load. Prudency requires that the Companies should have issued a competitive process to obtain the most cost-effective solution for mitigating future higher prices and undertaken all cost-effective actions to optimize load.

Q. HOW WOULD THE NON-COMPETITIVE PURCHASE AGREEMENT IMPACT WHOLESALE ENERGY AND CAPACITY MARKETS?

A. The Program improperly interferes with wholesale energy and capacity markets, which are preempted by the federal government. The Companies' Proposal is similar to New Jersey legislation, which was recently ruled invalid on federal preemption grounds in the 3rd Circuit Case of *PPL EnergyPlus, LLC v. Solomon*.[1] In *Solomon,* several merchant generators sued the New Jersey Board of Public Utilities ("BPU") for approving "contracts for differences" with new generating facilities. The contracts were authorized under a New Jersey law designed to counteract the state's heavy reliance on coal plants and the lack of new generating resources in the state. (Note how this rationale is similar to the Companies' rationale that the region relies too heavily on natural gas plants.) The law authorized the BPU to require utilities to enter into contracts for the construction of new natural gas plants. The owners of the new plants were to receive 15-year contracts at a predetermined price, and the plant owners were guaranteed to receive a fixed level of revenue during the 15-year contract term. The contracts required the plant owners to bid their capacity into the PJM capacity auction. The contracts provided for the utilities to pay the plant owners the difference between the predetermined price for capacity set forth in the contract and the capacity revenues received by the plant owners through the PJM

[1] *PPL EnergyPlus, LLC v. Solomon,* 766 F.3d 241 (3rd Cir. 2014).

auction. The Third Circuit Court of Appeals ruled, in a September 11, 2014 decision, that the New Jersey legislation and the contracts approved by the BPU were preempted by the Federal Power Act, which grants the federal government exclusive jurisdiction over interstate sales and transmission of energy.

In addition, it appears that even if the Commission approved the Program and the Companies bid the plants' energy and capacity into the PJM markets, and it survived a federal preemption challenge, it is very possible that PJM would apply mitigation measures to the bids, resulting in the bids not clearing the auctions. This could prevent the Companies from receiving a significant amount, and possibly all, of the revenues projected under the Non-Competitive Purchase Agreement.

In this respect, the Non-Competitive Purchase Agreement is similar to the programs adopted by New Jersey and Maryland, which PJM addressed by changing its rules to allow it to apply mitigation measures to bids from ratepayer-subsidized plants bidding into the PJM markets, and addressed in the 3rd Circuit Case of *New Jersey Bd. of Pub. Util. v. FERC.* [2]

The *New Jersey* case arose out of a tariff change implemented by PJM to allow it to apply market mitigation to capacity market bids by state-subsidized generating resources. PJM changed its tariff to address the New Jersey subsidy plan described above, and a similar subsidy program approved by Maryland. PJM eliminated a tariff provision which had previously allowed utilities to self-supply their capacity through utility-owned generation or power procured by the utility through a bilateral contract. This tariff change made the New Jersey and Maryland ratepayer-subsidized plants subject

[2] *New Jersey Bd. of Pub. Util. v. FERC,* 744 F.3d 74 (3rd Cir. 2014).

to market mitigation. The Third Circuit upheld FERC's order approving the PJM tariff change. Like the New Jersey and Maryland ratepayer-subsidized plants described in the *New Jersey* case, the Companies' plants in the present case could very well be subject to market mitigation. It appears that the Companies tried to distinguish their case from the New Jersey and Maryland programs by providing that the plants' output will not be used to serve default customers. But this is a distinction without a difference. The essential fact is that the Companies would be distorting the wholesale auction process by bidding in ratepayer-subsidized plants, and as a result could be subject to PJM market mitigation measures.

Q. THE COMPANIES CLAIM THAT A KEY REASON FOR THE PROGRAM IS TO PROVIDE RELIABILITY. DO YOU AGREE WITH THIS CLAIM?

A. No. The PJM Interconnection, LLC ("PJM") is responsible for the reliability of generation and transmission service in the areas served by the Companies. PJM's website explains its role:

- Acting as a neutral, independent party, PJM operates a competitive wholesale electricity market and manages the high-voltage electricity grid to ensure reliability for more than 61 million people.

- PJM's long-term regional planning process provides a broad, interstate perspective that identifies the most effective and cost-efficient improvements to the grid to ensure reliability and economic benefits on a system wide basis.

PJM's current Annual Report, available on its website at http://www.pjm.com/about-pjm/who-we-are/annual-report.aspx, elaborates on PJM's mission to ensure reliability:

Reliability and Resilience

> Reliability is the mission and traditional measure of performance for the organizations that operate the nation's electricity grid. PJM Interconnection embraces that mission wholeheartedly.
>
> Reliability means "keeping the lights on" in day-to-day operations and responding quickly and effectively to outages and emergency events that affect transmission and distribution systems.
>
> The nation and region PJM serves count on that commitment to reliability because electricity is the driving force in our digital economy. Our health and welfare and economic well-being depend on a reliable supply of electricity, delivered where and when it's needed at the speed of light.[3]

When FirstEnergy's transmission assets were transferred to PJM in 2009, FirstEnergy represented to the Commission and to FERC that this would not impair, but in fact would enhance, long-term reliability:

> Reliability will not be adversely affected in any way by the RTO alignment.[4]
>
> ATSI [American Transmission Systems, Inc., the Companies' transmission service affiliate] states that PJM's RPM [Reliability Pricing Model] auctions would also enhance the long-term reliability of service to ATSI's customers.[5]

FirstEnergy also acknowledges this in its Annual Report, stating that its only responsibility for reliability is to follow NERC operating, record-keeping and reporting requirements:

> **RELIABILITY MATTERS**
>
> Federally-enforceable mandatory reliability standards apply to the bulk electric system and impose certain operating, record-keeping and reporting requirements on the Utilities, FES, AE Supply, FG, FENOC, ATSI and TrAIL. NERC is the ERO designated by FERC

[3] PJM 2013 Annual Report at 12 (issued May 2014).
[4] *In the Matter of the Proposal of FirstEnergy Service Company to Modify its RTO Participation,* Case No. 09-778-EL-UNC (Comments of FirstEnergy Service Company at 4) (September 25, 2009).
[5] *American Transmission Systems, Inc.; FirstEnergy Service Company v. PJM Interconnection, LLC,* 129 FERC ¶ 61,249 at ¶ 61,344 (2009).

> to establish and enforce these reliability standards, although NERC has delegated day-to-day implementation and enforcement of these reliability standards to eight regional entities, including RFC. All of FirstEnergy's facilities are located within the RFC region. FirstEnergy actively participates in the NERC and RFC stakeholder processes, and otherwise monitors and manages its companies in response to the ongoing development, implementation and enforcement of the reliability standards implemented and enforced by RFC.[6]

The Companies' suggestion that these plants need to stay open for reliability purposes is a false premise. As noted above, the Companies are not responsible for ensuring reliability of generation and transmission service. PJM has this responsibility. If PJM determines that any of these plants need to remain open beyond their announced retirement dates for reliability purposes, then PJM can designate the plants as "reliability must run" plants. This would allow the plants to remain open beyond their planned retirement date. And the cost responsibility would be borne by PJM's customers, not exclusively by the Companies' default customers and shopping customers.

Q. COULD THE NON-COMPETITIVE PURCHASE AGREEMENT MAKE IT MORE COSTLY FOR OHIO TO COMPLY WITH THE EPA'S CLEAN POWER PLAN?

A. Possibly so, because the Program would cause a significant amount of coal generation to remain open beyond its normal retirement date. The Companies apparently did not include such additional costs in their cost/benefit analysis, so the Commission should reject the proposal.

[6] FirstEnergy 2013 Annual Report at 52, available at: https://www.firstenergycorp.com/content/dam/investor/files/annual-reports/2013/2013-FirstEnergy-Annual-Report.pdf:

Q. WOULD THE NON-COMPETITIVE PURCHASE AGREEMENT PROVIDE A WINDFALL FOR FIRSTENERGY AND THE COMPANIES?

A. Yes. After Ohio restructured its retail generation market beginning with the passage of S.B. 3 in 1999, the Companies filed a transition plan, claiming that the cost of its generating plants were higher than the plants' market value. As a result, the Commission allowed the Companies to recover this difference in value in the form of transition revenues. The Non-Competitive Purchase Agreement would unfairly enrich FirstEnergy because it would, in effect, provide for a double-recovery of transition costs for these plants, which the Companies admit are currently uneconomic. This is prohibited by R.C. 4928.38, which provides:

> **4928.38 Commencing and terminating transition revenues.**
>
> Pursuant to a transition plan approved under section 4928.33 of the Revised Code, an electric utility in this state may receive transition revenues under sections 4928.31 to 4928.40 of the Revised Code, beginning on the starting date of competitive retail electric service. Except as provided in sections 4905.33 to 4905.35 of the Revised Code and this chapter, an electric utility that receives such transition revenues shall be wholly responsible for how to use those revenues and wholly responsible for whether it is in a competitive position after the market development period. The utility's receipt of transition revenues shall terminate at the end of the market development period. With the termination of that approved revenue source, the utility shall be fully on its own in the competitive market. The commission shall not authorize the receipt of transition revenues or any equivalent revenues by an electric utility except as expressly authorized in sections 4928.31 to 4928.40 of the Revised Code.

Q. WHY DOES IT APPEAR THAT THE COMPANIES HAVE USED INCONSISTENT ENERGY AND CAPACITY PRICE FORECASTS THAN WHAT THE COMPANIES HAVE PREVIOUSLY SUBMITTED TO THE COMMISSION?

A. The Companies are required to file long-term forecast reports. The Companies' most recent long-term forecast was *Ohio Edison Company, The Cleveland Electric Illuminating Company, The Toledo Edison Company and American Transmission Systems, Incorporated 2014 Electric Long-Term Forecast Report to The Public Utilities Commission of Ohio,* Case No. 14-0625-EL-FOR (filed April 15, 2014). This forecast projects electricity usage for the next ten years. The amount of electricity usage is based on forecasts of energy and capacity prices. The Companies apparently did not use these price forecasts in developing the Non-Competitive Purchase Agreement, but rather hired Judah Rose, an outside expert, to do so. The Commission should not approve the Program unless the Companies establish that the energy and capacity prices used by Mr. Rose in his forecast are the same as used by the Companies to develop their long-term forecast report.

Q. PLEASE EXPLAIN HOW THE NON-COMPETITIVE PURCHASE AGREEMENT INVOLVES AN INHERENT AND UNACCEPTABLE CONFLICT OF INTEREST AMONG FIRSTENERGY AND ITS AFFILIATES.

A. FirstEnergy clearly has an inherent and unacceptable conflict regarding these plants. In past cases where the Commission has approved Electric Security Plans, the utilities dedicated their plants to serve default customers, the utilities dedicated their entire Ohio fleet, a price was set, the plans were short-term and market conditions justified the plans. But this plan is different because the wholesale energy and capacity markets are functioning effectively and FirstEnergy has culled out these plants from its fleet for the alleged benefit of their customers, for a risky, long-term deal.

These plants are currently operating in PJM's competitive wholesale energy and capacity markets, and are not dedicated to serve the Companies' default customers. If FirstEnergy expects these plants to be profitable during the next 15 years, it should retain this value for its shareholders. FirstEnergy has a fiduciary duty to its shareholders to do so.

The Companies claim in this case that the Non-Competitive Purchase Agreement is a great value because wholesale energy and capacity prices will substantially increase during the next 15 years, resulting in a net present value of $770 million for customers. But consider what FirstEnergy told its shareholders – that environmental and market conditions are so uncertain that *it cannot be determined* whether its plants will be profitable over the long term. This is the *exact opposite* of what the Companies are claiming in this case. Here is FirstEnergy's statement to its shareholders from its most recent Form 10-K filed with the Securities and Exchange Commission:

> There are a number of initiatives to reduce GHG emissions under consideration at the federal, state and international level. Environmental advocacy groups, other organizations and some agencies in the United States and elsewhere are focusing considerable attention on CO2 emissions from power generation facilities and their potential role in climate change. There is a growing consensus in the United States and globally that GHG emissions are a major cause of global warming and that some form of regulation will be forthcoming at the federal level with respect to GHG emissions (including CO2) and such regulation could result in the creation of substantial additional costs in the form of taxes or emission allowances. As a result, it is possible that state and federal regulations will be developed that will impose more stringent limitations on emissions than are currently in effect. Due to the uncertainty of control technologies available to reduce GHG emissions, including CO2, as well as the unknown nature of potential compliance obligations should climate change regulations be enacted, *we cannot provide any assurance regarding the potential impacts these future regulations would have on our operations.* In addition, any legal obligation that would require us

to substantially reduce our emissions could require extensive mitigation efforts and, in the case of carbon dioxide legislation, would raise uncertainty about the future viability of fossil fuels, particularly coal, as an energy source for new and existing electric generation facilities. *The impact that any new environmental regulations, voluntary compliance guidelines, enforcement initiatives, or legislation may have on our results of operations, financial condition or liquidity is not determinable*, but potential legislative or regulatory programs restricting CO2 emissions, or litigation alleging damages from GHG emissions could require significant capital and other expenditures or result in changes to its operations.[7]

IV. RECOMMENDATIONS IF THE COMMISSION APPROVES THE ECONOMIC STABILTY PROGRAM

Q. WHAT RECOMMENDATIONS DO YOU MAKE IF THE COMMISSION DECIDES TO APPROVE THE NON-COMPETITIVE PURCHASE AGREEMENT?

A. If the Commission is inclined to approve the Agreement, I recommend that the Commission impose the following requirements: (1) that the Commission hire an independent expert to develop a COMPETITIVE PROCESS which evaluates various types of generating resources, including centralized utility scale and distributed generation, energy efficiency, storage, and demand response (including time variant pricing) to accomplish the Companies' professed goal of mitigating the impact of long-term wholesale energy and capacity prices; (2) that the Companies amend their corporate separation plans to rule out any future wholesale power purchases from an affiliate;

Q. PLEASE EXPLAIN WHY YOU RECOMMEND THAT THE COMMISSION HIRE AN INDEPENDENT EXPERT TO DEVELOP A COMPETITIVE PROCESS WHICH EVALUATES VARIOUS TYPES OF GENERATING

[7] FirstEnergy Corp. 2013 Form 10-K Annual Report at 38. (Emphasis added).

RESOURCES, INCLUDING CENTRALIZED UTILITY SCALE AND DISTRIBUTED GENERATION, ENERGY EFFICIENCY STORAGE, AND DEMAND RESPONSE TO ACCOMPLISH THE COMPANIES' PROFESSED GOAL OF MITIGATING THE IMPACT OF LONG-TERM WHOLESALE ENERGY AND CAPACITY PRICES.

A. The Companies claim that the Agreement has a net present value of $770 million, due to projected increases in wholesale energy and capacity prices during the outer years of the 15-year term. The Companies propose to provide customers with the output from these plants and to obtain full cost recovery in the form of non-bypassable charges. But there is no evidence that the Companies considered any other alternative solutions to mitigate higher prices.

Prudency requires that the Company should hire an independent expert to develop an RFP which evaluates various types of generating resources, energy efficiency and demand response to accomplish the companies' professed goal of mitigating the impact of long-term wholesale energy and capacity prices. This would allow the Companies to obtain the best and most cost-effective solution to mitigate higher prices. It would be unjust and unreasonable to approve this Program without requiring such a competitive process.

The Companies have demonstrated that significant, cost-effective energy efficiency and demand response resources are available. For example, Chairman Johnson's November 24, 2014 report to the Energy Mandates Study Committee states that the Companies' energy efficiency programs used a third-party administrator to achieve 507 million kWh in energy savings at an average cost of 1.1¢/kWh. The

Companies' energy efficiency and peak demand reduction annual report for 2013, filed in Case No. 14-0859-EL-EEC, states that the Companies were able to achieve approximately 2.5 million MWh in cost-effective energy savings and 1,000 MW of peak demand reductions in calendar year 2013. Not only are these resources less expensive than conventional generation, but also these are clean energy resources, so they would not increase Ohio's cost to comply with the Clean Power Plan.

When the independent expert designs the RFP, they should base it on Mr. Rose's forecast for future wholesale energy and capacity prices. This will ensure that the Companies procure all cost-effective energy efficiency and demand response during the relevant time period. Using this approach, the Companies could obtain much greater value for their customers than the $770 million net present value claimed for the Non-Competitive Purchase Agreement.

Q. DO YOU HAVE AN OPINION AS TO WHETHER BARRIERS STILL EXIST TO FULL RETAIL COMPETITION IN OHIO?

A. Yes, in my opinion, barriers to retail competition in Ohio still exist. This case is an excellent example of how these barriers operate – with the Companies attempting to impose the costs of their sister company's uneconomic plants not only on the Companies' default customers but also on customers who purchase their generation from competitive retail electric service providers ("CRES") while at the same time failing to optimize load through proven strategies such as time variant pricing and demand response and under investing in technologies that empower customers to participate in energy choice or that squeezes more efficiency out of the grid through integrated volt var control. While the electricity market has been restructured in Ohio, "wires" utilities are not free market

competitors. They remain monopolies – enjoying a state-granted right to serve captive customers exclusively. In return for that right of exclusivity, what should we expect? In my opinion, the role of economic regulation for monopoly "wires" utilities in Ohio's restructured environment must be to ensure that they provide a platform for CRES services and services from other third-parties.

The former vertically integrated system was based upon centralized generation fired by tax-subsidized fossil fuels with transmission and distribution lines providing a one-way delivery system to meet customers' needs. The entire system was constructed with very little risk to private capital because the companies enjoyed state-granted monopoly rights to serve together with a safe, regulated return on investment (which is why utility stocks were called "widows and orphans stocks"). With the electrification of the United States, year after year load growth made large-scale generation an economically efficient choice. For a century, our energy needs were met by state-granted monopolies to serve. Corporate affiliates of the "wires" utilities still own the generating plants built through rate of return regulation which are located at all of the best sites – near load centers and transmission line access (which they own as well).

In this time of transformation, however, from a one-way power delivery network to a two-way flow of both power and information when load growth is modest or flat and distributed generation alternatives are becoming cost competitive, the monopoly "wires" utilities must become a platform for integration of the full range of competitive and innovative retail electric services. In order for customer choice to become truly operative, customers must receive information about their usage (when and how much electricity they use) and price signals indicating moment-by-moment the changing price

of electricity. Distributed resource alternatives must be given a fair chance to compete and smoothly integrated into the grid with no preference given to the incumbent centralized generation. The diversity of options will provide opportunities to customers to hedge risk for both price and reliability (customers may find that their electric vehicle may be plugged back into their home to provide power to ride out storm outages and to obtain the most efficient prices for electricity service.

To realize the economic and environmental gains made possible by harnessing this transformation and not blocking it, the monopoly "wires" system must be scrubbed of all artifacts of its former bias toward not only its corporate affiliates but toward centralized generation. A truly level competitive playing field means that the monopoly "wires" system is motivated only to meet its customers' needs . Its success would be based upon the access it provides to the full range of cost-effective solutions – whether from centralized generation or a distributed resource, including generation, demand response, and energy efficiency. If we fail to get regulation of the monopoly "wires" utility right, Ohio will fall behind other states. Technologies and opportunities that we cannot imagine today will not be built or available here. Imagine if protectionist legislation or regulation had been adopted to block wireless and internet adoption in Ohio, even though these technologies were adopted in other states. What technology applications and price choices would our families and businesses not be able to enjoy today? Getting regulation of monopoly "wires" in Ohio right means ensuring that they provide a platform for the full range of market competition for retail electric services free from market barriers.

Q. HOW SHOULD THE COMMISSION ADDRESS THESE MARKET BARRIERS TO COMPETITION?

A. The Commission should (1) open a statewide investigation into how the Commission can develop a new business model for utilities, using performance metrics and incentive regulation, to achieve desired outcomes; (2) require the Companies to open their billing systems to be used to finance clean energy projects; and (3) require the Companies to amend their corporate separation plans to eliminate power purchases from affiliates at a minimum.

Q. WHY SHOULD THE COMMISSION DEVELOP A NEW BUSINESS MODEL FOR UTILITIES?

A. Current regulatory rate structures continue to reward monopoly "wires" behavior consistent with the former structure of vertically integrated, centralized generation. The utilities have an opportunity to enhance earnings in three ways: (1) reduce their expenses below those documented during the last rate case; (2) sell more electricity than was captured in the billing determinants in the last rate case; or (3) invest in capital infrastructure. None of these opportunities provides a clear avenue for the utilities to earn more for providing unfettered access to competitive retail electricity choices or for providing "negawatt" services such as demand response and energy efficiency.

If the Commission develops a new utility business model, this would free the utility to be innovative. This would reward the monopoly "wires" utilities for performance consistent with their responsibility to provide a platform for competitive energy services. The following are features of monopoly "wires" operations that support a competitive platform:

- A partnership between the utility and "prosumers" (proactive consumers engaged not only in the consumption of a product or service but in its design or development) – with each party both buying and selling electricity and electrical services.
- The utility fully and timely recovers distribution system costs. All utility customers should pay the value of the distribution systems to them whether receiving electricity from or contributing electricity to the grid.
- The utility should pay for benefits it receives from customer-sited resources taking into account all the value it provides the system including the value of deferring distribution resources like substations and transformers, peak power prices where appropriate, and hedging benefits.
- The utility must invest in the technology to make both the grid and consumers smarter about the flow of electricity with sensors, telecommunications, and computer technology. The rate of return on these investments must be tied to providing benefits to consumers and the environment.
- The utility must make their customer data available to third party vendors, within privacy limits approved by the customers. Utilities should facilitate the use of customer data by third party vendors to develop energy applications for the customer.
- The system needs to be open up to third party innovation. Utilities must provide an open platform on a non-discriminatory basis to clean technology third party providers. The system should provide payments to the utility for each time a third

party innovation or the equivalent of a clean energy "app" is sold to give utilities incentives to maximize penetration of clean energy apps.

- Rules for Interconnection for third party generation including roof top solar and microgrids should be easy and predictable and be able to be completed quickly.
- The utility should be provided the ability to retain earnings when operational costs are reduced through enhanced distribution system efficiency.
- The utility should have an ability to earn more for superior performance (including metrics related to increased customers' competitive access to a broader range of energy services.)

Q. WHY SHOULD THE COMMISSION ORDER THE COMPANIES TO OPEN UP THEIR BILLING SYSTEMS?

A. Monopoly "wires" utilities have a direct relationship with their customers through their billing systems. The billing system is open for competitive retail electric suppliers. It is not, however, open to competitive financial providers or competitive energy service providers. Even though competitive providers are willing to offer financial products and energy services which would enable customers to invest their own money in cost-effective energy efficiency upgrades at no upfront cost and pay for them over time, these providers are not permitted access to the billing system to service these loans. As they operate today, the monopoly "wires" utilities preferentially provide access to their billing systems to energy providers while not providing the same access to energy efficiency or financial services providers. The Commission should solve this problem by requiring the Companies to add on-bill repayment programs. These products enable a customer to use private capital to choose to meet their energy needs in the manner that works

best for them. No rate payer or utility dollars are involved.

Q. PLEASE EXPLAIN WHY THE COMMISSION SHOULD REQUIRE THE COMPANIES TO AMEND THEIR CORPORATE SEPARATION PLANS TO EXCLUDE WHOLESALE POWER PURCHASES FROM AN AFFILIATE?

A. Monopoly "wires" utilities share senior management, investors, and a board of directors with their affiliate competitive generation company and their affiliate federally regulated transmission company. This corporate structure creates inherent and insurmountable conflicting mixed economic incentives. High performance by the monopoly "wires" utility in creating a platform for competition for the full range of retail electric services can only serve to disadvantage the sister affiliate. While the monopoly "wires" utility should be endeavoring to level the playing field between centralized generation and distributed generation, fossil-fuel generation and renewable generation, and energy and energy efficiency, the generation affiliates' economic success is built upon entrenching reliance upon existing fossil-fuel fired centralized generation. Competing financial interests put the affiliates at odds. When permitted to compete on a level playing field at the wholesale level, traditional generation will be and has been bumped off the stack by demand response, renewables, and energy efficiency. We should expect no less in our retail competitive environment. This corporate dilemma is documented in SEC statements by FirstEnergy, in which it acknowledges that its competitive energy services segment derives its revenue from the sale of generation which is exposed to market risk including energy efficiency and demand response.

Duke Energy and AEP have undertaken and are undertaking substantial investment in technology to support customer choice and access to information in the

form of smart meters. At the same time, FirstEnergy's monopoly "wires" utility has eschewed investing in enabling technology, leaving its customers blind to the meaningful energy usage data which would empower them to participate in market choices. Strategic under-investment in infrastructure circumventing access obligations is classic anti-competitive behavior. Additionally, after investigation, the Commission's expert found that FirstEnergy subjected its captive customers to procurement of renewable energy credits at prices of which it should have been aware reflected significant economic rents and were excessive. FirstEnergy's monopoly "wires" utility has been found by the Commission to have made procurement decisions which were not prudent or reasonable for renewable energy requiring FirstEnergy to refund in excess of $43 million dollars to its captive customers. The Commission acknowledged in its review that FirstEnergy purchased renewable energy credits from its affiliate. Of all monopoly "wires" utilities in Ohio, FirstEnergy has been the least successful in delivering energy efficiency opportunities to its captive customers. Under-investment, imprudent choices, lowest performing energy efficiency programs which harm customers but protect FirstEnergy's generation and transmission assets, these are logical responses from a corporate structure subject to inherent internal economic conflict. As a solution, the Commission should resolve this conflict by requiring the Companies to amend their corporate separation plans to rule out purchases of power from affiliates. Senate Bill 3 required corporate separation but permitted the possibility that it could be achieved through functional or structural corporate separation. Now that all of the monopoly "wires" utilities in the state are or soon will be acquiring energy on a competitive basis and given the inherent conflict that remains when less than full ownership corporate separation is achieved, it is

time to remove the corporate separation loophole by amending the Companies' corporate separation plans.

V. CONCLUSION

Q. DOES THIS CONCLUDE YOUR PRE-FILED DIRECT TESTIMONY?

A. Yes.

CERTIFICATE OF SERVICE

I hereby certify that a true copy of the foregoing has been served upon the following parties by electronic mail this 22nd day of December, 2014.

/s/Trent A. Dougherty
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