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January 10, 2011

Via Electronic Filing
Rosemary Chiavetta, Secretary
PA Public Utility Commission
PO Box 3265
Harrisburg, PA 17105-3265

Re: Joint Application of West Penn Power Company d/b/a Allegheny Power, Trans-Allegheny Interstate Line Company and FirstEnergy Corp. for a Certificate of Public Convenience under Section 1102(a)(3) of the Public Utility Code approving a change of control of West Penn Power Company and Trans-Allegheny Interstate Line Company, Docket Nos. A-2010-2176520 and A-2010-2176732

Dear Secretary Chiavetta:

On behalf of the Retail Energy Supply Association ("RESA") enclosed please find the original of its Exceptions along with the electronic filing confirmation page with regard to the above-referenced matter. Copies are being served in accordance with the attached Certificate of Service.

Sincerely yours,

Deanne M. O'Dell, Esq.

DMO/lww
Enclosure

cc: Hon. Wayne Weismandel, w/enc.
Hon. Mary Long, w/enc.
Office of Special Assistants w/enc (disk)
Cert. of Service, w/enc.

CERTIFICATE OF SERVICE

I hereby certify that this day I served a copy of RESA's Exceptions and upon the persons listed below in the manner indicated in accordance with the requirements of 52 Pa. Code Section 1.54.

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Dated: January 10, 2011

BEFORE THE
PENNSYLVANIA PUBLIC UTILITY COMMISSION

Joint Application of West Penn Power Company d/b/a Allegheny Power, Trans-Allegheny Interstate Line Company and FirstEnergy Corp. for a Certificate of Public Convenience under Section 1102(a)(3) of the Public Utility Code approving a change of control of West Penn Power Company And Trans-Allegheny Interstate Line Company	:	Docket No. A-2010-2176520 Docket No. A-2010-2176732

EXCEPTIONS OF THE RETAIL ENERGY SUPPLY ASSOCIATION

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I. INTRODUCTION

Approving the merger of West Penn Power Company d/b/a Allegheny Power ("Allegheny Power"), Trans-Allegheny Interstate Line Company ("TrAILCo") and FirstEnergy Corp. ("FirstEnergy")(collectively, "Joint Applicants"), as recommended by Administrative Law Judges Wayne L. Weismandel and Mary D. Long ("ALJs") in the Initial Decision dated December 14, 2010, is likely to result in a retail market that deprives consumers from taking advantage of a properly functioning and workably competitive retail generation market. The ALJs ignore this likely outcome by marginalizing the competitive retail market issues in this proceeding, claiming that the Commission's statutory duty requires absolute proof that anticompetitive and discriminatory conduct has occurred in the past and will continue to occur as the result of a proposed merger. This is a clear error of law. Then, compounding this initial error, the ALJs provide the most cursory analysis of the record evidence in opposition to the merger and the non-unanimous Partial Settlement, ignoring some of it and dismissing some of it, to reach the broad conclusion that the benefits of the merger outweigh the negative impacts. The decision, again in error, relies on the non-unanimous Partial Settlement which does not in any significant way address the competitive concerns raised in this proceeding. The Retail Energy Supply Association ("RESA")[1] does not support adoption of the Initial Decision which recommends approval of the merger as modified by the Partial Settlement.

Rather, the Commission should reverse the Initial Decision for several reasons: (1) it fails to apply the proper statutory standards to the proposed merger; (2) it fails to adequately

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[1] RESA's members include ConEdison *Solutions*; Constellation NewEnergy, Inc.; Direct Energy Services, LLC; Energy Plus Holdings, LLC; Exelon Energy Company; GDF SUEZ Energy Resources NA, Inc.; Green Mountain Energy Company; Hess Corporation; Integrys Energy Services, Inc.; Just Energy; Liberty Power; MXenergy; NextEra Energy Services; Noble Americas Energy Solutions LLC; PPL EnergyPlus; Reliant Energy Northeast LLC. The comments expressed in this filing represent the position of RESA as an organization but may not represent the views of any particular member of RESA.

address the record evidence showing that anticompetitive and discriminatory behavior is likely to result if this merger is approved; and, (3) it improperly refuses to apply any of RESA's proposals which are the minimum conditions to minimize the potential for the future merged entity to engage in anticompetitive and discriminatory behavior that must be imposed on the Joint Applicants if this merger is approved. These enhancements include:

(1) revise and strengthen the combined companies' code of conduct;

(2) implement a comprehensive program to inform customers about specific and available retail offers;

(3) implement a properly structured Purchase of Receivables ("POR") program for the service territory of Allegheny Power and expand the current POR program for Met-Ed, Penelec and Penn Power to large C&I customers;

(4) prohibit FirstEnergy from implementing its municipal aggregation programs in Pennsylvania until the Commission issues a final adjudication regarding the legality of such programs;

(5) require that each affiliated company incorporate certain changes in their next default service program filing, including a supplier load cap, so that default service is properly structured to encourage development of the competitive market;

(6) require that all affiliated companies update and revise their operational rules; and

(7) require FirstEnergy and Allegheny Power to retain an independent cost allocation expert to audit the companies' cost allocation practices and affiliate relationships to identify and remove any direct or indirect cross subsidies that provide a benefit to either default service or an affiliated retail supplier.

Without adoption of these meaningful and substantial conditions to stimulate development of a properly functioning and workable competitive market, the merger must be rejected.

II. EXCEPTIONS

The Commission must reverse the Initial Decision for several reasons. First, the Initial Decision is based on a flawed legal analysis and application of the requirements for merger

approval under Sections 1102, 1103 and 2811(e) of the Public Utility Code. Second, a proper application of these merger approval standards to the facts of this case – especially the evidence submitted by RESA but ignored or addressed superficially by the ALJs – requires either a rejection of the merger or the imposition of meaningful conditions to address the anticompetitive and discriminatory conduct likely to occur without them. Finally, the Initial Decision improperly relies on commitments in a non-unanimous Partial Settlement to justify its recommendation to approve the merger even though the record shows that the Partial Settlement commitments are either meaningless or merely restatements of currently imposed obligations on the merging electric distribution companies ("EDCs").

A. Exception No. 1: The Initial Decision is Based on a Flawed Legal Analysis And Application Of The Statutory Standards That Must Be Analyzed When Adjudicating A Proposed Merger Of Four EDCs (COL ## 23, 26, ID at 65-66)

Chapters 11 and 28 of the Public Utility Code include the standards the Commission must analyze and apply when an EDC seeks a change of control through a merger. Chapter 11 contains the Commission's general authority regarding mergers of any type of public utilities while Chapter 28 contains the Commission's authority when the merger involves EDCs. While the Initial Decision did acknowledge that the applicable provisions in both chapters of the Public Utility Code must be analyzed to adjudicate the merger requested in this case, the ALJs relied upon erroneous interpretations and applications of both sections. Further, the Initial Decision failed to adjudicate the Application instead analyzing whether adoption of the non-unanimous Partial Settlement was in the public interest. For these reasons, the Initial Decision must be reversed.

1. The Initial Decision erred in concluding that Joint Applicants are not required to show affirmative competitive benefits pursuant to Section 1103

The Initial Decision erroneously states that the Joint Applicants are not required to "affirmatively demonstrate benefits to competitors" and that Section 1103 only requires the Commission to view competitive impacts "as an integral part of the weighing of benefits against detriments."[2] While the decision minimizes the legal significance of the impact of the proposed merger on competitive retail markets, despite the requirements of both Section 1103 and 2811, to justify its ultimate recommendation, the analysis runs afoul of the clear requirements of Section 1103 and must be reversed.

Section 1103(a) of the Public Utility Code requires the Commission to find that the proposed merger is "necessary or proper for the service, accommodation, convenience, or safety of the public." This standard requires Joint Applicants to demonstrate that the merger will affirmatively promote the service, accommodation, convenience, or safety of the public by creating substantial and affirmative public benefits.[3] According to the Pennsylvania Supreme Court, "competitive impact is a substantial component of a rational net public benefits evaluation in the merger context" and Section 1103(a) gives the Commission the authority to impose just and reasonable conditions to satisfy the public benefit test "even where the Commission finds benefit in the first instance."[4] Thus, the affirmative public benefits test requires an assessment of

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2 I.D. at 65-66.

3 *City of York v. Pa. P.U.C.*, 295 A.2d 825 (Pa. 1972). To ensure that a proposed merger satisfies these standards, Section 1103(a) specifically permits the Commission to impose conditions in granting a certificate of public convenience. 66 Pa. C.S. § 1103(a).

4 *Popowsky v. Pa. P.U.C.*, 937 A.2d 1040, 1056-1057 n. 21 (Pa. 2007).

the effect of the proposed merger on existing and potential competition and whether competition will be affirmatively advanced if the proposed merger is approved.[5]

Here, Joint Applicants offered nothing in their initial application to show how the proposed merger will affirmatively benefit the competitive retail market, while RESA (and other parties) provided evidence showing how the proposed merger is likely to adversely affect competition in the post-merger FE service territories. In the face of the clear record evidence showing how the proposed merger is likely to result in anticompetitive or discriminatory behavior, Joint Applicants failed to offer anything to successfully rebut this evidence. Only at the 11th hour did Joint Applicants make a meager attempt to create the impression that they were taking competitive retail market concerns seriously by proffering the Partial Settlement which they claim – and the ALJs erroneously agree – fully satisfies competitive retail market issues. As discussed below in Section C, the Partial Settlement does not as a matter of fact or law address the competitive market concerns raised in this proceeding nor is it sufficient to satisfy the Joint Applicants' burden pursuant to Section 1103.

2. The Initial Decision erred in concluding that the merger of EDCs must be approved pursuant to Section 2811(e) unless there is a finding that anticompetitive or discriminatory conduct will result

While the ALJs accurately quote the requirement of Section 2811(e) that the Commission must consider whether the proposed merger "is likely to result in anticompetitive or discriminatory" conduct, the ALJs incorrectly conclude that "the statutory provisions support the view that the relevant inquiry is whether the merger will have an adverse impact upon retail

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5 *See, e.g., Joint Application of Commonwealth Telephone, CTSI, LLC and CT Telecom, LLC*, Docket No. A-310800F0010, et al. (Order entered February 8, 2007); *Joint Application of Verizon Communications, Inc. and MCI, Inc. For Approval of Agreement and Plan of Merger*, Docket No. A-310580F0009, et al. (Order entered January 11,2006)..

markets."[6] By focusing on whether the proposed merger "will" have an adverse impact upon retail markets, the ALJs have failed to engage in the analysis of this merger required by Section 2811(e) and, therefore, their determination that the merger meets the standard must be reversed.

Section 2811(a) is clear that the Commission is required to "monitor the market for the supply and distribution of electricity to retail customers and **take steps . . . to prevent anticompetitive or discriminatory conduct** and the unlawful exercise of market power."[7] The Commission is specifically charged with this duty when EDCs request "approval of proposed mergers, consolidations, acquisitions or dispositions" as the Joint Applicants are requesting here.[8] Pursuant to this statutory duty, the Commission is required to "consider whether the proposed [transaction] **is likely to result in** anticompetitive or discriminatory conduct, **including** the unlawful exercise of market power, which will prevent retail electricity customers in this Commonwealth from obtaining the benefits of a properly functioning and workable competitive retail electricity market."[9]

In other words, the Commission is not required – as a precondition to taking "steps" to "prevent" such actions from occurring in the future as required by Section 2811(e)(2) – to conclude that the Joint Applicants have in the past engaged in anticompetitive or discriminatory behavior or that they will engage in such behavior in the future. Rather, the Commission is required to analyze whether the merger "is likely to result in" anticompetitive or discriminatory conduct which, as discussed further below, has certainly been proven by any fair and objective view of the record evidence in this case.

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6 I.D. at 65-66 (emphasis added and original).

7 66 Pa.C.S. § 2811(a) (emphasis added).

8 66 Pa.C.S. § 2811(e).

9 66 Pa. C.S. § 2811(e)(1) (emphasis added).

If the ALJs' interpretation and application of the requirements of Section 2811(e) are adopted, then the General Assembly's special directives in Chapter 28 with respect to retail competition would effectively be rendered meaningless. This is because, pursuant to the ALJs' logic, consumers would first have to be harmed by anticompetitive and discriminatory behavior before the Commission could address it. This flies in the face of common sense and good public policy as well as the statutory language. This would also be detrimental to the public by placing the Commission in the helpless position of not being any to take proactive steps to prevent anticompetitive or discriminatory conduct from occurring. Clearly, Section 2811(e) is intended to permit the Commission to prevent the harm to consumers before it occurs. The ALJs' narrow and restrictive view of the legal standards governing the Commission's review of competitive issues in EDC mergers like the one in this case cannot be accepted.

3. The Initial Decision erred in failing to actually adjudicate the Application

In addition to misconstruing the applicable statutory standards, the ALJs erred in failing to adjudicate the Application. Rather, they focus on whether there is "substantial evidence consistent with the statutory requirements [to] support the proposed settlement" instead of focusing on whether there is substantial evidence to support approval of the Application.[10] The Partial Settlement here is a non-unanimous settlement, and the standards for reviewing a non-unanimous settlement are the same as those for deciding a fully contested case. In other words, the Commission is required to adjudicate the claims of the remaining active parties as if no settlement had been submitted. While the ALJs recognize this principle, the Initial Decision does not actually apply it. Rather, the ALJs state:

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[10] ID at 38 (citations omitted, emphasis added).

> The Commission encourages parties in contested on-the-record proceedings to settle cases.... By definition, a "settlement" reflects a compromise of the parties' positions, which arguably fosters and promotes the public interest. When parties in a proceeding reach a settlement, the principal issue for Commission consideration is whether the agreement reached suits the public interest. . . . The Joint Petitioners declare this Joint Petition is in the public interest and it should be approved for the reasons expressed in the foregoing sections of this decision.
>
> It is true, as Direct Energy, RESA and others point out, that not every consequence of the proposed merger is necessarily positive or a benefit. Nor do the modifications addressed by the petition for settlement address every concern raised by either the Settling Parties or the non-settling parties. However, neither the Code nor applicable legal precedent requires each and every interest of each and every party to be accommodated in a settlement. In *Middletown Township v. Pa. P.U.C.,* the Commonwealth Court stated that "when the 'public interest' is considered, it is contemplated that the benefits and detriments of the acquisition be measured as they impact on all affected parties, and not merely on one particular group or geographic subdivision as might have occurred in this case." Accordingly, we conclude that in its totality, the benefits of the proposed merger, as modified by the settlement agreement, outweigh the negative impacts and we will approve the requested certificate of public convenience.[11]

As is obvious from this candid explanation of their analysis, the ALJs failed to adjudicate the Application and instead focused on whether to accept or reject the Partial Settlement. In 2003 the Commonwealth Court warned against such action.[12] Moreover, the law requires the Commission to issue an adjudication in any contested proceeding and to include the findings of fact and conclusions of law relied upon to show whether proper weight was given to the

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11 ID at 74-75 (footnotes omitted).

12 "The danger of such an approach is obvious. Parties with a substantial interest in a utility proceeding can be left out of the decision-making process. . . . Furthermore, in their zeal to reap the benefits of the non-unanimous settlement process, commissions shift the burden of proof to the non-consenting parties by forcing them to prove the unreasonableness of the settlement. While both traditional regulatory hearings and the unanimous settlement process provide protection for all parties, the non-unanimous settlement process places some parties at a severe disadvantage...."*ARIPPA v. PA PUC,* 792 A.2d 636, 659 (Pa. Cmwlth. 2002) (quoting *Krieger*, Problems for Captive Ratepayers in Non-unanimous Settlements of Public Utility Rate Cases, 12 Yale J. on Reg. 257, 265 (1995)) , appeal denied, 815 A.2d 634 (Pa. 2003).

evidence."[13] An adjudication must rule on the matter before the agency – in this case the matter is whether the Application should be approved and whether a certificate of public convenience and necessity should be issued pursuant to Sections 1102, 1103 and 2811(e) of the Public Utility Code.

The Initial Decision, however, does not meet these due process and statutory standards. Instead, the framework of the ALJs' analysis is whether any objections raised by the non-settling parties are sufficient to warrant a rejection of the overall result proffered by the Partial Settlement.[14] Similarly, the Initial Decision's "findings" are singularly focused on accepting the Partial Settlement and not at adjudicating whether the evidence meets the statutory merger standards. The Commission has no statutory authority to proceed as the Initial Decision has done and, therefore, it must be rejected.

B. Exception No. 2: The Initial Decision Erred By Concluding That The Record Evidence Supports Approval Of The Merger (FOF#52, 54-59, 70)

The record makes clear that the proposed merger is likely to result in anticompetitive or discriminatory conduct based on the following three undisputed facts. First, the proposed merger will reduce the number of competitors in Pennsylvania's retail electricity market.[15] Second, and no less important than any of the other reasons, the transition of Allegheny Power's billing and customer information system to the FirstEnergy platform almost a year and a half after generation rate caps expire will disrupt the ability of competitive suppliers to provide service.[16] Finally, a significant increase in the combined entity's market power coupled with its avowed

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13 2 Pa. C.S. § 507; 66 Pa. C.S. § 703(e).

14 ID at 39, 74-75.

15 *See* RESA M.B. at 12-13 for further explanation including record cites.

16 *Id.* at 13-14.

retail marketing strategy to achieve market "dominance" will present greater opportunity and greater incentive for post-merger FirstEnergy companies to pursue actions to maximize profit to shareholders, at the risk of consumer welfare and competitive market development in the merged company's Pennsylvania service territories.[17]

The Initial Decision erred in its analysis of these three points, or, more accurately, the Initial Decision fails to seriously consider them. First, the Initial Decision downplayed the relevance of the fact that the proposed merger would reduce the number of competitors in Pennsylvania's retail electricity market. Second, the Initial Decision completely ignores the fact that the new billing and customer information system for Allegheny Power will have an adverse impact on the core EGS operational systems. Finally, the Initial Decision fails to give proper weight to post-merger FirstEnergy companies' ability and incentive to pursue anticompetitive and discriminatory actions to maximize profit at the expense of Pennsylvania consumers and competitive market development.

1. The Initial Decision erred in minimizing the impact of the Loss of Allegheny Energy Supply

According to Finding of Fact No. 53, "the loss of Allegheny Energy Supply as a competitor will only have a trivial impact on the market due to its small size."[18] The ALJs also seem to rely on the opinion that "there are many alternative suppliers" so, apparently, the loss of one through a voluntary merger is not legally significant.[19] This position, however, is not conducive to fostering the development of a properly functioning and workable competitive market as the Commission is statutorily obligated to do. A properly functioning and workable

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17 *Id.* at 15-23.

18 ID at 26.

19 *Id.* at 63-64.

competitive retail market requires a significant number of competitors in the market who – through competing with one another – will offer the most competitively priced and value added service possible. In this proposed merger, Allegheny Energy Supply will be supplanted by the FirstEnergy EGS affiliate, FirstEnergy Solutions Corp. ("FES"). The role of FES in the FirstEnergy corporate structure and the fact that the merger will increase its power and reach are factors that cannot be ignored when considering the removal of Allegheny Energy Supply from the market under the legal merger standards.

2. The Initial Decision erred in ignoring the disruptive impact of the proposed transition of Allegheny Power's billing and customer information system on the ability of competitive suppliers to provide service

After the merger, Joint Applicants propose to transition Allegheny Power's billing and customer information system to the SAP platform used by the FirstEnergy companies.[20] Transitioning to the FirstEnergy system is likely to result in a decreased ability of the post-merger EDCs to provide EDC operational systems necessary to support a properly functioning and workable competitive market thereby resulting in harm to the competitive market after the merger, solely due to the merger.[21] This, in combination with the structure of default service and the interplay of the FirstEnergy EDCs and their EGS affiliate, creates misaligned incentives for the combined entity to pursue anticompetitive and discriminatory behavior.

The ALJs never squarely address this issue. Rather, they rely on the Partial Settlement as the legally sufficient and proper resolution of this problem.[22] As discussed above in Section

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20 Tr. at 364-366; 428.

21 *See* RESA M.B. at 13-14.

22 ID at 55 ("the [Partial Settlement] represents a reasonable settlement to encourage further retail development in the Allegheny-West Penn service territory") and 59 ("many of the proposals [RESA] lists are adequately addressed by the [Partial Settlement]").

II.A.3, however, the ALJs erred by failing to assess the undisputed record evidence on this issue in the context of making a determination whether the Application should be approved. Beyond this, however, the ALJs erred in their analysis of the Partial Settlement which does not even begin to address all the operational concerns related to the transitioning of Allegheny Power's billing and customer information systems. In some cases, this transition will clearly lead to a "downgrading" of Allegheny Power's current functionality and commitments to match that of FirstEnergy and will be implemented, at the earliest, almost a year and half after the generation rate caps expire in Allegheny Power's service territory.[23] As such, the Initial Decision fails to properly address an undisputed issue in the manner required by due process and statutory standards and must be reversed.

3. The Initial Decision erred in concluding that the undisputed potential of the merged entity to engage in anticompetitive and discriminatory conduct to maximize profit does not warrant either rejection of the merger or the imposition of significant conditions to guard against such behavior

There is no dispute that FirstEnergy's market "dominance" business strategy consists of obtaining revenues through maximizing revenue from its unregulated EGS affiliate, FES. FES controls the generation assets of FirstEnergy and provides generation to default service customers indirectly through EDC default service wholesale procurements and directly as an EGS.[24] Likewise, there is no dispute that the proposed merger would enable FirstEnergy to expand this model – and generate more profits – through four EDC service territories covering approximately 70% of the Commonwealth and through providing service to more than one-third

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23 RESA M.B. at 1314.

24 *See Id.* at 15-23 with supporting record cites.

of all Pennsylvania's electric customers.[25] The question the Public Utility Code requires the Commission to adjudicate is whether the proposed merger should be approved considering FirstEnergy's business plan, coupled with the structure of default service and the increased scale and scope of assets and operations available to FES as a result of this combination of EDCs.

The ALJs do acknowledge that the acquisition of Allegheny Energy's generation assets "may provide [FirstEnergy] with some competitive advantage" and that FES "intends to be an aggressive marketer of retail electricity products."[26] However, the ALJs find that none of this will have an impact on the price of energy, the provision of default service, or the ability of EGSs to enter the market because "any concerns relative to FirstEnergy's intent are both speculative and not related to whether the merger should be permitted or not."[27] This is clearly wrong, and reflects, at worst, a fundamental misunderstanding of the statutory merger standards or, at best, the desire to approve the Partial Settlement regardless of the contrary evidence.

As discussed above in Section II.A, the ALJs have erroneously applied the standards of statutory review the Commission is required to undertake in this proceeding. Additionally, the ALJs have ignored the clear and undisputed record evidence conclusively demonstrating that the concerns related to post-merger anticompetitive and discriminatory conduct are more than just "speculation."

First, the record makes clear that Joint Applicants' current EDC interactions with EGSs are deficient and that, post-merger, these problems will only be exacerbated. These problems arise from the proposed transition of Allegheny Power's billing and customer information system to the SAP platform used by FirstEnergy and the deficiencies present in FirstEnergy's current

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25 RESA St. No. 1 at 6.

26 ID at 67, 74.

27 *Id.* at 26-27, 67, FOF #s 52, 54-57.

supplier support operational systems that, absent Commission action to the contrary, will be carried into the Allegheny Power system.[28]

Second, the record makes clear that post-merger FirstEnergy would have an increased ability to artificially distort the price of default service, thereby making it nearly impossible for competitors to enter and remain in the market. Because the FirstEnergy business model does not recover the costs of billing and other management service through the default service rates, the post-merger EDCs – serving more than a one-third of all Pennsylvanians – would be able to undercut the default service rates against which EGSs have to compete.[29] The more the combined entity is able to undercut these rates, by recovering the costs of service elsewhere within the corporate structure, the less likely EGSs, who must also recover these costs but who lack captive ratepayers from which to do so, will be able to compete.

Third, the record makes clear that the current default service plans of the Joint Applicants are deficient and the post-merger company will have the ability and incentive to extend over a greater area its deficient default service plans to advantage its affiliated generation-owing retail energy supplier. FES controls the generation assets of FirstEnergy and submits bids to its affiliated EDCs to provide wholesale generation for the EDC's default service customers. This creates an obvious incentive for the affiliated EDCs to propose default plan structures which advantage the ability of their affiliated wholesale supplier to submit and win the bid to supply default generation service because their common parent will receive revenue from two sources:

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28 RESA Reply Brief at 10-13.

29 RESA Reply Brief at 16-18.

the purchase by the EDC of the generation at wholesale and retail customers who pay the EDCs or FES for generation services.[30]

Despite all of this evidence – most of which was undisputed in the record – the ALJs still make the incredulous conclusory findings of facts that none of this will have any impact – much less an impermissible impact – on the price of energy, the provision of default service, or the ability of EGSs to enter and remain in the market.[31] The ALJs provide no analysis of this record evidence or any further explanation to support their conclusions. Since these conclusions are not based on any reasoned analysis of the evidence in the record and are further exacerbated by the incorrect application of the statutory merger standards, they cannot be accepted and must be reversed.

C. Exception No. 3: The Initial Decision erred in relying on the commitments in a non-unanimous Partial Settlement to satisfactorily address legitimate competitive retail market concerns and to reject RESA's proposed conditions without any type of detailed analysis (FOF ## 45, 81-82, ID at 55-59)

Importantly, nothing in the Application purported to address competitive retail market issues despite the requirements of Sections 1103(a) and 2811(e) of the Code. Accordingly, numerous parties including RESA raised serious and significant competitive retail market concerns arising from the proposed merger, as explained more fully in the preceding sections. Still, the record response of Joint Applicants was to deny or ignore these concerns. Only at the 11th hour did the Joint Applicants offer their meager Partial Settlement with the half-hearted claim that it sufficiently addresses the legitimate competitive retail market concerns raised in this proceeding based on the legal merger standards.

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30 *Id.* at 18-22.

31 ID at 26-27, FOF #s 52, 54-57.

On the contrary, the Partial Settlement is woefully legally inadequate in addressing the competitive retail market concerns resulting from this merger in the following ways:

•Partial Settlement offers nothing of any substance to mitigate the concerns that a strengthened Code of Conduct as proposed by RESA would resolve. *See* RESA M.B. at 24

•Partial Settlement addressing consumer education merely brings Allegheny Power in line with commitments made by Met-Ed and Penelec and merely addresses the bare minimum of what any EDC should do in terms of educating its distribution customers about retail electricity choice. *See* RESA M.B. at 26

•Partial Settlement offers a less attractive POR program than that offered currently by Allegheny Power. *See* RESA M.B. at 29

•Partial Settlement fails to address concerns regarding the default structure of the four EDCs nor how such structure could be used in an anticompetitive or discriminatory way to deprive customers of a fully functional and workable competitive retail market. *See* RESA M.B. at 30

•Partial Settlement fails to address concerns regarding implying a right of rescission to customers. *See* RESA M.B. at 31-32

• Partial Settlement fails to address providing historical customer usage information to EGSs without charge. *See* RESA M.B. at 32.

• Partial Settlement fails to contain any commitment to address very specific operational concerns raised by RESA regarding monthly operational calls, Advance Notice of Drop transaction, PLC factors, seamless moves, and addressing account attribute changes. *See* RESA M.B. at 32-33.

• Partial Settlement contains no commitment to work with EGSs in a cooperative manner to address the myriad of operational issues needed to support a vibrant competitive market. *See* RESA M.B. at 33.

• Partial Settlement offers no incremental improvement over current practices regarding access to customer data and what "improvements" are offered would not occur until after integration of the computer systems at least a year and a half after the generation rate caps expire in Allegheny Power's service territory. *See* RESA M.B. at 34.

•Partial Settlement introduces operational issues such as the structure of the PTC, eligible customer lists, EDI change requests, billing options which are already required either by the Commission's regulations or other pending Commission directives. *See* RESA M.B. at 34

The Initial Decision offers no analysis or discussion of these stated concerns of RESA regarding the Partial Settlement. Instead, it flippantly dismisses every one of RESA's competitive retail market concerns and proposed conditions as "unnecessary or more appropriately addressed in the context of default service plan proceedings."[32] These concerns are implicated by the statutory merger standards, the specific facts of this case and the way these markets will function if the merger is permitted to occur without conditions intended to mitigate the anticompetitive and discriminatory conduct the evidence shows is likely to occur. As Joint Applicants are seeking the merger and the Commission is statutorily obligated to assess whether that merger is likely to result in anticompetitive or discriminatory conduct, the ALJs' recommendation that these concerns should be deferred to some other future proceeding is inappropriate and just plain wrong. The Commission has a statutory obligation to address these issues now, and the record is clear that they are valid concerns and that anticompetitive and discriminatory conduct is likely to occur if this merger is adopted as proposed. Therefore, the ALJs' position that the Partial Settlement somehow "saves" this merger must be rejected.

Even if the Commission is inclined to approve this merger, then at a minimum the following conditions proposed by RESA must be adopted to prevent the anticompetitive and discriminatory behavior that the record clearly shows is likely to result if the merger is approved:

(1) revise and strengthen the combined companies' code of conduct;

(2) implement a comprehensive program to inform customers about specific and available retail offers;

(3) implement a properly structured Purchase of Receivables ("POR") program for the service territory of Allegheny Power and expand the current POR program for Met-Ed, Penelec and Penn Power to large C&I customers;

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32 *Id.* at 56.

(4) prohibit FirstEnergy from implementing its municipal aggregation programs in Pennsylvania until the Commission issues a final adjudication regarding the legality of such programs;

(5) require that each affiliated company incorporate certain changes in their next default service program filing, including a supplier load cap, so that default service is properly structured to encourage development of the competitive market;

(6) require that all affiliated companies update and revise their operational rules; and

(7) require FirstEnergy and Allegheny Power to retain an independent cost allocation expert to audit the companies' cost allocation practices and affiliate relationships to identify and remove any direct or indirect cross subsidies that provide a benefit to either default service or an affiliated retail supplier.

The ALJs presented no legally sufficient or sustainable reasons for rejecting RESA's recommendations.

(a) RESA's proposal to revise and strength the combined companies' code of conduct

RESA proposed to address the potential for anticompetitive and discriminatory conduct in favor of FES through imposition of an enhanced code of conduct. RESA's recommendations were made because of the specific facts and relationships present in this case and in view of how the specific provisions of the Commission's currently effective Code of Conduct could be strengthened to address these concerns.[33] If the dominance of FirstEnergy in Pennsylvania is permitted to grow through approval of the merger, an enhanced code of conduct specifically tailored to address the concerns related to this entity is a reasonable way to mitigate against anticompetitive and discriminatory behavior which will harm all consumers in the form of less competition and, potentially, increased prices. The Commission addressed similar competitive

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33 RESA M.B. at 23-25.

market concerns in FirstEnergy's previous merger, in part, by adopting (at least initially) a "GENCO" code of conduct.[34]

The ALJs, while recognizing that FirstEnergy's marketing strategies "create challenges to rival suppliers,"[35] fail to address why an enhanced code of conduct as proposed by RESA is not a reasonable way to attempt to mitigate competitive market concerns. The ALJs' failure to address this very important and legally significant issue must be rectified by the Commission.

(b) RESA's proposal to implement a comprehensive program to inform customers about specific and available retail offers

Regarding RESA's proposals to implement a comprehensive program to inform customers about specific and available retail offers, the ALJs dismiss them based on the following reasons: (1) the ALJs conclude that customer education will provide no incremental benefit to ratepayers; (2) the ALJs conclude RESA's proposals would require the EDC to become a "surrogate salesperson" for the EGS; (3) The ALJs state that the record lacks any estimate costs for implementation; (4) the ALJs state that the record lacks any direction at to the bearer of those costs; (5) the ALJs find RESA's proposals "impractical"; and, (6) the ALJs conclude further customer education is unnecessary because of the Partial Settlement.[36] None of these reasons or criticisms has merit.

RESA's proposals are intended to educate consumers who have been receiving electricity service from the same EDC, for years and sometimes decades, and to mitigate the anticompetitive and discriminatory effect of FES's attempting to leverage the "FirstEnergy"

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34 *ARIPPA v. PA PUC,* 792 A.2d 636, 669 (Pa. Cmwlth. 2002)(the Commonwealth Court reversed the Commission's subsequent decision not to require the GENCO code of conduct and required the Commission to reinstate it).

35 ID at 67.

36 *Id.* at 56-57.

name and "brand" and engaging in arguably illegal long-term community and municipal opt-out aggregation programs. The Commission has already concluded that the public interest would be served by consideration of what is commonly referred to as customer referral programs.[37] A program for the post-merger EDCs will address the hesitancy of residential and small commercial customers to seek out competitive market offerings because they are unsure or lack awareness of their choices.

Under RESA's proposal, the post-merger FirstEnergy EDCs would provide customers with information on specific and available retail offers through a variety of communication channels and facilitate customer enrollment with these offers. RESA set forth proposed elements for the proposal and recommended that the implementation details to be worked out in a collaborative with interested parties with final approval by the Commission.[38] The ALJs completely ignored the recommendation to convene a collaborative to address the issues and instead treated RESA's proposal as a "done deal," badly mischaracterized it and then rejected it on those erroneous mischaracterizations.

The ALJ's statement that "it is unclear from the RESA proposal where the funding for its suggested education programs should come from, or even how much additional spending would be needed to implement its program" is simply wrong.[39] RESA's Witness Hudson clearly addressed this issue in his testimony:

> My recommendations are designed to leverage existing communication channels. The EDCs already send bills to customers, so the cost of handling a bill insert with a list of offers should be minimal. The EDCs already send out welcome packets to customers, so the cost of including an additional sheet listing available retail offers should be minimal. The EDCs already have call centers and

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37 52 Pa. Code § 69.1815.

38 RESA M.B. at 25-26 with supporting record cites.

39 ID at 57.

> automated voice response systems that respond to customer inquiries. Call center scripts and/or voice response systems could easily be updated to include a listing of available retail offers. There is no reason to believe that the costs of implementing these measures would be prohibitive. RESA would also support applying a reasonable fee for participating EGSs to cover the true, incremental costs of implementing these programs. This should completely address Mr. Fullem's concern about the impact on consumers of paying for these programs.[40]

Likewise, the ALJs overlooked or ignored the fact that Mr. Hudson also made clear that RESA's proposals were not intended to and would not be designed to require EDCs to "become surrogate salespersons for the EGSs":

> RESA agrees that EDCs should not be in the role of marketing or explaining any particular offerings of individual EGSs, and that is not my recommendation. There are many ways to structure an effective customer referral program. For example, customers calling the EDC for a service-related issue can be asked whether they want to be educated about alternative supply options. Upon an affirmative response, there are several ways the customer could receive further information. For example, as in Connecticut, the customer can be switched to another automated phone system that lists prices for a particular product. Additionally, the same information could be provided by the call center employee who is then capable of switching interested customers to the call center of the alternative supplier for enrollment.

The ALJs also claim that the Partial Settlement in "eleven separate paragraphs encompassing five pages" addresses the areas of concerns intended to be addressed by RESA's customer education proposal.[41] In the Partial Settlement, the settling parties propose to address these consumer and competitive market concerns through a commitment by Allegheny Power to send mailing that "introduces" EGS offers to residential and small C&I customers twice during the period after merger consummation and prior to June 1, 2013.[42] Additionally, three months

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40 RESA St. No. 1-SR at 10.

41 ID at 57.

42 Partial Settlement Petition at ¶ 39.

following integration of the FirstEnergy billing system with the Allegheny Power system the settling parties propose to include in all "new customer" welcome packets an insert promoting the Commission's PAPowerSwitch.com website and the OCA's Residential Electric Shopping Guide.[43] Both of these commitments are meager and do not signify any real attempt to address the consumer and competitive market concerns shown on the record and to be addressed by RESA's customer education program proposal.[44]

The first commitment merely brings Allegheny Power in line with the commitments made by Met-Ed and Penelec in their default service cases. While RESA is supportive of the commitment by Allegheny Power to issue a mailing introducing retail offers to its customers, this commitment is only a minor incremental improvement over existing practices and falls far short of the comprehensive program recommended by RESA.

The second commitment – to include links to the OCA shopping guide and the www.papowerswitch.com websites in a bill insert – merely addresses the bare minimum of what any EDC should do in terms of educating its distribution customers about retail electricity choice. RESA's recommendation, however, would provide customers with a listing of specific and available retail offers in the customer welcome packets along with information on how to enroll in these offers.

Finally, while the Joint Applicants agree that customers on default service may not understand choice and that knowledge about choice could have some benefit,[45] neither of these two Partial Settlement commitments provides any substantial and meaningful benefit to consumers about their options. Neither will address the status quo bias nor the concern about use

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43 *Id.* at ¶ 39.

44 RESA St. No. 1-SR at 9-10.

45 Tr. at 464.

of the "FirstEnergy" name by FES. In contrast, RESA recommends a comprehensive program which will inform customers about specific and available retail offers through a variety of customer communication channels.

The Commission should reverse the ALJ's decision to reject RESA's proposal to require that a collaborative be convened to implement a comprehensive, worthwhile and viable program to inform customers about specific and available retail offers.

(c) RESA's proposal to implement a properly structured POR program

Given the well-established importance of a POR program and the potential anticompetitive and discriminatory incentives that will be created by this merger, RESA recommends that a POR program for the Joint Applicants include the following features:

- Available only for all accounts billed via the EDC consolidated billing option, with no "all in/ all out" restrictions, so an EGS can simultaneously use dual billing for non-POR customers.
- Includes only receivables associated with basic electricity supply services; non-generation products (such as appliance repair) or renewable or alternative energy credits that are not associated with delivered energy should be excluded. However, an EGS could bill a standard green energy product through POR, such as a 50% wind product that includes commodity service bundled with RECs.
- Maintains the current POR payments schedule and format (20 days for commercial customers and 25 days for residential customers).
- Uses a "zero discount" steady state POR discount rate (initially, the discount rate will recover implementation costs only).
- Tracks cost recovery and zeros out the discount when implementation costs are fully recovered from participating EGSs (remaining customers are not charged for implementation costs).
- Provides continued EDC recovery of its uncollectible accounts expense, including uncollectible amounts associated with generation service, in distribution base rates or in an unbundled nonbypassable, non-reconcilable default service support rider that would be submitted as part of the EDC's next base rate case.

- Change EDC electric retail tariffs to treat payment processing of EGS charges on the same basis as default generation service charges and to clarify termination of service for non-payment of purchased receivables.[46]

The ALJs rejected RESA's recommendations by finding that the Partial Settlement "thoroughly addressed the POR issue in this proceeding."[47] While a quick glance at the applicable Partial Settlement provisions ay look like a step forward, the record indicates that Allegheny Power was already in the process of proposing to implement a POR program, although the details were still being formulated.[48] In fact, on November 1, 2010, Allegheny Power filed its proposed supplier tariff which contains the details of its proposed POR program.[49] In its tariff, Allegheny Power proposes to make its POR program available to all customers.[50] Therefore, the proposed settlement term limiting the Allegheny Power POR program to only residential and small commercial customers is actually a less attractive POR program than what would be implemented without the merger, and a step backward, not forward.

(d) RESA's proposal to prohibit FirstEnergy from implementing its municipal aggregation program

RESA raised concerns about the ability of FirstEnergy to structure and utilize municipal aggregation programs in a way that is inconsistent with fostering a vibrant retail market and the best interests of Pennsylvania ratepayers. Accordingly, RESA proposed as a condition of merger approval that FirstEnergy be prohibited from engaging in the use of long-term community and

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46 RESA St. No. 1 at 18.

47 ID at 58.

48 Joint Applicants St. No. 8-R at 12-13.

49 See Docket Number Docket No. R-2010-2207938. On January 6, 2011, Allegheny Power filed an amended version of its Electric Generation Supplier Coordination Tariff which sets forth the details for its POR program.

50 Supplement No. 6 to Electric-Pa. P.U.C. No 1S, Original Page No. 35, Section 12.4.2.

municipal opt-out aggregation programs to increase revenue until the Commission issues a final adjudication of this matter.[51] The ALJs found that "any threat posed by municipal aggregation is too speculative and not sufficiently related to the proposed merger" and, therefore, declined to place any restrictions on the Joint Applicants in this regard.[52] While the Commission is currently addressing this issue in another proceeding, the ALJs erred in concluding that issues concerning FirstEnergy's opt-out municipal aggregation strategy are "outside" the scope of this proceeding, as this is an integral part of FirstEnergy's market "dominance" business strategy. This determination should be reversed.[53]

(e) RESA's proposal to require certain changes in their next default service program filings

As the structure of an EDC's default service procurement plan has a direct and significant impact on the success or failure of competitive retail market development and the result of this proposed merger will be to increase the size and reach of the FirstEnergy companies into the Pennsylvania market, RESA proposed that the post-merger EDCs be required to purse the following changes in their next default service plans submitted to the Commission for approval:

> (1) the post-merger EDCs should be required to implement hourly priced service for all customers with peak demand greater than 100 kW as a condition for approving the merger; and,
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> (2) lowering the amount of supply that can be served by any single wholesale supplier to 33 1/3%.[54]

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51 RESA M.B. at 19-21; Pending before the Commission are three petitions for declaratory order regarding the use of municipal aggregation programs. *See* Docket No. P-2010-2207062.

52 ID at 74.

53 *Id.* at 30, FOF # 79.

54 RESA. St. No. 1 at 20-22.

By requiring the post-merger EDCs to propose these changes in their next default service procurement plans, the Joint Applicants will be providing some reassurance that they will not use the default service plans of their affiliated-EDCs to provide an advantage to their affiliated wholesale supplier.[55] The result will give all wholesale suppliers a fair and equal opportunity to submit bids to supply default service which will result in a default service rate that is market-reflective and against which EGSs will be able to provide competitive retail offers for the benefit of consumers.

Ironically, the ALJs claimed that RESA's proposals related to the default service plans are more appropriately addressed in future default service proceedings yet choose to explain that the OCA's advocacy on this issue was "persuasive" to them. Regarding RESA's hourly priced proposal, the ALJ relied on the OCA's claim that the proposal is contrary to Act 129 requirements.[56] The ALJs erred in this determination because promoting retail competition continues to be a key policy objective of Chapter 28 of the Public Utility Code even after passage of Act 129 amendments. Accordingly, it is appropriate to implement default service pricing structures that will promote robust retail market development. Long-term contracts in many circumstances clearly cannot always be consistent with the objective to create a prudent mix of supply contracts; in other words, long-term, fixed price contracts are inconsistent with the statutory goal of promoting retail competition in certain situations, such as when the amount of future default service load is uncertain or diminishing. The objective of Act 129 is to provide for a default service plan that will lead to least cost generation service for customers. Because Act 129 continues to recognize competition (both wholesale and retail) as the best way of controlling

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55 RESA St. No. 1-SR at 14.

56 ID at 58-59.

energy costs, a default service procurement plan must produce sustainable retail competition, and this competitive retail market will deliver least cost service to customers.

Regarding RESA's load cap proposal, the ALJs similarly relied on the OCA's claim that load caps "could be harmful to ratepayers."[57] As explained by RESA Witness Hudson, a proper load cap will benefit Pennsylvanian ratepayers.[58] The ALJs were premature in rejecting the proposal in this proceeding.

(f) RESA's proposal that all affiliated companies update and revise their operational rules

In order to mitigate concerns regarding the ability of the EDCs to gain a competitive advantage in the retail market through the misuse of EDC-EGS coordination, RESA recommended a number of changes that the Joint Applicants should be required to implement.[59] The ALJs rejected these proposals based on the claim that "many of the proposals . . . are adequately addressed" by the Partial Settlement and that RESA and the post-merger EDCs can "sit down" and discuss the issues after the merger.[60]

As discussed above the Partial Settlement is woefully inadequate in addressing the competitive retail market concerns. Regarding the operational issues, the Partial Settlement offers some changes. But, there are important operational recommendations made by RESA that are not addressed.[61] On the operational issues that the Partial Settlement purports to address, the commitments made by the Joint Applicants either do nothing to mitigate the concern expressed,

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57 *Id.* at 59.

58 RESA St. No. 1-SR at 19.

59 RESA St. No. 1 at 23-26.

60 ID at 59.

61 RESA MB at 31-32.

represent matters that all EDCs are required to do, or include ones that the Joint Applicants would be required to undertake without Commission direction in the process of merging the operations of Allegheny Power.[62] The Partial Settlement also introduces additional operational issues such as the structure of the PTC, eligible customer lists, EDI change requests, billing options, and removal of a yet-to-be approved supplier administrative charge.[63] The PTC structure and eligible customer list commitments are already required either by the Commission's regulations or other pending Commission directives.[64] Likewise, it is RESA's understanding that Allegheny Power already provides both rate ready and bill ready billing, so the commitment to provide "flexible billing options" within three months following the integration provides no incremental benefit.

While RESA recognizes that the Partial Settlement contains an incremental improvement in the form of a modified budget billing platform for Allegheny Power, this improvement merely brings Allegheny Power in line with the practices of most other Pennsylvania EDCs. Further, the Partial Settlement commitment to "discontinue billing EGSs for a Commission-approved supplier administrative charge" is an empty commitment as Allegheny Power has offered no such charge in its currently pending Supplier Coordination Tariff amendments. [65]

Viewed holistically and in the context of the opportunity and incentive for the merged EDCs to engage in anticompetitive and discriminatory behavior related to EGS operational support issues, RESA's proposed operational conditions must be imposed as a condition of approval of the merger. The commitments set forth in the Partial Settlement, relied upon by the

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62 *Id.* at 32-34.

63 Partial Settlement ¶¶ 38, 40, 42, 44, 47.

64 52 Pa. Code § 54.182 (defines PTC); *see Interim Guidelines For Eligible Customer Lists*, Docket No. M-2010-2183412, Tentative Order entered July 15, 2010.

65 *See* Docket Number Docket No. R-2010-2207938.

ALJs, are not enough to address these issues and cannot be relied upon alone as legally sufficient justification for Commission findings that the merger satisfies the statutory standards applicable to competition related matters.

(g) RESA's proposal that the post-merger companies be required to retain an independent cost allocation expert

As the record is clear that the FirstEnergy companies may not be properly allocating to default service customers and FES their share of costs and such misallocation is against Commission policy and may be used to gain an improper advantage, RESA recommends that the Commission order an independent cost allocation and affiliate relationship audit to mitigate concerns regarding the ability and incentive of the combined entity to misallocate costs between and among the affiliated companies, or to bundle default service costs with distribution rates to advantage the EDCs (through default service) or the affiliated-EGS.[66]

The ALJs offered no analysis of their rejection of RESA's proposals in this regard. Rather they set forth three findings of fact which make no sense. First, Finding of Fact Number 88 states that RESA did not undertake a cost allocation analysis to support its proposal.[67] However, RESA's proposal is that a cost allocation audit be undertaken – based, in part, on the undisputed fact that Joint Applicants fail to include billing costs and other management service costs in default service rates.[68] There is no logical reason why RESA's recommendation to undertake an audit should be rejected because RESA did not already undertake the audit before making the recommendation.

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66 RESA MB at 37.

67 ID at 32.

68 Tr. at 517-518.

Second, Finding of Fact No. 89 states that FirstEnergy bills its unregulated subsidiaries directly for costs incurred by them.[69] This, however, does not address how indirect costs are billed to various company affiliates nor does it address the undisputed fact that FES does not get an "indirect" cost assignment of company-wide costs.[70] If FES is not required to pay its fair portion of FirstEnergy "company-wide" expenses because these costs are being born by the regulated affiliates (and their ratepayers), FES is receiving a unfair competitive advantage over their competitors who do not have the similar luxury of forcing their costs on captive ratepayers.

Finally, Finding of Fact No. 90 references the audits conducted by the Commission as well as the Commission's broad statutory powers.[71] Restating this undisputed authority of the Commission does not address the competitive concerns raised in this proceeding nor why RESA's recommendation to require a cost allocation audit as a condition of the merger should be rejected. In sum, the ALJs improperly refused to address the undisputed record evidence showing that the FirstEnergy companies may not be properly allocating to default customers and FES their share of costs. Therefore, the Initial Decision should be reversed.

III. CONCLUSION

For the reasons set forth above, RESA respectfully requests that the Commission reverse the ID and reject the merger proposed by Joint Applicants. If the Commission is inclined to approve the merger, then the below minimum conditions offered by RESA must be directed in an effort to minimize the potential for the future merged entity to engage in anticompetitive and discriminatory behavior:

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69 ID at 32.

70 TR. at 514-515; RESA Cross Exam Exh. No. 2.

71 ID at 32.

(1) revise and strengthen the combined companies' code of conduct;

(2) implement a comprehensive program to inform customers about specific and available retail offers;

(3) implement a properly structured Purchase of Receivables ("POR") program for the service territory of Allegheny Power and expand the current POR program for Met-Ed, Penelec and Penn Power to large C&I customers;

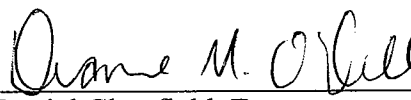
(4) prohibit FirstEnergy from implementing its municipal aggregation programs in Pennsylvania until the Commission issues a final adjudication regarding the legality of such programs;

(5) require that each affiliated company incorporate certain changes in their next default service program filing, including a supplier load cap, so that default service is properly structured to encourage development of the competitive market;

(6) require that all affiliated companies update and revise their operational rules; and

(7) require FirstEnergy and Allegheny Power to retain an independent cost allocation expert to audit the companies' cost allocation practices and affiliate relationships to identify and remove any direct or indirect cross subsidies that provide a benefit to either default service or an affiliated retail supplier.

Respectfully submitted,



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