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February 12, 2004

The Honorable Magalie Roman Salas  
Secretary  
Federal Energy Regulatory Commission  
888 First Street, NE  
Washington, D.C. 20426

**Re: The New PJM Companies and PJM Interconnection L.L.C., et al.;**  
**Docket No. ER03-262-009, et al.**

Dear Secretary Salas:

Pursuant to the procedural schedule established by Presiding Administrative Law Judge ("ALJ") William J. Cowan in "Order Establishing Procedural Schedule and Rules for the Case," issued December 3, 2003, the Coalition of Midwest Transmission Customers, PJM Industrial Customer Coalition, American Forest & Paper Association, and Electricity Consumers Resource Council (collectively, "Industrials") hereby file their Post-Hearing Brief in the above-captioned docket.

As evidenced by the attached Certificate of Service, copies have been served upon all parties of record, as required by the ALJ in "Order on Motion To Compel and Request for Restricted Service List," issued January 6, 2004.

Very truly yours,

McNEES WALLACE & NURICK LLC

By /s/ Robert A. Weishaar, Jr.

\_\_\_\_\_  
Robert A. Weishaar, Jr.

Counsel for the Coalition of Midwest Transmission  
Customers, PJM Industrial Customer Coalition, and on  
behalf of American Forest & Paper Association and  
Electricity Consumers Resource Council

VK/lmc

Enclosures

c: The Honorable Administrative Law Judge William J. Cowan  
All Parties

**UNITED STATES OF AMERICA  
BEFORE THE  
FEDERAL ENERGY REGULATORY COMMISSION**

The New PJM Companies and : Docket Nos. ER03-262-009, *et al.*  
PJM Interconnection, L.L.C., *et al.* :

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**POST-HEARING BRIEF OF THE  
COALITION OF MIDWEST TRANSMISSION CUSTOMERS,  
PJM INDUSTRIAL CUSTOMER COALITION,  
AMERICAN FOREST & PAPER ASSOCIATION, AND  
ELECTRICITY CONSUMERS RESOURCE COUNCIL**

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Consumers Resource Council

Dated: February 12, 2004

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## I. INTRODUCTION AND SUMMARY OF ARGUMENT

On November 25, 2003, the Federal Energy Regulatory Commission ("FERC" or "Commission") issued an order requiring that American Electric Power Company ("AEP" or "Company") fulfill its voluntary commitment to join a Regional Transmission Organization ("RTO"), *i.e.*, PJM Interconnection, L.L.C. ("PJM").<sup>1</sup> The Commission based the November 25 Order on the following preliminary findings, which have been set for hearing in the instant proceeding:

- (1) that AEP's application to join PJM is "designed to obtain economical utilization of facilities and resources in the Midwest and Mid-Atlantic areas" within the meaning of Section 205(a) ("Section 205" or "PURPA Section 205") of the Public Utility Regulatory Policies Act of 1978 ("PURPA");<sup>2</sup>
- (2) that "the laws, regulations, or rules of Virginia and Kentucky are preventing AEP both from fulfilling its merger commitment to join an RTO, and from complying with Order No. 2000;"<sup>3</sup> and
- (3) that Kentucky's and Virginia's (collectively, "States") laws, rules, or regulations at issue in this proceeding are "neither (a) required by any authority of Federal law, nor (b) designed to protect the public health, safety, or welfare, or the environment or conserve energy or are designed to mitigate the effects of emergencies resulting from fuel shortages."<sup>4</sup>

The Coalition of Midwest Transmission Customers ("CMTC"), PJM Industrial Customer Coalition ("PJMICC"), American Forest & Paper Association ("AF&PA"), and Electricity Consumers Resource Council ("ELCON") (collectively, "Industrials") support the Commission's preliminary findings and respectfully submit that the ALJ should reach the same conclusions, which are adequately supported by the evidence in this proceeding, as discussed below.

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<sup>1</sup> See *The New PJM Companies, et al.*, 105 FERC ¶ 61,251 at Ordering ¶ A (November 25, 2003) ("*November 25 Order*"); see also *id.* at PP 2-54 (providing a comprehensive overview of the events preceding the *November 25 Order*).

<sup>2</sup> *November 25 Order* at Ordering ¶ B; see also 16 U.S.C. § 824a-1(a) (2000).

<sup>3</sup> *November 25 Order* at Ordering ¶ C; see also *Regional Transmission Organizations*, 65 Fed. Reg. 809 (Jan. 6, 2000), FERC Stats. & Regs. ¶ 31,089 (1999) ("*Order No. 2000*"), *order on reh'g*, Order No. 2000-A, 65 Fed. Reg. 12,088 (Feb. 25, 2000), *petitions for review dismissed*, *Public Utility District No. 1 of Snohomish County, Washington v. FERC*, 272 F.3d 607 (D.C. Cir. 2001).

<sup>4</sup> *November 25 Order* at Ordering ¶ D.

The groups comprising the Industrials represent a broad and varied base of large customers that operate manufacturing and other facilities throughout the proposed footprint.

CMTC is an *ad hoc* coalition of large industrial end-users of electricity. All CMTC members operate one or more manufacturing facilities in the Midwest and purchase electric delivery service or bundled electric service from at least one of the transmission owners encompassed by the serving areas of the Midwest Independent Transmission Systems Operator, Inc. ("MISO" or "Midwest ISO") and the New PJM Companies. CMTC members consume more than 3 billion kilowatt-hours of energy annually

PJMICC is an *ad hoc* coalition of large commercial and industrial consumers of electricity. PJMICC members operate manufacturing and institutional facilities throughout Delaware, New Jersey, Maryland, and Pennsylvania, as well as West Virginia and Virginia, which are served by PJM West. PJMICC member companies consume more than 9.5 billion kilowatt-hours of electricity annually. Several PJMICC members are also Members of PJM, vote at PJM Members Committee meetings in the End-Use Customer sector, and actively participate in the PJM stakeholder process.

ELCON is a national association of industrial consumers of electricity organized to promote the development of coordinated and rational federal and state policies that will assure an adequate, reliable, and efficient electricity supply for all users at competitive rates. ELCON member companies produce a wide range of products from virtually every segment of the manufacturing community. The member companies of ELCON consume approximately five percent (5%) of all electricity in the United States.

AF&PA is the national trade association of the forest, pulp, paper, paperboard, and wood products industry in the United States. AF&PA's members are among the nation's largest

consumers of electric power, purchasing over 82 billion kilowatt-hours of electricity annually nationwide. In addition, many of AF&PA's members also own cogeneration and small power production facilities that are qualifying facilities ("QFs") under PURPA. QFs encompass both cogeneration facilities (in which the generating facility produces, in a sequential generation process, both electric energy as well as useful thermal energy, such as steam, that can be used in a productive process) and small power production facilities (such as hydroelectric facilities). Although AF&PA members certified as QFs typically operate cogeneration facilities, they own and operate all types of QF facilities, including about 100 small hydroelectric plants and a few small power production facilities that rely upon biomass for fuel. AF&PA's members include electricity consumers and producers (QFs and other self-generation) located within the AEP and PJM areas.

Prompt and decisive action by the ALJ is necessary to resolve the ongoing inter-state dispute regarding AEP's RTO participation, and to begin providing the customers identified above, and other customers, with the benefits of RTOs. This inter-state dispute stems from states' differing views of the import and impact of AEP's integration. On the one hand, the Virginia State Corporation Commission ("VSCC" or "Virginia"), Kentucky Public Service Commission ("KPSC" or "Kentucky"), and North Carolina Utilities Commission oppose the Commission's proposed exercise of preemption authority under PURPA Section 205 to facilitate AEP's integration into PJM. On the other hand, a majority of state commissions in the affected area, including the District of Columbia Public Service Commission, New Jersey Board of Public Utilities, Indiana Utility Regulatory Commission, Illinois Commerce Commission, Maryland Public Service Commission, Michigan Public Service Commission, Public Utilities Commission of Ohio, and Pennsylvania Public Utilities Commission generally support the

Commission's immediate preemption of RTO-inhibiting state laws. The Industrials support Commission action as set forth in the November 25 Order. Such action is not only permissible, but also absolutely necessary to resolve this increasingly divisive inter-state dispute and deliver to customers the long overdue benefits and safeguards provided by AEP's full integration into a fully functioning, Commission-approved RTO.

## II. ARGUMENT

### A. **AEP's Voluntary Commitment To Join PJM is Designed To Obtain Economical Utilization of Facilities and Resources in the Midwest and Mid-Atlantic Areas.**

VSCC and KPSC challenge the Commission's preliminary finding that AEP's commitment to join PJM constitutes a "voluntary coordination of electric utilities, including any agreement for central dispatch" that is "designed to obtain economical utilization of facilities and resources" in the Midwest and Mid-Atlantic areas within the meaning of Section 205.<sup>5</sup> VSCC and KPSC erroneously argue that the record in this proceeding lacks sufficient proof that AEP's integration into PJM is designed to realize "economical utilization."<sup>6</sup> The evidence is to the contrary, and demonstrates that: (1) AEP's joining PJM constitutes a voluntary coordination of electric utilities; (2) AEP's integration is designed to, and will, produce quantifiable benefits resulting from a more economical utilization of facilities in the combined region; (3) economical utilization correlates directly with the use of PJM's locational marginal pricing ("LMP") based redispatch of generation, in lieu of AEP's crude approach of cutting transactions via transmission line-loading relief ("TLR") actions; and (4) economical utilization produces market and

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<sup>5</sup> *November 25 Order* at PP 108-109.

<sup>6</sup> *See* Prepared Direct Testimony of Howard M. Spinner on Behalf of the Virginia State Corporation Commission at 26-39 ("VCC-19"); Prepared Direct Testimony of Cody Walker on Behalf of the Virginia State Corporation Commission at 29 ("VCC-1"); Prepared Direct Testimony of Charles Buechel on Behalf of the Kentucky Public Service Commission at 5 ("KYC-5").

operational efficiencies that customers throughout the Mid-Atlantic and Midwest regions will enjoy. Each of these issues is discussed below.

**1. The Commission's Interpretation of PURPA Section 205 Is Consistent with both the Plain Language and Legislative History of PURPA Section 205.**

As a threshold matter, an accurate understanding of PURPA Section 205 is fundamental to properly adjudicating this issue. Contrary to the claims of certain participants that oppose AEP's integration into PJM, Congress intended that Section 205 confer upon the Commission the authority to exempt from State regulation utilities seeking to engage in voluntary coordination, if such voluntary coordination was designed to realize economical utilization of facilities and resources in any area.<sup>7</sup> The testimony in this proceeding demonstrates that the plain text and legislative history of Section 205 support this conclusion.

Statutory interpretation "begin[s], as always, with the plain language of the statute in question."<sup>8</sup> Section 205 provides, in relevant part:

The Commission may, on its own motion, . . . after public notice and notice to the Governor of the affected State and after affording an opportunity for public hearing, exempt electric utilities, in whole or in part, from any provision of State law, or from any State rule or regulation, which prohibits or prevents the voluntary coordination of electric utilities, including any agreement for central dispatch, if the Commission determines that such voluntary coordination is designed to obtain economical utilization of facilities and resources in any area. No such exemption [from a contrary State law, rule, or regulation] may be granted if the Commission finds that such provision of State law, or rule, or regulation –

- (1) is required by any authority of Federal law, or
- (2) is designed to protect public health, safety, or welfare, or the environment or conserve energy or is designed to

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<sup>7</sup> See *infra* Section II.A.2.

<sup>8</sup> *Consumer Elec. Ass'n v. F.C.C.*, 347 F.3d 291, 297 (D.C. Cir. 2003) ("*Consumer*").

mitigate the effects of emergencies resulting from fuel shortages.<sup>9</sup>

A plain reading of the text indicates that Congress intended Section 205 to authorize the Commission to exempt electric utilities from any State laws, rules, or regulations that prevent or prohibit voluntary coordination designed to achieve economical utilization of their facilities and resources.

Notwithstanding, parties opposing AEP's integration challenge the Commission's jurisdiction under Section 205, arguing that AEP's commitment to join an RTO was not voluntary<sup>10</sup> and that Section 205 is limited to promoting the types of coordination agreements that were known to the industry in 1978 - centrally dispatched, cost-based power pools - not market-based pricing and the competitive, bid-based market that exists in PJM.<sup>11</sup> As discussed below, the record shows that AEP voluntarily committed to join an RTO and that the RTO it elected to join was PJM.<sup>12</sup> With respect to the argument that Section 205 may only be used to promote 1978-era coordination agreements, an ordinary reading of Section 205 indicates that any attempt to limit the statute's application to a specific time period is completely unfounded, given the absence of any limiting language in the statute itself. Moreover, an examination of the statutory history of Section 205 shows that Congress did not intend to define the phrase "any agreement for central dispatch" according to static 1978 industry standards.<sup>13</sup> The fact that a statute can be applied in situations not expressly anticipated by Congress demonstrates its intended breadth and flexibility.<sup>14</sup>

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<sup>9</sup> 16 U.S.C. § 824a-1(a).

<sup>10</sup> See, e.g., VCC-19 at 28; KYC-5 at 4-5.

<sup>11</sup> See VCC-19 at 20-26; Prepared Rebuttal Testimony of Howard M. Spinner on Behalf of the Virginia State Corporation Commission at 7 ("VCC-30").

<sup>12</sup> See *infra* Section II.A.3.

<sup>13</sup> See *infra* Section II.A.2.

<sup>14</sup> *Consumer*, 347 F.3d at 298.

**2. AEP's Joining PJM Constitutes the "Coordination of Electric Utilities, Including Any Agreement for Central Dispatch" Within the Meaning of Section 205.**

Section 205's legislative history firmly supports the conclusion that Congress intended to authorize the Commission to exempt electric utilities from any State laws, rules, or regulations that prevent or prohibit voluntary coordination of their facilities and resources in a manner designed to achieve economical utilization. Congress expressly identified agreements for central dispatch as a category of coordination measures subject to the provisions of Section 205.<sup>15</sup> According to Exelon witness Sharp, Section 205 represents a reconciliation of competing presidential and congressional bills that were proposed in response to the 1970s energy crisis and were intended to facilitate "greater coordination and integrated use of utility assets owned by separate entities within a region" for the purpose of improving efficiency throughout the electric system.<sup>16</sup> There is no evidence that Congress intended to limit the means by which such coordination would be achieved.<sup>17</sup>

The President's proposed bill focused on significantly expanding the federal government's authority over the electric industry, particularly with regard to transmission and the coordination of transmission service.<sup>18</sup> The House bill, the pertinent sections of which the Senate subsequently adopted unchanged,<sup>19</sup> proposed providing the Commission with express authority to order pooling and the establishment of "centrally dispatched power pools."<sup>20</sup> The House Report explained that expanding the Commission's authority in this area would yield "considerable economies and other benefits" given that "power pools offer substantial potential

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<sup>15</sup> See 16 U.S.C. § 824a-1(a).

<sup>16</sup> Prepared Direct Testimony of Philip R. Sharp on Behalf of Exelon Corporation at 2-3 ("EXE-30"); *id.* at 4-8.

<sup>17</sup> See Prepared Rebuttal Testimony of Philip R. Sharp on Behalf of Exelon Corporation at 2-3 ("EXE-100").

<sup>18</sup> See EXE-30 at 4-5.

<sup>19</sup> *Id.* at 7.

<sup>20</sup> *Id.* at 6; see also H.R. 8444 § 541(b) ("EXE-32").

for increased efficiency in the generation and supply of electricity" and "the potential to reduce costs to the ultimate consumer of electricity."<sup>21</sup> The House Report further explained that such benefits "clearly justify expanding and strengthening the Commission's authority . . . ."<sup>22</sup> In Conference Committee, the language ultimately embodied in Section 205 was created.<sup>23</sup> Although Section 205 did not include provisions giving the Commission express authority to order utilities to pool and centrally dispatch their resources and facilities, Section 205 does provide such authority when an electric utility voluntarily opts to engage in such coordination, as AEP has done in this case.<sup>24</sup> Section 205 embodies Congress' intent to empower the Commission to secure the potential efficiency benefits that result from electric utilities' voluntary coordination of resources and facilities in any area.<sup>25</sup> That Congressional intent is amply supported by evidence in this proceeding.

"If the intent of Congress is clear, that is the end of the matter; for the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress."<sup>26</sup> Based on the plain reading of Section 205 and its legislative history, it is clear that Congress intended to authorize the Commission to exempt electric utilities from any State laws, rules, or regulations that prevent or prohibit voluntary coordination of their facilities and resources that is designed to achieve economical utilization. Nothing in Section 205 or its legislative history indicates that the phrase "any agreement for central dispatch" should be defined pursuant to 1978 industry standards. Exelon witness Sharp's direct involvement in the development and passage of PURPA provides for a credible perspective into the meaning of Section 205, and supports this

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<sup>21</sup> H.R. Rep. 95-496 (iv), 1978 U.S.C.C. A.N. 8454, 8595; *see also* EXE-30 at 6.

<sup>22</sup> H.R. Rep. 95-496 (iv), 1978 U.S.C.C. A.N. 8454, 8595; *see also* EXE-30 at 7.

<sup>23</sup> *See* EXE-30 at 8.

<sup>24</sup> *Id.* at 8-9.

<sup>25</sup> *Id.* at 8.

<sup>26</sup> *Alabama Power Co. v. U.S.E.P.A.*, 40 F.3d 450, 454 (D.C. Cir. 1994).

conclusion. Self-serving interpretations by witnesses for opposing parties, who were not involved in the development or passage of PURPA, and who do not even claim to offer expert opinions on the meaning of PURPA, should not be given any relative weight.

Upon its integration into PJM, AEP will be required to sign a number of agreements that provide for central dispatch or other forms of coordination of the Company's resources and facilities.<sup>27</sup> These agreements include: the PJM Operating Agreement, which contains all the PJM market rules, including the requirement to perform centralized least-cost dispatch and protocols for the Regional Transmission Expansion Plan ("RTEP"); the PJM West Transmission Owners Agreement, which provides for coordination in various form, such as coordination of transmission maintenance schedules and information necessary to prepare the RTEP; and the PJM West Reliability Assurance Agreement, which provides for coordination of capacity to ensure adequate capacity to serve load in PJM.<sup>28</sup> Consequently, it is quite clear that, upon integrating into PJM, AEP will be entering into agreements providing for central dispatch and other forms of coordination of the Company's resources and facilities, all of which are designed to obtain economical utilization of regional resources and facilities. AEP's proposal falls squarely within the intent of Section 205.

Accordingly, the Industrials respectfully urge the ALJ to find and conclude that the coordination to which AEP has voluntarily committed qualifies as "coordination of electric utilities, including any agreement for central dispatch" within the meaning of Section 205.

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<sup>27</sup> See Prepared Rebuttal Testimony of Steven T. Naumann on Behalf of Exelon Corporation at 7 ("EXE-110").

<sup>28</sup> See *id.* at 7.

**3. AEP's Joining PJM Constitutes a "Voluntary" Coordination Within the Meaning of Section 205.**

Despite assertions to the contrary, AEP voluntarily agreed to a merger commitment requiring its participation in an RTO and voluntarily agreed to join PJM.<sup>29</sup> In the Commission proceedings regarding AEP's proposed merger with Central and South West Corporation ("CSW"), AEP voluntarily committed to join a fully functioning, Commission-approved RTO as a condition of obtaining Commission approval for its merger with CSW.<sup>30</sup> On March 15, 2000, approximately two months after the issuance of Order No. 2000, the Commission issued its order on the proposed AEP-CSW merger, in which it accepted AEP's voluntary RTO commitment and established December 15, 2001 as the deadline by which AEP must join an RTO as a condition to approval of the merger.<sup>31</sup> On March 27, 2000, AEP, by written correspondence to the Commission, accepted the Commission's RTO participation condition, which provided that AEP must transfer "operational control of its transmission facilities to a fully functioning Commission approved RTO."<sup>32</sup> On May 28, 2002, AEP voluntarily submitted an application to join PJM.<sup>33</sup> On April 1, 2003, the Commission approved the transfer of control of AEP's facilities to PJM.<sup>34</sup>

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<sup>29</sup> See Prepared Direct Testimony of Elizabeth Anne Moler on Behalf of Exelon Corporation at 6-7 ("EXE-1"); Prepared Rebuttal Testimony of Elizabeth Anne Moler on Behalf of Exelon Corporation at 3-4 ("EXE-90"); Prepared Direct Testimony of David A. Svanda on Behalf of the Midwest Independent Transmission System Operator, Inc., at 9 ("MIS-1"). VSCC and KPSC witnesses' claims that AEP's merger-related commitment was not voluntary ignore the obvious fact that AEP, and AEP alone, had the choice whether to accept the Commission's RTO participation condition and proceed with its merger with CSW. See, e.g., KYC-5 at 4-5; *id.* at 10-11. Importantly, AEP does not take issue with the conclusion that its acceptance of the RTO participation requirement was, indeed, voluntary.

<sup>30</sup> See EXE-1 at 6; see also *Stipulation of America Elec. Power Co., Central and South West Corp., and Commission Trial Staff* at 2-4, Docket No. EC98-40-000 (May 24, 1999) ("EXE-4").

<sup>31</sup> See EXE-1 at 6; see also *American Elec. Power Co., Opinion No., 442*, 90 FERC ¶ 61,242 at p. 61,786-90 (2000) ("Opinion 442"); *American Elec. Power Co. & Central and South West Corp.*, 91 FERC ¶ 61,208 (2000); *November 25 Order* at PP 5-6.

<sup>32</sup> See *Opinion No. 442* at p. 61,788; see also Prepared Direct Testimony of J. Craig Baker on Behalf of The American Electric Power System at 6 ("AEP-1"); EXE-1 at 6.

<sup>33</sup> See generally *Compliance Filing of American Elec. Power Serv. Corp.*, Docket No. EL02-65-005 (filed May 28, 2002) ("EXE-7").

<sup>34</sup> *American Elec. Power Service Corp., et al.*, 103 FERC ¶ 61,008 at P 17 and Ordering ¶ B (April 1, 2003).

The voluntariness of AEP's decision should be a non-issue; both Kentucky (through a KPSC order) and Virginia (through witness testimony in this proceeding) have acknowledged that AEP's commitment to join an RTO was voluntary. VSCC witness Spinner characterized AEP's decision as its "*voluntary* commitment to join an RTO."<sup>35</sup> The KPSC's order, dated July 17, 2003 ("KPSC Order"), rejecting AEP's application to join PJM, stated: "While Kentucky Power argues that RTO membership was a condition imposed by FERC in approving the AEP-CSW merger, *the record shows that AEP voluntarily agreed to such membership. It was this voluntary agreement that FERC then elevated to a merger condition.*"<sup>36</sup> AEP voluntarily agreed to accept its merger condition; AEP voluntarily agreed to satisfy that condition by joining PJM; and AEP is voluntarily agreeing to the coordination of AEP and PJM facilities.

**4. The Coordination of AEP and PJM Facilities and Resources Is Designed To, And Likely Will, Produce Quantifiable Benefits Resulting from a More Economical Utilization of Resources in the Combined Region.**

"Economical utilization of facilities and resources" will occur when the "transmission system is used day to day to lower the overall cost of unit commitment and dispatch for the region" and when "investment decisions about new generation and transmission facilities are made based on efficient price signals that reflect the locational value of generation and transmission expansion."<sup>37</sup> The Commission's analyses supporting Order No. 2000 indicate that RTO participation is designed to produce economical utilization.<sup>38</sup> The Commission explained that a key function of an RTO is to employ "a transmission pricing system that will promote

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<sup>35</sup> See VCC-19 at 28 (emphasis added); see also *Initial Brief of the Virginia State Corporation Commission*, Docket Nos. EL98-40-000, *et al.*, at 1, 3 (filed Aug. 31, 1999) ("EXE-91") ("The Applicants' [AEP and CSW] decision to propose a merger was voluntary, and their decision to accept any Commission conditions will be voluntary".) (emphasis added); EXE-90 at 3.

<sup>36</sup> See *Application of Kentucky Power Co. for Approval to Transfer Functional Control of Transmission Facilities Located in Kentucky to PJM Interconnection, L.L.C. Pursuant to KRS 278. 218, Case No. 2002-00475*, at 13 ("EXE-14"); see also EXE-90 at 4.

<sup>37</sup> Prepared Direct Testimony of Michael M. Schnitzer on Behalf of Exelon Corporation at 2 ("EXE-80").

<sup>38</sup> See EXE-1 at 4.

efficient use and expansion of transmission and generation facilities.<sup>39</sup> As a result, the language of Order No. 2000 regarding scope and configuration and market-based congestion management manifests an intent to "address the economic utilization of facilities and resources within the RTO by ensuring that an efficient regional commitment and dispatch is achieved."<sup>40</sup> Consequently, by definition, AEP's voluntary commitment to join a fully functioning, Commission-approved RTO is designed to achieve economical utilization of facilities and resources.

The record in this proceeding, however, goes much further and demonstrates conclusively that AEP's voluntary commitment is designed to achieve economical utilization. As discussed in more detail below, all cost-benefit studies presented in this proceeding demonstrate that integrating AEP into PJM will promote economical utilization.<sup>41</sup> In addressing the issue of economical utilization, however, the ALJ need not and should not rely exclusively upon these cost-benefit studies, as even KPSC witness Buechel testified that no cost-benefit study is necessary to decide the economic utilization issue.<sup>42</sup> Rather, these studies should be considered in combination with evidence of non-quantifiable benefits to conclude that AEP's full integration will increase the economical utilization of facilities and resources.<sup>43</sup> As several witnesses explained, cost-benefit analyses do not necessarily capture the many non-quantifiable considerations that are pertinent to the "economical utilization" inquiry.<sup>44</sup> For example, strict reliance on cost-benefit studies would preclude consideration of reliability, a benefit that is not

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<sup>39</sup> See EXE-80 at 2; *see also* Order No. 2000 at p. 31,106.

<sup>40</sup> EXE-80 at 3.

<sup>41</sup> In fact, no party to this proceeding offers any evidence demonstrating that integrating AEP into PJM's energy markets will disadvantage any particular parties. *See* Prepared Rebuttal Testimony of J. Stephen Henderson on Behalf of Exelon Corporation at 5 ("EXE-120").

<sup>42</sup> Transcript of January 30, 2004 Hearing at 1003 (Cross-Examination of Charles Buechel) ("Buechel Cross-Examination").

<sup>43</sup> *See e.g.*, AEP-1 at 26.

<sup>44</sup> *Id.*

readily quantified, but is certainly of significant value.<sup>45</sup> Undue reliance on cost-benefit studies would also preclude consideration of potential longer-term issues, such as the gradual replacement of older, less efficient generation units with newer, more efficient units.<sup>46</sup> The fact that benefits such as reliability, improved system planning and coordination, and increased competition are difficult to quantify should not remove them from consideration.<sup>47</sup>

Accordingly, cost-benefit studies are instructive, not determinative, of the economical utilization issue. Estimated production cost savings, the subject of these cost-benefit studies, constitute a single quantifiable benefit of improved economical utilization.<sup>48</sup> These cost-benefit studies are considered with numerous non-quantifiable factors to reach the conclusion that AEP's integration into PJM is designed to increase the economical utilization of resources and facilities in the combined region. As explained by Exelon witness Henderson, focusing solely on near-term quantifiable benefits threatens to preclude consideration of longer-term non-quantifiable benefits that are "likely to be the most important source of social benefits over the longer term."<sup>49</sup> Accordingly, each of the cost-benefit studies is discussed below, followed by a discussion of various non-quantifiable benefits, the totality of which demonstrates that AEP's full integration into PJM is designed to (and very likely will) produce a more economical utilization of facilities and resources than exists in the *status quo*.

**i. The AEP Study**

According to the cost-benefit study performed by AEP ("AEP Study"), integrating AEP into PJM will produce economic benefits for AEP and customers in the combined region,

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<sup>45</sup>*Id.*

<sup>46</sup>*Id.* at 27.

<sup>47</sup> See EXE-120 at 4.

<sup>48</sup>*Id.* at 6.

<sup>49</sup>*Id.*

including those customers in AEP's service territory.<sup>50</sup> Specifically, the AEP Study finds that AEP East Zone operating companies will realize "approximately \$333 million over a five year period" in increased off-system sales profits.<sup>51</sup> According to AEP witness Baker, this level of savings from full integration would increase AEP's off-system sales profits by 57% and produce total AEP system production cost savings of approximately 3%.<sup>52</sup> Although the VSCC and KPSC posed many questions regarding the impact of these savings, for large manufacturers competing in the global marketplace, these savings levels are certainly not inconsequential. The AEP Study also finds that AEP's integration into PJM will produce additional, albeit less quantifiable, benefits for the AEP system such as enhanced reliability, improved access to competitive markets, increased sources of generation supply, and improved operational coordination and communication.<sup>53</sup>

In addition to the aforementioned benefits to AEP's system, the AEP Study shows that AEP's RTO participation will yield regional benefits due, in large measure, to the elimination of through-and-out transmission rates in the PJM-MISO region.<sup>54</sup> These regional benefits will materialize in the form of lower market prices resulting from the displacement of higher cost generation in the region and reduced administrative fees for existing PJM members due to the impacts of increased billing determinants produced by the addition of AEP's load and generation to the PJM footprint.<sup>55</sup> The AEP Study determines that AEP's native load customers will ultimately realize these regional benefits.<sup>56</sup>

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<sup>50</sup> See AEP-1 at 22.

<sup>51</sup> *Id.* at 24.

<sup>52</sup> See Transcript of January 29, 2004 Hearing at 839 (Cross-Examination of J. Craig Baker) ("Baker Cross-Examination").

<sup>53</sup> See AEP-1 at 23-24.

<sup>54</sup> *Id.* at 24-25.

<sup>55</sup> *Id.* at 25 (referring to the Cambridge Energy Research Associate's dispatch simulation accompanying the AEP Study).

<sup>56</sup> *Id.* at 26.

The AEP Study supports a finding that AEP's full integration is designed to produce a more economical integration of facilities and resources.

**ii. The Tabors Study**

The cost-benefit study conducted by Cinergy Services, Inc. witness Dr. Richard D. Tabors ("Tabors Study") demonstrates that AEP's integration into PJM will enhance the economical utilization of facilities and resources in the Midwestern and Mid-Atlantic regions relative to a stand-alone AEP configuration.<sup>57</sup> The Tabors Study attributes the improvement in economical utilization to more efficient unit commitment and improved real-time dispatch resulting from a more efficient commitment scenario, which reduces wholesale prices to the ultimate benefit of consumers.<sup>58</sup> In quantitative terms, the Tabors Study projects that the incremental economic gains available to consumers as a result of AEP's integration into PJM would total *at least \$214 million for 2005* in the portion of the Eastern Interconnection encompassed by Dr. Tabors' analysis,<sup>59</sup> and anticipates benefits of a similar magnitude in subsequent years.<sup>60</sup> Of the \$214 million in consumer benefits, approximately \$149 million will be realized by customers in the ECAR and PJM regions.<sup>61</sup> The Tabors Study shows consumers in the PJM, AEP, and Dayton Power & Light Company ("DPL") regions alone realizing a benefit of approximately \$53.3 million in 2005.<sup>62</sup> The Tabors Study finds that the improvement in unit commitment resulting from AEP's integration into PJM will also cause wholesale energy costs in

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<sup>57</sup> See Prepared Direct Testimony of Dr. Richard D. Tabors on Behalf of Cinergy Services, Inc., at 3-4 ("CIN-1").

<sup>58</sup> *Id.* at 4-5.

<sup>59</sup> *Id.* at 6 (emphasis added); see also *id.* at 25; Summary of Consumer Benefits and Producer Surplus Impacts of AEP-PJM Integrated Operation at 1 ("CIN-2").

<sup>60</sup> See CIN-1 at 6; *id.* at 26.

<sup>61</sup> CIN-1 at 6. The Tabors Study conservatively assumes that wheeling charges between MISO and the AEP and PJM control areas will be eliminated irrespective of whether AEP joins PJM and that current interregional trading already captures the potential economic gain available by selling into marginally higher-priced regions from marginally lower-priced regions. *Id.* at 5; see also *id.* at 13; *id.* at 26.

<sup>62</sup> See CIN-1 at 6.

Virginia and Kentucky to decrease.<sup>63</sup> AEP retail customers in Virginia and Kentucky would realize approximately \$42.5 million in energy cost savings for 2005, whereas retail customers served by other Virginia and Kentucky electric utilities realize energy cost savings of approximately \$19 million.<sup>64</sup> It is important to note that all of these benefits are exclusive of any ancillary services coordination or reliability benefits that might arise due to AEP integration into the PJM system.<sup>65</sup>

The second part of the Tabors Study finds that the integration of AEP into PJM energy markets will allow for more efficient interregional congestion management across the AEP-PJM seam as well as the PJM-MISO seam.<sup>66</sup> Integration will permit regional LMPs to reflect the financial consequences of transmission constraints, which is not provided under the current TLR approach.<sup>67</sup> The Tabors Study highlights the importance of accurately representing transmission congestion in LMP pricing constructs in order to avoid the costly consequences of inefficient pricing.<sup>68</sup> In monetary terms, the cost of incomplete transmission system information due to uncoordinated LMP pricing models in the expanded PJM region would range from \$66 million to \$235 million in 2005.<sup>69</sup> To the extent that such potential efficiency gains have not been realized, the projected benefits set forth in the first part of the Tabors Study "reflect a lower bound of economic improvement available to the regions' consumers."<sup>70</sup> In short, under various

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

<sup>64</sup> *See id.* at 6; *id.* at 27.

<sup>65</sup> *See* CIN-1 at 6.

<sup>66</sup> *Id.* at 7.

<sup>67</sup> *Id.*

<sup>68</sup> According to the Tabors Study, without integration, the interface between AEP's non-market based congestion management protocols and PJM's market-based congestion management protocols would not provide the data necessary to permit PJM or MISO to represent fully and accurately the key AEP-region interfaces in their respective LMP pricing models. Consequently, unit commitment and real-time dispatch outcomes would be less efficient than they would be if AEP were integrated into PJM energy markets. *See* CIN-1 at 21.

<sup>69</sup> *See id.* at 9; *id.* at 28.

<sup>70</sup> *Id.* at 6.

scenarios, the Tabors Study demonstrates that AEP's integration into PJM will result in enhanced economical utilization of facilities and resources.

### iii. The Ott Study

The cost-benefit analysis performed by PJM witness Andrew L. Ott ("Ott Study") shows that the integration of AEP, DPL, and Commonwealth Edison ("ComEd") into PJM energy markets will significantly enhance economical utilization of facilities and resources in the Midwest and Mid-Atlantic regions.<sup>71</sup> Applying a less conservative approach than the Tabors Study,<sup>72</sup> the Ott Study finds that the combined region will realize approximately *\$300 million in annual net production cost savings*.<sup>73</sup> The Ott Study also finds that the magnitude of net production cost savings will be consistent over the ten-year period, totaling approximately *\$3 billion* over that period.<sup>74</sup> During hearings, PJM witness Ott testified that the benefits of full AEP integration would likely not be limited to the new, expanded PJM footprint.<sup>75</sup> Benefits outside the combined region are likely to occur, with little or no additional costs imposed on those external regions.<sup>76</sup>

According to the Ott Study, the larger combined market region resulting from AEP's integration would allow available generation resources and transmission facilities to be more efficiently utilized.<sup>77</sup> Such efficiency is realized by having a single regional market operator administering a single, voluntary unit commitment and economic dispatch of facilities across the

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<sup>71</sup> See Prepared Direct Testimony of Andrew L. Ott on Behalf of PJM Interconnection L.L.C., at 2 ("PJM-2"); *id.* at 14.

<sup>72</sup> Like the Tabors Study, the Ott Study relies on the GE MAPS modeling tool to examine unit commitment and dispatch with and without AEP and other new PJM transmission owners, and is based on a detailed representation of a large portion of the Eastern Interconnection. See Prepared Rebuttal Testimony of Andrew L. Ott on Behalf of PJM Interconnection L.L.C., at 3-10 ("PJM-6"). Unlike the Tabors Study, the Ott Study quantifies regional benefits in terms of total production cost savings for energy and reserves and employs a higher hurdle rate to simulate trade barriers between control areas operated under separate unit commitment and dispatch. *Id.* at 2-3.

<sup>73</sup> PJM-2 at 2 (emphasis added).

<sup>74</sup> *Id.* at 19 (emphasis added).

<sup>75</sup> See Transcript of January 28, 2004 Hearing at 565 (Cross-Examination of Andrew L. Ott).

<sup>76</sup> *Id.* at 565-566.

<sup>77</sup> See PJM-2 at 14.

region.<sup>78</sup> This construct eliminates inefficiencies associated with performing separate unit commitment, transaction scheduling, and economic dispatch for each control area, and enables lower cost generation resources to displace higher cost generation resources.<sup>79</sup>

Consequently, the Ott Study demonstrates that AEP's full integration will result in a more economical utilization of facilities and resources.

#### **iv. The Henderson Study**

The cost-benefit study conducted by Exelon witness J. Stephen Henderson ("Henderson Study") illustrates the benefits associated with replacing the inefficient TLR system with PJM's efficient market-based congestion management system.<sup>80</sup> According to the Henderson Study, the benefits stem from the fact that the available supply of redispatch is substantially larger under a joint dispatch; the maximum relief from a joint redispatch is more than twice the amount that could be obtained from the sum of the separate redispatches; and the cost of providing a given amount of relief is substantially less under the joint redispatch supply curve.<sup>81</sup> In short, the Henderson Study concludes that a joint redispatch could provide a substantially larger amount of total relief and could provide a given quantity of relief at substantially lower cost.<sup>82</sup> This means that redispatch options available under a region-wide PJM-AEP redispatch would represent a significant improvement over those that could be achieved by either of the systems operating on its own.<sup>83</sup>

By analyzing the relative cost of using TLRs versus a hypothetical redispatch option in relieving congestion of certain flowgates along the PJM-AEP seam, the Henderson Study

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<sup>78</sup> *Id.* at 14-15.

<sup>79</sup> *Id.* at 14.

<sup>80</sup> See Prepared Direct Testimony of J. Stephen Henderson on Behalf of Exelon Corporation at 2-3 ("EXE-50").

<sup>81</sup> *Id.* at 19.

<sup>82</sup> *Id.*

<sup>83</sup> *Id.* at 19-20.

illustrates the improved economical utilization of transmission facilities likely to result from the integration of AEP into PJM.<sup>84</sup> The Henderson Study notes that the efficiency benefits achieved by utilizing an LMP-based congestion management system, rather than a TLR mechanism, "most likely would be achieved above and beyond the efficiencies addressed in the studies based on the GE MAPS model."<sup>85</sup> Consequently, the Henderson Study demonstrates that AEP's full integration will result in a more economical utilization of facilities and resources.

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As demonstrated by the foregoing cost-benefit studies, AEP's full integration into PJM will produce quantifiable benefits that will accrue to customers in the Midwest and Mid-Atlantic regions. However, these cost-benefit studies, while instructive, are not determinative of the economical utilization issue. A thorough and reasoned analysis must give equal consideration to critical non-quantifiable factors such as reliability, improved system planning and coordination, increased competition, and other societal benefits. The totality of these quantifiable and non-quantifiable benefits demonstrates that AEP's integration into PJM is designed to, and very likely will, enhance the economical utilization of resources and facilities.

**v. Economical Utilization Correlates Directly with the Use of PJM's Market Based Congestion Management System.**

The economical utilization of facilities and resources produced by AEP's integration into PJM is attributable to the fact that PJM's market-based congestion management system is superior to AEP's crude, inefficient TLR congestion management method.<sup>86</sup> Although this

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<sup>84</sup> *Id.* at 25.

<sup>85</sup> EXE-120 at 4.

<sup>86</sup> See Prepared Direct Testimony of Seven T. Naumann on Behalf of Exelon Corporation at 4-5 ("EXE-40"); *id.* at 11-12; see also EXE-50 at 4-5; EXE-50 at 12-15; Prepared Direct Testimony of Reem J. Fahey on Behalf of Edison Mission Energy, Edison Mission Marketing & Trading, Inc. & Midwest Generation EME, LLC at 9-10 ("EME-

phenomenon is implicit in each of the cost-benefit studies, this issue alone is sufficient to support a finding of enhanced economical utilization. The aim of both congestion management methods is to manage external power flows on transmission facilities to preserve reliability by redispatching generation, *i.e.*, increasing the output of one generator while contemporaneously decreasing the output of another generator.<sup>87</sup> The superiority of PJM's congestion management system stems from its design; it redispatches generation according to an LMP-based system that recognizes the production costs of generators, in addition to their shift factors.<sup>88</sup> By focusing on the most economical combination of generators to ramp up or down to manage congestion, PJM's LMP-based redispatch of generation achieves greater economic efficiency than does a TLR approach.<sup>89</sup>

Unlike the "optimizing hand of the LMP dispatch engine," the TLR mechanism is crude and a blunt instrument, much like a sledgehammer, that indiscriminately curtails load flows exceeding operational limits.<sup>90</sup> The TLR mechanism is "blind to economics."<sup>91</sup> Two primary deficiencies in the TLR mechanism cause it to yield a less efficient outcome than a market-based congestion management system. First, TLRs curtail transactions solely on the basis of their "physical attributes – the impact they have on the constrained flowgate – with no consideration for what the most economic redispatch would be."<sup>92</sup> TLRs do not "consider the costs of changing generation or the costs of different dispatch options."<sup>93</sup> Given TLRs' insensitivity to

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A1"); Prepared Direct Testimony of Gary R. Sorenson on Behalf of PSEG Energy Resources & Trade LLC and Public Service Electric and Gas Company at 6-8 ("PS-1"); CIN-1 at 24.

<sup>87</sup> See EXE-50 at 7 (due to differences in shift factors of generators, redispatching reduces power flow on a flowgate); see also EXE-40 at 3-4.

<sup>88</sup> See EXE-50 at 7; see also EXE-40 at 11; PS-1 at 7-8.

<sup>89</sup> See EXE-50 at 7.

<sup>90</sup> CIN-1 at 24.

<sup>91</sup> EXE-40 at 6; see also CIN-1 at 24.

<sup>92</sup> EXE-40 at 11; see also *id.* at 5; ("Curtailed priority is based on 'firmness' and duration of the service under the OATT . . ."); EXE-50 at 4; EME-A1 at 16; EXE-80 at 9.

<sup>93</sup> EXE-40 at 12.

market forces, they have a material adverse effect on power markets because they result in the canceling of transactions at the direction of the reliability coordinator, not in response to pricing signals.<sup>94</sup> Exelon witness Naumann explains:

Market participants must respond to the directions of the Reliability Coordinators and control areas. In general, the response of individual market participants depends on their contracts and whether they control generation or serve load. Those that control generation must change the output of their generation (up or down) in response to a TLR. Those that have an obligation to serve load must find other sources of generation to serve their load. If there is no other generation that is deliverable to serve load, then load-serving entities must shed load. This latter step is unlikely and, in general, the effect on market participants of TLRs is that a different, more expensive generation dispatch is used to serve load.<sup>95</sup>

Second, under TLR protocols, market participants cannot "buy through" congestion.<sup>96</sup> In other words, transmission customers have no means of paying a transmission provider to redispatch generation that would provide the needed transmission congestion relief, even if that would accommodate potentially higher valued transactions.<sup>97</sup> As a result, requests for transmission service will be denied if transmission providers determine that providing the requested transmission service would cause transmission facilities to overload.<sup>98</sup> In general, transmission providers that are not located in organized markets are not required to redispatch to accommodate requests for transmission service.<sup>99</sup>

As illustrated in the Henderson Study, using PJM's LMP-based congestion management system to redispatch an integrated PJM-AEP system would increase generation costs by

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<sup>94</sup> *Id.* at 4.

<sup>95</sup> *Id.* at 6-7.

<sup>96</sup> See EXE-50 at 5; *see also* EXE-80 at 8.

<sup>97</sup> See EXE-50 at 5.

<sup>98</sup> See EXE-40 at 15; *see also* EXE-80 at 7.

<sup>99</sup> See EXE-40 at 15.

approximately \$9.30 per MW of congestion relief, far less than the \$77.86 per MW increase under the TLR mechanism.<sup>100</sup> Thus, under LMP dispatch, the total cost of managing transmission congestion is lower due to the economic optimization of resources.<sup>101</sup>

Contrary to the assertions of VSCC,<sup>102</sup> PJM's competitive markets are designed to obtain economical utilization.<sup>103</sup> PJM's LMP-based congestion management system uses a bid-based, security-constrained dispatch that evaluates bids from generators and interruptible load to calculate the least-cost dispatch, accounting for transmission constraints.<sup>104</sup> Under LMP dispatch, PJM continually adjusts dispatch to account for internal transmission constraints, load levels, and bid prices to maintain system reliability in real-time.<sup>105</sup> Because LMP dispatch is a market-based mechanism by which generators respond to economic price signals, it relieves transmission constraints in the most cost-effective manner.<sup>106</sup> Specifically, PJM's congestion management approach provides for economical utilization because, by "assigning a cost to the congestion relief, parties to affected transmission transactions can make the economic choice of whether continuation of their transaction is worth the cost of relieving the congestion."<sup>107</sup> Thus, PJM's bid-based security dispatch represents an economical use of resources at any given moment for the entire area that PJM serves,<sup>108</sup> a point to which VSCC witness Spinner ultimately conceded during hearings.<sup>109</sup> Applying PJM's congestion management approach will result in the economical utilization of resources and facilities across the combined region, as "[l]arge

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<sup>100</sup> See EXE-50 at 12.

<sup>101</sup> See EXE-50 at 13-14; *id.* at 19-20; *see also* EME-A1 at 27-28.

<sup>102</sup> See VCC-19 at 26-39.

<sup>103</sup> See Prepared Direct Testimony of Richard A. Wodyka on Behalf of PJM Interconnection, L.L.C. at 6 ("PJM-1").

<sup>104</sup> See EXE-40 at 9-10 (Generators are paid the LMP at their bus for what they dispatch and load pays LMP at their load bus for what they consume); *see also* EME-A1 at 16-17.

<sup>105</sup> See EXE-40 at 10.

<sup>106</sup> See *id.* at 11-12; *see also* EXE-50 at 6; EME-A1 at 17.

<sup>107</sup> PJM-1 at 9.

<sup>108</sup> *Id.* at 6.

<sup>109</sup> Transcript of January 30, 2004 Hearing at 1020 (Cross-Examination of Howard M. Spinner).

LMP-based markets therefore are likely to create greater trading opportunities and increase overall efficiency.<sup>110</sup> Additional aspects of PJM's market design that enable PJM to obtain economical utilization of resources include: facility outage coordination, regional planning, generation interconnection, demand response, capacity commitment coordination, ancillary services, market monitoring, and reliability safeguards.<sup>111</sup>

**vi. Economical Utilization Produces Market and Operational Efficiencies that Customers Throughout the Mid-Atlantic and Midwest Regions Will Enjoy.**

The economical utilization of facilities and resources resulting from AEP's integration into PJM will produce market and operational efficiencies that inure to the benefit of customers throughout the Mid-Atlantic and Midwest regions. PJM's unit commitment and dispatch methods will more efficiently and fully use the real-time capacity of the transmission system given that physical use of the system would not be limited to those who have secured specific transmission rights in advance.<sup>112</sup> Increasing the geographical scope of the control area will give system operators more options for quickly and cost-effectively resolving transmission overloads.<sup>113</sup> The interconnection process will improve.<sup>114</sup> Optimized economic dispatch would also conserve energy.<sup>115</sup>

The combined region will also realize reliability benefits.<sup>116</sup> Because LMP dispatch involves continually adjusting dispatch in real-time, transmission facilities subject to redispatch are not overloaded in the first place.<sup>117</sup> TLRs are triggered by overloading of the system and

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<sup>110</sup> PJM-1 at 10.

<sup>111</sup> See generally *id.* at 6-20.

<sup>112</sup> See EXE-50 at 5.

<sup>113</sup> *Id.* at 6.

<sup>114</sup> See PS-1 at 15.

<sup>115</sup> See MIS-1 at 5.

<sup>116</sup> See EXE-40 at 13 (In addition to the economic efficiency benefit, LMP dispatch, unlike the TLR mechanism, provides reliability benefits).

<sup>117</sup> *Id.*

require at least 30 minutes to become effective.<sup>118</sup> TLRs may fail to provide full relief in the first instance, causing further delays.<sup>119</sup> Certain classes of transactions are non-curtable, except under emergency conditions, which encourages market participants to arrange transactions in a manner that attempts to avoid TLRs.<sup>120</sup> Integration will also improve reliability by increasing the amount of generation available to serve the load of both regions in the event of an emergency.<sup>121</sup> Reliability would be further enhanced insofar as the MISO-PJM region would have a single organizational interface.<sup>122</sup>

PJMICC's and CMTC's testimony provides two, real-life examples of how the benefits produced by AEP's integration into PJM will inure to retail customers, the intended beneficiaries of the Commission's restructuring initiatives. PJMICC/CMTC testimony also provides examples of how AEP's full integration into PJM will increase the economical utilization of demand response resources, which is incremental to the increased economical utilization of generation and transmission facilities that is more directly addressed in other witnesses' testimony.

AEP's integration will produce benefits for MG Industries, a manufacturer of industrial gases, similar to those produced for MG Industries by Allegheny Power's integration into PJM, such as more stable wholesale market prices and increased reliability.<sup>123</sup> Upon AEP's integration into PJM, MG Industries anticipates that, at a minimum, there would be no changes in MG Industries' electricity supply costs or level of reliability at its Ashland, Kentucky facility, which supports an evidence-based conclusion that the net benefits of integration will at least offset the

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<sup>118</sup> *Id.*

<sup>119</sup> *Id.*

<sup>120</sup> *Id.* at 14.

<sup>121</sup> See PS-1 at 16.

<sup>122</sup> See MIS-1 at 5.

<sup>123</sup> See Prepared Direct Testimony of Paul R. Williams on Behalf of the Coalition of Midwest Transmission Customers and PJM Industrial Customer Coalition at 6 ("IND-1").

implementation costs of AEP's integration.<sup>124</sup> In fact, MG Industries believes that it is reasonable to expect that its costs in Kentucky will *decrease* given that an integrated AEP should be able to more readily generate additional off-system sales revenues through the PJM market utilizing their rate-based assets, a conclusion that is fully consistent with AEP's expectations as expressed through AEP witness Baker.<sup>125</sup>

Additional benefits that MG Industries reasonably expects include enhanced opportunities for participation in market-based demand response programs that are far superior to what AEP has developed to date.<sup>126</sup> MG Industries also believes that AEP's integration into PJM will facilitate the prompt implementation of the Joint and Common Market for the combined footprint of PJM, MISO, and the Southwest Power Pool, Inc., as the Commission has required in several prior Orders.<sup>127</sup>

BOC Gases anticipates that integrating AEP into PJM will result in "more robust and more transparent wholesale electricity markets" that will enable consumers to procure cost-effective and reliable electric supply.<sup>128</sup> Price transparency, coupled with PJM's demand response programs, will enable BOC Gases and other market participants to react to prices and, thus, drive the market towards greater economic efficiency.<sup>129</sup> AEP's integration will also produce lower energy costs and higher levels of reliability because of increased generation diversity, lower generation reserve requirements, improved system planning, and better coordination among the current conglomerate of control areas.<sup>130</sup> AEP integration will increase BOC Gases' economical utilization of its facilities located within the combined footprint, by

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<sup>124</sup> *Id.* at 6-7.

<sup>125</sup> *Id.* at 7; *see also supra* Section II.A.4.i.

<sup>126</sup> *See* IND-1 at 7.

<sup>127</sup> *Id.*; *see also Southwest Power Pool, Inc.*, 106 FERC ¶ 61,110 at P 63 (Feb. 10, 2004).

<sup>128</sup> Prepared Direct Testimony of Larry Stalica on Behalf of the Coalition of Midwest Transmission Customers and PJM Industrial Customer Coalition at 5 ("IND-2").

<sup>129</sup> *See id.* at 8.

<sup>130</sup> *Id.*

enabling BOC Gases to economically load its facilities based on energy prices and production requirements in the Joint and Common Market.<sup>131</sup> A Joint and Common Market with consistent market rules and without market seams would be an easier market in which to participate.<sup>132</sup>

As demonstrated above, AEP's integration into PJM will provide customers in the combined region with meaningful benefits. Moreover, integration will avoid a host of negative consequences. First, PJM's status as an RTO and the plans of ComEd to join PJM may be jeopardized.<sup>133</sup> Second, the viability of the RTO choices of the other former Alliance companies would also be "seriously and adversely" impacted.<sup>134</sup> Third, RTO development efforts in the Midwest would be faced with "an irreparable loss of time, talent and effort if it turns out that the Midwest ISO has been engaged in a meaningless exercise by AEP's incapacity or continued unwillingness to join an RTO."<sup>135</sup> Fourth, AEP's absence in PJM would increase the complexity of the already complex task of grid management, as the "disaggregation of generation, transmission and distribution functions" makes the "unified control of independent systems . . . much more difficult."<sup>136</sup> Fifth, without AEP's participation in PJM, the "potential for the exercise of market power and gaming by AEP and market participants within the AEP footprint is greater . . ."<sup>137</sup> Sixth, AEP's non-participation in the integration process would necessitate further changes in the multi-faceted integration plan, undermine other stakeholders' momentum, and require stakeholders to devote additional time and resources to address issues related to non-continuous integration.<sup>138</sup>

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<sup>131</sup> *Id.* at 9.

<sup>132</sup> *Id.*

<sup>133</sup> *See* MIS-1 at 4-5.

<sup>134</sup> EME-A1 at 7.

<sup>135</sup> MIS-1 at 11.

<sup>136</sup> *Id.* at 7.

<sup>137</sup> EME-A1 at 24.

<sup>138</sup> *See* PJM-1 at 23.

Accordingly, the Industrials respectfully urge the ALJ to find and conclude that AEP's joining PJM constitutes a voluntary coordination of electric facilities designed to obtain economical utilization of facilities and resources within the meaning of Section 205.

**5. Alternative Proposals Advanced by AEP and the Muni-Coop Coalition Must Be Rejected.**

**i. AEP's "Partial Integration Proposal"**

AEP proposes "partial integration" as an alternative to preemption of Kentucky and Virginia laws.<sup>139</sup> In brief, AEP's proposal would integrate the Company's transmission system into PJM, but would not: integrate AEP's generation into PJM's energy markets, require AEP to participate in centralized economic dispatch, or require AEP to participate in LMP dispatch for market-based congestion management.<sup>140</sup> AEP's "partial integration" proposal should be rejected.

AEP's alternative is essentially identical to a prior proposal, which the Commission already considered and rejected on the basis that it "would not comply with AEP's merger commitment" and "AEP would not be committed to an organization that operates a balancing market and manages congestion through market mechanism, thus failing to meet the requirements of Order No. 2000."<sup>141</sup> As PJM witness Wodyka correctly notes, "Joining PJM with an open-ended exemption from participation in those functions is not really joining PJM."<sup>142</sup> As acknowledged by AEP witness Baker during hearings, AEP's "partial integration"

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<sup>139</sup> See generally AEP-1 at 28-36.

<sup>140</sup> *Id.* See also EXE-90 at 15 (dubbing this alternative as the ("PJM-Lite" proposal).

<sup>141</sup> See *November 25 Order* at PP 100-101; see also EXE-90 at 15-16; Prepared Rebuttal Testimony of Reem J. Fahey on Behalf of Edison Mission Energy, Edison Mission Marketing & Trading, Inc., and Midwest Generation EME, LLC at 5 ("EME-14"); Prepared Rebuttal Testimony of Michael Schnitzer on Behalf of Exelon Corporation at 8 ("EXE-130").

<sup>142</sup> See Prepared Rebuttal Testimony of Richard A. Wodyka on Behalf of PJM Interconnection, L.L.C. at 2 ("PJM-4") (testifying that PJM stakeholders would be "very unlikely" to approve necessary changes in the OATT that would enable AEP to participate in a manner "radically different" from all other transmission owners); see also

alternative merely preserves the *status quo* and provides nothing that the Commission did not consider in its November 25 Order.<sup>143</sup>

Even if partial integration were a viable alternative, AEP witness Baker conceded that the Company has not formally filed its partial integration proposal with any state commission, even though such approval would be needed in the absence of preemption.<sup>144</sup> To date, no approvals of partial integration have been received; no assurances that such approvals could be received in a timely fashion have been given.<sup>145</sup> Consequently, AEP's proposal is not subject to any finite time limitations because the States are not subject to any fast deadlines.

## **ii. The Muni-Coop Coalition's "Staged Implementation" Approach**

The Muni-Coop Coalition also proposes an alternative, which involves a "staged" implementation that would bring AEP under the PJM tariff "as soon as practicable," but defer AEP's integration into the PJM energy markets, purportedly for a "finite period," until any concerns about the "undue impacts on customers" arising from the switch to LMP can be addressed.<sup>146</sup> This alternative proposal should likewise be rejected.

Like AEP's "partial integration" proposal, discussed above, the concept behind the Muni-Coop Coalition's staged implementation proposal was considered and rejected in the November 25 Order.<sup>147</sup> Specifically, the Commission rejected a "phased approach" proposed by Ameren, pursuant to which AEP, ComEd, and DPL would be included in MISO and eventually

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Transcript of January 28, 2004 Hearing at 839 (Cross-Examination of Richard A. Wodyka) (testifying that PJM stakeholders are generally opposed to any proposal to partially integrate AEP).

<sup>143</sup> See Baker Cross-Examination at 910 (testifying that nothing changed between the *November 25 Order* and the time he put the plan in his Direct Testimony); see also EME-14 at 4.

<sup>144</sup> See Baker Cross-Examination at 919.

<sup>145</sup> *Id.*

<sup>146</sup> Prepared Rebuttal Testimony of Seth W. Brown on Behalf of the Coalition of Municipal and Cooperative Users of New PJM Companies' Transmission at 4-5 ("MCC-1").

<sup>147</sup> See *November 25 Order* at P 104.

transferred to PJM "when the issues involving state authorizations . . . have been resolved."<sup>148</sup>

The Commission firmly rejected this proposal on the basis that it would "contravene the goal of reducing uncertainty by delaying AEP's integration into PJM" and would "do nothing" to address the obstacles to integration posed by Kentucky and Virginia.<sup>149</sup> Like Ameren's "phased approach," the Muni-Coop Coalition's "staged implementation" approach only delays AEP's integration into an RTO and does nothing to address the Kentucky and Virginia laws impeding integration. Consequently, for the reasons discussed by the Commission in its November 25 Order, the Muni-Coop Coalition's proposal should be rejected.

Moreover, although Muni-Coop Coalition witness Brown claims that the implementation stages would be confined to a "finite period," the conditions to which he cites in his testimony could require many years to implement.<sup>150</sup> For example, he suggests that transmission upgrades may be a necessary precondition to AEP's full integration.<sup>151</sup> However, in the very same piece of testimony, Mr. Brown observes that one significant transmission upgrade - the Wyoming-Jacksons Ferry 765 kV Project - has taken ten years to build.<sup>152</sup> The Commission should not delay AEP's full integration ten months, much less ten years. Finally, although Mr. Brown's proposal is designed to protect all customers against any adverse impact from AEP's full integration, he conceded on cross-examination that, if a net-benefit can be demonstrated for the combined footprint, full integration should not be delayed as a result of an adverse impact on customer or a subset of customers.<sup>153</sup> Given the results of the various cost-benefit studies

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<sup>148</sup> *Id.*

<sup>149</sup> *Id.*

<sup>150</sup> *See* MCC-1 at 18.

<sup>151</sup> *Id.* at 21.

<sup>152</sup> *Id.* at 29-30.

<sup>153</sup> *See* Transcript of January 30, 2004 Hearing at 981-982 (Cross-Examination of Seth W. Brown).

discussed above showing a regional net benefit,<sup>154</sup> it appears that Mr. Brown's proposal is not only inconsistent with the Commission's November 25 Order, but also unnecessary.

Neither the AEP nor the Muni-Coop Coalition proposal to delay AEP's full integration should be accepted. Virtually all of the economic benefits anticipated by the Commission when it accepted AEP's voluntary commitment to join PJM are premised upon AEP's full participation in the PJM markets.<sup>155</sup> As the Commission stated in the November 25 Order, "full integration of AEP into PJM best addresses" the considerations at stake in this proceeding.<sup>156</sup> The Industrials oppose anything less than full integration of AEP into PJM. PJM Stakeholders generally oppose partial integration of AEP.<sup>157</sup> The state commissions of Indiana, New Jersey, and the District of Columbia have also expressly indicated their dissatisfaction with AEP's partial integration proposal, and other state commissions are sure to follow.<sup>158</sup> Partial integration fails to satisfy Order No. 2000 requirements because it involves excluding precisely those RTO functions necessary to improve economical utilization of resources and facilities and, consequently, fails to satisfy AEP's merger commitment to join a "fully functioning, Commission-approved RTO."<sup>159</sup> Accordingly, AEP's "partial integration" proposal and the Muni-Coop Coalition's "staged implementation" approach must be rejected.

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<sup>154</sup> See *supra* Sections II.A.4.i-iv.

<sup>155</sup> See EME-14 at 4.

<sup>156</sup> *November 25 Order* at P 93.

<sup>157</sup> See *supra* note 142 and accompanying text.

<sup>158</sup> See Baker Cross-Examination at 874-875.

<sup>159</sup> See generally EXE-4; see also *Rebuttal Testimony of J. Craig Baker on Behalf of American Electric Power Co., Inc., and Central and South West Corp.*, Docket No. EC98-040-000, *et al.* at 6 (July 15, 1999) ("S-10") (supporting the proposition that AEP's merger condition required participation in a fully functional, Commission-approved RTO and that AEP's partial integration proposal does not provide the Minimum Characteristics and Functions necessary under Order No. 2000).

**B. The Laws of Virginia and Kentucky Are Preventing AEP From Fulfilling Both Its Voluntary Commitment in 1999, as Part of Merger Proceedings, To Join an RTO, and its Application to Join an RTO Pursuant To Order No. 2000.**

To date, AEP remains derelict in its compliance with the Commission's conditional approval of AEP's merger with CSW by not immediately transferring operational control of its transmission facilities to PJM and fully integrating into PJM's energy markets. The VSCC and KPSC have hinted that AEP's prior attempts to form the Alliance RTO may be relevant to this proceeding. They are not. AEP's prior attempts to form an RTO, including efforts related to the establishment of the proposed Alliance RTO,<sup>160</sup> are simply irrelevant to the adjudication of the issues in this proceeding.<sup>161</sup> AEP's prior efforts failed to satisfy various standards of the Federal Power Act, *e.g.*, the justness and reasonableness and public interest standards.<sup>162</sup> Any VSCC or KPSC argument premised upon the Alliance RTO proposals should not be considered, as it is irrelevant to a Section 205 analysis.

The language of Section 205 focuses on exempting electric utilities from any provision of state law that "prohibits or prevents" the voluntary coordination of electric utilities.<sup>163</sup> The use of the present tense in Section 205 indicates that the Commission must consider those state laws that are *currently* prohibiting or preventing coordination. The record demonstrates that the primary obstacle to AEP's full integration, and perhaps the only reason for AEP's undue delay, are Virginia and Kentucky laws that prohibit and prevent AEP from integrating into PJM.<sup>164</sup> Importantly, nothing in Section 205 or its legislative history requires that state law be the only impediment to voluntary coordination, only that such state laws "prohibit or prevent" the

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<sup>160</sup> AEP-1 at 4-13.

<sup>161</sup> See Transcript of January 27, 2004 Hearing at 353-354 (Cross-Examination of Elizabeth Anne Moler).

<sup>162</sup> *Alliance Cos., et al.*, 97 FERC ¶ 61,327 at p. 62,525 (Dec. 20, 2001) (rejecting the proposed formation of an Alliance RTO in favor of an "RTO structure that . . . best serves the public interest in the Midwest").

<sup>163</sup> 16 U.S.C. § 824a-1(a).

<sup>164</sup> See Prepared Direct Testimony of John P. Mathis on Behalf of Edison Mission Energy, Edison Mission Marketing & Trading, Inc., and Midwest Generation EME, LLC at 4-8 ("EME-10A").

voluntary coordination. Consequently, Virginia and Kentucky's claims that other steps need to be taken prior to AEP's full integration are simply irrelevant to the analysis.

The laws of Virginia and Kentucky are impeding AEP's integration into an RTO.<sup>165</sup> AEP itself has repeatedly cited these laws as impediments to its integration. Recently, AEP stated that:

The most obvious impediments [to AEP's participation in PJM] are the Kentucky Public Service Commission's initial disapproval of AEP operating company Kentucky Power Company's application for approval to participate in PJM, and the Virginia law prohibiting any Virginia utility from participating in any RTO until July, 2004, and thereafter only with the Virginia Commission's approval.<sup>166</sup>

The specific laws that are preventing AEP from participating in PJM are: Kentucky statute Section 278.218 ("Kentucky Statute"), and the KPSC Order pursuant thereto,<sup>167</sup> and Virginia statute Section 56-579 ("Virginia Statute"), and the lack of approval to date by the VSCC under that statute.<sup>168</sup>

**1. The Laws of Virginia Are Prohibiting or Preventing AEP from Joining PJM, Within the Meaning of Section 205.**

The Virginia Statute provides:

No such incumbent electric utility shall transfer to any person any ownership or control of, or any responsibility to operate, any portion of any transmission system located in the Commonwealth prior to July 1, 2004, and without obtaining, following notice and hearing, the prior approval of the [VSCC], as hereinafter provided. However, each incumbent electric utility shall file an application

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<sup>165</sup> See MIS-1 at 6-7; PJM-1 at 22-23; EXE-1 at 10-11; EME-10A at 4-5; and AEP-1 at 15 & 27.

<sup>166</sup> See EXE-1 at 10-11; *see also* Prepared Direct Testimony of Susan Tomasky and J. Craig Baker on Behalf of AEP, Docket Nos. ER03-262-001, *et al.*, at 6 (Sept. 23, 2003) ("EXE-11"). For other instances in which AEP identified Virginia and Kentucky laws as obstacles to integration *see also* AEP's Motion for Leave to File Answer to Motion to Dismiss Out of Time and Answer, Docket Nos. ER03-262-000, *et al.*, at 4-5 (February 7, 2003) ("EXE-9"); AEP's February 28, 2003 Compliance Report at 2 ("EXE-8"); AEP's Response to Motion for Expedited Consideration, Docket Nos. ER03-262-000, *et al.*, at 9 (March 31, 2003) ("EXE-10"); Transcript of Deposition of J. Craig Baker on December 23, 2003, at 57 ("EXE-12").

<sup>167</sup> See generally Ky. Rev. Stat. Ann. § 278.218 (2002) ("EXE-2"); EXE-14; *see also* EXE-1 at 5.

<sup>168</sup> See Va. Code Ann. § 56-579 ("S-3"); *see also* EXE-1 at 5.

for approval pursuant to this Section by July 1, 2003, and shall transfer management and control of its transmission assets to a regional transmission entity by January 1, 2005, subject to [VSCC] approval as provided in this section.

[...]

Any request to the Commission for approval of such transfer of ownership or control of or responsibility for transmission facilities shall include a study of the comparative costs and benefits thereof, which shall analyze the economic effects of the transfer on consumers, including the effects of the transmission congestion costs. The [VSCC] *may* approve such a transfer if it finds, after notice and hearing, that the transfer satisfies the conditions contained in this section.<sup>169</sup>

The Virginia Statute expressly prohibits the VSCC from authorizing any incumbent utility to transfer control of its transmission system to an RTO prior to July 1, 2004. Additionally, although the Virginia Statute appears to mandate that a utility join a RTO prior to January 1, 2005, this "requirement" is expressly subject to VSCC's exclusive approval, which appears to vest absolute discretion with the VSCC.<sup>170</sup>

The VSCC does not appear to be inclined to approve AEP's full integration into PJM any time soon. VSCC witness Walker's testimony during hearings further underscores this point:

Q Do you expect the commission [VSCC] to rule from the bench in this case?

A I doubt it, because this is a complex case.

[...]

Q Following the submission of briefs in a case of this nature before the Virginia State Corporation Commission, how long would you expect the Virginia commission to deliberate on the issues before it renders a decision?

A It's very difficult to provide an estimation on that, because the deliberations usually are related to how much controversy there is in

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<sup>169</sup> EXE-2 at §§ 56-579 (A) (1) & (F) (emphasis added); *see also* EXE-1 at 14-15.

<sup>170</sup> *See* EXE-15 at 15.

the case. If the case is relatively noncontroversial, if, for example, there was a settlement that was being presented or something of that nature, the decision could be fairly quickly.

Q Based on your current understanding on the level of controversy in the matter, whatever your current understanding of that is, how long would you expect it to take, based upon your experience in Virginia commission proceedings, for the commission to render a decision following the submission of briefs?

A I'm not sure I can give you a good answer to that question. . . .<sup>171</sup>

It is also important to note that the VSCC Staff engaged a consultant to conduct a cost-benefit analysis, which has not been completed.<sup>172</sup> In fact, the VSCC subsequently recommended that the Virginia Legislature "continu[e] the moratorium on the transfer of control of Virginia's electric transmission systems to federally-regulated regional transmission entities."<sup>173</sup> According to the VSCC, an extension of the moratorium was necessary to "preserve" State jurisdiction.<sup>174</sup> Also, in correspondence to the Commission on Electric Utility Restructuring (formerly Legislative Transition Task Force), the VSCC urged rebundling rates or suspending customer choice in an effort to "protect the Commonwealth's jurisdiction to ensure reliable electric service at reasonable rates."<sup>175</sup> Thus, evidence in the record supports the conclusion that the VSCC prompted the establishment of the moratorium in a likely attempt to prevent AEP from joining

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<sup>171</sup> Transcript of January 29, 2004 Hearing at 789-790 (Cross-Examination of Cody Walker) ("Walker Cross-Examination").

<sup>172</sup> *Id.* at 790.

<sup>173</sup> *Id.* see also Virginia State Corporation Commission, Report to the Commission on Electric Utility Restructuring of the Virginia General Assembly and the Governor of the Commonwealth of Virginia, Status Report: The Development of a Competitive Retail Market for Electric Generation Within the Commonwealth of Virginia, Exec. Summ. at 2 and Part III, Recommendations to Facilitate Effective Competition in the Commonwealth at 20-21 (August 29, 2003) ("EXE-18").

<sup>174</sup> EXE-18 at 20.

<sup>175</sup> See Walker Deposition Exh. 8 and Data Response to S/VSCC-3.01 by Cody Walker with Commissioner Moore letter (March 20, 2003) and Deposition Pages 77-79 ("S-5") at 2.

PJM.<sup>176</sup> As a result, it is quite probable that VCSS would be disinclined to grant AEP's application to join an RTO.

**2. The Laws of Kentucky Are Prohibiting or Preventing AEP from Joining PJM, Within the Meaning of Section 205.**

The Kentucky Statute requires a utility to obtain approval from the KPSC before the utility may:

transfer ownership of or control, or the right to control, any assets that are owned by a utility ... without prior approval of the [KPSC], if the assets have an original book value of one million (\$1,000,000) or more and:

- (a) The assets are to be transferred by the utility for reason other than obsolescence; or
- (b) The assets will continue to be used to provide the same or similar service to the utility or its customers.<sup>177</sup>

The Kentucky Statute requires prior KPSC approval before a utility can transfer operational control of its transmission facilities to another entity, including a Commission-approved RTO.<sup>178</sup>

As a result, the Kentucky Statute provides the KPSC with approval authority (and the authority to withhold such approval) for any Kentucky utility's plans to participate in a RTO, including AEP's request to participate in PJM.<sup>179</sup>

The KPSC exercised its authority under the Kentucky Statute in July 2003, when it denied the request of Kentucky Power Company, an AEP subsidiary, for approval to join PJM.<sup>180</sup> According to the KPSC Order, Kentucky Power failed to make a sufficient showing that the benefits of AEP's participation in PJM would outweigh the costs borne by Kentucky ratepayers.<sup>181</sup> The KPSC Order also expressed "grave concern" about "surrendering even a

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<sup>176</sup> EXE-1 at 16.

<sup>177</sup> See generally EXE-2; see also EXE-1 at 12.

<sup>178</sup> See EXE-1 at 12; see also EXE-14.

<sup>179</sup> *Id.*

<sup>180</sup> *Id.*

<sup>181</sup> See EXE-14 at 21; see also EXE-1 at 13.

portion of [its] authority to protect Kentucky Power's customers," particularly regarding "resource adequacy, transmission rates, transmission planning, and cost allocation of transmission upgrades."<sup>182</sup> The KPSC Order based its rejection on the possibility that PJM could revise its rules in the future "to require all member generation to be sold in the PJM market," the financial impact of which would be "devastating" to Kentucky ratepayers given that "the cost of generation for the existing PJM members is significantly higher."<sup>183</sup> Finally, the KPSC asserted that approving Kentucky Power's application to join PJM would violate a state statute, *i.e.* Section 278.214, which requires Kentucky Power to give transmission curtailment priority to Kentucky retail customers.<sup>184</sup>

Both AEP and PJM sought rehearing of the KPSC Order and AEP submitted the necessary cost-benefit study, which demonstrated substantial net benefits to Kentucky ratepayers from AEP's PJM integration.<sup>185</sup> By order dated August 25, 2003, the KPSC granted rehearing.<sup>186</sup> Nonetheless, the KPSC has not yet authorized AEP to join PJM.<sup>187</sup> There is also no deadline by which the KPSC must issue its order on rehearing, nor any indication that KPSC will even approve AEP's application.<sup>188</sup> Consequently, the Kentucky Statutes and the KPSC Order are preventing AEP from joining PJM and satisfying its commitment to join an RTO.<sup>189</sup>

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<sup>182</sup> See EXE-14 at 19-20; *see also* EXE-1 at 13.

<sup>183</sup> See EXE-14 at 20; *see also* EXE-1 at 13-14.

<sup>184</sup> See EXE-14 at 20; *see also* EXE-1 at 14.

<sup>185</sup> See EXE-1 at 14.

<sup>186</sup> See Prepared Direct Testimony of Thomas M. Dorman on Behalf of the Kentucky Public Service Commission at 2 ("KYC-1"); *see also* Application of Kentucky Power Co., d/b/a/ American Elec. Power for Approval, to the Extent Necessary, to Transfer Functional Control of Transmission Facilities Located in Kentucky to PJM Interconnection, L.L.C., Pursuant to KRS 278.218, Order dated Aug. 26, 2003, in Case No. 2002-00475 ("KYC-3").

<sup>187</sup> See EXE-1 at 14.

<sup>188</sup> See Buechel Cross-Examination at 1006-1007.

<sup>189</sup> See EXE-1 at 14.

### **3. Delaying Ruling, While Waiting On The VSCC and KPSC, Is Not a Reasonable Outcome.**

The States' arguments that further delay by this Commission could obviate the need for preemption are unavailing. Based on the series of delays from the initial December 2002 deadline for AEP's integration into PJM, the deadline will likely be subject to significant additional delay, unless the Commission acts under Section 205.<sup>190</sup> Neither Virginia nor Kentucky has provided any assurances that AEP will be permitted to integrate into PJM under their respective state laws. Moreover, "Virginia law pointedly does not provide any final date by which the VSCC must approve an application."<sup>191</sup> Virginia law vests sole discretion to approve or disapprove any such application with the VSCC, without imposing any obligation to approve AEP's plans.<sup>192</sup> The States' actions with respect to RTO development and Standard Market Design ("SMD") developments have reflected "nothing but antipathy" toward this Commission's market development initiatives.<sup>193</sup> Any claim that VSCC and/or KPSC approval of AEP's integration could occur in the near future is severely undermined by the States' resistance to the Commission's actions in this very proceeding. Quite simply, if the States had any intention of approving AEP's integration into PJM at any time in the near future, then why are they fighting so hard here?<sup>194</sup>

Currently, AEP is faced with "the choice of either violating FERC's November 25, 2003 order to join PJM or arguably violate state law by joining PJM without state commission approval."<sup>195</sup> Only Commission action is capable of eliminating this stalemate; specifically, this situation necessitates prompt action by the Commission under Section 205 to allow AEP's

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<sup>190</sup> *Id.* at 17.

<sup>191</sup> EXE-90 at 5.

<sup>192</sup> *Id.*

<sup>193</sup> *Id.* at 6.

<sup>194</sup> Transcript of January 28, 2004 Hearing at 623-636 (Cross-Examination of John P. Mathis).

<sup>195</sup> EME-10A at 8.

compliance with its outstanding merger commitment while excusing AEP from state laws that are serving as obstacles to its full integration into PJM.<sup>196</sup>

**C. The Laws, Rules, or Regulations of Virginia and Kentucky are Neither Required by Any Authority of Federal Law, Nor Designed To Protect "Public Health, Safety or Welfare, or the Environment or Conserve Energy or To Mitigate the Effects of Emergencies Resulting from Fuel Shortages."**

**1. The Laws, Rules, or Regulations of Virginia and Kentucky Are Not Required by any Authority of Federal Law Within the Meaning of Section 205.**

Neither Kentucky nor Virginia (nor any other party, for that matter) contends that the Virginia and Kentucky laws, rules, and regulations in question are "required by an authority of Federal law."<sup>197</sup> Consequently, this exception to Section 205 authority need not be considered here.

**2. The Laws, Rules, or Regulations of Virginia and Kentucky Are Not Designed To Protect the Public Health, Safety or Welfare or the Environment or Conserve Energy or Designed To Mitigate the Effects of Emergencies Resulting from Fuel Shortages Within the Meaning of Section 205.**

VSCC's and KPSC's obstacles to AEP's prompt and full integration into PJM do not fall within the other safe harbors of Section 205's limited exceptions. As a threshold matter, VSCC and KPSC attempt to unduly broaden the scope of the Section 205 exceptions to preemption by equating them to the more common "public interest standard."<sup>198</sup> In essence, Virginia and Kentucky claim that all of their utility-related statutes are designed to promote the public interest and, therefore, should be exempt from Commission preemption under Section 205. Virginia attempts to broaden the scope of the Section 205 exceptions even further by claiming that state laws, rules, or regulations that are nominally designed to promote reliability should also be read

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<sup>196</sup> *Id.*; see also EXE-1 at 17.

<sup>197</sup> Neither Virginia nor Kentucky argued that their laws are required by federal law so analysis of the first exception under Section 205 is irrelevant. See EXE-90 at 10; see also KYC-5 at 9.

<sup>198</sup> See, e.g., VCC-1 at 15; Prepared Rebuttal Testimony of Charles Buechel).

into the second exception.<sup>199</sup> As demonstrated below, VSCC's and KPSC's interpretations contradict both the plain reading of, and Congressional intent behind, Section 205. Evidence in this proceeding demonstrates that the narrowly worded statutory exceptions set forth in Section 205 do not provide Virginia or Kentucky with a means for further obstructing AEP's full integration into PJM.

To interpret the meaning of a federal statute administered by a single agency, courts engage in a two-step analysis.<sup>200</sup> The first step is to determine whether Congress has directly spoken to the question at issue.<sup>201</sup> If the answer is yes, effect must be given to that express intent.<sup>202</sup> In performing the first step, courts apply traditional tools of statutory construction.<sup>203</sup> If the statute is silent or ambiguous, courts give deference to the interpretation of the administering agency, if that interpretation is reasonable and consistent with the underlying statutory purpose.<sup>204</sup> This type of deference is generally known as *Chevron* deference.

Section 205 provides, in relevant part, that:

. . . No such exemption [from a contrary State law, rule, or regulation] may be granted if the Commission finds that such provision of State law, or rule or regulation –

- (1) is required by any authority of Federal law, or
- (2) is designed to protect public health, safety, or welfare, or the environment or conserve energy or is designed to mitigate the effects of emergencies resulting from fuel shortages.<sup>205</sup>

As noted above, exception (1) is not relevant. The sole focus of this inquiry is whether Virginia and Kentucky laws at issue are "designed to protect public health, safety, or welfare, or the

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<sup>199</sup> See VCC-1 at 15-16.

<sup>200</sup> *Indep. Ins. Agents v. Hawke*, 211 F.3d 638, 643 (D.C. Cir. 2000) (applying and citing to *Chevron U.S.A. Inc. v. NRDC*, 467 U.S. 837, 842-43 (1984)).

<sup>201</sup> *Hawke*, 211 F.3d at 643.

<sup>202</sup> *Id.*

<sup>203</sup> *Id.* at 643; see also *Chevron*, 467 U.S. at 843 n.9; *INS v. Cardoza-Fonseca*, 480 U.S. 421, 446 (1987).

<sup>204</sup> *Hawke*, 211 F.3d at 643 (citing *Nuclear Info. Resource Serv. v. Nuclear Regulatory Comm'n*, 969 F.2d 1169, 1173 (D.C. Cir. 1992) (*en banc*)).

<sup>205</sup> 16 U.S.C. §§ 824a-1(a)(1) & (2).

environment or conserve energy or . . . designed to mitigate the effects of emergencies resulting from fuel shortages."<sup>206</sup> A straightforward reading of Section 205, in conjunction with other electricity-related provisions of federal statutes, supports the conclusion that Congress did not intend to apply a "public interest standard" when defining which state laws are exempt from the Commission's preemption authority. If Congress had intended to craft exceptions based on the "public interest standard," it certainly would have included that language in Section 205, given that the "public interest standard" is found elsewhere in electricity-related statutes but not in Section 205. As a common rule of statutory construction, statutory provisions must be read to achieve as much consistency as possible.<sup>207</sup> Accordingly, one cannot reasonably conclude that Congress meant to say "public interest" when it actually said "public health, safety, or welfare." The States' claims to the contrary must be rejected.

Similarly, the issue of state reliability objectives - while admittedly important - is not a relevant concern when analyzing Section 205, as "reliability is not listed among the factors that a state law may be 'designed to protect' under PURPA Section 205(a)."<sup>208</sup> Congress addresses reliability issues in several sections of PURPA.<sup>209</sup> For instance, PURPA Section 205(b)(1)(C) expressly directs the Commission to study "opportunities for . . . increased reliability, through pooling arrangements" and Section 209 orders the Secretary of Energy to perform a "reliability" study "in consultation with the Commission."<sup>210</sup> Therefore, "the failure to list state laws related to reliability as a category of state law immune from Section 205(a) exemption cannot be

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<sup>206</sup> *Id.*

<sup>207</sup> See *Atwell v. Merit Sys. Prot. Bd.*, 670 F.2d 272, 286 (D.C. Cir. 1981) ("In reaching this result, we are guided as well by the cardinal canon of statutory construction that dictates that provisions should, whenever possible, be construed to achieve consistency.").

<sup>208</sup> EXE-100 at 4.

<sup>209</sup> *Id.*

<sup>210</sup> *Id.*

construed as merely an accidental omission."<sup>211</sup> The exceptions in Section 205 must be read as not pertaining to or encompassing reliability motivations for state laws, rules, and regulations. This interpretation is consistent with the statutory interpretation rule of "*expressio unius est exclusio alterius*," *i.e.*, "a mention of one thing implies the exclusion of another."<sup>212</sup> The fact that Congress did expressly mention reliability in other PURPA sections, but did not mention reliability in Section 205, justifies and compels the inference that reliability was "excluded by deliberate choice, not inadvertence."<sup>213</sup> Any claims that certain Virginia and Kentucky laws, rules, and regulations are designed to promote reliability, while admirable, are simply not germane to the analysis in this proceeding.

Even if Section 205 could reasonably be deemed "silent" or "ambiguous," which it cannot, deference must be given to the Commission's interpretation of Section 205 because it is reasonable and consistent with the Congressional intent behind Section 205.<sup>214</sup> As discussed *supra*, Congress enacted Section 205 for the sole purpose of giving the Commission the authority to "prevent state interference with voluntary transmission and similar arrangements that would bring about *economical utilization of facilities*."<sup>215</sup> While reliability may have been among the benefits the Congress sought to realize through the enhancement of the economical utilization of facilities and resources, reliability motivations do not offer state laws any protection from the Commission's authority to preempt. One of the principal purposes of Section 205 was to provide the Commission with "the authority to act to enable improvements in the bulk power transmission system it believed would be gained through voluntary coordination among electric

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<sup>211</sup> *Id.*

<sup>212</sup> *Hawke*, 211 F.3d at 644; *see also American Methyl Corp. v. E.P.A.*, 749 F.2d 826 (D.C. Cir. 1984); *Chevron U.S.A. Inc. v. Echazabal*, 536 U.S. 73 (2002).

<sup>213</sup> *See, e.g., Barnhart v. Peabody Coal Company, et al.*, 537 U.S. 149 (2003).

<sup>214</sup> *See Hawke*, 211 F.3d at 643 (citing *Nuclear Info. Resource Serv.*, 969 F.2d at 1173).

<sup>215</sup> EXE-30 at 11 (emphasis added).

utilities in situations where a state might disagree with FERC's judgment."<sup>216</sup> Virginia and Kentucky are simply incorrect that reliability motivations warrant full protection of their laws from preemption.

Finally, applying Virginia's and Kentucky's overly broad interpretations of Section 205 exceptions would cause the statutory exceptions to swallow the statutory rule. By way of illustration, VSCC witness Walker testified during hearings that *every* Virginia law dealing with electric utility matters is designed to promote the public health, safety and welfare.<sup>217</sup>

Q Well, which provisions of the laws and regulations governing Virginia's regulation of electric utilities are designed to protect the public health, safety, and welfare within the meaning of 205(a), in your opinion?

A All of them.<sup>218</sup>

If this were indeed the case, PURPA Section 205 could never reach any Virginia laws preventing or precluding voluntary coordination because the laws would always conveniently fall into the exceptions category, thus rendering Section 205 a nullity. Virginia's interpretation cannot be accepted.

Virginia and Kentucky also argue that their laws are subject to exemption under Section 205's "public health, safety and welfare" clause because they are designed to address traditional concerns related to state regulation of electric utilities.<sup>219</sup> Contrary to these arguments, however, Virginia and Kentucky laws impeding AEP's integration are not based on the type of state interests immune from the Commission's exemption authority under Section 205.<sup>220</sup> The Conference Committee report on the meaning of Section 205 provides an illustrative list of the

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<sup>216</sup> EXE-100 at 4.

<sup>217</sup> Walker Cross-Examination at 774.

<sup>218</sup> *Id.*

<sup>219</sup> See EXE-90 at 2 & 10-11.

<sup>220</sup> See EXE-1 at 6 & 20-21.

types of state laws that *would* be subject to the second exception under Section 205.<sup>221</sup> This includes "state siting laws, regulations under the Clean Air Act, and zoning laws, *among others*."<sup>222</sup> The inclusion of the phrase "among others" demonstrates that, while this list is illustrative, it is by no means exhaustive. Its purpose is to provide examples of the types of laws that qualify for exemption from the Commission's authority under Section 205.

Virginia laws governing AEP's integration into PJM are designed to protect Virginia's economic interests and erosion of any VSCC jurisdiction to the exclusion of broader efficiencies – the very type of law that Section 205 was designed to target, not to exempt.<sup>223</sup> By way of illustration, in its order addressing AEP's application to join PJM, dated November 7, 2003 ("VSCC Order"), the VSCC stated that an examination of "specific *net cost/benefits outcomes* of AEP-VA's proposal on relevant populations" was necessary and requested financial information such as "Transmission *Costs*, production of Generation *Costs*; Congestion *Costs*; Production *Revenues*; Transmission *Revenues*; *Revenues* Associated with Transmission Rights and Net Operating Income Available for Equity in order to evaluate the "overall impact" of AEP's proposed integration."<sup>224</sup> Like the KPSC Order, the VSCC Order focuses on "economic protectionism"; it does not even mention concerns related to public health, safety, and welfare, the environment or energy conservation as part of its determination of whether AEP's request to participate in PJM will satisfy the Virginia statute.<sup>225</sup> The conclusion that the Virginia law is designed to protect the economic interests of Virginia citizens is underscored by the discourse preceding passage of the Virginia Statute. For example, the Virginia legislature's floor debate of the Virginia Statute reflects an almost exclusive focus on economics that are traditionally the

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<sup>221</sup> See EXE-30 at 10.

<sup>222</sup> *Id.* (emphasis added).

<sup>223</sup> See EXE-1 at 21.

<sup>224</sup> *Id.* at 22-23 (emphasis added).

<sup>225</sup> *Id.*

focus of utility regulation.<sup>226</sup> One Delegate summarized the concerns addressed by the state as follows: "pay attention closely to this because the amounts of money you're talking about and the burden on your constituents is going to be extremely prejudicial to them."<sup>227</sup>

Likewise, Kentucky's laws are based on the state's desire to protect the economic interest of the state. For example, in the KPSC Order, Kentucky's rejection of AEP's request to participate in PJM focused on retaining or obtaining economic benefits for, and the economic impact on, Kentucky ratepayers.<sup>228</sup> The KPSC Order provides, in relevant part:

Kentucky Power was unable to quantify any benefits to Kentucky customers from PJM membership . . . . Although [day-ahead and real-time markets and the PJM congestion management system] may benefit PJM's multi-state wholesale market, they bring no discernable benefits to Kentucky Power's retail customers. . . . Simply creating a larger wholesale market that extends from the Midwest region to the mid-Atlantic region will not bring cheaper power to Kentucky. . . . Consequently, we find that Kentucky Power's request to transfer functional control of its transmission assets to PJM is not in the public interest and should be denied.<sup>229</sup>

The KPSC Order does not identify public health, safety and welfare, the environment, or energy conservation as grounds for denying AEP's request to participate in PJM.<sup>230</sup> Thus, the evidence before the Commission demonstrates that Kentucky's laws are designed to promote "economic protectionism," which is not the type of state interest that is immune from PURPA preemption under Section 205.<sup>231</sup>

In addition to "economic protectionism," Kentucky's and Virginia's laws are motivated by a desire to delay AEP's RTO participation as a means of securing additional time to analyze the economics of AEP's and other companies' decisions and the impact on state jurisdiction over the

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<sup>226</sup> See EXE-90 at 11; *see also* H.B. 2453 Floor Debate Transcript ("EXE-92") at 3, 5, 15-16, 18, 21-22, & 24-26.

<sup>227</sup> EXE-1 at 12; EXE-92 at 24-25.

<sup>228</sup> EXE-1 at 20-21; *see also* EXE-14 at 17-19.

<sup>229</sup> See EXE-14 at 17-21.

<sup>230</sup> See *generally* EXE-14 at 17-21; *see also* EXE-1 at 21.

<sup>231</sup> See EXE-1 at 20.

"rates, terms, and conditions of service" to retail customers.<sup>232</sup> All of these objectives are driven by economics; none constitutes a permissible exception to valid preemption under Section 205. Finally, although MISO witness Svanda testified that AEP's full participation in an RTO would contribute positively to the health, safety, and welfare of consumers served by AEP affiliates in Kentucky,<sup>233</sup> the ALJ should reject any attempt by Virginia and Kentucky to manipulate this opinion to support their unsubstantiated claims of exemption. The States' claims are not supported in the record. Moreover, MISO witness Svanda's references to "public health, safety and welfare" are made in a "general, region-wide sense, not in the context of offering an opinion on the meaning of Section 205."<sup>234</sup> MISO witness Svanda is not an attorney, did not participate in the development or passage of PURPA, and claims no particular expertise on the meaning of PURPA Section 205.<sup>235</sup> These characteristics pertain to all or nearly all of the States' witnesses that opined on the meaning of Section 205(a); when contrasted with the testimony of former Congressman Sharp, who participated directly in the development of Section 205(a), the testimony of the States' witnesses on this issue must yield.

Accordingly, the Industrials respectfully request the ALJ to interpret Section 205 in accordance with the arguments detailed herein, and find and conclude that Kentucky and Virginia laws do not fall within the scope of the exceptions set forth in Section 205 and, consequently, are not exempt from the Commission's preemption authority.

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<sup>232</sup> PJM-1 at 25.

<sup>233</sup> MIS-1 at 8.

<sup>234</sup> Transcript of January 28, 2004 Hearing at 470-475 (Cross-Examination of David A. Svanda).

<sup>235</sup> *See generally* MIS-1 at 1-12.

### **III. CONCLUSION**

**WHEREFORE**, the Coalition of Midwest Transmission Customers, PJM Industrial Customer Coalition, American Forest & Paper Association, and Electricity Consumers Resource Council respectfully request the Presiding Administrative Law Judge to find and conclude that substantial evidence supports the Commission's preemption of Virginia and Kentucky laws, rules, and regulations that are preventing AEP's full integration into PJM.

Respectfully submitted,

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By \_\_\_\_\_

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Paper Association and Electricity Consumers  
Resource Council

Dated: February 12, 2004

**CERTIFICATE OF SERVICE**

In accordance with the requirements of 18 C.F.R. § 385.2010, I hereby certify that I have this day served the foregoing document electronically upon each person designated on the official electronic service list compiled by the Presiding Administrative Law Judge and served hard copies on those parties so designated for receipt by the Presiding Administrative Law Judge, pursuant to the "Order on Motion to Compel and Request for Restricted Service List," issued January 6, 2004 in this proceeding.

Dated at Washington, D.C., this 12th day of February, 2004.

/s/ Robert A. Weishaar, Jr.

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