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SUPREME COURT OF APPEALS
OF WEST VIRGINIA

No. 13-1126

IN THE
SUPREME COURT OF APPEALS
OF WEST VIRGINIA

WEST VIRGINIA CITIZEN ACTION GROUP,
Petitioner,

v.

PUBLIC SERVICE COMMISSION OF WEST VIRGINIA, MONONGAHELA POWER COMPANY, and THE POTOMAC EDISON COMPANY,
Respondents.

(Nos. 12-1571-E-PC and 13-1272-E-PW, Public Service Commission of West Virginia)

RESPONSE OF MONONGAHELA POWER COMPANY AND THE POTOMAC EDISON COMPANY TO PETITION FOR APPEAL OF WEST VIRGINIA CITIZEN ACTION GROUP

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I. STATEMENT OF THE CASE

In its October 7, 2013 Order ("Order"), the Public Service Commission of West Virginia ("Commission") approved a generation resource transaction between Monongahela Power Company ("Mon Power") and its affiliate, Allegheny Energy Supply Company, LLC ("AE Supply"). In the Order, the Commission approved Mon Power's acquisition of AE Supply's interest in the Harrison Power Station ("Harrison") located in Harrison County, West Virginia, and Mon Power's recovery of a portion of its investment in that acquisition. Although the Order approved a settlement recommended by Mon Power, its sister company, The Potomac Edison Company ("PE," and with Mon Power, the "Companies"), the Commission Staff, the Consumer Advocate Division ("CAD"), and other intervenors, the Commission added conditions beyond those agreed to in the settlement designed to reduce customer risk and protect customer interests. Only the petitioner here, West Virginia Citizen Action Group ("WVCAG"), opposed the settlement, and only WVCAG contends that the Transaction, as conditioned and approved by the Commission, fails to satisfy the standards for approval in W. Va. Code § 24-2-12.

The Order is supported by overwhelming evidence that the Commission's approval comports with the statutory test of § 24-2-12, and that a "Merger Stipulation" approved in a 2010 Commission proceeding did not preclude Commission approval of the Transaction. This Court should affirm the Order and dismiss the WVCAG appeal.

A. Procedural History

On November 16, 2012, the Companies filed a Joint Petition seeking approval of a generation resource transaction ("Transaction") to address a significant deficit in generating capacity available to serve their West Virginia combined load. Mon Power proposed to purchase from AE Supply, at AE Supply's net book value, AE Supply's entire 79.46% ownership in Harrison, resulting in Mon Power becoming Harrison's sole owner. As part of the Transaction, Mon Power would sell to AE Supply its 7.69% interest in the Pleasants Power Station ("Pleasants"), located in Pleasants County, West Virginia, at fair market sales value, making AE Supply the sole owner of Pleasants. JA 135 (Jt. Pet.).[1,2] Mon Power would pay the ***lower*** of market value or book value for AE Supply's interest in Harrison, but would receive the ***higher*** of market value or book value for its interest in Pleasants. *Id.* at 142-43. Mon Power also sought approval for a temporary surcharge ("Surcharge") to recover Transaction-related capital and operating costs until new base rates were placed in effect.

The Transaction was subject to intense scrutiny by the Commission Staff, the CAD, and intervenors including the West Virginia Energy Users Group; the Utility Workers Union of America; the AFL-CIO and its Local 304; the West Virginia State Building and Construction Trades Council; the West Virginia Coal Association; the Sierra Club; and WVCAG. The Commission held a three-day evidentiary hearing in May 2013, receiving testimony from over twenty witnesses. In August 2013, the Companies and eight other parties reached a comprehensive settlement, which they documented in a Joint Stipulation filed on August 21, 2013 ("Joint Stipulation"). WVCAG objected to the Joint Stipulation, and on September 13, 2013, the Commission held a hearing on the Joint Stipulation to determine its reasonableness.

In addition to recommending approval of the Transaction, the Joint Stipulation incorporated many public benefits, including energy efficiency and renewable energy provisions

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1 References to the Joint Appendix are cited as "JA," followed by the page number and a parenthetical identification of the witness or the document itself.

2 Mon Power would also assume AE Supply's obligations under a $73.5 million promissory note ("Note") secured by a lien on certain facilities at Harrison and would receive a $73.5 million credit against the purchase price. The total estimated purchase price for the Harrison Acquisition was $1.251 billion. Thus, when the par value of the Note and the price for Pleasants were deducted, the net payment from Mon Power to AE Supply for the Transaction was approximately $1.1 billion. JA 142-43 (Jt. Pet.).

endorsed by intervenors such as the Sierra Club, a commitment to increase employment levels in West Virginia important to the Staff, an enhanced process for procuring capacity under certain circumstances that several parties promoted, and a variety of home weatherization and energy assistance financial commitments that will be available to low-income customers. JA 966-75 (Jt. Stip.). These commitments responded to various intervenor concerns, had not been included in the Transaction as proposed, and helped to gain the support of the Joint Stipulation's many signatories.

The Commission was not the only regulator to evaluate aspects of the Transaction. The Federal Energy Regulatory Commission ("FERC") approved Mon Power's request to dispose of jurisdictional facilities under Section 203 of the Federal Power Act (16 U.S.C. §824b (2006)), and it approved the financing of the Transaction under Section 204 of the Federal Power Act (16 U.S.C. §824c (2006)).[3] In approving the Transaction, FERC found that the Transaction will not result in cross-subsidization between Mon Power and AE Supply.

The Commission entered the Order on October 7, 2013, approving the Transaction as modified by the Joint Stipulation but imposed three additional conditions ("Conditions") on the Companies, AE Supply, and their parent, FirstEnergy Corp. ("FirstEnergy"). Subject to acceptance of the Conditions, the Commission found the Transaction to be fair, reasonable, and in the public interest. Mon Power, PE, AE Supply, and FirstEnergy filed statements accepting the Conditions on October 9, 2013, and thereupon closed the Transaction. On October 18, 2013, the Companies filed tariff sheets with the Commission reflecting implementation of the rate decrease approved in the Order and occasioned by the Transaction's closing. Without seeking

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[3] FirstEnergy Service Company, Order Authorizing Disposition and Acquisition of Jurisdictional Facilities, 143 FERC ¶ 61062 (April 23, 2013), filed with the Commission on May 15, 2013, at 14. FERC's approval of the financing was made in a letter order dated May 13, 2013 in Docket No. ES13-11-000, also filed with the Commission on May 15, 2013.

reconsideration or a stay from the Commission, WVCAG filed its petition for appeal on November 6, 2013.

B. Statement of Facts Relevant to Petitioners' Assignments of Error

1. The Companies Had a Need for Additional Capacity.

The Companies operate electric transmission and distribution systems in West Virginia that collectively serve approximately 515,000 customers. JA 138 (Jt. Pet.). To address a serious shortfall in Mon Power's owned generation capacity and a growing reliance on purchases of capacity and energy in the PJM wholesale market,[4] the Companies developed a long-term plan to identify the best resources to meet their future energy and capacity obligations. *See* JA 17-116 ("2012 Resource Plan"). The 2012 Resource Plan considered capacity needs, energy outlook, reserve requirements, market pressures, economic conditions, and regulatory drivers, and compared the Companies' projected peak demands with Mon Power's current and planned resources. *Id.* at 67. Based upon conservative projected average annual growth rates of 1.4% for energy and 1.2% for peak demand, peak demand was projected to increase by 31 to 35 megawatts ("MW") per year through 2028. *Id.* at 65.

This projected load growth, coupled with the September 2012 deactivations of the Albright, Rivesville, and Willow Island facilities ("Deactivations"),[5] sharpened the focus on Mon Power's capacity deficit. The Deactivations reduced Mon Power's installed capacity by 660 MW, worsening a preexisting 2013 capacity shortfall; without additional capacity, Mon Power's

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4 Mon Power owns all of the generation capacity and contractual rights to generation for both Companies, and provides energy and capacity to PE's West Virginia customers.

5 The Commission reviewed the Deactivations in early 2012 and found them to be reasonable. Monongahela Power Co. and The Potomac Edison Co., Case No. 11-1274-E-P (Commission Order dated July 13, 2012) at 5. The Deactivations were due in part to new EPA regulations that were too costly for those plants to meet.

capacity coverage would have decreased from 84% in 2012 before the Deactivations to 60% by 2026, resulting in deficits of 938 MW in 2013 and over 1,400 MW in 2026.[6] JA 936 (Order at 25).

Continued reliance on capacity purchases in the market, viewed in light of the Deactivations and projected load growth, created unacceptable exposure to market price volatility. JA 177-78 (Delmar) and 759 (Hornby). The Commission found that regardless of whether the Companies' or WVCAG's calculations were used, the Companies had a serious deficiency that justified acquisition of additional capacity. JA 955 (Order at 44).

2. The Transaction Resolved the Capacity and Energy Shortfalls.

The Commission found that the 2012 Resource Plan, in its identification of Harrison as the most cost-effective alternative, produced a solution representing the "most reasonable priced capacity" for the Companies. JA 936 (Order at 25). Aside from Harrison, the 2012 Resource Plan considered a range of alternatives, including several options for repurposing the Albright Power Station to biomass or a natural gas facility or constructing a natural gas combined cycle ("NGCC") plant at that site. Additionally, three types of new base load generation plants (coal, nuclear, and NGCC) were reviewed in terms of cost-effectiveness, affordability, planning flexibility, asset mix optimization, risk adaptability, and long-term environmental compliance planning. JA 183 (Delmar). The Companies used "levelized cost analysis" to identify differences between alternatives that can be difficult to analyze in simulation modeling. JA 462 (Delmar). Levelized cost analysis incorporates reasonable assumptions on load growth, capacity factors, and energy

6 WVCAG employed a different calculation method, but even using its own method, WVCAG projected a shortfall in 2013 of 770 MW and 1,211 MW in 2026. *See* JA 935-36 (Order at 24-25).

market prices, and uses sensitivities to evaluate different rates of growth and price assumptions. JA 53-57 (2012 Resource Plan).

The Companies proved that acquiring Harrison was better than constructing a new NGCC plant because unlike an NGCC, Harrison would "hedge" Mon Power's capacity and energy requirements through 2018 by ensuring enough Mon Power-owned generation to provide for the needs of the Companies' West Virginia customers. To achieve the same installed capacity, Mon Power would need 2.25 NGCC plants, requiring a capital outlay 1.28 times greater than the Transaction; to match Harrison's energy output, 6.75 NGCC plants would be needed at a capital outlay 3.85 times greater. JA 186-87 (Delmar). Construction of new facilities would also be subject to potential cost overruns and delay, whereas Harrison had a set price and was available immediately.

Not only was Harrison the most cost-effective long-term capacity resource (JA 149 (Delmar)), but the Companies showed that Harrison would benefit customers by (i) helping to ensure an ample supply of reliable, low-cost electricity; (ii) minimizing reliance on market energy and capacity purchases, providing a hedge against market volatility and stabilizing customer rates; (iii) allowing the Companies to take advantage of lower energy prices if they occur; and (iv) providing the opportunity for incremental net revenues from energy sales to reduce ENEC rates.[7] *Id.* at 171-72, 190 (Delmar). In addition, Mon Power's 100% ownership would provide the potential for more economic benefits to the regional and state economy than would its minority

[7] "ENEC" stands for "Expanded Net Energy Cost," describing the annual case in which the Companies' fuel, purchased power, and power sales revenues are adjusted on January 1 each year based on over or under-recoveries of expense and projections for the succeeding period. ENEC rates cover the variable costs of generating, buying, and selling energy and capacity, whereas "base" rates take into account revenues and O&M expenses and provide for a return of and on invested equity capital.

interest under joint ownership. None of these differences was effectively controverted at hearing, and the Commission recognized their significance in the Order. JA 942 (Order at 31).

3. Harrison is a Valuable Asset.

Harrison is a 1,984 MW supercritical coal plant in Haywood, West Virginia that began commercial operation in 1972. Harrison is a thoroughly modern facility, with a host of important environmental control investments needed to continue cost-effective operations under existing and anticipated environmental regulations. The Commission Staff and the CAD agreed that Harrison is a solid, reliable asset from a technical perspective. It is well maintained, has many years of useful life ahead, and is on schedule for compliance with the EPA's Mercury and Air Toxics Standards ("MATS"). JA 340 (Walker) and 223-24 (Gregg). Based on recent improvements, including a cooling tower rebuild, water remediation projects, and initial investments to comply with MATS, Harrison is expected to have many years of productive service. JA 133 (Walker).

Other attributes gave Harrison a high asset value relative to other generation resources. Judah Rose of ICF Resources, an expert on utility asset values, opined that Harrison is a "huge power plant" with "remarkably low" operating costs. JA 677-78 (Rose). Harrison's delivered coal cost and dispatch prices are low, owing to its location in the heart of the Northern Appalachian coal fields, its ability to use discounted high-sulfur coal, and its very close proximity to a major fuel supply source, the Robinson Run mine. Harrison benefits from a favorable position in the PJM wholesale market and its location outside of areas with more stringent state environmental controls, particularly those arising from regional CO2 emissions regulations. *Id.* at 510-516.

4. Mon Power Acquired Harrison at a Fair, Below-Market Price.

AE Supply's interest in Harrison was obtained through arm's-length negotiations between two affiliates, consistent with Federal Energy Regulatory Commission ("FERC") guidelines. JA 481 (Szwed). The Companies proved that this negotiation resulted in a fair, below-market price.

As authorized in the Order, Mon Power acquired the remaining interest in Harrison in October 2013 at AE Supply's book value—the fair value of the asset when FirstEnergy purchased it, along with Allegheny Energy's other assets and liabilities, from Allegheny Energy in 2011. The fair value of AE Supply's interest in Harrison was based on the value KPMG determined in 2011 pursuant to Generally Accepted Accounting Principles governing purchase accounting. The net book value of Harrison was approximately $1.164 billion, which included a purchase fair value measurement component of $589 million. JA 165 (Wise).

The fair market value of AE Supply's Harrison interest proved to be substantially more than its net book value (both pre and post-merger). Mon Power engaged an independent appraisal company, Navigant Capital Advisors ("Navigant"), in 2012 to estimate Harrison's prospective "fair market sales value"—the value obtained in an arm's-length transaction for cash between an informed and willing buyer and willing seller, neither of which is under any compulsion to buy or sell. JA 118 (Navigant Appraisal). The Navigant report established a fair market sales value for Harrison of $846/kW, equating to a value of AE Supply's 79.46% share of approximately $1.333 billion, a result consistent with, but higher in value than, the KPMG study from 2011. JA 117-24 (Navigant Appraisal) and 211 (Houlihan).[8] The Navigant appraisal was a current, independent third-party valuation by a nationally recognized consulting firm, and supported the reasonableness of the KPMG book values and the levelized cost Mon Power used to compare the Transaction against other alternatives. JA 184-85 (Delmar).

ICF provided a third valuation of Harrison in the spring of 2013. JA 517-18 (Rose). ICF's financial models incorporated key assumptions on natural gas prices, demand growth, demand side

[8] Navigant's analysis considered conditions in the power generation industry and economic outlooks, general market data, Harrison's history and future operations, Harrison's financial results and capital investments, financial data for comparable companies, recent arm's-length transactions involving similar companies, and information gathered at a site visit.

resources, environmental regulations, capital and financing costs for new plants, capacity prices, transaction vintage, transmission adjustments, and delivered coal prices. *Id.* at 519-29. Based on Harrison's attributes in the areas of delivered coal costs, power plant dispatch, wholesale power prices, environmental controls, plant size, and non-fuel O&M and non-environmental capital expenditures, ICF determined that Harrison had a higher value than any of the coal plants offered as comparables. *Id.* at 530-38. ICF's value for Harrison was not only higher than KPMG's, but higher than Navigant's as well. *Id.* at 511. None of the other Parties presented expert testimony setting a value for Harrison. The Commission noted the KPMG and Navigant valuations in the Order. JA 936 (Order at 25).

Mon Power's negotiation efforts were led by two seasoned veterans, Michael B. Delmar, Director, Regulated Generation and Dispatch, and Stanley F. Szwed, Vice-President, Compliance and Regulated Services and Chief FERC Compliance Officer. Their job was to acquire needed generation resources—preferably in West Virginia—and persuade AE Supply to accept a significant discount to Harrison's market value. JA 472-73 and 644-54 (Delmar); and 476-81, 719-25, and 732-39 (Szwed). Mr. Szwed left no doubt that their responsibility lay squarely with the regulated side of the FirstEnergy business (Mon Power), and that he took that responsibility very seriously in negotiating terms with AE Supply. He explained Harrison's identification as a solution to the capacity shortfall, the development of the 2012 Resource Plan, and early discussions with FirstEnergy senior management on options to solve the capacity shortfall, including building new generation, acquiring existing generation, energy efficiency, and continued market reliance. Only after meetings in April 2012 to address resources, valuation risks, and the pros and cons of assets did Mon Power initiate discussions with AE Supply. *Id.* at 477. Mr. Szwed stressed Mon Power's preference for a West Virginia asset, the need for an asset big enough to meet growing capacity needs, the importance of Mon Power's familiarity with Harrison, and the prospect of Mon Power's full control over that asset rather than the minority position Mon Power then held. *Id.* at 478.

Discussions continued into June 2012. Negotiating points included whether certain additional assets would be included and how long AE Supply would be willing to hold open the offer. As to price, both parties were aware of FERC guidelines for sales between affiliates, yet AE Supply "firmly believed that the market price was greater than the book price and wanted Mon Power to agree to a market price for the transaction." *Id.* at 480. Mon Power pressed for AE Supply's book value, wanting to demonstrate the absence of any cross-subsidization from Mon Power to its affiliate. Rejecting the suggestion that the Transaction was not at arm's length, Mr. Szwed expressed confidence in his team's efforts:

> I believed then and still believe now that Mon Power has the opportunity to obtain an exceptional asset that will be beneficial to Mon Power, its employees, its customers and the State of West Virginia at a reasonable price – not in spite of the affiliate relationship but because of it.

Id. at 481. Moreover, in his role as Chief FERC Compliance Officer, Mr. Szwed ensured that the negotiations complied with FERC affiliate restrictions that maintain physical and functional separation between regulated and competitive businesses. JA 740-43 (Szwed). There was true separation between those negotiating for Mon Power and AE Supply management, and there was absolutely no evidence presented of collusion or undue influence exercised by AE Supply or FirstEnergy. The Delmar and Szwed explanations of the negotiation process were entirely consistent with the Commission's findings on this issue. JA 945 (Order at 34).

5. The Transaction Benefits the State.

Mon Power's acquisition of the remainder of Harrison will also enhance the economy and well-being of north-central West Virginia. Harrison produces electricity with locally mined coal, consuming more than five million tons annually (JA 190 (Delmar)), and Mon Power's 100% ownership would support the West Virginia coal industry, help preserve mining jobs, and benefits the overall economy. JA 151-52 (Jt. Pet.), 437-39 (Delmar). The Transaction ensures a significant tax stream and provides a reliable, low-cost energy source to help attract and maintain manufacturing business. JA 426 (Laurita).

The Transaction enjoyed widespread support in the business and labor community—especially among the unionized workforces at Harrison and Robinson Run, the mine adjacent to Harrison—reflecting its positive economic impact. Harrison supports high-wage employment for plant employees and outside maintenance and construction contractors, and its operation supports coal mining employment and related businesses. This activity has ripple effects in the overall economy, and anchors the local and state tax base. JA 437-38 (Delmar). The active support of Affiliated Construction Trades, the Utility Workers Union of America, the International Brotherhood of Electrical Workers, the West Virginia Coal Association, and Consol Energy and its employees reflected Harrison's importance to the area's economic livelihood. Regulated ownership of Harrison would provide long-term operational and ownership stability—factors that prompted support from several of these groups[9] and letters from Harrison employees.

9 The Affiliated Construction Trades' witness, its director Steve White, stressed the long-standing relationship the West Virginia Building and Construction Trades has had with the Harrison plant, and the positive economic benefits arising from it. JA 420-23 (White). William Raney and James Laurita stressed the value of Harrison in preserving highly skilled, high-paying jobs in the coal industry and the substantial tax revenue associated with the plant, mining operations, and related economic activity. JA 430-32 (Raney) and 425-28 (Laurita). Consol and the employees of its Robinson Run complex, the mine that provides much of Harrison's fuel, sounded many of these same themes in an emphatic letter filed with the Commission and attached (less its nearly 400 employee signatures) as Exhibit A to this brief.

II. STANDARD OF REVIEW

The standard of review this Court applies to a challenged Commission order is well known: the Commission must act within its statutory authority and must base its decisions upon the evidence, and this Court has otherwise deferred to the Commission's judgment within the sphere of its regulatory expertise. This Court summarized the detailed standard of review as a three-part test: "(1) whether the Commission exceeded its statutory jurisdiction and powers; (2) whether there is adequate evidence to support the Commission's findings; and (3) whether the substantive result of the Commission's order is proper." Syl. Pt. 1, Central W.Va. Refuse, Inc. v. Pub. Serv. Comm'n., 190 W.Va. 416, 438 S.E.2d 596 (1993). Moreover, an Order based upon the Commission's finding of facts "will not be disturbed unless such finding is contrary to the evidence, or is without evidence to support it, or is arbitrary, or results from a misapplication of legal principles." State *ex rel.* Pub. Serv. Comm'n v. Town of Fayetteville, Mun. Water Works, Syl. Pts. 4-6, 212 W.Va. 427, 573 S.E.2d 338 (2002) (citations omitted). The Court's responsibility is "not to supplant the Commission's balance of these interests with one more nearly to its liking, but instead to assure itself that the Commission has given reasoned consideration to each of the pertinent factors." Affiliated Constr. Trades Found. v. Pub. Serv. Comm'n, Syl. Pt. 1, 211 W.Va. 315, 565 S.E.2d 778 (2002).

As long as a regulatory agency's interpretation of its own rule or regulation does not violate the constitution or a statute, "it is generally entitled to substantial or 'great' deference by the courts, especially when the implementation of the regulatory scheme requires particular administrative or scientific expertise, or the meaning of a provision is within the expertise of the agency." 73 C.J.S. Public Administrative Law and Procedure § 212 (updated Dec. 2011).

III. SUMMARY OF ARGUMENT

The Commission's approval of the Transaction was legally correct and should be upheld on appeal. In addition, this Court should determine whether the relief WVCAG requests—vacating the Order—is moot, requiring dismissal of the appeal. The Companies' argument is divided into five sections:

Section IV.A – *Relief Requested is Moot.* The Transaction, together with a corresponding reduction in customer rates, was implemented on October 9, 2013. WVCAG did not request a stay of the Order's effectiveness, and there was no legal impediment to Closing. For these reasons, the substance of the appeal is moot.

Section IV.B – *Commission Approval Supported by Substantial Evidence.* The record demonstrates that the Companies had a serious capacity shortfall, that a prompt remedy was necessary, and that Harrison was both an exceptionally high-value, West Virginia-based asset and the most cost-effective long-term solution.

Section IV.C – *Allowing Acquisition Adjustment Was Proper* (WVCAG Assignment of Error A). WVCAG incorrectly contends that the regulatory principle of cost-based rates precluded the Commission from allowing an "acquisition adjustment" which, in this case, is the difference between the authorized rate recovery and AE Supply's pre-Merger net book value. Cost-based ratemaking recognizes the reasonable cost of a purchased asset.

Section IV.D – *No Violation of "Merger Stipulation"* (WVCAG Assignments of Error B, C). The Commission correctly determined that Mon Power's acquisition of Harrison at a price exceeding AE Supply's pre-Merger net book value (but less than its market value) does not violate the Merger Stipulation, and that the intent of the Merger Stipulation was never to preclude its future regulatory authority to evaluate affiliate transactions. A contrary result would undermine the Commission's regulatory authority over public utilities and potentially deprive customers of the benefit of favorable affiliate transactions.

Section IV.E – *No "Undue Advantage" in Negotiations* (WVCAG Assignment of Error D). There was no evidence that Mon Power's representatives failed to protect customer interests in negotiating the Transaction with AE Supply. The only evidence was that Mon Power identified and pursued the Transaction as a means to resolve the capacity shortfall, and negotiated it with a goal to persuade AE Supply to accept a purchase price below market value. The fact that AE Supply had independent reasons for selling Harrison is immaterial and did not preclude Commission approval.

IV. ARGUMENT

A. The Subject Matter of the Appeal Is Moot, as the Transaction Has Already Closed.

The Transaction authorized by the Order, together with a corresponding reduction in customer rates, was consummated on October 9, 2013. Mon Power and AE Supply repeatedly announced their desire to close as soon as possible on Commission approval. Both in the Stipulation and at the September 13 hearing, the Companies urged the Commission to quickly approve the Transaction and allow Closing to occur. JA 855-56 (Wise) and 976 (Jt. Stip.). WVCAG did not request a stay of the Order's effectiveness, there was no legal impediment to closing the Transaction, and Mon Power and AE Supply closed it. For these reasons, the substance of the appeal is now moot.

Closing the Transaction involved much more than paper entries at FirstEnergy. Mon Power and AE Supply are operated separately and participate separately in wholesale energy and capacity markets. With 100% Harrison ownership, Mon Power now dispatches and makes financial decisions independently from AE Supply. PJM Interconnection, which dispatches generation within a thirteen-state area, has already made modifications to reflect new pricing signals from Mon Power for Harrison. Closing the Transaction also required both Mon Power and AE Supply to make different market arrangements to cover their respective post-Transaction load obligations—AE Supply's reflecting 1,476 MW less generation capacity, and Mon Power's reflecting 1,476 MW more. JA 135 (Jt. Pet.).

Moreover, financing the acquisition was a substantial undertaking. Mon Power financed the Transaction through a series of steps: (i) an equity contribution from FirstEnergy of approximately $527 million, (ii) issuing a short-term note from AE Supply of approximately $573 million; (iii) assuming the Note of $73.5 million (see note 2 above); and then (iv) issuing first mortgage bonds in a combined principal amount of $1 billion, using these proceeds primarily to repay the note and refinance two series of bonds. Mon Power's capital structure and rate base are completely different post-Closing, and it has a different set of bondholders looking to a different range of assets for repayment in the event of default.

The Closing also provided the Companies' customers with immediate rate benefits in two ways. First, the Transaction enabled a reduction in ENEC rates arising from higher net PJM market revenues corresponding with the increase in generation ownership at Harrison. This enabled the Companies, with the Stipulating Parties' support, not to file an ENEC case in late 2013, instead reducing ENEC rates. JA 973-74. Second, the Stipulating Parties agreed to amortize Mon Power's gain on the Pleasants sale over the 16-month period preceding the next base rate case, moderating the impact of the Surcharge. JA 971. The Commission approved both of these strategies, and thus a rate decrease of approximately 1.5% for all customer classes other than large industrial (which got a 5% decrease) has been in effect since Closing. Customers are receiving this benefit today, and would not be unless the Transaction closed.

Commission Orders are final when entered and remain effective (subject to any conditions on their effectiveness stated in them) unless stayed. *See* Howell Sanitation, Inc., M. C. Case No. 22705-AC (Commission Order dated May 13, 1988) at 2-5 (discussing process by which Commission considers requests for stay of final orders). Notwithstanding WVCAG's involvement throughout the Commission proceedings, at no point did it ask the Commission to delay or stay the effectiveness of the Order approving the Transaction. Consequently, once the Companies had complied with the Order's conditions, Mon Power was free to complete the Transaction and undertake the Financing, and the Companies' customers were entitled to have their rates immediately reduced.

In short, without a stay, the parties were free to consummate the Transaction as approved by the Commission; having done so, a justiciable controversy no longer exists. *See* Jackson v. Bibb County School District, 271 Ga. 18, 515 S.E.2d 151 (1999) (appeal of denial of injunction to prohibit school district's acquisition of land was mooted by the sale's occurrence; court observed that appellants were on notice, during the lower court proceeding, that the school district planned to immediately consummate the deal, yet they failed to seek a stay from that court while before it); Brown v. Spann, 271 Ga. 495, 520 S.E.2d 909 (1999) (analogous facts regarding sale of broadcast license; same ruling); Thorn v. Walker, 912 A.2d 1192, 1196 (D.C.App. 2006) (appellant's failure to seek a stay of real estate sale or other measure like placing proceeds in escrow rendered appeal moot).

"'Moot questions or abstract propositions, the decision of which would avail nothing in the determination of controverted rights of persons or of property, are not properly cognizable by a court.'" Syllabus Point 1, State ex rel. West Virginia Secondary Schools Activities Comm'n v. Oakley, 152 W.Va. 533, 537, 164 S.E.2d 775, 778 (1968), *quoting* Syllabus Point 1, State ex rel. Lilly v. Carter, 63 W.Va. 684, 60 S.E. 873 (1908). The Transaction presents just such a case.

Because the Transaction has already been completed, the financing undertaken, and the Rate Reduction implemented, the questions WVCAG has presented on appeal are abstract, and deciding them at this point would not benefit anyone. Ample authority from other jurisdictions supports the sensible notion that the closing of a contested transaction renders appeals like the instant case moot. *See* Monty v. Leis, 193 Cal.App.4th 1367, 123 Cal.Rptr.3d 641, 644 (2011) (observing generally that "[w]here a merger or acquisition takes place after [a] trial court has refused to issue a preliminary injunction, courts have refused to set aside the transaction"); DaimlerChrysler Corp. v. Delaware Dep't of Insurance, 938 A.2d 623 (Del. 2007) (granting stay of state insurance commissioner's approval of one insurer's acquisition of another, because otherwise, affected insured's appeal of that order would be mooted by the closing of the transaction). As the California appellate court explained:

> "Mergers and acquisitions are often followed by a commingling of assets and other substantial changes in the structures of the enterprises involved. Once those changes occur, it is often impossible ... to compel a return to the status quo, and the legality of the challenged merger or acquisition may become essentially a moot question."

Monty, 123 Cal.Rptr.3d at 644 (quoting Federal Trade Comm'n v. Exxon Corp., 636 F.2d 1336, 1342 (D.C.Cir. 1980).

Does the closing or consummation of a transaction – in and of itself – ***inevitably*** render a case challenging that transaction moot? Of course not, and hence examples exist where courts review the propriety of consummated transactions on the merits. *See, e.g.*, State ex rel. Intercon Gas, Inc. v. Public Service Comm'n of Missouri, 848 S.W.2d 593 (Mo.App. 1993). But as review of cases involving mootness questions arising from consummated commercial transactions would suggest, the operative issue is not simply whether the contested "deal" has been consummated; rather, the underlying inquiry is the one that drives mootness determinations generally – can the appellate court grant the relief that the appellant or petitioner seeks? *See* Akron Development Fund I, Ltd. v. Advanced Coatings Int'l, Inc., 2011 WL 2571618, *5 (Oh.App. 2011) ("The key inquiry ... [is] whether the relief sought on appeal [is] available."); Thorn, 912 A.2d at 1195 (case is moot if "the appellate court can provide no effective relief"); Intercon Gas, 848 S.W.2d at 596 (although completion of PSC-approved transaction did not "*of itself* render an appeal moot," cases can be moot "when circumstances change so as to alter the position of the parties or subject matter so that the controversy ceases and a decision can grant no relief") (emphasis added).

Here, WVCAG's request for relief would be impossible to implement, and even if it were feasible, would be disruptive, destabilizing for Mon Power, and enormously expensive for customers. In effect, it would mean unwinding the Transaction, reconstructing previous ownership interests with PJM, recapitalizing Mon Power, redeeming recently issued mortgage bonds (at a premium of over $100 million), and—worst of all for customers—a revocation of the recent rate decrease and the Companies' need for interim relief to raise ENEC rates that the Transaction had just reduced. Unwinding the Transaction would be impractical, unwise, and against the public interest.

Moreover, the entire process to resolve the Companies' capacity deficit would be back at square one, with market exposure still present and no alternative in sight. Mon Power would be faced with choosing between building new capacity, with cost overrun risks and the inability to build a coal plant under current EPA regulation, or buying an unfamiliar out-of-state asset from a seller who would factor in the uncertainty and delay of regulatory approval into its price, and with additional transmission costs and constraints to contend with. Reversing the Transaction would place the Companies right back where they started in mid-2012: with a growing capacity deficiency and growing exposure to market risk, but with the capacity acquisition that makes the most sense – acquiring the remaining ownership interest in a high-value, coal fired asset in the heart of Mon Power's service territory – effectively off the table. It would also make Mon Power a minority owner of Harrison once again, removing the benefits of Mon Power's current sole ownership with the ability to make the decisions for Harrison.

Finally, unwinding the Transaction would take away other public interest benefits that the Commission found the Transaction embodied. The benefits of the Transaction in the form of protection against market energy and capacity risk – benefits that accrue not simply to the Companies, but to local miners, local laborers, large industrial consumers, and residential rate payers – would be lost in the event of an appellate outcome requiring an unwind of the Transaction, which is the express goal of the WVCAG appeal. Attempting to compel a return to the "pre-closing status quo" would be an administrative, financing, and public interest nightmare.

B. The Evidence Supports Commission Approval of the Transaction as Recommended in the Stipulation and Modified in the Order.

WVCAG completely ignores the Commission's justifications for approving the Transaction and minimizes the customer risks arising from the capacity deficiency. The Commission relied on compelling evidence for Mon Power's acquisition of Harrison—evidence that fully justified Commission approval and shows the Order's substantive result to be proper. Under the Central West Virginia Refuse standard of review (Section II above), the Order should be upheld.

1. A Serious Shortfall in Generating Capacity Motivated Mon Power to Propose and Pursue the Transaction.

The Order documents the Companies' serious capacity deficiency, showing it to be an urgent problem requiring a timely, effective solution. The Deactivations reduced Mon Power's installed generation capacity by 660 MW and contributed, in the Commission's words, to the "need and the urgency of added capacity." Taking into account projected increases in peak demand through 2028, Mon Power's capacity was expected to fall from 84% in 2012 to 60% by 2026 relative to the Companies' generation requirements (in industry parlance, their "load"). JA 935 (Order at 24), citing JA 72, 93 (2012 Resource Plan). The Commission found that failing to deal with the market risks inherent in this capacity deficit would be unacceptable. WVCAG's Mr. Schlissel generally agreed with the projection of sustained increases in market capacity prices due to the prospect of meaningful CO2 emissions regulation and the retirement of nuclear units. The CAD's Mr. Hornby agreed that the risks associated with capacity deficits were present then and should not be permitted to continue indefinitely. JA 935 (Order at 24).

2. Harrison is an Exceptionally Valuable, High Performing Plant that Resolves the Capacity Shortfall.

Harrison is the crown jewel of FirstEnergy's coal-fired generating fleet. According to impartial reviews by Staff and CAD experts, Harrison is a high value asset with many years of useful life remaining, is on schedule for compliance with MATS, and is well maintained – a good, reliable asset from a technical perspective. It sits on a coal field, has very low operating costs, and benefits from an array of pollution control equipment. JA 677-78 (Rose).

In light of these attributes, it is no surprise that over time, Harrison's value was projected to exceed that of a new NGCC. WVCAG's Ms. Kunkel conceded that Harrison is less expensive than market capacity purchases after only seven years at the rate recovery amount recommended in the Stipulation, and thereafter would result in a positive net present value of approximately $400 million over Harrison's remaining life. If her analysis had incorporated the lower 10% return on equity and the 25% income tax rate included in the Stipulation's Surcharge calculation, the net present value benefit to customers would have been even greater. JA 930 (Order at 19), citing JA 888-89 (Kunkel). The 2012 Resource Plan showed a $74 per MW hour ("MWh") levelized cost of generation from Harrison at the proposed acquisition price as compared with $115/MWh for a NGCC plant, even when based on the full rate base recovery initially proposed. Using the lower rate base value in the Stipulation, the Commission found that "using any reasonable assumptions continues to result in the Transaction providing the lowest levelized cost as compared to the alternatives considered by MP/PE." JA 937 (Order at 26). The Commission conducted its own sensitivity analyses at different capacity factors, including some that included a value for carbon emissions, and still found Harrison to be the lowest cost solution. JA 937-39 (Order at 26-28).

Another critical advantage of Harrison as compared with an NGCC is its potential for off system sales of energy and capacity that can offset the costs of new capacity and reduce rates. JA 938 (Order at 27). These rate benefits were prominent in the West Virginia Coal Association's support for the Transaction (JA 431 (Raney)), in addition to the positive impacts on mining and related industries their witnesses cited (JA 430-32 (Raney) and 425-28 (Laurita)).

In summary, the Commission found "substantial evidence that Harrison is a sound and well-maintained generating facility "with low operating costs, historically high capacity factors, installed environmental controls and ongoing plans for additional controls for MATS compliance." JA 937 (Order at 26) The Companies had a need for additional capacity, and the Commission found that the "proposed Transaction is a reasonable plan to acquire that capacity." JA 936 (Order at 25).

3. Under the Stipulation, Customers Acquired Harrison at Far Less than Market Value, Moderating the Rate Impacts of the Transaction.

The Commission authorized the Harrison acquisition at an effective cost dramatically lower than the lowest of the three market value determinations. Much of the evidentiary hearing was devoted to evaluating the market value of Harrison to show how the purchase price—approximately $1.2 billion—compared to its market value. The Companies provided three independent valuations (KPMG, Navigant, and ICF), each of which exceeded the proposed Transaction price. The Stipulation, which reduced the rate impact of the Transaction by $332 million, meant that the Order's customer rate impact was far less than the Companies initially proposed. JA 941 (Order at 30). "The Joint Stipulation proposes that we approve a write-off of approximately $332 million of the Acquisition Adjustment and allow only $257 million of the Acquisition Adjustment in rate base." This reduced the annual revenue requirement for the Surcharge by $59.6 million (to $113.4 million from $193 million). JA 926 (Order at 15).

4. The Stipulation Incorporated Commitments that Increased the Transaction's Value to Customers and the State.

In evaluating the Stipulation, the Commission pointed out an entire category of voluntary commitments by the Companies that differentiated the Transaction from the one initially proposed. These new terms, which the Stipulating Parties negotiated with the Companies, provided for expanded employment opportunities as well as financial, energy efficiency and capacity acquisition commitments, and were "part of the reason that Staff, CAD, WVEUG and the Sierra Club support the settlement embodied by the Joint Stipulation." JA 926 (Order at 15).[10] These

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[10] These commitments are found in subparagraphs 11(a), (b), (c), (d), (m), and (o) of the Stipulation (JA 966-75), and were summarized at page 15 of the Order (JA 926) as follows:

> These include (i) a commitment to increase employment in West Virginia by 50 employees, mostly in the distribution sector; (ii) a 2-year rate credit

commitments had substantial value to the Companies' large industrial customers, the Commission Staff, the West Virginia Coal Association, and workers at the Harrison Station represented by the UWUA. JA 927, 951 (Order at 16, 40 (Finding of Fact 8)).

5. The Commission Imposed Three Powerful Conditions on its Transaction Approval to Reduce Customer Risk.

Although the Stipulating Parties' recommendations on a fair resolution of this case were valuable and persuasive, the Commission cited its obligation to reach a "reasoned end result based on the record and a consideration of its statutory duties." JA 928 (Order at 17). The Commission's lingering concerns about the regulatory cost of carbon emissions, future "off systems sales," and the value of Harrison itself led it to impose three conditions never contemplated by the Stipulating Parties that, considered together, significantly shifted future risks from customers to the Companies.

The Commission expressed these concerns in its discussion of the "long-term benefit of Harrison." JA 939-40 (Order at 28-29). Despite substantial evidence of Harrison's high value, its operational costs are "dependent on a number of unknowns, the most significant being the possibility of future new costs imposed on carbon emissions and the possibility of low market prices for power in the PJM market." *Id.* The Commission grappled with whether the benefits of the increased Harrison capacity will continue into the foreseeable future, and pointed to "expected

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for Rate Schedules K and PP customers; (iii) a $100,000 retirement of renewable energy credits to spur the development of renewable energy resources; (iv) three separate $500,000 contributions over a 5-year period for the purposes of low-income energy assistance, home weatherization assistance, and to spur energy efficiency initiatives in public schools in MP/PE service territories; (v) increased energy efficiency targets; and (vi) a commitment to develop an RFP for capacity resources in the future. In addition, MP/PE are committed to file, to redirect, and reflect in rates a $250,000 per year customer-funded contribution, currently directed to weatherization, to dollar energy or an alternative low-income energy assistance agency.

profits from future system sales" as a significant factor in this analysis. JA 940 (Order at 29). These uncertainties caused the Commission to conclude that including the $257 million acquisition adjustment in rate base is reasonable only if there are mechanisms in place for "sharing of the risk of future carbon costs, market prices, or other factor that might diminish the value of Harrison . . . ." JA 945 (Order at 34). To provide for an "equitable sharing of risks," the Commission imposed these three Conditions:

- If FirstEnergy does not makes an additional equity investment to cover the decline in equity caused by the write-off of the $332 million Acquisition Adjustment, then Mon Power dividends could not be paid until its equity ratio returns to 45%;

- FE, AE Supply, Mon Power, and Potomac Edison had to agree that the $257 Acquisition Adjustment included in the Harrison sale price to Mon Power be subject to adjustment through refund if FERC determines that the purchase price exceeds the fair market valuation of Harrison; and

- The return requirement of the $257 million Acquisition Adjustment would only be allowed in rates to the extent that 50% of net margins from off-system transactions for the additional Harrison capacity acquired by Mon Power will support return requirements associated with the acquisition adjustment.

JA 946-47, 957-58 (Order at 35-36, 46-47 (Conclusion of Law 31)). The Conditions unquestionably strengthened the Order from the perspective of the Companies' customers, assigning more risk of future market uncertainties to Mon Power's shareholders.

C. The Commission Was Not Precluded from Allowing an "Acquisition Adjustment" in Rate Base, and Doing So Does Not Violate Cost Based Ratemaking.

WVCAG's extended discussion of the proposition that utility rates should be based on the utility's cost of service (Petition at 1 (Assignment of Error A), 25-26) does not govern a utility's acquisition of assets from an affiliate seller, even at a price above the seller's own net book value. The Commission correctly applied regulatory principles to reach this result, and the Order should be upheld in this respect under the Town of Fayetteville standard of review for Commission legal determinations.

The Transaction involved a utility buying a non-regulated asset, not already paid for by customers, from an affiliate. This kind of transaction falls under a different subsection of § 24-2-12 (subsection (f) instead of (g)) and involves a transaction between affiliates, not one between unaffiliated parties. When a utility seeks to buy or sell an asset from an affiliate, different concerns arise: the utility is prohibited from subsidizing the non-regulated affiliate by (i) buying an asset for more than it is reasonably worth or (ii) selling an asset for less than it is worth. When the Commission considers these such transactions, the litmus test is whether the cost is equal to or less than the market price, sometimes expressed as an industry average. If the cost of the goods or services charged to the utility affiliate is less than or equal to the industry average or market cost, the Commission is more likely to approve the affiliate transaction because there is no cross subsidization between affiliates.[11]

The Companies applied the regulatory test, often referred to as "asymmetric pricing," to both the Harrison acquisition and the Pleasants sale (it was also used for FERC approval purposes). They proposed to purchase Harrison for the lower of AE Supply's cost (*i.e.*, net book value) or its

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[11] *See e.g.*, Monongahela Power Co., Case No. 12-0506-E-PC (Commission Order dated December 12, 2012) at 3 (consent to inter-affiliate fuel procurement arrangement conditioned on FERC-approved commitments ("[a]ny fuel transferred from a market-regulated affiliate for use by Mon Power will be priced at the lower of cost or market price, and, conversely, any fuel transferred from Mon Power to a market-regulated affiliate will be priced at the higher of cost or market price")); Verizon West Virginia, Inc., Case No. 08-1127-T-PC (Commission order dated July 29, 2008) (approving billing services agreement and exempting amendments from Commission approval since FCC regulations will assure that services will remain at a fair market rate); West Virginia-American Water Company, Case No. 07-0628-W-PC (Commission Order dated July 6, 2007) (comparing the costs under of a Granular Activated Carbon Services Agreement to the industry standard for such services to determine reasonableness).

market value, and to sell Pleasants for the higher of its cost or its market value. This analysis does not turn on whether there is a premium or "acquisition adjustment" to be paid.

The Commission correctly noted some confusion surrounding the use of these terms JA 933-34, 940-41 (Order at 22-23, 29-30), and that its conclusion that the Transaction does not violate the Merger Stipulation turned on reasons "unrelated to the technical arguments regarding GAAP accounting for fair value adjustments, acquisition premiums, or goodwill . . . ." JA 934 (Order at 23). These are complex concepts in a highly arcane area in which the Companies and the Commission must work. Pointing out the confusion here, as the Commission did, does not mean the Commission "concoct[ed] an alternative reality to explain Mon Power's case," as WVCAG alleges (Petition at 38). Nor does it prove the Commission's decision to be "results driven" (Petition at 39) in the sense that it looked past an actual violation of the Merger Stipulation to accomplish the Companies' objectives. All parties to this Harrison Stipulation—including three significant ones who also joined in the Merger Stipulation (Staff, CAD, and WVEUG)—urged the Commission to approve the Transaction. If these parties were "results driven," it was for good reason—they wanted to see Mon Power own Harrison because of the many benefits it provides, and the huge capacity deficit its acquisition helps address. Only WVCAG opposes the Transaction as modified by the Commission.

If a utility commission determines that a utility should be permitted to acquire an asset for a reasonable, agreed price, then it is that price—and not the seller's initial investment—that represents the "cost" on which the utility's rates can be made. Any other interpretation would mean that no utility could purchase an asset at any price other than the seller's depreciated original cost, no matter what the circumstance. This outcome would obviously thwart most acquisitions of existing utility assets, especially valuable ones that might benefit utility customers. The principle of cost-based ratemaking does not stand for this proposition at all.

D. The Commission Correctly Found that the Merger Stipulation Does Not Prohibit Later Approval of an Affiliate Transaction.

WVCAG's focus on appeal is an alleged violation of the "Merger Stipulation"—one component of a stipulated settlement in 2010 in which all parties recommended approval of FirstEnergy's acquisition of Allegheny Energy, the Companies' corporate parent. (Petition at 1 (Assignment of Error B), 21, 25-29). WVCAG argues that the inclusion of any portion of the Acquisition Adjustment in rate base violates the Merger Stipulation. WVCAG's interpretation of the Merger Stipulation is incorrect, and the Commission's legal determinations on this issue were valid under the Town of Fayetteville standard.

1. The Merger Stipulation Cannot Be Read to Preclude Future Affiliate Transactions that Independently Require Commission Approval.

The Commission correctly determined that Mon Power's acquisition of Harrison at a price exceeding AE Supply's net book value does not violate the Merger Stipulation. JA 933 (Order at 22). The intent of the Merger Stipulation, the Commission noted, was to prevent FirstEnergy and the Companies from requesting an increased rate base valuation associated with FirstEnergy's purchase price for the Allegheny Energy stock "in excess of book value at the time of the merger." *Id.* In other words, FirstEnergy could not "push down or allocate any return requirement or expenses that would be intended to compensate it for the excess purchase price of Allegheny Energy." *Id.* Critically, the Commission found no evidence that the value of the Companies' "current assets" had been affected by merger-related accounting entries. *Id.*

Furthermore, WVCAG's restrictive interpretation would improperly constrain the Commission and undermine its regulatory authority. The Commission correctly refused to interpret the Merger Stipulation to hamstring its future regulatory authority over affiliate transactions. The Commission found the intent of the Merger Stipulation was to prevent FirstEnergy and the Companies from requesting an increased West Virginia jurisdictional rate base valuation related to the FirstEnergy purchase price of Allegheny Energy in excess of book value at the time of the merger. JA 955 (Order at 44). The Commission specifically found the Merger Stipulation was not intended and could not reasonably be extended to apply to all possible future transactions, including the Transaction. *Id.*

Restricting the Commission's full jurisdiction and control over West Virginia public utilities would contravene the public interest, yet it is exactly what WVCAG urges here. The Commission correctly rejected this argument:

> The merger stipulation was not intended and could not reasonably be extended to apply to all future affiliated asset transfers, such as the Transaction, but would have to come before us for approval. We believe that FirstEnergy always was free to request a sale of assets to Mon Power at any price.

JA 933 (Order at 22). WVCAG's position would prohibit the Commission from determining whether Mon Power's acquisition of any AE Supply asset at a price exceeding original net book value is, in fact, in the public interest.

This outcome would handcuff the Commission and be inconsistent with the Legislature's broad delegation of authority. The Legislature conferred upon the Commission sweeping powers and duties to enforce and regulate the practices, services, and rates of West Virginia public utilities, including powers:

> (1) To ensure fair and prompt regulation of public utilities in the interest of the using and consuming public;
>
> (2) To provide the availability of adequate, economical and reliable utility services throughout the state;

(3) To encourage the well-planned development of utility resources in a manner consistent with state needs and in ways consistent with the productive use of the state's energy resources, such as coal;

(4) To ensure that rates and charges for utility services are just, reasonable, applied without unjust discrimination or preference, and based primarily on the costs of providing the services; and

(5) To encourage energy conservation and the effective and efficient management of regulated utility enterprises.

W.Va. Code § 24-1-1(a). The Commission is specifically charged with the responsibility for appraising and balancing the interests of current and future utility service customers, the general interests of the state's economy and the interests of the utilities subject to its jurisdiction in its deliberations and decisions. W. Va. Code § 24-1-1(b). To carry out its duties properly, the Commission must necessarily have the flexibility to address properly the needs of the public as well as the interests of utilities.

Citing its October 4, 2012 order in Century Aluminum of West Virginia, Case No. 12-0613-E-PC, the Commission focused on this Court's characterization of the Commission's authority as legislative and encompassing:

> "[T]he Court has consistently and emphatically held that the Commission is the sole authority to determine the public interest in utility regulatory matters. In 1914, the Court stated "it is not for a review in Court to substitute its judgment for that of the Commission, on questions of expediency, or as to what would be best in the interest of the petitioner, or the public served. On all such questions we think the Legislature intended that the judgment of the Commission should prevail."

JA 933-34 n.5 (Order at 22-23 n.5)(*quoting* United Fuel Gas Co. v. Pub. Serv. Comm'n, 73 W. Va. 571, 591, 80 S.E. 931, 939 (1914)). The Commission found that this delegated legislature authority is inconsistent with the WVCAG contention that the Merger Stipulation somehow restricts its jurisdiction in this case and future cases.

WVCAG argues (Petition at 35) that if the Merger Stipulation parties had only thought of it, they never would have let Mon Power acquire AE Supply's interest in Harrison at anything more than AE Supply's original cost net book value. This is wrong. Yet the Court can ask the same question from the Commission's perspective: If the Commission had known the parties interpreted the Merger Stipulation to frustrate affiliate asset purchases in the future, would the Commission have approved it? This interpretation would have meant that in a subsequent affiliate transaction filing—even one many years down the road—the Commission would be unable to approve a Mon Power purchase of any affiliate assets covered by a Merger-related fair value adjustment, no matter how valuable the asset might have become on the market, or how useful to the Companies' customers in Mon Power's hands. In rejecting the preclusive effect of the Merger Stipulation WVCAG urges, the Commission wasn't doing "intellectual backflips" that were "designed to defeat" the purposes of the Merger Stipulation (Petition at 36); it was trying to do what is best for customers (as were several Joint Stipulation signatories, including Staff, CAD, and WVEUG, who had themselves signed the Merger Stipulation three years earlier).

2. WVCAG's Contract Arguments Do Not Translate to Utility Regulation, and Do Not Constrain Commission Action Here.

Joint stipulations are agreed resolutions that parties before the Commission recommend, and like the Stipulation here, are entered into subject to the Commission's acceptance, rejection, or modification. JA 929 (Order at 18). All parties know that stipulated settlements are subject to future Commission regulation and modification, and that parties' expectations may be affected if the Commission later determines that modifying stipulation terms is in the public interest. Because giving the parties the benefit of their agreements promotes settlement, the Commission generally tries to honor them; however, like the rest of Commission regulation, the terms of these agreements are not inviolate, especially in the case of subsequent Commission oversight and action. In any event, the Commission correctly found that the Merger Stipulation did not govern the Transaction at all.

3. The Commission Properly Approved Recovery of a Portion of the Fair Market Adjustment (WVCAG Assignment of Error C).

It was the Commission's role to review the Transaction and impose any modifications it deemed necessary and appropriate to protect the public interest. The Commission believed that Harrison was the right asset to solve a known problem, but wanted additional protections for customers and so conditioned its approval on the acceptance of the three Conditions by the Companies, AE Supply, and First Energy. There is nothing "arbitrary and capricious" about the Conditions (Petition at 1 (Assignment of Error C), 22, 40-41); instead, the Commission closely tailored them to address its concerns about the Joint Stipulation as proposed. The fact that the Commission had a "stated discomfort" with the Transaction as proposed in the Joint Stipulation (*id.*) does not mean that its "conditional" approval of the Joint Stipulation was unreasonable – the Commission is, after all, authorized in § 24-2-12 to condition its approval of jurisdictional transactions. From the Commission's perspective, it is the Conditions that help to protect customers from potential risks, while preserving to those same customers the benefits of the Transaction. In this way, the Commission's conditions are not unlike the other protective and beneficial conditions the parties themselves proposed in the Stipulation. Had the parties themselves included the Commission's own conditions in the Joint Stipulation, and the Commission then approved it, the same outcome would have resulted.

Moreover, WVCAG's explanation of this "arbitrariness" (*id.* at 40-41) does not make any sense. WVCAG contends that while the Commission protected customers against the financial impact of the $332 million write-off with the first Condition, the dividend limitation, it did not do the same thing with the "potential $257 million write off" (*id.* at 40 n.16), choosing instead to limit rate recovery of the $257 million acquisition adjustment (through Condition 3) to situations in which the incremental capacity generated off-system sales more than sufficient to pay the associated return requirement. WVCAG suggests that this decision is "per se . . . an adverse effect on the public that is fatal to this transaction" under W. Va. Code § 24-2-12. *Id.* at 40. WVCAG misunderstands the effect of, and the protections afforded by, Condition 3. There is no adverse effect on customers associated with the pass-through of the $257 million unless 50% of net incremental sales completely pay for the return requirement associated with the $257 million (leaving another 50% of those revenues as "gravy" on top, to benefit customers). In other words, before there is any pass through in rates, the investment first has to pay for itself ***and*** then generate additional revenues to reduce ENEC rates. In essence, customers bear no risk for the recovery of the $257 million. It should be noted that as to Mon Power's minority investment in Harrison before the Transaction closed, there were no such protections.

Second, there is no "arbitrary linking" between "one third of the cost of the Harrison purchase" to "one half of the earnings of Harrison," as WVCAG contends (Petition at 40). This link is a rational one, because it connects that portion of the fair market adjustment conditionally permitted in rates ($257 million) to the additional generation capacity its payment facilitated. To the contrary, the comparison WVCAG makes—between the $257 million conditional recovery and the entire purchase price of Harrison (*id.*)—***is*** arbitrary. Linking these together suggests that customers should be protected against any risk associated with the entire value of the acquired asset, including the portion representing AE Supply's pre-Merger net book value. Owning generation that participates in wholesale market sales entails some risk, and there is no reason to question the Transaction's reasonableness because shareholders have not been made to protect against risks associated with the ***entire*** purchase price. Instead, the Commission and the

Stipulating Parties all concluded that increased ownership of Harrison generation protects against more market risk than it creates; that is why they supported the Transaction.

E. There was Affirmative Evidence that Mon Power and AE Supply Negotiated the Transaction, and No Evidence that Mon Power's Representatives Failed to Protect Customer Interests.

WVCAG's Assignment of Error D, that the Order violated § 24-2-12's prohibition against "undue advantage" in inter-affiliate transactions (Petition at 1, 41-43), is demonstratively wrong. As the Commission succinctly concluded:

> The unrebutted testimony by MP/PE is that the Transaction was arm's-length and that negotiations were sensitive to FERC rules regarding affiliated transactions and cross-subsidization and carefully adhered to FERC rules . . . ***There is no evidence in the record to the contrary.***

JA 945 (Order at 34; emphasis added). The Companies presented affirmative evidence that the Transaction was negotiated, that FERC-required segregation between FirstEnergy's competitive and regulated affiliates was observed, and that those responsible for regulated operations zealously advanced Mon Power's interests and those of the Companies' customers. WVCAG's only arguments are circumstantial and conjectural: it essentially claims that because both AE Supply and Mon Power are owned by FirstEnergy, and because AE Supply had a financial reason to sell Harrison, there must have been undue influence at play. Petition at 41-42. Yet this set of circumstances underpins any affiliate transaction, and indulging WVCAG's argument would render meaningless the statutory construct for approval of affiliate transactions.

West Virginia Code § 24-2-12(f), which requires prior approval before any public utility enters into "any contract or arrangement for management, construction, engineering, supply or financial services or for the furnishing of any other service, property or thing, with any affiliated corporation, person or interest[,]" governed Commission approval of the Harrison Acquisition. JA 152-53 (Jt. Pet.). Section 24-2-12's three-part standard requires a finding that "the terms and conditions are reasonable and that neither party thereto is given an undue advantage over the other, and do not adversely affect the public in this state." W.Va. Code § 24-2-12(f). The Transaction satisfied each prong of the test. Under the Central West Virginia Refuse standard of review, there was adequate evidence to support the Commission's findings on this issue, and the substantive result it achieved was proper.

1. The Companies Presented Strong, Affirmative Evidence on Mon Power's Negotiation of the Transaction.

The evidentiary record proves, and WVCAG even concedes, that Mon Power's need for additional generation capacity was the impetus for the Transaction. The Transaction was Mon Power's idea, and it was Mon Power that first pursued it with FirstEnergy management and then AE Supply. Petition at 12. The Transaction identification and negotiating efforts between April and November 2012 (Section I.B.4 above) prove that Mon Power's focus was to keep the price of Harrison at AE Supply's post-Merger net book value, which effectively required persuading AE Supply to take a $169 million discount from its market value. AE Supply firmly believed that the market price was greater than that book value, and wanted Mon Power to agree to a higher price that reflected the market price. Contrary to WVCAG's contention (Petition at 13), Mon Power did not fail to secure a price lower than AE Supply's book value because of some concern about violating the Merger Stipulation. No such violation was even alleged until after the case was filed in November 2012; in any event, according to WVCAG ***any*** amount exceeding the pre-Merger net book value, no matter how small, would be a violation.

WVCAG's repeated assertions that neither Mr. Delmar nor Mr. Szwed was directly employed by Mon Power (Petition at 12) are meaningless. The Commission knows that FirstEnergy Service Company employed both men, and that they were assigned to the regulated side of the FirstEnergy business, with responsibility for Mon Power, FE's primary owner of regulated generation. The Commission's "undue advantage" evaluation must take into account its baseline understanding of the FERC "Code of Conduct" separating their responsibilities and actions from the competitive side of FE's business.

WVCAG's argument that Mr. Delmar and Mr. Szwed did not negotiate whether the Transaction would be a stock or asset deal (Petition at 13) is illusory. Because Mon Power would purchase only part of a single asset, designing the Transaction as a stock deal would have caused it to be re-characterized as an asset deal anyway. JA 717 (Wagner). WVCAG mischaracterizes the record in suggesting that a $411 million savings would have been available had a stock deal been completed (Petition at 13-14): there was no evidence that the Transaction could have successfully been set up this way.

WVCAG also argues the fact that the Harrison sale initially was a component of AE Supply's business plan, and that proceeds from the sale would help AE Supply pay down outstanding debt, "demonstrates conclusively (Petition at 41) that FirstEnergy enjoyed an "undue advantage over its wholly-owned subsidiaries," including Mon Power. WVCAG contends that paying down debt and shoring up AE Supply's "highly leveraged balance sheet" was the "one and only clear need" driving the Transaction making the Commission's finding of no undue advantage nothing but a "fatuous charade." (Petition at 42.)

These arguments completely ignore an entire body of evidence the Companies presented and no party effectively refuted. The Commission properly found that

- a significant capacity deficiency existed at Mon Power;
- the Companies prepared the 2012 Resource Plan to evaluate options to resolve it;
- that planning effort identified the Harrison acquisition as a reasonable, cost-effective solution;

- the capacity deficiency was serious and must be addressed through means other than continued market reliance that the capacity afforded by Harrison resolves the shortfall entirely;

- Harrison is an exceptionally high value capacity resource – with low operating costs;

- Mon Power already owned part of Harrison and achieved real benefits in protecting its ownership interest by converting the decision-making for the plant from AE Supply to Mon Power; and

- Harrison is located in the heart of Mon Power service territory providing ease for energy delivery to its customers and benefits to the local economy.

Despite all of this evidence, WVCAG still contends that Mon Power did not want Harrison for the right reasons, and that the presence of "undue influence" forced Mon Power to buy Harrison from AE Supply—something the Commission found no evidence at all to support. JA 945, 953 (Order at 34, 42 (Finding of Fact 32)). It is incorrect for WVCAG to contend (Petition at 42) that the evidence left "no doubt that FirstEnergy's financial requirements—not the purported electric generation needs of Mon Power – were the driving forces because this Transaction."

2. Affiliate Transactions Are Not *Per Se* Invalid.

Commission jurisdiction over affiliate transactions is intended to ensure that the utility and its customers are not being taken advantage of. The asymmetric pricing standards the Commission has applied are grounded in common sense: a competitive affiliate should not be able to sell an asset to a utility affiliate for more than it is worth, but a utility should be able to purchase that asset for what the competitive affiliate paid for it, as long as that payment does not exceed what the asset is worth on the market. The Commission has recognized that affiliate transactions offer value to customers in many cases, including asset location, combined operations, sharing of resources, the affiliate's greater purchasing power, and economies of scale.

WVCAG essentially contends that if a selling affiliate or its parent has anything to gain, a resulting affiliate transaction is unavoidably tainted by undue influence, and therefore cannot be approved. (Petition at 41-42.) Yet the entire purpose of § 24-2-12(f) is to enable the Commission to evaluate and approve transactions between affiliates, and nothing in the statute or the Commission's application of it over the years[12] suggests that a transaction's benefit to an affiliate or a parent is disqualifying, or per se evidence of an undue advantage exercised by the unregulated affiliate over the utility.

WVCAG is incorrect to argue that the case improperly focused on what Mon Power and its customers were getting out of the Transaction, and not what AE Supply would be paid for the asset (Petition at 42). The Commission's primary focus here, as in any regulatory proceeding, was to evaluate the regulated aspects of the transaction and protect the interests of West Virginia consumers. The Commission correctly based its decision on the evidence, not innuendo. Its finding that no undue advantage motivated or resulted from the Transaction should be upheld.

V. CONCLUSION

Of the thirteen parties to the Commission proceeding, only one ultimately opposed the Transaction's approval: WVCAG. Not only is WVCAG's requested relief effectively moot, but it erroneously objects to the Commission's authority and governance over public utilities and its findings on the Transaction's negotiation and fairness to customers. The Transaction as modified in the Joint Stipulation enjoyed broad support from customer interests, business, labor, and even

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12 The Commission reviews affiliate transactions quite routinely. In addition to the cases cited at note 11 above, see these recent orders approving affiliate agreements: Birch Communications of the Northeast, Inc., Case No. 13-0907-T-PC (Commission Order dated October 3, 2013)(financing transaction with affiliate approved); Hope Gas, Inc., Case No. 13-0937-G-PC (Commission Order dated September 9, 2013)(transfer of fluid truck to affiliate approved); Appalachian Power Co., Case No. 12-1006-E-PC (Commission Order dated December 17, 2012)(service agreement between utility and affiliated service corporation approved).

the Sierra Club because it was a fair, cost-effective solution to known capacity and energy deficiencies that threatened the Companies' customers. Providing adequate electric generation resources for West Virginia customers is a paramount responsibility for the Companies and the Commission. The Commission correctly and lawfully approved the Harrison acquisition and the Pleasants sale in the Order, and this Court should either dismiss the appeal or uphold the Commission's decision.

Respectfully submitted this 26th day of December, 2013.

MONONGAHELA POWER COMPANY

and THE POTOMAC EDISON COMPANY

By Counsel

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No. 13-1126

IN THE
SUPREME COURT OF APPEALS
OF WEST VIRGINIA

WEST VIRGINIA CITIZEN ACTION GROUP,
Petitioner,

v.

PUBLIC SERVICE COMMISSION OF WEST VIRGINIA, MONONGAHELA POWER COMPANY, and THE POTOMAC EDISON COMPANY,
Respondents.

(Nos. 12-1571-E-PC and 13-1272-E-PW, Public Service Commission of West Virginia)

CERTIFICATE OF SERVICE

I, Carte P. Goodwin, do hereby certify that I have served the foregoing RESPONSE OF MONONGAHELA POWER COMPANY AND THE POTOMAC EDISON COMPANY TO PETITION FOR APPEAL OF WEST VIRGINIA CITIZEN ACTION GROUP on December 26, 2013, upon the parties of record by U.S. Mail as follows:

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