**BEFORE**

**THE PUBLIC UTILITIES COMMISSION OF OHIO**

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| In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Authority to Establish a Standard Service Offer Pursuant to §4928.143, Ohio Rev. Code, in the Form of an Electric Security Plan.  | )))))) | Case No. 11-346-EL-SSOCase No. 11-348-EL-SSO  |
| In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of Certain Accounting Authority. | )))) | Case No. 11-349-EL-AAMCase No. 11-350-EL-AAM |

**MEMORANDUM CONTRA OHIO POWER COMPANY’S**

**APPLICATION FOR REHEARING**

**BY**

**THE OFFICE OF THE OHIO CONSUMERS’ COUNSEL**

**AND**

**THE APPALACHIAN PEACE AND JUSTICE NETWORK**

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**On Behalf of the Appalachian Peace and Justice Network**

**TABLE OF CONTENTS**

 **PAGE**

[I. INTRODUCTION 1](#_Toc335661273)

[II. ARGUMENT 4](#_Toc335661274)

[A. Base Generation Rates Should Be Reduced Consistent With The PUCO’s Findings In The Capacity Charge Case That AEP Ohio’s Capacity Cost
Is Not $355/MW-Day But $188/MW-Day. 4](#_Toc335661275)

[B. If An RSR Is To Be Adopted, Which Adoption Would Be Unlawful
And Unreasonable, Use Of A 9% ROE Value Is Not Unreasonable. 7](#_Toc335661276)

[C. Under R.C. 4928.144, More Than A Post-ESP Deferral Balance Verification Is Needed Of The Deferred Capacity Costs. 10](#_Toc335661277)

[D. The Commission’s Rulings Deferring Corporate Separation Issues, And Ordering That Customers Be Held Harmless For The Cost Of Bonds Or Generation Related Debt Retained By The Company Were Appropriate, Reasonable, And Lawful. 12](#_Toc335661278)

[E. The Company’s Proposal To Tweak The Commission’s More Favorable In The Aggregate Analysis Is Not Lawful, Reasonable, Or Of Consequence To The Ultimate Findings Of The Commission. 14](#_Toc335661279)

[F. The Commission Properly Reduced The Distribution Investment Rider
For Accumulated Deferred Income Taxes. 15](#_Toc335661280)

[G. Any Commission Clarification Should Limit The Carrying Costs That Customers Will Be Required To Pay. 17](#_Toc335661281)

[H. The Commission’s Threshold For The Significantly Excessive Earnings Test Is Reasonable And Lawful. 18](#_Toc335661282)

[I. The Commission Should Not Allow The Company To Collect The Cost Of The Competitive Bidding Process From Customers. If The Commission Does Not Require The Company To Absorb The Cost Of The Bidding Process, The Cost Should Be Collected From CRES Providers. 22](#_Toc335661283)

[J. The Commission Should Reject AEP Ohio’s Attempt To Make SSO Customers Pay For All Costs Associated With The Auction Process. 24](#_Toc335661284)

[K. The Commission Should Provide More Detail Regarding the 12% Cap
on Customer Rate Increases, But Should Avoid Creating More
Deferrals. 25](#_Toc335661285)

[III. CONCLUSION 28](#_Toc335661286)

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# I. INTRODUCTION

The Office of the Ohio Consumers’ Counsel (“OCC”), on behalf of the approximately 1.2 million residential utility customers of Ohio Power Company (the “Company” or “AEP Ohio”), and the Appalachian Peace and Justice Network (“APJN”), a not for profit organization whose members include low-income customers in southeast Ohio, submit this Memorandum Contra AEP Ohio’s Application for Rehearing[[1]](#footnote-1) in order to protect customers from paying higher rates that would result if the Company’s application for rehearing is granted. At issue in these proceedings are the rates customers will pay for retail electric service over the next three years as AEP Ohio transitions to a competitive auction of 100% of its load in 2015.

On August 8, 2012, the Public Utilities Commission of Ohio (“PUCO” or “Commission”) issued an Opinion and Order (“August 8 Order”) in these proceedings in which the Commission approved an electric security plan (“ESP”) for AEP Ohio. Through its August 8, Order the Commission approved rates which will impose significant rate increases on customers that will impede the Commission’s ability to ensure that reasonably priced electric retail service is made available to consumers, a policy of the State under R.C. 4928.02(A). The harms that residential customers will be subjected to because of the August 8 Order were detailed in the Application for Rehearing filed by OCC and APJN on September 7, 2012.

On September 7, 2012, several parties, including AEP Ohio, also filed an Application for Rehearing of the August 8 Order.[[2]](#footnote-2) The Company seeks rehearing on several issues. Regarding the energy auctions established in the Order, the Company asked the Commission to (1) freeze base generation rates during the entire ESP term, (2) allow the energy auction costs to be collected through the Fuel Adjustment Clause (“FAC”), (3) declare that the State Compensation Mechanism adopted in the Capacity Charge Case[[3]](#footnote-3) does not apply to auctions for non-shopping customers, including standard service offer (“SSO”) customers, (4) allow the Company to collect prudently incurred costs associated with the energy auctions, and (5) state that the auction rate impact docket will address only revenue-neutral solutions.

Concerning the Retail Stability Rider (“RSR”), AEP Ohio asked the Commission to (1) recalculate the target revenue using the 10.5% return on equity (“ROE”) the Company had recommended, (2) confirm that the determination of future collection of deferrals refers only to the post-ESP deferral balance verification process, (3) state that the August 8 Order complies with R.C. 4928.144 by providing for non-bypassable collection of deferrals over a three-year period after the ESP term, and (4) make competitive retail electric service (“CRES”) providers automatically responsible for the entire $189/MW-day capacity charge should either the establishment of the deferral or the deferral collection mechanism be reversed or vacated on appeal.

The Company also asserted that the Commission erred by not explicitly providing for a final reconciliation of the FAC, the gridSMART Rider and the Distribution Investment Rider (“DIR”), and by adjusting the DIR for accumulated deferred income taxes (“ADIT”). In addition, the Company asked for clarification of the storm damage rider, and for clarification regarding the disposition of Pollution Control Bonds given that the Commission has not approved corporate separation. Further, the Company claimed it was unreasonable and unlawful for the Commission to impose the Significantly Excessive Earnings Test (“SEET”) threshold and to impose the 12% rate cap without further clarification, and asserted that the Commission underestimated the relative benefits of the ESP in comparing it to the results expected under a market rate offer (“MRO”). As a final matter, AEP Ohio asked the Commission to consolidate this proceeding with the Capacity Charge Case for rehearing purposes.

In this Memorandum Contra, OCC and APJN refute many of the arguments put forth by AEP Ohio.[[4]](#footnote-4) The Commission should deny AEP Ohio’s application for rehearing on the issues discussed herein and deny, at this late date, consolidation of this case with the Capacity Charge Case.

# II. ARGUMENT

## A. Base Generation Rates Should Be Reduced Consistent With The PUCO’s Findings In The Capacity Charge Case That AEP Ohio’s Capacity Cost Is Not $355/MW-Day But $188/MW-Day.

In its Application for rehearing, the Company urges the PUCO to order that base generation rates will remain frozen throughout the entire ESP period. [[5]](#footnote-5) The Company also asks for clarification that the State compensation mechanism adopted in its Capacity Case does not apply to SSO auctions or non-shopping customers in general.[[6]](#footnote-6) Although the Company itself originally had proposed to reduce base generation rates from the current level to the level equal to $255/MW-day for capacity at the 100% auction in January through May 2015, it now believes it would be “unreasonable” to retain this feature.[[7]](#footnote-7) The Company maintains that the RSR was modified and the auctions were accelerated and expanded and alleges “there could be adverse financial impacts on AEP Ohio associated with the early auction modifications.”[[8]](#footnote-8)

The Company’s application for rehearing should be denied. As explained in OCC/APJN’s Application for Rehearing,[[9]](#footnote-9) the Commission’s Order failing to reduce base generation rates for SSO customers is unlawful and unreasonable for numerous reasons. It violates R.C. 4928.02(A), (B), and R.C. 4928.141, all which require the Company to provide “comparable” and “non-discriminatory” retail electric rates. It violates R.C. 4905.33, 4905.35, and 4928.02(H). These provisions preclude discriminatory pricing and subsidies.

While OCC/APJN agrees that the SCM cannot be construed to force SSO customers to pick up the cost of capacity provided to CRES suppliers,[[10]](#footnote-10) the Commission’s underlying finding that the Company’s cost of capacity is $188.88 is a finding that cannot be ignored in the context of the ESP, given the requirements of the law that prohibits discriminatory pricing. Capacity is capacity. The capacity provided to CRES providers is the very same capacity provided to SSO customers.

While the SCM does not mandate what SSO customers must pay for retail capacity, it would be unreasonable and unlawful to ignore the PUCO’s finding regarding the cost of providing capacity and not apply that finding to SSO service. According to AEP, “a rate that is based on cost is inherently reasonable.”[[11]](#footnote-11) Cost based generation service is also appropriate for SSO service because it is the only way to fulfill the mandates of the law, given the Commission’s holding in the Capacity Charge Case. The law requires that the utility “shall provide consumers on a *comparable and non-discriminatory basis* within its certified territory a standard service offer of all competitive retail electric services necessary to maintain essential electric service to consumers.”[[12]](#footnote-12) Charging CRES providers RPM based capacity and SSO customers AEP’s fully embedded cost of capacity ($355/MW-day) is not comparable and non-discriminatory pricing of capacity. And capacity is part of the competitive retail electric services necessary to maintain essential electric service to consumers.

Moreover, the fact of the matter is, in the Company’s application it recognized the importance of matching the discounted capacity provided to CRES providers to the capacity provided to SSO customers. This was part of *its* proposal for the 100% energy auction in January through May 2015, whereby it would reduce base generation rates from the current level to the level equal to $255/MW-day. But now the Company attempts to walk away from its proposal because the RSR was modified, auctions were accelerated and expanded, and “there could be adverse financial impacts on AEP Ohio associated with the early auction modifications.”[[13]](#footnote-13) None of these factors can overcome the fact that under the law consumers are entitled to SSO service that is based upon all elements of service being comparable and non-discriminatory. This means that the same capacity provided by the Company – either to CRES providers or SSO customers- must be comparably priced. Without adjusting the base generation rates of SSO customers, the Commission cannot assure that the law is being met. AEP’s rehearing application should be rejected.

## B. If An RSR Is To Be Adopted, Which Adoption Would Be Unlawful And Unreasonable, Use Of A 9% ROE Value Is Not Unreasonable.

The Company alleges that use of a 9% ROE value in calculating the revenue target for the RSR is unreasonable. It relies in part on fact that parties to the Company’s recent distribution cases stipulated to higher returns for Ohio Power and CSP, with returns on equity of 10.0% and 10.3%, respectively. These returns were approved by the Commission when it adopted the Stipulation and Recommendation in the distribution case.[[14]](#footnote-14) Such returns “demonstrate that a 9 percent ROE for combined companies is too low.”[[15]](#footnote-15) And because the distribution operations of AEP face risks lower than those faced by the generation service business, “it is beyond contradiction that the appropriate ROE for the combined operations \*\*\*is higher than the 10.0/10.3 percent values approved for the pre-merger companies in the distribution rate cases.” The Company also relies upon the Commission’s decision in the Capacity Charge Case where it found the “appropriate ROE to use in establishing those prices is 11.15%.”[[16]](#footnote-16)

AEP’s rehearing on this matter should be rejected. First, the Company’s reliance on the Commission decision in the Capacity Charge case is inconsistent with its assertions that the state compensation mechanism adopted in the Capacity Charge Case does not apply to SSO service or the capacity auctions. It was only through determining the state compensation mechanism that the ROE was derived. So if the SCM does not apply to SSO generation rates, the ROE derived through setting the SCM should also not be applied in the context of setting RSR rates paid by SSO customers.

Second, AEP improperly relies on returns on equity that were stipulated in AEP’s recent distribution case, Case No. 11-351-EL-AIR. The Stipulation that AEP cites as precedent for establishing a return higher than 9% contained the following provision:

Except for Enforcement purposes or to establish that the terms of the Stipulation are lawful*, neither this Stipulation nor the information and data contained herein or attached hereto shall be cited as a precedent in any future proceeding for or against any Signatory Party, or the Commission itself, if the Commission approves the Stipulation*. Nor shall the acceptance of any provision within this settlement agreement be cited by any party or the Commission in any forums so as to imply or state that any signatory party agrees with any specific provision of the settlement. More specifically, no specific element or item contained in or supporting this Stipulation shall be construed or applied to attribute the results set forth in this Stipulation as the results that any Signatory Party might support or seek, but for this Stipulation in these proceedings or in any other proceeding. This Stipulation contains a combination of outcomes that reflects an overall compromise involving a balance of competing positions, and it does not necessarily reflect the position that one or more of the Signatory Parties would have taken on any individual issue. [[17]](#footnote-17)

The “information or data” that was contained in the Stipulation included the 10.0 and 10.3 percent returns on equity. The Company however directly uses these returns as precedent against the stipulating parties and the Commission. Specifically, the Company uses the stipulated returns and the PUCO’s approval of those returns to attack the 9% return adopted here. It declares that “the understatement of the ROE value is demonstrated by the fact that just 8 months ago, in AEP Ohio’s distribution rate case, *the parties stipulated, and the Commission approved* ROEs for the distribution service business of OPCO and Columbus Southern Power Company (CSP) of 10.0 and 10.3 percent. Case Nos. 11-351 and 11-352-EL-AIR, Opinion and Order at 5 (December 14, 2011). Those very *recently approved ROEs* for the two companies (which subsequently merged) demonstrate that a 9 percent ROE for combined companies is too low.” [[18]](#footnote-18)

This was an improper use of the distribution case stipulation. It directly violates the plain language of the Stipulation Agreement that was signed by OCC, APJN, the Company, the PUCO Staff, and numerous other intervenors. The Company ignores one very essential term of that stipulation, and indeed all stipulations – the stipulation cannot be used as precedent.

Use of a singular provision of the Stipulation is also contrary to the inherent nature of a Stipulation. A stipulation, such as the AEP Distribution Stipulation, represents a resolution of a number of issues in a proceeding or multiple proceedings. A Stipulation is a package composed of many different provisions—provisions which may not be acceptable on a stand-alone basis, but when put together with other terms constitute an acceptable compromise. Indeed as the Distribution Stipulation stated “[t]his Stipulation contains a combination of outcomes that reflects an overall compromise involving a balance of competing positions, and it does not necessarily reflect the position that one or more of the Signatory Parties would have taken on any individual issue.” [[19]](#footnote-19) It simply does not represent the position that parties would have taken outside the context of a package agreement. To extricate distinct provisions of a Stipulation and attempt to apply those under a different set of facts, in a different case, perverts the whole stipulation process.

 Sound regulation should not discourage dispute-resolution through settlements. Litigation can be expensive and without settlements dollars may have to be diverted to pay for the time of lawyers, consultants, and staffs. These expenditures often eventually flow through to the electric bills and tax bills of Ohio citizens. Settlement may also bring about regulatory certainty that may otherwise be delayed until the termination of all litigation. Thus, because there is the potential for cost savings and regulatory certainty, the PUCO should not discourage settlements.36

If parties to a settlement are not assured that the terms of the settlement agreed to and eventually approved by the PUCO, will be held inviolate, parties will not be inclined to sign onto settlements. The Company has once again overstepped the dictates of another stipulation, just as it did in its filed comments in its corporate stipulation proceeding[[20]](#footnote-20) — and on that basis the Commission struck portions of the Company’s reply comments.[[21]](#footnote-21) The Commission should do the same here. The Company’s arguments relying upon the Stipulation are inappropriate and should be stricken and not relied upon by the Commission to determine whether rehearing should be granted on this matter.

## C. Under R.C. 4928.144, More Than A Post-ESP Deferral Balance Verification Is Needed Of The Deferred Capacity Costs.

In the Company’s Capacity Charge case the Commission determined that $188.88/MW-day is the appropriate charge to enable the Company to collect its capacity costs under its FRR obligations from CRES providers.[[22]](#footnote-22) The Commission also determined that the Company should charge CRES providers RPM based capacity rates in order to promote retail competition.[[23]](#footnote-23) The Commission then unreasonably and unlawfully authorized the Company to defer the difference between Ohio Power’s cost and the RPM capacity rates charged to CRES providers.[[24]](#footnote-24)

Ultimately in this case, the Commission unreasonably and unlawfully found that the deferrals could be collected from retail customers-shoppers and non-shoppers. It authorized the collection of the deferrals beginning in 2015, for three years, with carrying costs. It concluded that “[a]ll determinations for future recovery of the deferral shall be made following AEP-Ohio’s filing of its actual shopping statistics.”[[25]](#footnote-25) The Company in its application for rehearing seeks clarification from the PUCO that its statement refers only to a post-ESP deferral balance verification process. Its rehearing should be denied because otherwise the PUCO will not be complying with the mandates of R.C. 4928.144.

While the Commission has certain authority under R.C. 4928.144 to approve any “just and reasonable phase in” of any EDU rate or price established under R.C. 4928.141 to 4928.143 of the Revised Code, it must make a finding that the phase in is “necessary” to ensure rate or price stability for customers. This statutory language is consistent with the Commission’s Order which provides, at the conclusion of the modified ESP term, it will determine the deferral amount “and make appropriate adjustments based on AEP-Ohio’s actual shopping statistic and the amount that has been collected towards the deferral through the RSR, *as necessary*.”[[26]](#footnote-26) Thus recovery of the deferrals is to occur “as necessary” indicating that the Commission will conduct additional analysis (beyond deferral balance verification) to determine the appropriate recovery of capacity deferrals and carrying costs. Such an approach is consistent with the Commission’s approach to the phase in recovery rider approved for the Company.[[27]](#footnote-27) And it is consistent with the words of R.C. 4928.144. Rehearing should be denied.

## D. The Commission’s Rulings Deferring Corporate Separation Issues, And Ordering That Customers Be Held Harmless For The Cost Of Bonds Or Generation Related Debt Retained By The Company Were Appropriate, Reasonable, And Lawful.

In the Opinion and Order the Commission appropriately determined that because AEP did not request consolidation of the pending corporate separation plan in its modified ESP application, the Commission would consider corporate separation in a separate docket.[[28]](#footnote-28) The PUCO also determined that AEP could retain the pollution control bonds contingent upon a finding that the Company’s customers are held harmless for the cost of the bonds and any other generation related debt retained by AEP Ohio. AEP was also ordered to file information with the PUCO to demonstrate that customers have not and will not incur “any costs” associated with the cost of servicing the associated debt.

The Company however, seeks rehearing and argues the PUCO should approve structural legal separation and rule on AEP Ohio’s corporate separation plan and related asset transfers in the corporate separation proceeding “forthwith.” Additionally, the Company seeks rehearing on the PUCO’s decision on the pollution control revenue bonds (PCRBs). The Company claims that the Commission’s conclusion was “not in the record and, thus, never addressed by parties.” Further the Company alleges that the Commission should have ruled that the Company must demonstrate that customers have not and will not incur any “additional” costs caused by corporate separation and that the hold harmless obligation also pertains to “additional” costs caused by corporate separation.

The Company’s application for rehearing on this matter should be rejected. As the Commission correctly noted, there were very limited issues pertaining to corporate separation that were properly part of the ESP proceeding. Those issues included whether the termination of the pool agreement and corporate separation facilitates the Company’s transition to a competitive market, and the rate impact of the generation asset divestiture on the Company’s SSO customers for the term of the modified ESP.[[29]](#footnote-29)

The litany of other corporate separation issues are appropriately considered in the corporate separation proceeding. There parties must, under R.C. 4928.17(B), be afforded a full and fair opportunity to object to the plan, and must be afforded a hearing on those aspects of the plan that the PUCO determines require a hearing. It is also that docket where the Commission must, before approving corporate separation, determine that the Company’s corporate separation plan complies with the law, R.C. 4928.17. Under that provision of the Code, the Company’s plans for corporate separation must 1) include measures as are necessary to effectuate the policy specified in R.C. 4928.02 of the Revised Code 2) satisfy the public interest in preventing unfair competitive advantage; 3) ensure that the utility will not extend any undue preference or advantage to any affiliate; 4) contain provisions to ensure ongoing compliance with the policies of R.C. 4928.02.

Any suggestion that the Commission bypass these statutory findings and approve the corporate separation plan “forthwith” is a circumvention of the statute, and the Commission has no jurisdiction to do so.

The Commission’s determination that customers should be held harmless as it relates to the Company retaining the PCRBs was proper, though it certainly would have been an issue worthy of consideration in the corporate separation proceeding. Customers should be held harmless. It is not in the public interest to push any costs of the PCRBs onto customers, let alone “additional” costs. Pushing costs of the PCRBS onto customer is inconsistent with the provisions of R.C. 4928.17, because it 1) is inconsistent with the policies of R.C. 4928.02(A), (H), and (L); it creates an unfair competitive advantage to AEP’s affiliate; and it extends an undue preference to AEP’s affiliate. The Commission correctly acted to protect consumers and it should stand by its holding in this respect and accordingly reject the Company’s application for rehearing.

## E. The Company’s Proposal To Tweak The Commission’s More Favorable In The Aggregate Analysis Is Not Lawful, Reasonable, Or Of Consequence To The Ultimate Findings Of The Commission.

The Company in its rehearing application argues that the Commission’s finding that the MRO yielded a $386 million quantifiable advantage over the ESP is “substantially overstated.”[[30]](#footnote-30) The Company alleges the overstatement is attributable to two errors. First, the Company notes that the Commission only evaluated a 24 month period from June 2013 through May 2015 in its MRO/ESP comparison and yet included the cost of the RSR over the entire three year term of the modified ESP. Second, the Company alleges that the $508 million value for the RSR is based on 36 months of collection while the RSR will only be recovered over a 33 month period. In the end, the Company concludes that there is at least a $30 million overstatement of the net quantifiable benefits of the alternative MRO.[[31]](#footnote-31)

As explained in OCC/APJN Application for Rehearing, the Commission erred in unreasonably and unlawfully comparing prices that excluded the first ten months of the Company’s ESP term.[[32]](#footnote-32) That is in evaluating only 24 months of the ESP period in the price comparison, the PUCO failed to comply with R.C. 4928.143(C)(1). Any suggestion that the RSR effect should only be considered during that 24 month period, would only add to the error in the Commission’s analysis. Rehearing should be denied.

Assuming arguendo the Company is correct about the $508 million value for the RSR being based on 36 months of collection, the issue of a $30 million discrepancy does not alter the fundamental conclusion that the quantifiable benefits of the MRO far outweigh the quantifiable and non-quantifiable benefits of the ESP.[[33]](#footnote-33) The Commission should reject this assignment of error.

## F. The Commission Properly Reduced The Distribution Investment Rider For Accumulated Deferred Income Taxes.

In the Order, the Commission correctly concluded that it was “not appropriate to establish a DIR mechanism in a manner which provides the Company with the benefit of ratepayer supplied funds.”[[34]](#footnote-34) The Commission then ordered the Company to reduce the DIR to reflect an offset for accumulated deferred income taxes (“ADIT”). In its rehearing AEP-Ohio argues that DIR should not be reduced for ADIT because the revenue credit to customers in the distribution case (Case No. 11-351-EL-AIR)[[35]](#footnote-35) was based on the Company collecting *full* DIR revenues (with no ADIT offset) in the amount of $86 million in 2012. Had the revenue credit to customers in the distribution case reflected a ADIT offset, customers would have received a smaller revenue credit of approximately $21 million.

AEP-Ohio’s argument is flawed because the distribution rate case was resolved by a Stipulation that AEP-Ohio agreed to. That Stipulation does not include any provision that allows the Company to adjust the revenue credit to customers based on any future action by the PUCO pertaining to the approval of the DIR.

AEP-Ohio notes that Kroger witness Higgins admitted during cross-examination that the DIR was an issue for consideration in the distribution rate case.[[36]](#footnote-36) To the extent that AEP-Ohio is arguing that the DIR was an issue for the distribution rate case, then the language from the Distribution Rate Case Stipulation and PUCO Order approving the Stipulation should govern. To that end, the Distribution Rate Case Stipulation states:

Therefore, to the extent the Commission materially modifies the DIR in the ESP II to the detriment of AEP Ohio then AEP Ohio has the right to withdraw from this agreement and litigate the issue as if the settlement in these cases had not been reached. AEP Ohio must exercise this right no later than thirty (30) days of the final non-appealable order in the ESP II proceeding.[[37]](#footnote-37)

 The Joint Stipulation and Recommendation in the distribution rate case explicitly and in detail addresses DIR revenues and the manner in which the revenue credit would be distributed.[[38]](#footnote-38) Furthermore in this Opinion and Order, the Commission repeated much of the same DIR discussion and noted that the Stipulation was “ \*\*\* intended to resolve all of the issues raised in these proceedings \*\*\* ”.[[39]](#footnote-39) Finally, as noted in the Distribution rate case Stipulation, the Stipulation reflected an overall compromise and did not reflect the position that any Signatory Party would necessarily take on a position if litigated.[[40]](#footnote-40)

In addition, to the extent that AEP-Ohio was the party responsible for drafting the distribution rate case Stipulation, Ohio case law clearly holds that any ambiguities in the document, must be construed against the drafting party, “[M]oreover, to the extent we encounter an ambiguity in the contract, that ambiguity must be construed against the drafting party.”[[41]](#footnote-41) Thus to the extent that the distribution rate case Stipulation did not provide for the clarification that AEP-Ohio is seeking now, that ambiguity or failure falls on the Company and the PUCO should deny rehearing.

## G. Any Commission Clarification Should Limit The Carrying Costs That Customers Will Be Required To Pay.

OCC and APJN oppose the AEP-Ohio requested clarification because it could result in customers having to pay additional carrying costs and thus further burden customers with higher costs as a result of the Modified ESP. The Clarification requested by AEP-Ohio concerning the storm cost recovery mechanism would establish a cutoff date of September 30 of the year in which AEP-Ohio incurs costs due to one or more unexpected large scale storms. As a result of a September 30 cut off, any costs that are incurred between October 1st and December 31st of that same year would not be recovered until the following year, thus adding the expense of additional carrying cost that customers would have to pay.

Under the Commission’s Order, deferrals are reconciled in the same year that they occur, thus reducing the need for and the amount of carrying costs. AEP-Ohio’s proposed clarification to the Order results in customers paying at least an additional quarter of carry charges. For example, the Company would not seek storm cost recovery for a major event that occurred on October 1st until December 31st of the following year. As an alternative, OCC and APJN suggest that if a clarification to the Order is needed, the Commission could enable the Company to amend the December 31st filing within 30 days of the filing to include any storm costs from the month of December that were not included in the original filing.

## H. The Commission’s Threshold For The Significantly Excessive Earnings Test Is Reasonable And Lawful.

Because of the revenue target established through the RSR, the Commission determined that it should also establish a SEET threshold “to ensure that the Company does not reap disproportionate benefits from the ESP.”[[42]](#footnote-42) The Commission found that, based on the evidence in the record, a 12% ROE “would be at the high end of a reasonable range for return on equity” for SEET purposes.[[43]](#footnote-43)

AEP Ohio asserts that the SEET threshold established in the August 8 Order is unlawful. The Company claims that the Commission did not follow the statute, R.C. 4928.143(F), in deriving the threshold. In this regard, the Company argues that the threshold is neither a calculation nor an estimate of the return on common equity actually earned by companies that face business and financial risk comparable to AEP Ohio’s,[[44]](#footnote-44) and that the Commission did not consider the capital requirements of AEP Ohio’s future committed investments in Ohio.[[45]](#footnote-45) In addition, AEP Ohio contends that the threshold is not significantly in excess of the ROE earned by firms having a comparable risk, and is thus too low.[[46]](#footnote-46) The Company is wrong, however.

First, the Commission followed the statute in establishing the SEET. The statutory basis for the SEET is found in R.C. 4928.143(F), which states in pertinent part:

With regard to the provisions that are included in an electric security plan under this section, the commission shall consider, following the end of each annual period of the plan, if any such adjustments resulted in excessive earnings as measured by whether the earned return on common equity of the electric distribution utility is significantly in excess of the return on common equity that was earned during the same period by publicly traded companies, including utilities, that face comparable business and financial risk, with such adjustments for capital structure as may be appropriate. Consideration also shall be given to the capital requirements of future committed investments in this state. The burden of proof for demonstrating that significantly excessive earnings did not occur shall be on the electric distribution utility.

The SEET threshold, however, is nothing more than a rebuttable presumption that an EDU’s earnings above the ROE would be significantly excessive.

The Commission established the SEET threshold for AEP Ohio’s second ESP at 12%. Using the Commission’s SEET analysis guidelines, the Commission apparently determined the mean of the comparable group would be a 10% ROE, given that the SEET threshold is the mean of the comparable group plus 200 basis points.[[47]](#footnote-47) Based on the testimony the Commission cited for support in establishing the threshold, the Commission might actually give AEP Ohio a higher SEET threshold than the record indicates.

The Commission cited to five specific exhibits to support the SEET threshold for AEP Ohio: OEG Ex. 101 (Kollen); Kroger 101 (Higgins); Ormet Ex. 107 (Wilson); Wal-Mart Ex. 101 (Chriss); and FES Ex. 102 (Lesser). Although none actually makes the statutory analysis required under R.C. 4928.143(F), they do offer a reasonable basis for the Commission’s conclusion. In fact, they show that the Commission may have given the Company too much leeway under SEET.

In his testimony Mr. Kollen described a reasonable ROE range for his proposed equity stabilization plan. The range he used was 7% to 11%, with the Company allowed to collect any deficiency up to a 7% ROE and refund to customers any ROE above 11%.[[48]](#footnote-48) Mr. Kollen apparently does not represent his range as the mean of the comparable group,[[49]](#footnote-49) but instead is a “zone of reasonableness.”[[50]](#footnote-50) This zone consists of an “earnings benchmark at 9.0%, with a bandwidth set at 200 basis points above and below the benchmark.”[[51]](#footnote-51) Thus, the Commission’s 12% benchmark is one percent higher than what Mr. Kollen would consider reasonable.

Similar to Mr. Kollen, Ormet witness Wilson suggested that a maximum 9% ROE would be reasonable,[[52]](#footnote-52) and thus the threshold established by the Commission would be higher than would be allowed under the SEET guidelines. Wal-Mart witness Chriss recommended no higher than a 10.2% ROE,[[53]](#footnote-53) and FES witness Lesser did not recommend an ROE, but merely recognized that AEP Ohio accepted an ROE of 10.2% for its distribution companies.[[54]](#footnote-54) A 10.2% ROE, although not derived strictly from a SEET analysis, would support the Commission’s threshold.

Kroger witness Higgins provided what may be the closest proxy for a SEET analysis. He noted that Regulatory Research Associates listed the average ROE awarded to electric utilities in the United States as 10.22%.[[55]](#footnote-55) Thus, if this average can be considered as “the mean of the comparable group,” then the Commission’s 12% SEET threshold would be reasonable.

Second, the results of other cases involving the SEET have no bearing in this case. The Company argues that because the Commission used a 60% adder in the Company’s first SEET proceeding, it should do so again here.[[56]](#footnote-56) The Commission, however, has twice rejected AEP Ohio’s recommendation that a bright line test should be used to determine significantly excessive earnings.[[57]](#footnote-57) The Commission has chosen to analyze EDUs’ earnings on a case-by-case basis, and reasonably followed its precedent here.

The Company also tries to compare the SEET threshold established in this proceeding with threshold approved in the Duke Energy Ohio (“Duke”) ESP proceedings, in which a 15% ROE was approved for Duke.[[58]](#footnote-58) The SEET threshold in the Duke case, however, was developed through a stipulation among parties to the proceeding.[[59]](#footnote-59) Thus, those cases had an entirely different dynamic than this proceeding. And, as the stipulations in those cases stated, the stipulations and the orders approving them are not to be used as precedent in any other proceeding.[[60]](#footnote-60) It is thus inappropriate for the Company to use the terms of those stipulations as precedent in this proceeding, and the Commission should strike the portion of AEP Ohio’s application for rehearing discussing the Duke stipulations.

AEP Ohio’s arguments against the SEET threshold established in the August 8 Order are not persuasive. The Commission should deny the Company’s rehearing application on this issue.

## I. The Commission Should Not Allow The Company To Collect The Cost Of The Competitive Bidding Process From Customers. If The Commission Does Not Require The Company To Absorb The Cost Of The Bidding Process, The Cost Should Be Collected From CRES Providers.

AEP Ohio’s modified application in this proceeding called for an energy-only, slice of system auction based on 5% of the SSO load before January 2015, with a transition to an auction for 100% of the SSO load in January 2015.[[61]](#footnote-61) In the August 8 Order, the Commission determined that the 5% load was too low and directed AEP Ohio to increase the auction amount to 10% of the SSO load.[[62]](#footnote-62) The Commission also found that the Company is capable of conducting an energy auction for delivery on January 1, 2014, and directed the Company to auction 60% of its energy load for delivery on January 1, 2014, with the remainder to be auctioned for delivery on January 1, 2015.[[63]](#footnote-63) Further, in order “to maximize the number of participants in AEP-Ohio’s auctions through an open and transparent auction process,”[[64]](#footnote-64) the Commission directed the Company to establish a competitive bidding process that includes “guidelines to ensure an independent third party is selected to ensure there is an open and transparent solicitation process, a standard bid evaluation, and clear product definitions.”[[65]](#footnote-65)

In its application for rehearing, the Company argued that it was unreasonable for the Commission to modify the competitive bidding process without specifically allowing for collection of the Company’s costs associated with establishing the competitive bidding process.[[66]](#footnote-66) The Company asked the Commission to explicitly provide for collection of the costs. The Commission should deny the Company’s request.

The competitive bidding process was part of AEP Ohio’s modified application in this proceeding. Any costs associated with conducting the auction should have been accounted for in the modified application. The Company has not shown that the modified auction process would increase its costs over those incurred through its original auction proposal. Thus, the Commission need not make any special dispensation for collection of costs associated with the modified auction.

If, however, the Commission grants the Company’s request, it should specify that the costs associated with the auction are to be borne by CRES providers, and by not the Company’s customers. The costs associated with the auction process are caused by the need to accommodate CRES providers who participate in the auction. Thus, cost causation principles demand that the costs be borne by CRES providers.

## J. The Commission Should Reject AEP Ohio’s Attempt To Make SSO Customers Pay For All Costs Associated With The Auction Process.

In the August 8 Order, the Commission approved the Company’s proposal to freeze base generation rates until all rates are established through a competitive bidding process.[[67]](#footnote-67) The Commission also addressed the possibility of disproportionate rate impacts on customers when all rates are set by auction:

[A]s AEP-Ohio raised the possibility of disproportionate rate impacts on customers when class rates are set by auction, we direct the attorney examiners to establish a new docket within 90 days from the date of this opinion and order and issue an entry establishing a procedural schedule to allow Staff and any interested party to consider means to mitigate any potential adverse rate impacts for customers upon rates being set by auction. Further, the Commission reserves the right to implement a new base generation rate design on a revenue neutral basis for all customer classes at any time during the term of the modified ESP.[[68]](#footnote-68)

In its rehearing application, AEP Ohio asked the Commission to specify that “any remedy or solution to be considered in the rate mitigation docket will be implemented on a revenue neutral basis.”[[69]](#footnote-69) The Company bases this request on speculation that the docket will not only address broad tariff issues, but also narrow rate mitigation (e.g., for electric heating customers) that may arise from the auctions.[[70]](#footnote-70) AEP Ohio claims that “[i]t is important for the Company to understand that the Commission is fully committed to flowing the full cost of energy auctions through to SSO customers.”[[71]](#footnote-71) The Commission should reject the Company’s request.

The Commission cannot at this time anticipate all the issues that may arise regarding disparate rate impact on customers because of the auctions. The Commission should not box itself into implementing solutions that make the Company whole without knowing whether such solutions are appropriate in all cases. The Commission should deny AEP Ohio’s application for rehearing on this issue.

## K. The Commission Should Provide More Detail Regarding the 12% Cap on Customer Rate Increases, But Should Avoid Creating More Deferrals.

In order to ease the burden of unexpected rate impacts on customers, the Commission directed AEP Ohio to “cap customer rate increases at 12% over their current ESP I rate plan billschedules for the entire term of the ESP….”[[72]](#footnote-72) The Commission cited its authority under R.C. 4928.144,[[73]](#footnote-73) which allows the Commission to “authorize any just and reasonable phase-in of any electric distribution utility rate or price established under sections 4928.141 to 4928.143 of the Revised Code, and inclusive of carrying charges, as the commission considers necessary to ensure rate or price stability for consumers.” Under the Order, the 12% limit will be determined on an individual customer-by-customer basis, and applies to items approved within the modified ESP.[[74]](#footnote-74) Rate changes that “arise as a result of past proceedings, including any distribution proceedings, or in subsequent proceedings are not factored into the 12% cap.”[[75]](#footnote-75) The cap “shall be normalized for equivalent usage to ensure that at no point any individual customer’s bill impacts shall exceed 12%.”[[76]](#footnote-76)

AEP Ohio seeks rehearing of two aspects of the cap. First, the Company asks for 90 days after the rehearing decision to make the billing changes necessary to track rate impacts on customers’ bills in order to properly implement the cap.[[77]](#footnote-77) AEP Ohio states that calculations would still date back to September 2012 and the Company would provide any applicable credits related to the cap.[[78]](#footnote-78) The Company also asks the Commission to clarify that costs associated with the billing system upgrade be deferred as a regulatory asset for future collection.[[79]](#footnote-79)

OCC and APJN have no objection to the Company having a reasonable time to upgrade its billing system (if that is what is needed). As we pointed out in our Application for Rehearing, the August 8 Order was vague as to how the cap would be enforced.[[80]](#footnote-80) Giving the Company some time to ensure compliance with the cap would be fair.

OCC and APJN, however, object to collecting costs from customers for a new or updated AEP billing system. And OCC and APJN object to the creation of a deferral for the costs associated with the billing system upgrade. The cap that gives rise to the need for a billing system upgrade is only needed because the new authorized rates are too high. The result is that customers will pay for the protection of a cap with even more of their money, because the deferrals are a “pay me now or pay me later” situation and the billing system changes will add more costs in addition to the deferral costs. The real remedy for consumers is to limit rate increases.

The creation of yet another deferral would merely add to the costs consumers will pay for service. In addition, the Company has not shown that the upgrade associated with the cap cannot be done as part of the Company’s regular billing system maintenance or upgrading. The Commission stated that is “generally opposed to the creation of deferrals….”[[81]](#footnote-81) This is one deferral the Commission should reject. At a minimum, the PUCO should allow investigation into the billing system upgrades that AEP Ohio claims will cost customers money.

Second, the Company asserts that it was unreasonable and unlawful for the Commission to impose the rate cap without authorizing a non-bypassable collection of any deferrals created by the cap, plus carrying charges, and without setting a period for collection. The Company contends that R.C. 4928.144 makes clear that deferrals “are not subject to jeopardy of non-recovery when the bill comes due under the phase-in plan” and that the deferrals are “money in the bank.”[[82]](#footnote-82)

R.C. 4928.144 states, in pertinent part:

If the commission’s order includes such a phase-in, the order also shall provide for the creation of regulatory assets pursuant to generally accepted accounting principles, by authorizing the deferral of incurred costs equal to the amount not collected, plus carrying charges on that amount. Further, the order shall authorize the collection of those deferrals through a nonbypassable surcharge on any such rate or price so established for the electric distribution utility by the commission.

The statute does not contain the phrase “money in the bank.” Thus, the need for the separate proceeding the Commission ordered “to consider, among other things, the deferral costs created” by the cap.[[83]](#footnote-83)

As OCC and APJN pointed out in our Application for Rehearing, the August 8 Order was vague in many respects regarding the cap and the deferrals.[[84]](#footnote-84) If the Commission allows these deferrals, it must clarify the process for adjusting the deferrals at the end of the ESP. OCC and APJN urge the Commission to use the Company’s cost of long-term debt in calculating the deferrals.

# III. CONCLUSION

As discussed herein, AEP Ohio’s arguments against the August 8 Order are baseless. The Commission should deny the Company’s request for rehearing on the issues addressed above. But to protect consumers, the Commission should grant the Application for Rehearing filed by OCC and APJN.

Respectfully submitted,

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**On Behalf of the Appalachian Peace and Justice Network**

**CERTIFICATE OF SERVICE**

 I hereby certify that a copy of the *Memorandum Contra Ohio Power Company’s Application for Rehearing* was served on the persons stated below via electronic transmission, this 17th day of September, 2012.

 */s/ Maureen R. Grady*\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_

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1. Pursuant to Ohio Adm. Code 4901-1-35(B). [↑](#footnote-ref-1)
2. Separate applications for rehearing of the Order also were filed by The Kroger Co., Industrial Energy Users-Ohio and Ohio Energy Group. Buckeye Association of School Administrators, Ohio Association of School Business Officials, Ohio School Boards Association and Ohio Schools Council filed a joint application for rehearing. [↑](#footnote-ref-2)
3. *In the Matter of the Commission Review of the Capacity Charges of Ohio Power Company and Columbus Southern Power Company*, Case No. 10-2929-EL-UNC. [↑](#footnote-ref-3)
4. If OCC and APJN do not address an issue AEP Ohio raised in its application for rehearing, OCC and APJN do not necessarily acquiesce to that issue. [↑](#footnote-ref-4)
5. Application for Rehearing at 7. [↑](#footnote-ref-5)
6. Id. [↑](#footnote-ref-6)
7. Id. at 11. [↑](#footnote-ref-7)
8. Id. at 12. [↑](#footnote-ref-8)
9. Assignment of Error 2, OCC/APJN Application for Rehearing at 21-36. [↑](#footnote-ref-9)
10. See Assignment of Error 7(C), OCC/APJN Application for Rehearing at 68-70. [↑](#footnote-ref-10)
11. See AEP Initial Brief Capacity Charge Case at 9 (May 9, 2012). [↑](#footnote-ref-11)
12. See R.C. 4928.141(A). [↑](#footnote-ref-12)
13. Id. at 12. [↑](#footnote-ref-13)
14. *In the Matter of the Application of Columbus Southern Power company and Ohio Power Company, Individually and, if Their Proposed Merger is Approved, as a Merged Company (collectively AEP Ohio) for an Increase in Electric Distribution Rates*, Case No. 11-351-EL-AIR et al. , Opinion and Order (Dec. 14, 2011). [↑](#footnote-ref-14)
15. Id at 21. [↑](#footnote-ref-15)
16. Id. [↑](#footnote-ref-16)
17. See *In the Matter of the Application of Columbus Southern Power company and Ohio Power Company, Individually and, if Their Proposed Merger is Approved, as a Merged Company (collectively AEP Ohio) for an Increase in Electric Distribution Rates*, Case No. 11-351-EL-AIR et al. , Joint Stipulation and Recommendation at 14 (Nov. 23, 2011) (Emphasis added). [↑](#footnote-ref-17)
18. Application for Rehearing at 21. (Emphasis added). [↑](#footnote-ref-18)
19. Joint Stipulation and Recommendation at 14. [↑](#footnote-ref-19)
20. See *In the Matter of the Application of Ohio Power Company for Approval of an Amendment to its Corporate Separation Plan,* Case No. 11-5333-EL-UNC. [↑](#footnote-ref-20)
21. Id. Finding and Order at ¶32 (Jan. 23, 2012). [↑](#footnote-ref-21)
22. Capacity Charge Order at 33-36. [↑](#footnote-ref-22)
23. Id. at 22. [↑](#footnote-ref-23)
24. Id. [↑](#footnote-ref-24)
25. Opinion and Order at 36. [↑](#footnote-ref-25)
26. Id. (Emphasis Added). [↑](#footnote-ref-26)
27. See *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Authority to Establish a Standard Service Offer Pursuant to 4928.143, Ohio Rev. Code, in the Form of an Electric Security Plan,* Case No. 110346-EL-SSO et al., Entry on Rehearing at 13 (April 11, 2012)(finding that the Order in the ESP I proceedings permitted AEP to seek recovery of deferrals, but did not establish a rider or other tariff provision for AEP –Ohio to recover deferred fuel costs or set a hard deadline for when recovery shall begin. “To the contrary, as FES points out, in the ESP I Order the Commission explicitly provided that any recovery shall occur as necessary, indicating the Commission would conduct an additional analysis\*\*\*.). [↑](#footnote-ref-27)
28. Opinion and Order at 58-59. [↑](#footnote-ref-28)
29. Opinion and Order at 59. [↑](#footnote-ref-29)
30. Company Application for Rehearing at 45. [↑](#footnote-ref-30)
31. Company Application for Rehearing at 47. [↑](#footnote-ref-31)
32. See OCC/APJN Application for Rehearing, Assignment of Error 1 A, B, and C. [↑](#footnote-ref-32)
33. See OCC/APJN Application for Rehearing, Assignment of Error 1E (where it was argued that the non-quantifiable benefits of the ESP do not outweigh the hundreds of millions of dollars of costs of the ESP. [↑](#footnote-ref-33)
34. Opinion and Order and 47. [↑](#footnote-ref-34)
35. AEP Ohio Application for Rehearing at 29. [↑](#footnote-ref-35)
36. AEP-Oho Application for Rehearing at 29, citing Tr. VII at 2239. [↑](#footnote-ref-36)
37. *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company, Individually and, if Their Proposed Merger is Approved, as a Merged Company (collectively, AEP Ohio) for an Increase in Electric Distribution Rates*, Case No. 11-351-EL-AIR, Joint Stipulation and Recommendation (Nov. 23, 2011) at 5-6. (“Distribution Rate Case”). [↑](#footnote-ref-37)
38. Distribution Rate Case, Joint Stipulation and Recommendation (Nov. 23, 2011) at 12. [↑](#footnote-ref-38)
39. *Distribution Rate Case*, Case No. 11-351-EL-AIR, Opinion and Order (Dec. 14, 2011) at 4 [↑](#footnote-ref-39)
40. *Distribution Rate Case*, Case No. 11-351-EL-AIR, Joint Stipulation and Recommendation (Nov. 23, 2011) at 15. [↑](#footnote-ref-40)
41. *McKay Machine Company v. Rodman* (1967), 11 Ohio St. 2d 77, 80. [↑](#footnote-ref-41)
42. August 8 Order at 37. [↑](#footnote-ref-42)
43. Id. (citations omitted). [↑](#footnote-ref-43)
44. Application for Rehearing at 32. [↑](#footnote-ref-44)
45. Id. at 34. [↑](#footnote-ref-45)
46. Id. at 32. [↑](#footnote-ref-46)
47. See *In the Matter of the Investigation into the Development of the Significantly Excessive Earnings Test Pursuant to Amended Substitute Senate Bill 221 for Electric Utilities*, Case No. 09-786-EL-UNC, Finding and Order (June 30, 2010) (“09-786 Order”) at 29. [↑](#footnote-ref-47)
48. OEG Ex. 101 at 5. [↑](#footnote-ref-48)
49. See Tr. X at 2821, where Mr. Kollen stated that his equity stabilization plan “is patterned to follow precisely after the SEET computation with the exception of the off-system sales and the thresholds.” [↑](#footnote-ref-49)
50. See id. at 2844. See also OEG Ex. 101 at 9. [↑](#footnote-ref-50)
51. OEG Ex. 101 at 8. [↑](#footnote-ref-51)
52. Ormet Ex. 107 at 9. [↑](#footnote-ref-52)
53. Wal-Mart Ex. 101 at 9. [↑](#footnote-ref-53)
54. FES Ex. 102 at 79. [↑](#footnote-ref-54)
55. Kroger Ex. 101 at 10. [↑](#footnote-ref-55)
56. Application for Rehearing at 32. [↑](#footnote-ref-56)
57. *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Administration of the Significantly Excessive Earnings Test under Section 4928.143(F), Revised Code, and Rule 4901:1-35-10, Ohio Administrative Code*, Opinion and Order (January 11, 2011) at 23; 09-786 Order at 29. [↑](#footnote-ref-57)
58. Application for Rehearing at 33. [↑](#footnote-ref-58)
59. Id. [↑](#footnote-ref-59)
60. *In the Matter of the Application of Duke Energy Ohio for Approval of an Electric Security Plan*, Case Nos. 11-3549-EL-SSO, et al., Stipulation and Recommendation (October 27, 2008) at 2; *In the Matter of the Application of Duke Energy Ohio for Approval of an Electric Security Plan*, Case Nos. 08-920-EL-SSO, et al., Stipulation and Recommendation (October 27, 2008) at 2. [↑](#footnote-ref-60)
61. AEP Ex. 100 at 11. [↑](#footnote-ref-61)
62. August 8 Order at 39. [↑](#footnote-ref-62)
63. Id. at 40. [↑](#footnote-ref-63)
64. Id. [↑](#footnote-ref-64)
65. Id. [↑](#footnote-ref-65)
66. Application for Rehearing at 18-19. [↑](#footnote-ref-66)
67. August 8 Order at 15. [↑](#footnote-ref-67)
68. Id. at 15-16. [↑](#footnote-ref-68)
69. Application for Rehearing at 20. [↑](#footnote-ref-69)
70. Id. [↑](#footnote-ref-70)
71. Id. [↑](#footnote-ref-71)
72. August 8 Order at 70. [↑](#footnote-ref-72)
73. Id. [↑](#footnote-ref-73)
74. Id. [↑](#footnote-ref-74)
75. Id. [↑](#footnote-ref-75)
76. Id. [↑](#footnote-ref-76)
77. Application for Rehearing at 35-36. [↑](#footnote-ref-77)
78. Id. at 36. [↑](#footnote-ref-78)
79. Id. at 35. [↑](#footnote-ref-79)
80. OCC/APJN Application for Rehearing at 98-99. [↑](#footnote-ref-80)
81. August 8 Order at 36. [↑](#footnote-ref-81)
82. Application for Rehearing at 38. [↑](#footnote-ref-82)
83. August 8 Order at 70. [↑](#footnote-ref-83)
84. OCC/APJN Application for Rehearing at 88. [↑](#footnote-ref-84)