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BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Columbus Southern Power Company for Approval of its Electric Security Plan; an Amendment to its Corporate Separation Plan; and the Sale or Transfer of Certain Generating Assets.	)	Case No. 08-917-EL-SSO
In the Matter of the Application of Ohio Power Company for Approval of its Electric Security Plan; and an Amendment to its Corporate Separation Plan.	)	Case No. 08-918-EL-SSO

APPLICATION FOR REHEARING AND MEMORANDUM IN SUPPORT OF INDUSTRIAL ENERGY USERS-OHIO

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APPLICATION FOR REHEARING OF INDUSTRIAL ENERGY USERS-OHIO

Pursuant to Section 4903.10, Revised Code, and Rule 4901-1-35, Ohio Administrative Code ("O.A.C."), Industrial Energy Users-Ohio ("IEU-Ohio") respectfully submits this Application for Rehearing of the Opinion and Order ("Order") issued by the Public Utilities Commission of Ohio ("PUCO" or "Commission") on March 18, 2009 on the electric security plan ("ESP") of Columbus Southern Power Company and Ohio Power Company (individually "CSP" and "OP", respectively, and collectively "Companies" or "AEP-Ohio"). As explained in more detail in the attached Memorandum in Support, the Commission's Order in this case is unreasonable and unlawful for the following reasons:

I. The Commission erred by granting stunning rate increases while failing to issue a written decision in this contested proceeding that sets forth, in sufficient detail and based on the facts and law, the reasons prompting the decision.

II. The Commission's rate increase for ninety percent of AEP-Ohio's requested POLR revenue requirement is unjust, unreasonable and unlawful.

III. The Commission's authorization of a rate increase for recovery of costs of ownership and other interests in generating assets is unjust, unreasonable, unlawful and unsupported by the evidence.

IV. The Commission's selective distribution rate increases, for gridSMART and a service reliability plan are unjust, unreasonable and unlawful.

V. The Commission's failure to require AEP-Ohio to limit the total bill increases to the percentage amounts specified in the Order is unjust, unlawful and unreasonable and the Commission must immediately require AEP-Ohio to comply with the Order and to refund amounts billed and collected in excess of such caps.

VI. The Commission's conclusion that the ESP is more beneficial in the aggregate than the alternative under Section 4928.142, Revised Code, is unjust, unreasonable, unlawful and unsupported by the evidence.

VII. The Commission's unbundling of the non-fuel and fuel component of the generation rate based on something other than 2008 actual fuel costs is unjust and unreasonable.

VIII. The scope of the fuel and other cost recovery mechanism authorized by the Commission is unreasonable, unlawful and unjust both because of the types of costs that are subject to recovery through the mechanism and the substantial negative effect that the kWh-based mechanism has upon larger, high load factor customers.

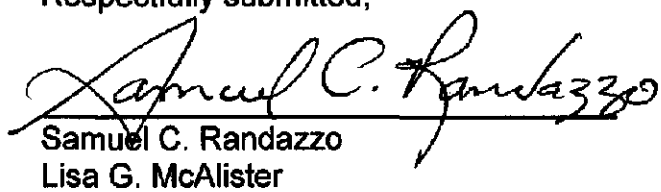
IX. The Commission's determination that interruptible load may not be counted towards OP's and CSP's determination of their peak demand response compliance requirements is unjust, unreasonable and unlawful.

X. The combined effect of the unexplained conclusions in the Commission's Order is unreasonable, unjust and unlawful because the Commission arbitrarily and capriciously exercised its discretion to allow CSP and OP to bill and collect excessive rates.

For these reasons, discussed in greater detail below, IEU-Ohio requests that the Commission grant this Application for Rehearing and modify AEP-Ohio's ESP as

described herein and in the attached Memorandum in Support. This is not a situation that will permit the public interest to be protected or served by the Commission granting rehearing and then letting the large increases produced by the Order continue to grind on customers and Ohio's economy until the Commission gets around to issues on rehearing. If the Commission does not have serious intentions to right the wrongs that were embedded in the Order and do it quickly, IEU-Ohio urges the Commission to not erect procedural barriers to an appeal to the Ohio Supreme Court by granting rehearing for the purpose of allowing the Commission more time. Justice delayed in this situation is surely justice denied at a time when Ohio's electric customers can least afford it.

Respectfully submitted,



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MEMORANDUM IN SUPPORT

I. The Commission erred by granting stunning rate increases while failing to issue a written decision in this contested proceeding that sets forth, in sufficient detail and based on the facts and law, the reasons prompting the decision.

Ohio's electricity consumers (big and small) are struggling on many fronts. Residential consumers that still have jobs are worried about a trend line that seems to bring more bad news by the day. Ohio's businesses are unable to make both ends meet and are trying to cope with the trauma that comes from large and sudden reductions in their sales.

Ohio's leaders can often be heard these days talking about what Ohio should do to make things better. Even the Commission has been, in some cases, mindful of the present difficulties.[1] During the course of his testimony before the Finance and

[1] *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company and the Toledo Edison Company for Authority to Establish a Standard Service Offer Pursuant to Section*

Appropriations Committee on the Commission's budget, Chairman Alan Schriber recently specifically addressed the current difficulties customers are having. In response to an observation made by Representative Yates that "The ordinary citizen feels like they're taking it on the chin," Chairman Schriber stated, "We are very intent, in this day and age, to mitigate rate increases," adding that the Commission's goal is to have "virtually no increase in utility rates."[2] Chairman Schriber went on to say, "I think we're doing a pretty decent job this year of doing that. This is not the year when you want to increase rates. There is no question that, over time, rates are going to go up."[3]

IEU-Ohio does not mention the significant stress that customers are under because it wants or needs the PUCO to provide customers with an ***unfair or unlawful*** advantage. On the contrary, the Commission must fairly balance the interests of customers and the utilities subject to the PUCO's regulatory jurisdiction.

The purpose of mentioning Ohio's hard times here is to highlight how important it is in times like these for the PUCO to clearly and carefully explain why it chooses to resolve contested issues in ways that produce large electric rate increases that add to already difficult consumers' burdens or how the actions taken to increase rates now will make things better in the future. Clear communications from the Commission through

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4928.143, Revised Code, in the Form of an Electric Security Plan, Case No. 08-935-EL-ESP, Opinion and Order at 17 (December 19, 2008) (hereinafter cited as the *FirstEnergy ESP Case).*

[2] Gongwer News Service, Gongwer House Activity Report (March 5, 2009) (Attachment A).

[3] *Id.* Regardless of what Chairman Schriber may have said in his recent testimony before the General Assembly, the Order is a clear blow to the chin of customers. As discussed below, each opportunity that the Commission had to exercise its discretion about the magnitude of the increase was accompanied by a selection that made the increase as high as possible. This is not an outcome that can be reconciled with doing a "pretty decent job" of meeting the goal of virtually no increase.

its orders also provide consumers with information they want and need to predict where rates are likely to go in the future and how they might engage in self-help.

Clearly reasoned decision-making and clear communications by the PUCO are also important from a legal perspective. Section 4903.09, Revised Code, requires the PUCO to issue written decisions in contested proceedings "...setting forth the reasons prompting the decisions...". This obligation must be satisfied by the PUCO to permit the Ohio Supreme Court to properly discharge its duties on appeal.[4] To meet the requirements of Section 4903.09, Revised Code, the PUCO's orders must show, in sufficient detail, the facts in the record upon which the order is based and the reasoning followed by the Commission to get to the conclusion.[5] Unfortunately, the Commission's Order omits a merit-based examination and reasoned disposition of the contested issues based on the evidence, the law and conceals its real effect. Despite the heading at page 73 of the Opinion and Order, there are **no findings of fact or conclusions of law in the Opinion and Order** that relate to any substantive issue. On the way to authorizing excessive increases, the Order effectively treats the hard litigation work undertaken by customer representatives and the commands of the General Assembly as little more than background noise.

The conclusions that are contained in the Order suggest that the PUCO resolved contested issues in ways that produce significant rate increases for Ohio consumers.

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[4] *MCI Corp. v. Pub. Util. Com.*, 38 OS3rd 266, 270 (1988). An administrative agency's explanation of the reasons for its decision is required not only for appellate review but also to assure the parties that their factual allegations and legal arguments have been fully considered. *See Riverside General Hospital v. N.J. Hospital Rate Setting Com'n*, 98 N.J. 458, 468 (1985); *Application of Howard Savings Institution of Newark*, 32 N.J. 29, 52 (1960).

[5] *MCI Telecommunications Corp. v. Pub. Util. Comm.*, 32 OS3rd 306 (1987).

Adding insult to injury (from a consumer's perspective),[6] the PUCO also acted to make sure that the electric distribution utilities ("EDUs") get a full year's value out of the PUCO-sanctioned increases in the balance of 2009 that remains. By cramming 12 months of revenue increase into the remainder of 2009, the PUCO permitted AEP-Ohio to go deeper into customers' empty pockets. Regardless of words creatively used by the Commission to describe the retroactive effect of the large rate increases, the numbers that are now appearing on customers' bills make the consequences unmistakable.

The PUCO's Order seems inclined to diminish the significance of these regulator-sanctioned increases by characterizing (perhaps as part of the PUCO's public relations spin) the rates resulting from the Order as the lowest in Ohio. However, this comparison is without any basis in the record evidence (particularly since the future rates of other Ohio electric utilities are presently unknown). And, the low-rates-spin appears to be built on assumptions about AEP-Ohio rate levels that will ultimately depend on variables (such as the cost of fuel, carbon taxes and carrying costs) that are likely to accelerate the upward movement of AEP's electric rates when compared to the ESPs that have been approved by or submitted to the PUCO.

Contrary to the PUCO's spin, the record evidence shows that CSP and OP are generating the **highest** level of margin per MWH (gross revenue less fuel costs) within the entire American Electric Power ("AEP") system, including the operating companies

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[6] In the testimony referenced above, Representative Yates stated that it was his sense that consumers feel their positions are not considered and Representative Goodwin stated that there is a perception that the Commission is "run by utilities." Chairman Schriber responded that the Commission tries to balance the needs of consumers and utilities and that it is difficult to convince Ohioans that the Commission's actions are in the best interest of the State. Gongwer News Service, Gongwer House Activity Report (March 5, 2009) (Attachment A).

just across the Ohio border in Michigan, Kentucky, Indiana and West Virginia. Even if AEP-Ohio's rapidly escalating rates might be the lowest in Ohio (a comparison that seems to suggest that the PUCO is only interested in eliminating this condition by making AEP-Ohio's rates even higher), AEP-Ohio's rates appear to put Ohio at a relative disadvantage when compared to the other areas served by nearby affiliates.

The gross revenue margin (revenue **less** fuel and purchased power expense)[7] per MWH of AEP-Ohio[8] suggests that its Ohio customers are and have been carrying their weight (and perhaps more) when it comes to fairly compensating OP and CSP. As IEU-Ohio demonstrated,[9] the gross margin per MWH reported for AEP-Ohio for the third quarter of 2008 was $43.9 per MWH compared to $46.8 per MWH for the corresponding quarter in 2007. In both quarters, the next highest gross margin per MWH contribution to earnings per share by any AEP business unit came from Off System Sales (at between $32 and $33 per MWH). And, in case the relationship between the gross margin achieved by AEP-Ohio and the gross margin from Off System Sales was lost on the Commission the first time that IEU-Ohio pointed out these figures, the lower gross margin from Off System Sales indicates that the go-to-market opportunity lusted after by AEP-Ohio is less compensatory than retail rate revenue collected by AEP-Ohio.[10]

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[7] Tr. Vol. IV at 285. The "East Integrated Utilities" line includes Appalachian Power Company, Kentucky Power Company, I&M [Indiana Michigan Power], Wheeling Power and Kingsport Power Company. Tr. Vol. IV at 287.

[8] The term "Ohio Companies" refers to CSP and OP. Tr. Vol. IX at 112.

[9] IEU-Ohio Exhibit 2 at 11, which is the 2008 earnings release presentation for the third quarter that was issued by AEP on October 31, 2008. *See also,* Tr. Vol. IV at 285.

[10] The evidence on the relative rate levels in Ohio and the balance of the AEP system includes more than gross margin comparisons discussed above. For example, IEU-Ohio Exhibit 7, at pages 20 through 39, shows that the average per-kWh historical prices of CSP and OP have been well above retail prices of their affiliates operating in other states.

Quarterly Performance Comparison

American Electric Power
Financial Results for 3rd Quarter 2008 Actual vs 3rd Quarter 2007 Actual

		2007 Actual			2008 Actual		
		Performance Driver	($ millions)	EPS	Performance Driver	($ millions)	EPS
	UTILITY OPERATIONS:						
	Gross Margin:						
1	East Regulated Integrated Utilities	18,677 GWh @ $28.6 /MWhr =	534		18,060 GWh @ $27.6 /MWhr =	499	
2	Ohio Companies	13,464 GWh @ $46.9 /MWhr =	629		13,127 GWh @ $43.9 /MWhr =	577	
3	West Regulated Integrated Utilities	12,469 GWh @ $26.9 /MWhr =	336		12,070 GWh @ $28.2 /MWhr =	341	
4	Texas Wires	7,721 GWh @ $19.6 /MWhr =	152		7,961 GWh @ $19.3 /MWhr =	153	
5	Off-System Sales	10,164 GWh @ $32.4 /MWhr =	329		9,777 GWh @ $33.0 /MWhr =	322	
6	Transmission Revenue - 3rd Party		81			85	
7	Other Operating Revenue		126			160	
8	Utility Gross Margin		2,187			2,127	

Rather than making its reasoned review and resolution of the contested issues transparent, the Commission's Order contains a discussion of the various positions of the parties followed by a naked conclusion. There is a beginning and end in the text, but the Order omits the required documentation of the Commission's reasoning from the facts and law to the conclusions reached on the contested issues. In the context of customers who are under siege by very difficult circumstances, the Commission's inability or unwillingness to document its reasoning and explain its choices constitutes a stunning disregard for its legal and practical responsibilities as an arbiter, an agent of the General Assembly **and** communicator that appreciates, particularly now, the need for all government agencies to inspire the public's confidence.

The discussion below highlights the absence of reasoned decision-making and the flip-flopping conclusions that dominate the Order.

A. The Fuel Adjustment Clause ("FAC")

CSP and OP proposed an ESP pursuant to Section 4928.143, Revised Code, that included the establishment of an automatic adjustment mechanism (referred to as

the fuel adjustment clause or "FAC") to recover the cost of fuel, non-fuel items, fixed costs and variable costs. Despite its significance, AEP-Ohio's proposal was accompanied by little detail. The parties to the proceeding raised issues and presented evidence that required the Commission to, among other things, address questions about the scope of the FAC, the baseline value that should be used to initiate the FAC mechanism and set the non-FAC portion of the rate, the lack of substantive detail, the lack of process detail, the unfairness of the mismatch between costs and benefits, whether forecasted or actual prudently incurred costs were subject to recovery through the FAC and the reasonableness of effectively allocating fixed costs on a volumetric or kWh basis through the FAC mechanism. The Order does not disclose how these issues were resolved by the Commission.

The Order states that the Commission believes that the establishment of an FAC mechanism as part of an ESP is authorized pursuant to Section 4928.143(B)(2)(a), Revised Code, to recover prudently incurred costs associated with fuel, including consumables related to environmental compliance [consumables are nowhere mentioned in the law], purchased power costs, emission allowances, and costs associated with carbon-based taxes and other carbon-based regulations [regulations are nowhere mentioned in the law].[11]

The Commission held that purchased power is not a prerequisite for adequately serving additional load requirements assumed by AEP-Ohio because there is no rational basis to approve recovery of such purchased power in the absence of a

[11] Order at 14.

demonstrated need.[12] But without any requirement that need be first demonstrated, the Commission authorized AEP-Ohio to increase rates (FAC and non-FAC) to include costs of generating units in which AEP has an ownership or other interest.[13]

The Commission rejected a recommendation that revenue from off-system sales be used as a credit to costs recovered through the FAC mechanism saying that it was not "persuaded" by the intervenors' arguments and that it did not **believe** that off-system sales should be a component of the ESP. The Commission did not explain the basis of this belief or explain what its beliefs have to do with its statutory duties to resolve contested issues based on the record evidence and the law.

The Order states that intervenors cannot have both an off-system sales offset to the FAC and inclusion of off-system sales revenue for purposes of the significantly excessive earnings test ("SEET").[14] But, the Order states that off-system sales revenue will also **not** be considered for purposes of the SEET.[15] Thus, it appears that what the Commission actually did (contrasted with what it suggested it was doing) was to hold that the costs absorbed by customers will not be mitigated by either an FAC offset or any consideration of the benefits of off-system sales in the SEET context. Additionally, the Commission's SEET determinations specific to AEP-Ohio followed a PUCO holding

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[12] *Id.* at 16.

[13] *Id.* at 52.

[14] *Id.* at 17.

[15] *Id.* at 69.

that the subject matter should **not** be addressed on a case-by-case or utility-specific basis.[16] Heads, AEP-Ohio wins. Tails, consumers lose.

The Order rejected the use of 2008 actual fuel costs as a basis for setting a baseline to separate the FAC and non-FAC components of current rates. The recommendation to use the 2008 actual costs was designed to make sure that the FAC baseline value was not too low and the non-FAC rate set too high.[17] The Commission elected to not use actual 2008 costs, saying that actual costs were not known at the time of the hearing. Instead, it adopted a Staff-sponsored proxy for 2008 costs perhaps believing that a wrong number was close enough.

Regardless of what was known at the time of the hearing, the Commission could have nonetheless found in favor of the methodology that set the baseline based on 2008 actual costs and required AEP-Ohio to observe this requirement for purposes of developing rates.

Since 2008 actual fuel costs are now known, since they are significantly higher than the "proxy" adopted by the Commission, and since the "proxy" is, by definition, not the prudently incurred costs authorized in Section 4928.143(B)(2)(a), Revised Code, the Order results in the non-FAC portion of rates being too high and the risk of increases in the FAC portion as well as the amount of deferrals too great. In fact, in public presentations during 2008 and 2009, AEP indicated that its average price of coal delivered in 2007 was $36.58/ton, while its 2008 cost was reported to be $46.61/ton; a 27.4 percent increase over 2007. These data indicate that the Staff proxy for

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[16] *Id.* at 68.

[17] *Id.* at 19.

determining the 2008 baseline FAC costs produced a baseline FAC cost that was too low. Similarly, actual results for 2008, as reported in the SEC 10K Report, indicate that OP had a $148 million increase in fuel and consumables compared to 2007, and that CSP had a $65 million increase in fuel, allowance, and consumables expenses in 2008. Based on the 3 percent escalation that Staff applied to CSP's 2007 FAC costs and the 7 percent escalation applied to OP's 2007 FAC costs to arrive at its 2008 proxy, the proxy baseline FAC costs are understated by tens of millions of dollars, whether the 2008 SEC actual data are used or the Commission uses the 2008 actual data otherwise publically reported by AEP.

Now that AEP's books have been closed for 2008 and the actual fuel costs are known, it would have been straightforward to require AEP-Ohio to develop its rates based on these actual costs as was recommended during the litigation phase of this proceeding. There is no good reason for the PUCO to unbundle the FAC and non-FAC rate components based on a proxy when the actual costs are readily available.

B. The Missing Rate Increase Cap

The Commission's Order states that an increase in excess of 15 percent would, during this difficult economic climate, impose a severe hardship on customers and that a 15 percent cap is too high.[18] The Order states that AEP-Ohio must observe a limit on increases during 2009 of 7 percent of the **total bill** for CSP customers and 8 percent of the **total bill** for OP customers.[19] Yet, and as the Commission well knows, the rates

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[18] *Id.* at 22.

[19] *Id.*

that the Commission has now authorized AEP-Ohio to charge customers in 2009 produce actual total bill increases substantially in excess of the total bill caps established by the Commission. In some cases, the actual total bill increases in 2009 will be above the 15 percent level that the Commission said would cause severe hardship. In all cases, the actual increases are well above the "virtually no increase" expectation which Chairman Schriber created in his recent testimony before the General Assembly.

Despite being informed of this problem (the mismatch between the total bill cap established by the Commission and actual, much larger, increases), the Commission did nothing to correct this problem before the Commission allowed AEP-Ohio's rates to go into effect.

C. Carrying Costs

AEP-Ohio's ESP proposal included a provision to increase rates for carrying costs (about **$110 million annually**) on environmental expenditures made during the period 2001 through 2008. Over the three-year term of the ESP, it appears that this aspect of the Order will cost customers some **$330 million**.

The intervenors opposed this proposal on several grounds. They cited Section 4928.143(B)(2)(b), Revised Code, that limits any allowance for an environmental expenditure or cost to those incurred on or after January 1, 2009. The intervenors pointed to the requirement in Section 4928.143(B)(2)(b), Revised Code, for any allowance authorized under this Section to be related to construction work in progress and the fact that the requested carrying charges were unrelated to any construction work in progress. The Commission's Order does not address the intervenors' legal

claim that a pre-2009 environmental expenditure cannot be used to increase rates as part of an ESP.

Also related to this pre-2009 carrying charge proposal, the Commission disregarded the uncontested facts that show that carrying charges associated with environmental assets are not properly based on a weighted average cost of capital and must reflect the favorable cost of capital that is made available as a result of various types of special financing available to environmental or pollution control assets. The Commission's bent-over-backwards accommodation of a carrying cost rate based on the overall weighted cost of capital and the use of a hypothetical capital structure that pushed the weighted cost of capital calculation result even higher are circumstantial but nonetheless clear indications of the Commission's unwillingness to keep the magnitude of any rate increases as low as reasonably possible. It is also worthwhile to note that the Commission has often approved the use of a debt cost rate, not the weighted cost of total capital, for purposes of establishing carrying costs.[20] The Commission's choice of a carrying cost rate computed based on the weighted cost of capital is a choice that unreasonably and unjustly favors higher electric prices.

D. Provider of Last Resort ("POLR")

There is not one bit of evidence in the record that suggests that any AEP-Ohio customers have switched and if, as the Order asserts, AEP-Ohio's rates will be the

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[20] *See,* for example, *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company to Adjust Each Company's Transmission Cost Recovery Rider,* Case No. 08-1202-EL-UNC, Finding and Order at 4 (December 17, 2008); *see also, In the Matter of the Application of The Dayton Power and Light Company for Authority to Modify its Accounting Procedure for Certain Storm-Related Services Restoration Costs,* Case No. 08-1332-EL-AAM, Finding and Order at 1 (January 14, 2009).

lowest in Ohio, there is little reason to expect this condition will change. Nonetheless, CSP and OP proposed a non-cost-based distribution POLR rider claiming that it was required to cover the **cost** of providing customers with the ability to remain with AEP-Ohio, switch and then return to CSP or OP.[21]

Since the AEP-Ohio POLR proposal is a distribution-related and non-competitive service element, one might expect that the Commission's determination, at page 32 of the Order, would apply to defeat this rate increasing proposal. At page 32 of the Order, the Commission found that AEP-Ohio should file a full distribution rate case so that all components of distribution rates can be examined prior to authorizing AEP-Ohio to incrementally increase distribution charges. But this expectation is undone by the PUCO's response on the incremental distribution rate increase for POLR. And, contrary to the impressions conveyed by the Order that customers may avoid the POLR rate increase by agreeing to stay with AEP during the term of the ESP, AEP's administration of the Order is leaving no opportunity for customers to avoid the POLR increase by agreeing to stay with AEP during the term of the ESP.

AEP-Ohio used the Black-Scholes Model to develop a POLR price tag (revenue requirement) and this approach was criticized by every other party (including the Staff), with the other parties citing facts and the law to support their objections to AEP's POLR proposal.[22] After a summary recital of some (but no analysis) of the opposing parties'

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[21] *Id.* at 38.

[22] Yes, it is true. The PUCO relied on the same Black-Scholes Model that was used to value mortgaged backed securities that now have the distinction of sending the Nation's and the World's economy into an abyss. *Onslaught. Crisis of the World Financial System: The Financial Predators Had A Ball*, William Engdalf, Global Research, February 23, 2009 (available *via* the Internet at http://www.globalresearch.ca/index.php?context=va&aid=8158). The devastation from Main Street to Wall Street has caused even Myron Scholes, one of the developers of the Black-Scholes Model, to

positions on the POLR proposal, the Commission awarded AEP-Ohio a POLR revenue requirement of **$152.2 million per year, ninety percent of the $169.1 million AEP proposed**. The Order ignores the opposing parties' demonstration that the Black-Scholes Model (as applied by AEP-Ohio) was invalid, did not include any actual costs of providing POLR, was tied to ridiculous assumptions about shopping and relied on a market price (about $88 to $85 per MWH) which was rejected (implicitly) by the Commission for purposes of comparing the ESP and market rate option ("MRO") options.

The Order's treatment of AEP-Ohio's POLR proposal also ignores the significance of AEP-Ohio's participation in PJM LLC. OP and CSP currently participate in PJM LLC, a regional transmission organization ("RTO") subject to the jurisdiction of the Federal Energy Regulatory Commission ("FERC"). All of OP's and CSP's available generating capacity is bid into the PJM market (it is not dispatched to serve retail customers in Ohio). In other words, AEP, acting on behalf of each of its operating companies, offers the output of available generating units to PJM. It is up to PJM to determine what to do in response to these offers.[23] On any given day, the actual retail load presented by the OP and CSP customers could, in accordance with PJM's determinations, be served by generators other than those owned or operated by the Companies.[24] Regardless of who actually owns the generation capacity, PJM will

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suggest that the model's assumptions may not reflect the real world. *Myron Scholes Says Regulators Need to 'Blow Up or Burn' OTC Derivatives Markets*, Ces Quirijns, March 9, 2009 (available via the Internet at http://quirijns.especialreports.com/2009/03/09/myron-sholes-says-regulators-need-to-blow-up-or-burn-otc-derivatives-markets/.

[23] Tr. Vol. XI at 56-57, 65.

[24] Tr. Vol. XI at 58.

dispatch available generation capacity to serve load and maintain real-time reliability.[25] Under the PJM rules, all suppliers with load serving responsibilities (including OP and CSP) must maintain adequate resources to reliably meet their customers' needs.[26] The Order acknowledges that the cost of meeting the PJM generating resource adequacy requirement (Fixed Resource Requirement or "FRR" in AEP's case) is already reflected in rates.[27] And prior to these proceedings, AEP entered into a commitment to meet the generation resource adequacy requirement of **all retail suppliers** within its PJM zone for a period of five years (ending after the ESP period).[28] Under PJM's rules, the cost of a default by a load serving entity is "socialized" throughout the PJM footprint.[29]

As discussed below, IEU-Ohio believes that authorizing OP and CSP to collect $152.2 million annually for POLR risk is unwarranted based on the facts and law. But if the Commission elects to rule against IEU-Ohio's position, it is obligated to explain the basis for the ruling. During the three-year ESP period, the Order will give AEP the opportunity to collect some **$456 million in POLR revenue**.

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[25] Tr. Vol. XI at 59-60.

[26] Tr. Vol. XI at 60-61.

[27] Order at 58.

[28] Tr. Vol. XI at 61.

[29] Tr. Vol. XI at 70. According to the April 6, 2009 edition of *Energy Daily*, PJM has recently socialized some $80 million associated with a default by one market participant.

E. Transformed Request for Generation Asset Transfer Approval

Amended Substitute Senate Bill 221 ("SB 221") modified Section 4928.17, Revised Code, so that no EDU could transfer any generating asset without the PUCO's prior approval.

Although AEP-Ohio had no plans to do so, it included requests in its ESP application for PUCO approvals of potential transfers of certain generating units or it gave the PUCO a "heads up" that it might someday transfer interests in generating units. Because AEP-Ohio had no plans to transfer any of these interests or assets, the intervening parties and the Staff asserted that AEP's request was premature.[30] Even though AEP-Ohio acknowledged that it had no current plans to transfer any interest in such assets, it pushed for authority to do so claiming (on rebuttal) that if the PUCO did not approve the plan-deficient transfer request, that the costs of such assets should be included in rates.

AEP-Ohio's litigation position – that the costs of such assets are not in current rates – suffered from the obvious problem that AEP-Ohio's rates are not based on costs and the PUCO has steadfastly precluded any cost-based examination of AEP-Ohio's generation rates. In the end, the Order selectively transformed AEP-Ohio's open-ended, plan-deficient request to transfer certain interests in generating assets and current rates that are not cost-based to begin with into a conclusion that current rate revenue is inadequate to cover the costs of such generating interests and that the non-

[30] Order at 51.

FAC and FAC[31] revenue produced by current electric rates must be increased by **$120 million per year**. During the three-year ESP period, the total extra burden that AEP-Ohio customers will carry as a result of this transformative and rate-increasing determination amounts to about **$360 million**.

The Order makes no reference to any provision of Ohio law that authorizes the PUCO to establish cost-based generating rates for some of AEP's generating assets and there is nothing in the evidence of record that would allow a determination of what revenues might be warranted based on the cost of providing generating service.[32] The information that is in the record shows that AEP-Ohio is fully recovering all of its costs and is collecting a very "healthy" return on equity (using balance sheet equity values that include all interests in generating assets).[33] There is nothing in the Order or the evidence that suggests that these assets are needed to serve AEP-Ohio's customers. And, there is a substantial amount of record evidence that shows that AEP is making large amounts of wholesale or off-system sales, the benefit of which the Order withholds

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[31] By increasing the non-FAC and FAC rate components (which are not based on a total cost of service evaluation) to include costs related to the operation of the generating assets that AEP-Ohio may transfer at some point, the Order boosts the total rate revenue that will be collected by AEP-Ohio during the ESP period and increases the size of the deferrals that the Opinion and Order permits AEP-Ohio to amortize through a non-bypassable charge during the 2012-2018 period. Another blow to the chin of customers.

[32] AEP-Ohio has strongly opposed cost-based ratemaking for purposes of developing standard service offer ("SSO") electric generation supply prices. Yet, AEP-Ohio selectively invited cost-based ratemaking during this proceeding. AEP-Ohio's selective application of a cost-based methodology is no doubt influenced by its opinion about how its rates would look if its total revenue were determined on a cost basis. "AEP's power pool's competitive, largely coal-based production costs are among the lowest in the nation." IEU-Ohio Exhibit 7 at 12. The Order's selective application of cost-based ratemaking produces a result for customers that is the worst of both worlds. The actual cost of providing service is ignored unless its consideration allows for an upward adjustment to rates. This is not a ratemaking approach that can be reconciled with the goal of keeping rate increases as low as possible.

[33] As Mr. Cahaan testified, the Companies were obviously recovering their fuel costs (**which he defined to include purchased power**) in 2007 or their earnings would have been insufficient. Staff Exhibit 10 at 3.

from AEP-Ohio's retail customers. If AEP-Ohio's retail customers are required by the Order (and not anything in Ohio law) to pay even higher rates to cover costs of generating assets for which no need has been demonstrated, why is it that the same customers are not entitled the benefits of the revenue generated through the use of these assets? This result cannot be reconciled with the goal of keeping rate increases as close to zero as possible.

The Order's authorization of a $120 million increase in AEP-Ohio's annual retail revenues (and rates paid by customers) to cover the costs of the above-described generating assets is also remarkable based on the PUCO's response to AEP's request for a rider to recover costs associated with early closure of generating plants. Again, AEP-Ohio identified no plans to prematurely close any generating plants as part of promoting this portion of its ESP proposal. Numerous parties, including the Commission's Staff, opposed the proposed early-closure-cost rider -- demonstrating that the rider was unlawful and that it would not take into account **the positive economic value of the rest of AEP-Ohio's generating fleet**. The Commission agreed that the positive economic value of the fleet must be recognized.

F. gridSMART and Other Distribution Increases

Despite other conclusions that distribution rates should not be increased incrementally and must await a full examination of distribution revenues and expenses, the Order awards a 2009 distribution rate increase of **$17.5 million** for CSP and **$17.3 million** for OP that is now being charged and collected through the rates which the PUCO allowed to go into effect. This component of the extra rate burden placed on customers contrasts with Staff's recommended increase of $0 for distribution costs and

this extra burden was approved by the PUCO with no regard for any cost-effectiveness requirements.[34] Additionally, the Order did not address the intervenors' legal argument that the gridSMART proposal was not shown to satisfy the cost-effectiveness requirements of Sections 4928.02(D) and 4928.64(E), Revised Code. Instead, the Order resorts to a discussion of what the Commission believes might be the case if there is a properly designed and implemented program (something that was not put forward in evidence). The Order indicates that the Commission is a strong supporter of elements of the gridSMART proposal[35] while acknowledging that additional information is required before successful implementation is possible.[36] Yet, the Order commands full speed ahead by increasing 2009 distribution rates by $17.5 million for CSP and $17.3 million for OP. This result cannot be reconciled with the goal of keeping rate increases as close to zero as possible.

G. ESP and MRO Comparison

The Order concludes that the ESP manufactured in the Order is more favorable than the alternative under Section 4928.142, Revised Code (MRO).[37] The conclusion appears after a discussion of the issues raised by the parties, including the Staff. As with the rest of the Order, there is no explanation of how the Commission resolved the issues raised by the parties to reach the conclusion.

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[34] Order at 36.

[35] Order at 37.

[36] *Id.* at 38.

[37] *Id.* at 72.

While the Order itself offers not the slightest clue, the Order work paper (summary sheet attached hereto as Attachment B) indicates that the "market price" information relied upon by the Commission is the same information that was included with Staff witness Johnson's testimony. Staff witness Johnson testified that his market price estimate (about $74 per MWH) was at the high end of the range[38] which he developed when he prepared his testimony. He agreed that market prices continued to fall after he prepared his testimony.[39] Since the close of the record in this proceeding, it is common knowledge that the wholesale price of electricity has continued to plunge; a condition that would likely be of interest to a regulator working hard to keep rate increases as small as possible.[40]

If there is any doubt about the unreasonably high market price that was embedded in the ESP v. MRO comparison, the Commission need look no further than its decision in another recent ESP case. More specifically, the market price the Commission appears to have used for the MRO v. ESP comparison in the AEP-Ohio case is almost identical to the average generation price of $75 per MWH which the

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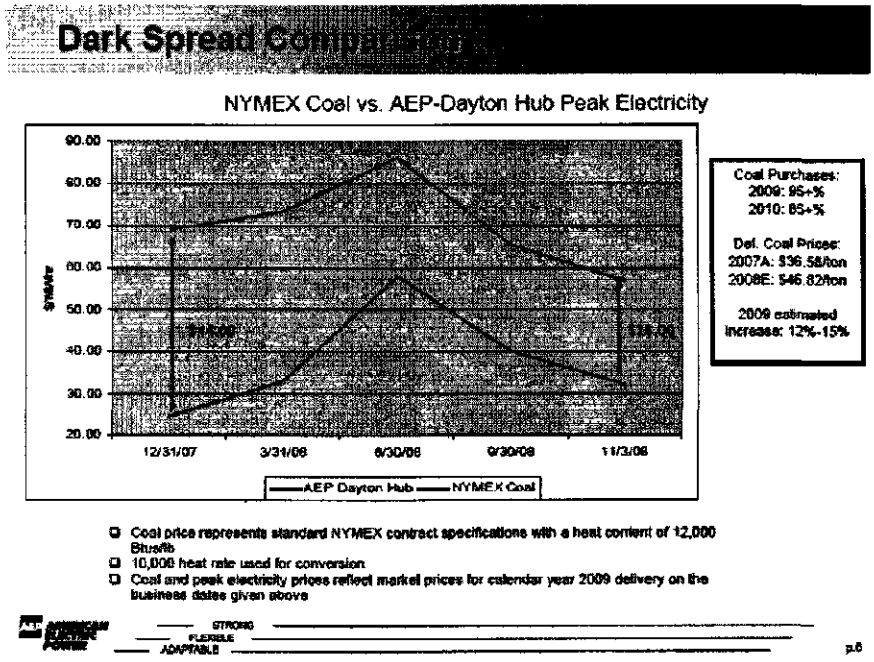
[38] Staff witness Johnson revealed on cross-examination that he had developed a market price range after starting with AEP-Ohio's ridiculously high $88 and $85 per MWH market prices for CSP and OP. During his cross examination, Mr. Johnson's answers indicated that he was not inclined to proactively share information that would allow his analysis to be more fully understood or evaluated.

[39] Tr. Vol. XII at 182, 187; Staff Exhibit 9 at 6.

[40] For example, on April 8, 2009, the New York Independent System Operator ("NYISO") reported that wholesale electricity prices in New York State dropped to their lowest level since 2003. It reported that the average cost of wholesale electricity in the state was $45.63 per MWH in March, and that the last time wholesale electricity prices were this low was in November 2003 when the average cost was $43.40 per MWH. It stated that the March prices were down sharply from $73.28 in January of this year. See the NYISO Press Release at http://www.nyiso.com/public/webdocs/newsroom/press_releases/2009/NYISO_Wholesale_Power_Prices_Drop_to_Lowest_Level_04082009.pdf.

Commission found to be excessive (by almost $8 per MWH) in the December 19, 2008 Opinion and Order modifying the ESP proposed in the *FirstEnergy ESP Case.*[41]

If there is any doubt about the unreasonably high market price that was embedded in the PUCO's ESP v. MRO comparison, the information which AEP presented to the public and the financial community shows that the doubt must be resolved against the PUCO. Page 6 of IEU-Ohio Exhibit 6, AEP presentation slides from a conference that took place in November 2008, shows the sharp decline in electricity market prices (for 2009 delivery).



The Order work paper (attached hereto as Attachment B[42]) shows that the MRO scenario included a generation-related revenue requirement based on the maximum blending percentages allowed by Section 4928.142, Revised Code, thereby using a

[41] *FirstEnergy ESP Case* at 69.

[42] It should be noted that the total MRO cost figures on the work paper agree with the Opinion and Order figures at p. 72 but for some reason the ESP cost figures on the work paper do not agree with the Opinion and Order.

worst case MRO assumption to show an ESP advantage. The Commission did this even after the General Assembly amended Section 4928.143, Revised Code, to make it absolutely, unmistakably clear that the blending percentages that were used for purposes of the Order were **not** required.

The same work paper shows that the MRO scenario relied upon by the Commission included $366 million in "cost" for POLR even though POLR as proposed by AEP-Ohio and approved by the PUCO is a distribution charge and even though there is nothing in Section 4928.142, Revised Code, that even hints that the PUCO has authority to approve a POLR charge in a Section 4928.142, Revised Code, proceeding.

Rather than reasoned decision-making on the MRO v. ESP comparison issues, the Order contains a naked conclusion that appears to be based on the highest market price the Staff could come up with when the Staff prepared its testimony and a market price that is nearly $8 per MWH higher than the Commission found to be appropriate for purposes of conducting the same test in the *FirstEnergy ESP Case*. In other words, the Order suggests that the Commission's decision was not reasonably balanced but tilted to produce an outcome that unreasonably favors AEP-Ohio, prejudices customers and ignores the commands of the General Assembly.

Among other things, and as the contested issues demand of the Commission, customers deserve to be told ***by the Commission*** just how and why:

1. The Commission picked the high end of the Staff's market price range when the record evidence shows that the generation price trend line was decidedly downward not upward (as discussed in the *FirstEnergy ESP Case*);

2. $74 per MWH is just-right for AEP-Ohio and $8 per MWH too high in the *FirstEnergy ESP Case*;

3. The MRO v. ESP comparison was based on the maximum blending percentage allowed by Section 4928.142, Revised Code;

4. The Commission included costs in the MRO scenario that are not legally within the MRO authority of the PUCO;

5. The Commission included a phantom POLR revenue requirement estimate using an economic model that contributed to the largest financial collapse since the Great Depression and a market price that is even higher than the market price used for the MRO v. ESP comparison itself;

6. The gridSMART costs were excluded from the ESP costs used in the ESP v. MRO comparison; and,

7. Customers must resort to forensic analysis to try to figure out how the Commission could have possibly come to such a conclusion while the Commission is telling elected officials that it is working hard to keep rate increases as low as possible.

Whatever the legal consequences of the Commission's failure to explain how it got from A to B to resolve the contested issues, the Commission owes customers a clear and auditable explanation of how and why the Commission's choices were made so decidedly in favor of outcomes that sequentially and excessively raise AEP-Ohio's electric prices.

II. The Commission's rate increase for ninety percent of AEP-Ohio's requested POLR revenue requirement is unjust, unreasonable and unlawful.

The Order states that the Commission **believes** that AEP-Ohio has some risks associated with customers switching to CRES providers and returning to the EDU's SSO rate. With this belief as its foundation, the Order then embraced AEP-Ohio's witness' quantification of risk to equal ninety percent of AEP-Ohio's hypothetical POLR costs. The Order states that AEP-Ohio may establish a rider to collect a POLR revenue requirement of $97.4 million for CSP and $54.8 million for OP (or ninety percent of the

POLR revenue requirement requested by AEP).[43] The Commission's authorization of AEP-Ohio to collect the POLR revenue requirement is unjust, unreasonable and unlawful for the following reasons.

1. AEP-Ohio did not demonstrate that it has any POLR risk.

2. Assuming for argument sake that AEP-Ohio does have POLR risk, AEP-Ohio did not demonstrate that it could not mitigate the risk through options.

3. Assuming for argument sake that AEP-Ohio does have POLR risk that cannot be mitigated, AEP-Ohio did not demonstrate that there is a change in its risk profile that merits substantially increasing rates for POLR.

4. Assuming for argument sake that AEP-Ohio has POLR risk that cannot be mitigated and there has been a change in the risk profile, there has been no demonstration that AEP-Ohio's estimate of the POLR revenue requirement is based on the prudently incurred cost of POLR or is otherwise reasonable and lawful.

5. The Commission has not provided any reasoning for its holding.[44]

As IEU-Ohio noted in its Reply Brief, AEP-Ohio currently participates in PJM.[45] Under the PJM rules, all suppliers with load serving responsibilities (including AEP-Ohio) must maintain adequate resources to reliably meet their customers' needs.[46] AEP-Ohio has elected to meet the capacity requirements as an FRR entity under the reliability pricing model ("RPM") or the capacity market inside of PJM.[47] AEP-Ohio has

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[43] Order at 40.

[44] As discussed above, Section 4903.09, Revised Code, requires the Commission to make a complete record in all contested cases heard by the Commission, including a written opinion setting forth the reasons prompting the decisions arrived at, based upon findings of fact.

[45] IEU-Ohio Reply Brief at 16.

[46] Tr. Vol. XI at 60-61.

[47] Tr. Vol. IX at 52; Tr. Vol. X at 61.

elected the FRR option for five years.[48] PJM's resource adequacy requirements and generating resource dispatch responsibilities have significance relative to AEP-Ohio's claims regarding risks associated with any default supplier obligations.

Specifically, all of AEP's available generating capacity is bid into the PJM market. In other words, AEP, acting on behalf of each of its operating companies including OP and CSP, offers the output of available generating units to PJM and it is up to PJM to determine what to do in response to these offers.[49] On any given day, the actual load presented by AEP-Ohio's customers could, in accordance with PJM's determinations, be served by generators other than those owned or operated by AEP.[50] Regardless of who actually owns the generation capacity, PJM will dispatch available generation capacity to serve load and maintain real-time reliability.[51] Moreover, even if AEP-Ohio did not own any generation at all, PJM would still dispatch generation in order to meet the needs of AEP-Ohio's customers.[52] By electing the FRR option for five years, AEP committed to being the sole load-serving entity for retail load within the AEP zone to meet the resource adequacy requirements specified by PJM. That means that AEP has committed to being responsible for meeting the reserve requirements even for retail

[48] Tr. Vol. X at 61.

[49] Tr. Vol. XI at 56-57, 65.

[50] Tr. Vol. XI at 58.

[51] Tr. Vol. XI at 59-60.

[52] Tr. Vol. XI at 59-60.

customers that elect to take service from a competitive retail electric service ("CRES") provider as if that customer remained a retail customer of AEP.[53]

Moreover, AEP receives benefits associated with its FRR election as opposed to participating in PJM's RPM auction process. For example, Staff witness Johnson indicated that there is a significantly large cost advantage as a result of the difference between RPM and FRR that could be as much as the difference between RPM and the depreciated book value of AEP's generating capacity.[54] Additionally, AEP has the opportunity to sell and has sold generating capacity into the other capacity market (RPM).[55] Once AEP has met the PJM requirements of its load times 1.155 to meet the PJM dictated reserve margin plus 450 megawatts, if AEP has capacity in excess of that amount, it may sell the next 1,300 megawatts into the RPM market.[56] When AEP has a capacity surplus within that bandwidth, it has sold the excess capacity into the market for a profit.[57]

In other words, AEP voluntarily assumed the risk of customer switching through its FRR election in PJM and is being adequately compensated through the PJM process with the option to do better through sales opportunities in the PJM markets. The Order allows AEP-Ohio to retain the full benefit of these sales even when the Order increases rates for costs associated with additional generating assets. Allowing AEP-Ohio to

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[53] Tr. Vol. XI at 61.

[54] Tr. Vol. XII at 186.

[55] Tr. Vol. XI at 63-64.

[56] Tr. Vol. XI at 63-65.

[57] Tr. Vol. XI at 64.

collect a POLR charge from customers provides AEP-Ohio and its parent with a windfall that is inconsistent with any definition of the type of regulatory action that might be motivated by the goal of keeping increases to the lowest amount possible.

For the sake of argument, even assuming that AEP-Ohio did have some POLR risk of customers migrating which it has not already voluntarily taken on and for which it is not already being compensated, AEP-Ohio did not demonstrate that it cannot mitigate the risk through various options, including obtaining agreements from customers to not switch during the ESP period. Throughout the hearing, AEP-Ohio referred to the POLR risk as a put (the risk of customers leaving AEP-Ohio's SSO) and a call (the risk of customers returning).[58] Further, based on the discredited Black-Scholes Model, AEP-Ohio indicated that "the majority of the value comes about as a result of the put part of the series of options; less of it is related to the call."[59] Despite this acknowledgment, AEP-Ohio said it has not determined whether it will actually purchase any options to cover the risk.[60] In fact, AEP-Ohio witness Baker did not even believe that its decision to cover the put risk through an option was relevant to the ESP – most likely because the proposed POLR charge more than covered any risk that AEP-Ohio could conceive.[61]

AEP-Ohio has the burden of proof. The Commission has said that it wants to keep rate increases as small as possible. Requesting a revenue requirement of nearly

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[58] *See*, for example, Tr. Vol. X at 211.

[59] *Id.*

[60] *Id.* at 211-212.

[61] *Id.* at 212.

$170 million based on the costs of an option that AEP-Ohio might never exercise without even requiring an examination of lower cost alternatives to cost-effective risk management is unjust and unreasonable. The Commission decision to give AEP-Ohio a revenue collection opportunity equal to ninety percent of AEP-Ohio's request has no redeeming qualities and is entirely inconsistent with any serious regulatory effort to keep rate increases as low as possible.

Even assuming for argument sake that AEP-Ohio has POLR risk that cannot be mitigated, AEP-Ohio did not demonstrate that there has been a change in its risk profile that necessitates a rate increase to compensate it for its actual POLR cost beyond what might already be embedded in current SSO rates.

The Commission authorized a POLR rider in AEP's rate stabilization plan ("RSP") case.[62] While SB 221 was enacted between the approval of AEP-Ohio's RSP and the time when AEP-Ohio filed its ESP application, nothing else has changed. AEP's witness Baker indicated wrongly that SB 221 enhanced AEP's POLR risk in two ways: 1) Mr. Baker incorrectly asserted that, without SB 221, AEP could have gone to market and would no longer have had the POLR obligation;[63] and, 2) SB 221 promoted governmental aggregation.

OP and CSP, as Ohio EDUs, had the obligation to provide default generation service prior to the enactment of SB 221, they would have carried the same legal obligation even had they gone to market-generation supply pricing under Amended

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[62] *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of a Post-Market Development Period Rate Stabilization Plan*, Case No. 04-169-EL-UNC, Opinion and Order at 27 (January 26, 2005).

[63] Tr. Vol. X at 219-220.

Substitute Senate Bill 3 ("SB 3"), and they continue to have the obligation post-SB 221 enactment. Moreover, governmental aggregation was created under SB 3, not SB 221. While Section 4928.20(K), Revised Code, now states: "The Commission shall adopt rules to encourage and promote large-scale government aggregation in the state," there are no specific provisions that enhance the legal authority of municipalities to aggregate as compared to those available prior to the enactment of SB 221. Moreover, the Companies did not conduct any studies to assess that risk and AEP-Ohio's witness Baker conceded that whether there will be any governmental aggregation is "very dependent on the future price of power in the wholesale market."[64]

Despite the facts, the record evidence, and the law, the Commission authorized AEP-Ohio to collect ninety percent of the POLR revenue requirement it requested. And remarkably, the Commission sanctioned the use of market price estimates of $88.15/MWH for CSP and $85.32/MWH for OP ($86.74 on average) to quantify the POLR-related revenue requirement for AEP-Ohio thereby picking an even higher market price than the excessively high market price that the Commission used for purposes of the ESP and MRO comparisons. For purposes of the ESP v. MRO comparison, the PUCO used excessively high market price values of $74.71/MWH for CSP and $73.59/MWH for OP.[65] The Commission has provided no explanation for why the unwarranted rate increase for POLR should be inflated even further by using an estimated market price that the Commission determined was too high. The Order's selective and inconsistent use of excessively high estimates of market prices cannot be

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[64] Tr. Vol. X at 221.

[65] Order at 72.

reconciled with an outcome that indicates that the Commission is working hard to keep rate increases as low as possible.

Finally, as discussed above, the Commission failed to provide reasons setting forth the decision to authorize AEP-Ohio to increase rates by over $100 million for a POLR obligation for risks that AEP-Ohio does not have except by its own choices and, in any event, for which it is already being compensated. The Commission's entire discussion of this issue[66] consists of the observation that "the Companies do have some risks associated with customers switching to CRES providers and returning to the electric utility's SSO rate at the conclusion of CRES contracts or during times of rising prices"[67] and an acceptance of the Companies' witness' "quantification of that risk to equal 90 percent of the estimated POLR costs."[68] There are no findings of fact connected to any conclusions of law.

Perhaps equally bad, the Order misapplies the few citations to record evidence it does offer while summarizing the parties' positions. For example, in describing AEP-Ohio's arguments for its proposed POLR revenue requirement level, the Commission indicates that, "Companies added that their current POLR charge is significantly below other Ohio electric utilities' POLR charges... ."[69] First, this reference is confusing at

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[66] The Commission devotes one paragraph to its discussion of its "consideration" of the reasonableness of this issue. Moreover, as noted above, the "Findings of Fact and Conclusions of Law" section of the Order, other than a list of procedural events, fails to include a single finding of fact and includes only that the "proposed ESP, as modified by this opinion and order, including its pricing and all other terms and conditions, including deferrals and future recovery of deferrals, is more favorable in the aggregate as compared to the expected results that would otherwise apply under Section 4928.142, Revised Code." Order at 73.

[67] Order at 40.

[68] Order at 40.

[69] Order at 38 (citing Cos. Ex. 2 at 8).

best, particularly since the Commission has approved an ESP for FirstEnergy that does not have a POLR charge. In fact, the stipulation and recommendation approved by the Commission in FirstEnergy's case states, "There shall be no minimum default service rider or standby charges as proposed by the Companies in their ESP filed on July 31, 2008 in Case No. 08-935-EL-SSO. There will be no rate stabilization charges ('RSC') starting June 1, 2009. Unless otherwise noted, all generation rates for the Stipulated ESP period are bypassable and there are no shopping credit caps."[70] Second, while the Commission seems to be using the claim of a relatively low POLR charge argument to justify its authorization, the reference cited in the Order does not support the conclusion. The PUCO reference is to AEP witness Baker's rebuttal testimony, which was limited to issues related to AEP's proposal for the interim period between January 1, 2009 and the time the Commission issued an Order – not the ESP period. Moreover, had the Commission read and applied the meaning of the very next sentence of the testimony, it would have realized that AEP conceded that "[i]n light of the very low level of the Companies' current POLR charges, both on an absolute basis and relative to Ohio's other electric distribution utilities, I believe that, as part of the interim ESP rate, the Companies' POLR charge should be increased to reflect half of the increase in POLR rates proposed by the Companies in their application." If half of what AEP-Ohio sought in its application would suffice, the Commission authorization of ninety percent of AEP-Ohio's request is even more unreasonable. Neither outcome can, of course, be reconciled with the goal of keeping increases as low as possible.

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[70] *FirstEnergy ESP Case*, Stipulation and Recommendation at 10 (February 19, 2009).

The unreasonableness of the Commission's authorization of the POLR charge becomes more clear when the impact of the increased POLR rider alone on customer bills is examined. For example, an industrial customer on rate schedule GS-4 using 6 million kWh per month paid a POLR charge of $2,827 per month to CSP prior to the implementation of the Commission's March 18, 2009 Order. As a result of the PUCO's effort to keep rate increases as low as possible, the same customer will now pay **$26,757 or about 10 times more per month** for the POLR charge alone. Similarly, a GS-4 customer of OP using 6 million kWh per month will see its POLR charge increase from $6,601 to **$12,913 per month**. In other words, the rates approved by the Commission (and according to simple typical bill analysis for an individual customer) allow for over $320,000 per year in POLR revenue to be collected by CSP and nearly $155,000 per year by OP based on hypothetical risks, a market price input variable that is laughably high and application of an economic model that has brought financial markets to their knees because of its unwarranted assumptions and manipulation potential. This is not the type of regulatory scrutiny that can be reconciled with the goal of keeping rate increases as low as possible.

III. The Commission's authorization of a rate increase for recovery of costs of ownership and other interests in generating assets is unjust, unreasonable, unlawful and unsupported by the evidence.

AEP-Ohio's ESP proposal requested authority to sell or transfer two recently-acquired generating facilities (Waterford Energy Center and the Darby Electric Generating Station). AEP-Ohio also stated that both Companies might sell or transfer their portion of the output entitlement in certain generating facilities of the Ohio Valley Electric Corporation ("OVEC") and that CSP's affiliate, AEP Generating Company, might

sell or transfer its ownership in the Lawrenceburg Generation Station (CSP has a contract for the entire output of this combined-cycle natural gas-powered plant).

IEU-Ohio and all other parties opposed AEP's request for authority to sell or transfer these assets until the Companies provide sufficient detail to permit evaluation on how the sale/transfer might serve to advance state policy.[71] The Commission agreed and held that AEP's requests are premature and AEP should file a separate application when it wishes to sell or transfer the generation facilities.[72]

However, without any reference to the law, the Commission held that AEP-Ohio may obtain recovery for the Ohio customers' jurisdictional share of any costs associated therewith, through the FAC and, to the extent not recovered in the FAC, through the non-FAC portion of the generation rate.[73]

The Commission's authorization to recover costs from Ohio customers runs afoul of the Commission's SB 221 authority and traditional ratemaking concepts. First and most importantly, as AEP-Ohio asserted throughout this proceeding, generation rates are no longer cost-based.[74] SB 221 provides the Commission with the alternative authority to establish pricing for competitive services and this alternative authority has been described as a hybrid. But SB 221 does not require the Commission to selectively

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[71] Moreover, IEU-Ohio pointed out that because the output of OVEC's generating units is priced based on a traditional cost of service model rather than market-based pricing (with average expected costs of $40 per MWH for 2008), it would be prudent for the Companies to use OVEC entitlement to meet Ohio customers' needs prior to resorting to market-based purchases.

[72] Order at 52.

[73] Order at 52. While the PUCO directed AEP-Ohio to adjust its ESP accordingly, it did not provide any procedural direction or indication of whether it would determine that AEP-Ohio's calculation of the jurisdictional share of the associated costs is reasonable or accurate.

[74] *See* AEP-Ohio Initial Brief at 15 (December 30, 2008). *See also* Tr. Vol. XI at 86-87.

increase rates (which are not based on costs) because the non-cost-based rates do not reflect a particular category of costs. The Commission cannot use traditional cost-based ratemaking selectively to increase rates where it believes particular categories of generation costs are not currently reflected in rates. Even if legally permissible to do so, once an analysis starts with non-cost-based rates, it is not possible to say what particular costs are adequately covered or not covered by the revenue available from the non-cost-based rates.

Even if default generation supply service was priced pursuant to traditional ratemaking concepts, as IEU-Ohio explained in its briefs, the traditional ratemaking process does not track costs by individual category; it produces a regulatory authorization to collect revenue through the application of rates and charges to the service provided by the utility. Once the ratemaking process has produced authority to bill and collect revenue for service, the rates and resulting revenue are presumed to be reasonable (for both the utility and customers).[75] A party seeking to increase the total revenue has the burden of proof and this allocation of the burden of proof is repeated in Section 4928.143(C), Revised Code.

A showing that a particular category of costs is not currently reflected in rates may be, circumstantially speaking, some indication that current rates and revenue may not provide adequate compensation, but it is not proof that current rates and charges and the revenue derived therefrom are inadequate or unreasonable.

Also, while the Commission has effectively shifted cost responsibility to AEP's Ohio customers by increasing rates, the Commission appears to have not given

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[75] Section 4909.03, Revised Code. *See* IEU-Ohio's cross-examination of Mr. Cahaan at Tr. Vol. XII at 221-222.

customers credit for purposes of calculating the POLR charge discussed above. If the costs of these generating assets are being recovered through rates, customers should receive credit for the functional performance of the assets.

Finally, while the Commission directed AEP-Ohio to adjust its ESP accordingly, it did not provide any procedural direction or indication of whether it would determine that AEP-Ohio's calculation of the jurisdictional share of the associated costs is reasonable or accurate.

For these reasons and for the Commission's failure to provide its reasoning as described above, allowing AEP-Ohio to modify its ESP to increase rates selectively for costs associated with the above-mentioned generating assets is unjust, unreasonable and unlawful.

IV. The Commission's selective distribution rate increases for gridSMART and a service reliability plan are unjust, unreasonable and unlawful.

AEP-Ohio requested automatic distribution rate increases of 7 percent for CSP and 6.5 percent for OP. The meager explanation which AEP-Ohio offered in support of these automatic distribution rate increases includes vague references to illusory plans to implement an enhanced service reliability proposal ("ESRP") and a gridSMART proposal that were strongly opposed. The Order's conclusions indicate that the Commission agreed with most parties' arguments (including IEU-Ohio); distribution service elements would be better addressed in a traditional distribution rate case where the Commission could consider all revenue and expense categories.[76] But despite this holding, the Order proceeds to approve distribution rate increases for the mysterious

[76] Order at 32.

gridSMART and service reliability plans. More specifically, the Order approves rate increases to recover gridSMART expenditures of $54.5 million, with initial recovery through a rider of $33.6 million of projected costs (not actually incurred costs), subject to annual true-up and reconciliation.[77]

In addition to the gridSMART rate increase, the Commission increased rates for projected incremental costs associated with a vegetation management program which may or may not improve service reliability.[78]

But, there is absolutely no basis in the record evidence or law for the Commission's approval of these distribution rate increases. Notwithstanding provisions in SB 221 that require the Commission to ensure that costs passed on to customers are prudent, actually incurred and that customers should only be responsible for the costs based on the benefits they will derive, the PUCO approved these distribution rate increases with little regard for the speculative character of the plans and programs.

The Order's rate increases for these two distribution initiatives (gridSMART and the ESRP) provide another example of how the Commission strayed from the goal of keeping rate increases as low as possible.

While the language in the Order indicates that the Commission rejected AEP-Ohio's automatic distribution-related rate increase request and was selectively limiting AEP-Ohio to recovery of two parts of its total distribution plan, the Order's bottom line (as measured by AEP-Ohio's compliance tariffs) essentially produces a distribution rate

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[77] Order at 38.

[78] Order at 34. The estimated incremental revenue requirements for each year of the three-year ESP are $17.5, $4.3 and $1.7 million for CSP and $17.3, $1.9 and $1.9 million for OP.

increase in 2009 that is worse for customers than AEP-Ohio's proposal would have produced in 2009. Based on the compliance tariffs filed for CSP, which the Commission allowed to go into effect over the objections of customers, the combination of the gridSMART and vegetation management cost recovery riders produces a distribution rate increase of 7.28531 percent, which exceeds AEP-Ohio's requested distribution rate increase for 2009. In the case of OP, the compliance tariffs reflect an increase of 7.46876 percent in distribution rates. So on its way to rejecting AEP-Ohio's proposed 7 and 6.5 percent automatic annual distribution rate increases, the Order increased distribution rates in 2009 by more than the level proposed by AEP-Ohio.

For these reasons and because the Commission failed to provide reasoning for its conclusions as discussed above, the Commission's approval of the distribution rate increases is unjust, unreasonable and unlawful.

V. The Commission's failure to require AEP-Ohio to limit the total bill increases to the percentage amounts specified in the Order is unjust, unlawful and unreasonable and the Commission must immediately require AEP-Ohio to comply with the Order and to refund amounts billed and collected in excess of such caps.

The Commission's Order states that an increase in excess of 15 percent would, during this difficult economic climate, impose a severe hardship on customers and that a 15 percent cap is too high.[79] The Order states that AEP-Ohio must observe a limit on increases during 2009 of 7 percent of the total bill for CSP customers and 8 percent of the total bill for OP customers.[80] Yet, and as the Commission well knows, the rates that the Commission permitted AEP-Ohio to begin charging over the objections of customers

[79] *Id.* at 22.

[80] *Id.*

produce actual total bill increases substantially in excess of the total bill caps established by the Commission. In some cases, the actual total bill increases in 2009 will be above the 15 percent level that the Commission said would cause severe hardship. In all cases, the actual increases are well above the "virtually no increase" expectation which Chairman Schriber created in his recent testimony before the General Assembly.

Despite being informed of this problem (the mismatch between the total bill cap established by the Commission and actual, much larger, increases produced by the compliance tariffs submitted by AEP-Ohio), the Commission did nothing to correct this problem before AEP-Ohio's rates were allowed to go into effect. The Commission's failure to require AEP-Ohio to limit the total bill increases to the caps specified in the Order is unjust, unlawful and unreasonable and cannot be reconciled with the goal of keeping rate increases as low as possible.

VI. The Commission's conclusion that the ESP is more beneficial in the aggregate than the alternative under Section 4928.142, Revised Code, is unjust, unreasonable, unlawful and unsupported by the evidence.

As discussed above, the Order concludes that the ESP manufactured in the Order is more favorable than the alternative under Section 4928.142, Revised Code (MRO).[81] While the Order itself offers little useful insight on just how this comparison was framed, the Order work papers (summary sheet attached hereto as Attachment B) indicate that the "market price" information relied upon by the Commission is the same information that was included with Staff witness Johnson's testimony. Staff witness

[81] *Id.* at 72.

Johnson testified that his market price estimate (about $74 per MWH) was at the high end of the range which he developed (but did not proactively disclose) when he prepared his testimony. He agreed that market prices continued to fall after he prepared his testimony.[82]

Since the close of the record in this proceeding, it is common knowledge that the wholesale price of electricity has continued to plunge; a condition that would likely be of interest to a regulator on a mission to keep rate increases as small as possible.

If there is any doubt about the unreasonably high market price that was embedded in the ESP v. MRO comparison, the Commission need look no further than its decision in another recent ESP case. More specifically, the market price the Commission appears to have used for the MRO v. ESP comparison in the AEP-Ohio case is almost identical to the average generation price of $75 per MWH which the Commission found to be excessive (by almost $8 per MWH) in the December 19, 2008 Opinion and Order modifying the ESP proposed in the *FirstEnergy ESP Case*.[83]

Further, information which AEP presented to the public and the financial community shows that the doubt must be resolved against the conclusion reached but not explained in the Order. Page 6 of IEU-Ohio Exhibit 6, AEP's presentation slides from a conference that took place in November 2008, shows the sharp decline in electricity market prices (for 2009 delivery).

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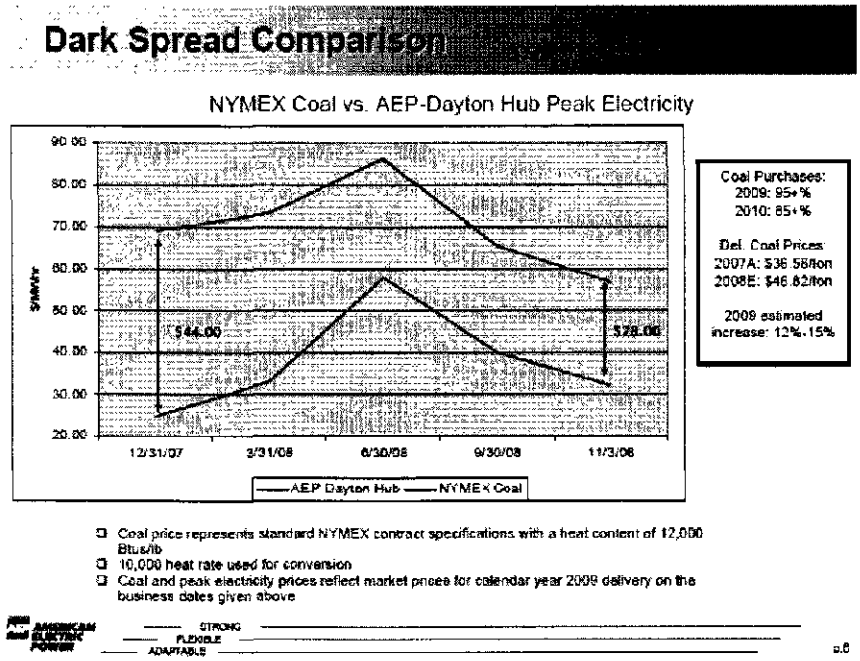
[82] Tr. Vol. XII at 182, 187; Staff Exhibit 9 at 6.

[83] *FirstEnergy ESP Case* at 69.



The Order work paper (attached hereto as Attachment B) indicates that the MRO scenario included a generation-related revenue requirement based on the maximum blending percentages allowed by Section 4928.142, Revised Code, thereby using a worst case MRO assumption to show an ESP advantage. The Commission did this even after the General Assembly amended Section 4928.143, Revised Code, to make it absolutely unmistakably clear that the blending percentages that were used for purposes of the Order were **not** required. If the Commission was interested in keeping rate increases as low as possible, why would it assume that the MRO alternative scenario would be based on the maximum amount of wholesale market purchases permitted by law? Why did the Commission seek to obtain legislative authority to adjust the blending percentages if it does not intend to use the authority to mitigate rate increases on customers?

The same work paper shows that the MRO scenario relied upon by the Commission included $366 million in "cost" for POLR even though POLR as proposed

by AEP-Ohio and approved by the PUCO is a distribution charge and even though there is nothing in Section 4928.142, Revised Code, that even hints that the PUCO has authority to approve a POLR charge in a Section 4928.142, Revised Code, proceeding.

Rather than reasoned decision-making on the MRO v. ESP comparison issues, the Order contains a naked conclusion that appears to be based on the highest market price the Staff could come up with when the Staff prepared its testimony, a market price that is nearly $8 per MWH higher than the Commission found to be appropriate for purposes of conducting the same test in the *FirstEnergy ESP Case* and the Commission's self-imposed blindness to the fact that the forward market price of electricity has steadily declined since SB 221 became effective. In other words, the Order suggests that the Commission's decision was not reasonably balanced but tilted to produce an outcome that unreasonably favors AEP-Ohio, prejudices customers and ignores the commands of the General Assembly.

The Order's comparison of the MRO and ESP is unreasonable and unlawful.

VII. The Commission's unbundling of the non-fuel and fuel component of the generation rate based on something other than 2008 actual fuel costs is unjust and unreasonable.

CSP and OP proposed an ESP pursuant to Section 4928,143, Revised Code, that included the establishment of an automatic adjustment mechanism (referred to as the fuel adjustment clause or "FAC") to recover the cost of fuel, non-fuel items, fixed costs and variable costs. Despite its significance, AEP-Ohio's proposal was accompanied by little detail.

To evaluate and potentially implement this proposal, it is necessary to unbundle the FAC and non-FAC portions of the current retail electric generation price and

determine what level of FAC costs should be attributed to the currently bundled retail electric service generation price. The required unbundling was complicated in this case by a lack of detail on just what AEP-Ohio was seeking in the way of relief. As Ms. Smith testified, AEP-Ohio's proposal was not accompanied by a "fully fleshed out FAC tariff."[84]

In this context, the Order rejected the use of 2008 actual fuel costs as a basis for setting a baseline to separate the FAC and non-FAC components of current rates. The recommendation to use the 2008 actual costs was designed to make sure that the FAC baseline value was not too low and the non-FAC rate set too high.[85] The Order indicates a decision was made to not use actual 2008 costs, saying that actual costs were not known at the time of the hearing even though the Order itself was issued well after the hearing concluded. Rather than use actual 2008 prudently incurred cost levels as a basis for separating or unbundling the FAC and non-FAC rate elements, the Order is based on the use of a proxy that is not authorized by Section 4928.143, Revised Code.

Regardless of what was known at the time of the hearing, the Commission could have nonetheless found in favor of the methodology that set the baseline based on 2008 actual prudently incurred costs and required AEP-Ohio to observe this requirement for purposes of developing compliance tariffs or rate schedules. Since 2008 actual fuel costs are now known, since they are significantly higher than the "proxy" adopted by the Commission, and since the "proxy" is, by definition, not the prudently incurred costs authorized in Section 4928.143(B)(2)(a), Revised Code, the

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[84] Tr. Vol. VI at 79; OCC Exhibit 9 at 31.

[85] *Id.* at 19.

Order results in the non-FAC portion of rates being too high and the risk of future increases in the FAC portion, as well as the amount of deferrals, too great. The Commission's failure to use actual prudently incurred costs as the basis to unbundle the FAC and non-FAC rate elements is not consistent with the goal of minimizing rate increases and is otherwise unreasonable, unjust and unlawful.

In public presentations during 2008 and 2009, AEP indicated that its average price of coal delivered in 2007 was $36.58/ton, while its 2008 cost was reported to be $46.61/ton; a 27.4 percent increase over 2007. These data indicate that the Staff proxy for determining the 2008 baseline FAC costs produced a baseline FAC cost that was too low. Similarly, actual results for 2008, as reported in the SEC 10K Report, indicate that OP had a $148 million increase in fuel and consumables compared to 2007, and that CSP had a $65 million increase in fuel, allowance, and consumables expenses in 2008. Based on the 3 percent escalation that Staff applied to CSP's 2007 FAC costs and the 7 percent escalation applied to OP's 2007 FAC costs to arrive at its 2008 proxy, the proxy baseline FAC costs are understated by tens of millions of dollars, whether the 2008 SEC actual data are used or the Commission uses the 2008 actual data otherwise publically reported by AEP.

Now that AEP-Ohio's books have been closed for 2008 and the actual fuel costs are known, it would have been straightforward and lawful to require AEP-Ohio to unbundle its FAC and non-FAC rate elements based on these actual costs as was recommended during the litigation phase of this proceeding. There is no good reason for the PUCO to unbundle the FAC and non-FAC rate components based on a proxy

when the actual costs are readily available. Using a proxy in this context is not consistent with the goal of keeping rate increases as small as possible.

VIII. The scope of the fuel and other cost recovery mechanism authorized by the Commission is unreasonable, unlawful and unjust both because of the types of costs that are subject to recovery through the mechanism and the substantial negative effect that the kWh-based mechanism has upon larger, high load factor customers.

AEP-Ohio's proposed FAC mechanism made it clear that the proposed FAC included costs related to much more than the costs of fuel consumed to produce electricity; the costs which were historically subject to recovery through the Electric Fuel Component ("EFC") rate.[86] As the Commission knows, the EFC was established by rule (Chapter 4901:1-11, O.A.C.) for uniform application to all electric utilities.[87] Under Rule 4901:1-11-1(O), O.A.C., "fuel costs" were defined as the "... actual acquisition and delivery costs of fuel consumed, including the amortized costs of nuclear fuel expended, to generate electricity, unless otherwise provided in this chapter." But the opportunity to use the EFC to recover costs through an active adjustment clause came with obligations and a defined process by which compliance could be audited and evaluated by the Commission.

The EFC mechanism was also predicated on the Commission's ability to regulate the operation of the utility's generating units. For example, Rule 4901:1-11-02(A), Ohio

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[86] OCC Exhibit 11 at 20. These additional elements comprise 21 percent of CSP's and 11 percent of OP's estimated FAC.

[87] In 1998, the Commission completed its periodic review of Chapter 4901:1-11, Ohio Administrative Code, as required by Section 119.032(B), Revised Code, in Case No. 98-967-EL-ORD, concluding that no amendments to the rule were necessary. For purposes of this Brief, IEU-Ohio's citations to the EFC rule are citations to the rule attached to the Commission's July 2, 1998 Entry in Case No. 98-967-EL-ORD, which was the version of the rule in place when the EFC was eliminated by Ohio's electric restructuring legislation.

Administrative Code, required an electric utility to "... procure fuel, purchase power, and operate its generation, dispatch, transmission, and distribution systems at a ***minimum overall cost***, taking into consideration its voltage, frequency, reliability, safety, environmental, and service quality requirements, as well as its existing contractual obligations." (emphasis added). And, Rule 4901:1-11-02(B), Ohio Administrative Code, required an electric utility to "... operate on an economic dispatch basis."

AEP-Ohio's FAC proposal was focused exclusively on obtaining authority to automatically adjust rates to recover a broad range of costs. AEP-Ohio did not propose to take on the obligations that have been historically part of a fuel adjustment clause, including the obligation to operate generation, transmission and distribution systems for the benefit of its retail customers subject to the regulatory oversight of the Commission. Therefore, AEP-Ohio's proposal was fundamentally unbalanced. For this reason alone, IEU-Ohio urged the Commission to not give AEP-Ohio authority to implement the proposed FAC. The Order indicates that IEU-Ohio's concerns were ignored.

As explained above, AEP-Ohio's FAC proposal included a broad range of costs[88] that were not previously recoverable under the Commission's EFC rule.[89] For example, AEP-Ohio's FAC proposal included the ability to recover demand and capacity-related costs that were not subject to recovery through the Commission's EFC rule.[90] Recovery of these costs through the FAC results in capacity or demand-related costs being

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[88] Tr. Vol. IV at 249-252.

[89] OCC Exhibit 11 at 20.

[90] Tr. Vol. IV at 249-257; Tr. Vol. VI at 203-204; § 4901:1-11-04(D), Ohio Admin. Code; *See In Re the Electric Fuel Component of Ohio Power Company and Columbus Southern Power,* Case Nos. 98-101-EL-EFC and 98-102-EL-EFC, Opinion and Order (May 26, 1999).

allocated and recovered from customers on an energy or kilowatt-hour ("kWh") basis.[91] As Mr. Gorman explained, "... the Company's proposal to recover non-variable [or fixed] costs through the FAC, is inappropriate for several reasons."[92] Recovery of fixed, capacity or demand-related costs on a volumetric or kWh basis also conflicts with the long-standing precedent of the Commission.[93]

AEP-Ohio's FAC proposal was designed to make the FAC play a "catch all" role which partly explains its broad scope. For example, the proposed FAC is where AEP-Ohio proposed to recover the "slice-of-system" costs and the FAC approved by the Commission appears to allow for inclusion of a portion of the costs associated with interests in generating assets that AEP-Ohio asked for authority to transfer while not having any plans to do so. While the Commission Staff provided some support for the scope of the Companies' proposed FAC, Mr. Strom made it clear that the scope of the proposed FAC should only be approved if the costs to be recovered through the FAC are not being recovered someplace else.[94] Unfortunately, the evidence does not

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[91] Tr. Vol. IV at 257; Tr. Vol. V at 204.

[92] Commercial Group Exhibit 1 at 4.

[93] *In the Matter of the Complaint and Appeal of Columbia Gas of Ohio, Inc., from Ordinance No. 1192-76, of Columbus, Ohio, on July 19, 1976, to continue the Presently Established Schedules of Rates Being charged by Columbia Gas of Ohio, Inc., for Gas Service in the City of Columbus, Ohio, until August 1, 1978,* Case No. 76-704-GA-CMR, Opinion and Order at 7 (June 29, 1977); *In the Matter of the Application of Columbus Southern Power Company to Adjust its Power Acquisition Rider Pursuant to its Post-Market Development Period Rate Stabilization Plan*, Case No. 07-333-EL-UNC, Application for Rehearing by the Office of the Ohio Consumers' Counsel and Ohio Partners for Affordable Energy at 7-8, 10, 17-18 (July 27, 2007); *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Approval of a Market Rate Offer*, Case No 08-936-EL-SSO, Opinion and Order at 22-24 (November 25, 2008), subject to application for rehearing); *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Authority to Establish a Standard Service Offer Pursuant to Section 4928.143, Revised Code in the Form of an Electric Security Plan*, Case No 08-935-EL-SSO, Opinion and Order at 19-23 (December 19, 2008).

[94] Staff Exhibit 8 at 3.

include a showing that current revenues are inadequate to provide compensation for any of the costs subject to collection through the FAC. As Mr. Cahaan testified, OP and CSP were obviously recovering their fuel costs (which he defined to include purchased power) in 2007 or their earnings would have been insufficient.[95]

Beyond the question of where the FAC and non-FAC line drawing should take place for purposes of unbundling the existing rates, there is no basis in law or fact for the PUCO to approve an FAC with the scope identified in the Order. The scope of the FAC is unreasonable and unlawful. In addition, and regardless of the scope of the FAC, the use of a kWh-driven FAC mechanism to recover fixed and demand-related costs is unreasonable, unjust and unlawful based on Commission precedent. Also, recovery of demand and fixed cost through a kWh-based collection mechanism may be playing a role in creating the large mismatch that larger customers are observing as they compare the actual total bill increase to the total bill increase caps identified in the Commission's Order. In any event, the scope of the FAC described in the Commission's Order and the kWh allocation of fixed and demand-related costs through the FAC cannot be reconciled with the goal of keeping rate increases as low as possible or providing customers with predictable rates.

IX. The Commission's determination that interruptible load may not be counted towards OP's and CSP's determination of their peak demand response compliance requirements is unjust, unreasonable and unlawful.

Without a single reference to the record or any reasoning whatsoever, the Commission held that it "agrees with the Staff and OCEA that interruptible load should

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[95] Staff Exhibit 10 at 3.

not be counted in the Companies' determination of its EE/PDR [energy efficiency and peak demand response] compliance requirements unless and until the load is actually interrupted."[96] The lack of reasoning extends further to Staff's and the Ohio Consumer and Environmental Advocates' ("OCEA") positions, apparently relied upon by the Commission. Specifically, the extent of Staff's discussion on the topic can be found in the testimony of Greg Scheck and is limited to the following question and answer:

> Q. What is the Staff's view with respect to crediting AEP Ohio's distribution utilities interruptible programs towards the annual peak demand reduction targets?
>
> A. Staff believes that such reductions must actually occur and be measured retrospectively in order to receive such credit.[97]

Similarly, OCEA's discussion on this matter suffers from the same lack of reasoning, justification and record evidence. Specifically, on brief OCEA argued that counting interruptible load that has not actually been interrupted is contrary to SB 221, which mandates a peak reduction program "in order to improve the reliability of the grid"; "would provide a false representation of the grid's reliability, and thus would thwart the objectives of S.B. 221"; and, because customers are able to control part of the load when non-mandatory reductions are requested, it should not be counted.[98] OCEA's arguments are contrary to the record evidence in the case and common sense.

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[96] Order at 46.

[97] Staff Exhibit 3 at 11. Moreover, the discussion of this issue in Staff's brief is limited to the following sentence: "But Staff does not recommend any credits being given towards the annual peak demand reduction targets for the Companies' interruptible programs unless reductions actually occur." Brief at 19 (citing Staff Exhibit 3 at 11).

[98] Initial Brief of Ohio Consumer and Environmental Advocates at 104 (December 30, 2008).

First, as Staff witness Scheck conceded, Section 4928.66(A)(1)(b), Revised Code, requires the Companies to implement peak demand reduction programs ***designed to achieve*** a one percent reduction in peak demand in 2009. Mr. Scheck acknowledged that a requirement to implement programs "designed to achieve" a reduction is different from a requirement to achieve a one percent reduction in peak demand.[99] Moreover, as the Companies explained, interruptible service arrangements provide an on-system capability to satisfy reliability and efficiency objectives as part of a larger planning process.[100] As the record shows, the interruptible load of customers can be and have been used to meet resource obligations established by RTOs regardless of the actual duration and frequency of interruptions.[101] Thus, the goals of SB 221 are not thwarted, but rather are furthered by interruptible programs.

OCEA's argument that, because customers control whether they buy-through a non-mandatory interruptible event, it should not count as a utility program, is unreasonable at best. Section 4928.66(2)(c), Revised Code, specifically encourages the use of mercantile demand response programs by reducing the EDU's baseline for calculating compliance with the law to exclude the effects of all such peak demand reduction programs so long as the customer commits the capability for integration into the Companies' portfolio. These customer-sited programs are clearly controlled by the customers as they are designed and completed by customers and customers choose to commit them to the EDU's portfolio. Thus, the General Assembly clearly signaled that

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[99] Tr. Vol. VIII at 208.

[100] AEP Brief at 112-115.

[101] Tr. Vol. IX at 53.

such customer-controlled programs should be counted towards the EDUs' portfolio obligations. The buy-through opportunity, if any, only gives an interruptible customer the option to obtain an alternative supply and pay market-based prices for the alternative supply if an alternative supply is available.

Finally, as IEU-Ohio noted on brief, the Commission's holding that interruptible capacity be counted only if it is actually interrupted will require the Companies to offer programs inferior to those available from RTOs and ultimately work against the type of resource planning that can provide reliability and price benefits for all customers.

The Commission's holding, coupled with its lack of reasoning, demonstrates that the Commission did not weigh the evidence or consider the result of its holding on ultimate customers. For these reasons, the Commission should reverse its determination that interruptible load may not be counted towards OP's and CSP's peak demand response compliance requirements.

X. The combined effect of the unexplained conclusions in the Commission's Order is unreasonable, unjust and unlawful because the Commission arbitrarily and capriciously exercised its discretion to allow CSP and OP to bill and collect excessive rates.

IEU-Ohio believes the Order is in error for each of the reasons described above. But even if each individual error might be regarded as forgivable based on the objective of keeping rate increases as low as possible or the requirements of Ohio law, the collective weight of the errors makes the Order unreasonable, unjust and unlawful. The goal of keeping rate increases as low as possible cannot be reconciled with the combined choices the Commission made to allow AEP-Ohio to bill and collect the surprisingly large rate increases that are showing up in customers' bills. And, with all

the regulatory emphasis on stable and predictable bills, the Order effectively leaves customers guessing about what their rates will be in 2010, just a few months from now.

XI. Conclusion

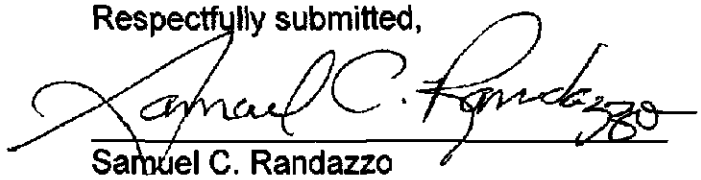
The Commission's Order unreasonably, unjustly and unlawfully sanctions rate increases that, in the aggregate, will cause AEP-Ohio customers to pay AEP-Ohio an additional $1.5 billion over the three-year ESP period and sets in motion obligations on the part of customers to pay non-bypassable charges for six years thereafter. The bottom line conclusions that appear in, or can be attributed to, the Order, cannot be reconciled with the goal of keeping rate increases as low as possible or with the letter and spirit of Ohio law.

On the simplest level of analysis, the total bill limitation on the amount of the 2009 rate increase produced by the Order has been ignored by AEP-Ohio in developing the rates that it is presently billing and collecting under the Commission's supervision. And, the total bill increase limitation is being ignored in ways that produce increases that the Commission found would result in an unacceptable hardship on customers who have been hard hit by conditions in the general economy.

For the reasons contained herein, IEU-Ohio urges the Commission to grant rehearing and, on an immediate and interim basis, order AEP-Ohio to revise its rates so that no rate schedule is subject to a greater total bill increase than the total bill increase limitation percentage specified in the Order computed based on the rates and charges in effect prior to the March 18, 2009 Order and make AEP-Ohio's collection of any increase subject to refund. By these actions, the Commission can begin to correct the

mismatch between what the Commission has said and what the Commission has actually done to fix the electric rates and charges paid by the customers of AEP-Ohio.

Respectfully submitted,



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HB 61 ESTATE TAXES (Hottinger, Grossman) To reduce the estate tax by increasing the credit amount, to authorize townships and municipal corporations, or electors thereof by initiative, to exempt from the estate tax and any estate property located in the township or municipal corporation, and to distribute all estate tax revenue originating in a township or municipal corporation that does not exempt property from the tax to the township or municipal corporation. Full Text

COMMITTEE HEARING

Finance & Appropriations: Agriculture & Development Sub.

Alan Schriber, chairman of the Public Utilities Commission of Ohio, testified in support of the executive proposal for the utility regulating body.

While he noted that the PUCO is funded through assessments on utilities and not the general revenue fund, he said the commission's operations are not free. Given that, he said, the agency strives to work as efficiently as possible.

The chairman said the commission does occasionally help generate money for the state, on the occasion that it issues civil fines against regulated companies. He said commission fines over the last two years delivered about $7 million to the general revenue fund.

The chairman said the agency has spent a significant amount of time over the last year implementing the state's new electric law, a process that he said is nearing completion. "It's been a significant drain on our resources," he said.

Mr. Schriber said the commission continues to field consumer calls and concerns, and also processes formal complaint proceedings. In an era with more competition in the telecom industry, he noted that the PUCO has also seen an increase in complaints filed by one company against another.

He also noted that the commission recently revised guidelines for programs involving low-income consumers, and said commissioners are sensitive to the current economic conditions.

"The ordinary citizen feels like they're taking in on the chin" with utility costs, Rep. Yates observed.

Mr. Schriber said the commission has heard those sentiments in its public hearings on the electric rate plans. "We are very intent, in this day and age, to mitigate rate increases," he said, adding that the commission's goal, for the time being, is to have virtually no increase in utility rates.

"I think we're doing a pretty decent job this year of doing that," he said. "This is not the year when you want to increase rates. There is no question that, over time, rates are going to go up."

Rep. Yates said it is his sense that consumers feel their positions are not considered.

Rep. Goodwin advised the chairman that there's a perception that the PUCO is run by the utilities.

Mr. Schriber said the commission tries to balance the needs of consumers and utilities. "Nobody likes the utilities," he said, adding that it is difficult to convince Ohioans that commission actions are in the best interest of the state. "We don't make friends anywhere."

The chairman also offered a brief run-down on the status of electric companies' rate plans under the new law, and expressed concern about private company water rates that are increasing. "It needs to be addressed," he said.

	Columbus Southern Power Company				Ohio Power Company			
	2009	2010	2011	Total	2009	2010	2011	Total
Estimated Cost of Market Rate Option								
MWH Load to be Purchased under 10%/20%/30% MRO	2,271,512	4,543,023	6,814,535		2,815,095	5,630,189	8,445,284	
Estimated Market Price ($/MWH)	$74.71	$74.71	$74.71		$73.59	$73.59	$73.59	
Estimated Purchase Cost of 10%/20%/30%	$170	$339	$509	$1,018	$207	$414	$622	$1,243
2001 - 2008 Incremental Environmental (90%/80%/70%)	$23	$21	$18	$62	$76	$67	$59	$202
POLR (90%/80%/70%)	$88	$78	$68	$234	$49	$44	$38	$132
Estimated Cost of 10%/20%/30% Market Rate Option	**$281**	**$438**	**$596**	**$1,314**	**$332**	**$525**	**$719**	**$1,576**
Estimated Cost of Companies' ESP								
SSO Cost 10%/20%/30%	$108	$216	$325	$649	$106	$212	$318	$636
2001 - 2008 Incremental Environmental	$26	$26	$26	$78	$84	$84	$84	$252
POLR	$97	$97	$97	$292	$55	$55	$55	$164
Annual 1.5%/3.5% non-FAC Increase	$0	$0	$0	$0	$0	$0	$0	$0
Generation Assets	$67	$67	$67	$200	$54	$54	$54	$161
Annual Distribution Increase	$43	$21	$22	$85	$17	$19	$21	$58
Economic Development Contribution	$0	$0	$0	$0	$0	$0	$0	$0
Estimated Cost of Companies' ESP	$341	$427	$536	$1,304	$316	$424	$532	$1,271
Estimated Benefit of Companies' ESP	**($60)**	**$11**	**$59**	**$10**	**$16**	**$102**	**$187**	**$305**

Attachment B
EXHIBIT JEH-1

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing *APPLICATION FOR REHEARING AND MEMORANDUM IN SUPPORT OF INDUSTRIAL ENERGY USERS-OHIO* was served upon the following parties of record this 16th day of April 2009, *via* electronic transmission, hand-delivery or first class mail, postage prepaid.

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