BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

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

INITIAL POST-HEARING BRIEF BY THE OFFICE OF THE OHIO CONSUMERS' COUNSEL AND THE APPALACHIAN PEACE AND JUSTICE NETWORK

BRUCE J. WESTON
CONSUMERS' COUNSEL

Maureen R. Grady, Counsel of Record
Terry L. Etter
Joseph P. Serio
Assistant Consumers' Counsel
Office of the Ohio Consumers' Counsel
10 West Broad Street, Suite 1800
Columbus, Ohio 43215-3485
(614) 466-9567 – Grady
(614) 466-7964 – Etter
(614) 466-9565 – Serio
grady@occ.state.oh.us
etter@occ.state.oh.us
serio@occ.state.oh.us

Michael Smalz
Joseph V. Maskovyak
Ohio Poverty Law Center
555 Buttles Avenue
Columbus, Ohio 43215
Telephone: 614-221-7201
msmalz@ohiopovertylaw.org
jmaskovyak@ohiopovertylaw.org

On Behalf of the Appalachian Peace and Justice Network

June 29, 2012

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I. INTRODUCTION

In the above-captioned proceedings, Columbus Southern Power Company ("CSP") and Ohio Power Company ("OP") (collectively, "AEP Ohio" or "Companies") seek approval of a modified version of their second standard service offer ("SSO") which takes the form of a modified Electric Security Plan ("ESP"). The Office of the Ohio Consumers' Counsel ("OCC"), on behalf of AEP Ohio's 1.2 million residential utility customers, and the Appalachian Peace and Justice Network ("APJN"), a not for profit organization whose members include low-income customers in southeast Ohio, (collectively, "Residential Consumer Advocates") jointly submit their Initial Post-Hearing Brief with recommendations to protect customers from hundreds of millions of dollars in proposed rate increases.

The Residential Consumer Advocates urge the Public Utilities Commission of Ohio ("PUCO" or "Commission") to reject AEP Ohio's Modified ESP. As discussed herein, the Modified ESP is not more favorable in the aggregate than a market rate offer ("MRO"), and thus fails the General Assembly's test for evaluating ESPs under R.C. 4928.143(C)(1). Quantitatively, the Modified ESP is less favorable than an MRO by at least $552.3 million.[1]

Qualitatively, the major benefit of the Modified ESP touted by AEP Ohio -- a quicker move to market rates required under Ohio law[2] -- is a benefit that may or may not result in reduced electricity rates. Moreover, during the term of the ESP, only those customers who shop will experience the benefits of moving to market rates. SSO service for non-shopping customers during the majority of the term of the ESP will not be market based. These non-shopping customers are primarily residential customers.

Given that the great majority of residential customers are not shopping in the AEP Ohio service area and thus will not receive the benefit of market rates under AEP Ohio's Modified ESP, the Commission should overcome this deficiency by ordering modifications to the Companies' proposed ESP that will result in a reasonably priced standard service offer, in keeping with R.C. 4928.02(A). This approach means that, among other things, customers' base generation rates should not be burdened with excessive charges such as the Companies' proposed Retail Stability Rider ("RSR"). In order to ensure that AEP Ohio's customers receive adequate service at reasonable rates,[3] the Commission should reject the Modified ESP.

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[1] See OCC Ex. No. 114 at 22. (Hixon).

[2] Companies' Ex. No. 119 at 1. (Dias Supplemental).

[3] R.C. 4905.22.

II. BACKGROUND

This is in essence the third iteration of the Companies' second ESP. The Companies filed their original application in these proceedings on January 27, 2011. That proposal included significant base rate increases and numerous riders, including several that were "placeholder" riders, which would have no initial rate but could (and in some cases, would) add to the rates customers would pay during the term of the ESP.

During the pendency of that application, negotiations took place among the Companies, intervenors and the PUCO Staff aimed at settling the case. The result was a Stipulation and Recommendation ("Stipulation") that was docketed at the Commission on September 7, 2011. The Stipulation -- which the Residential Consumer Advocates declined to sign -- was ostensibly designed to provide a "glide path" to competition in the Companies' service territories. As the Residential Consumer Advocates pointed out in testimony and on brief,[4] however, the rate increases and several other provisions of the Stipulation did not benefit customers, were not in the public interest and violated several regulatory principles. The Residential Consumer Advocates urged the Commission to reject the Stipulation.

Nevertheless, the Commission originally approved the Stipulation, with modifications, on December 14, 2011. On rehearing, and after considerable public outcry about the rate increases resulting from the Modified Stipulation, the Commission rejected the ESP plan contained in the Modified Stipulation on February 23, 2012. The Commission gave AEP Ohio 30 days to advise it regarding the Companies' plans to go forward with an ESP. AEP Ohio, on March 5, 2012, notified the Commission of the

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[4] See OCC/APJN Initial Post-Hearing Brief (November 10, 2011) at 24-45.

Companies' intent to submit a Modified ESP, and the Companies filed an application containing the Modified ESP on March 30, 2012.

The Modified ESP for which the Companies seek PUCO approval is similar to the ESP in the September 7, 2011 Stipulation. Like the Stipulation, the SSO proposed in the Modified ESP is an amalgam of several rates, in this instance the base generation rate and the present Environmental Investment Carrying Charge Rider.[5] The base generation portion of customers' bills would remain constant throughout the term of the Modified ESP.[6] Increases in other bill components, however, would result in increases to the total bill for residential customers in the CSP Rate Zone of at least 6.21% at the outset of the Modified ESP term, an additional 0.26% on June 1, 2013 and an additional 0.42% on June 1, 2014.[7] For customers in the OP Rate Zone, the increases would be at least 5.64% at the outset of the Modified ESP term, an additional 5.65% on June 1, 2013 and additional 0.37% on June 1, 2014.[8]

Like the rejected Stipulation, AEP Ohio proposes to have a two-tiered structure providing for capacity with static pricing based in part on PJM's reliability pricing model ("RPM"). The first tier would be priced for the entire ESP term at the RPM rates in effect on the day the Application was filed (i.e., $146/MW-day).[9] This capacity rate would be available to approximately 21% of each customer class through December 31, 2012, approximately 31% of each customer class during 2013, and approximately 41% of each

[5] See AEP Ohio Ex. No. 100 at 7. (Application).

[6] See id.

[7] See AEP Ohio Ex. No. 111 at Exhibit DMR-1. (Roush).

[8] See id.

[9] See AEP Ohio Ex. No. 101 at 15. (Powers).

class from January 1, 2014 through May 31, 2015.[10] Any capacity purchased after these thresholds are met would be offered at a non-RPM based price of $255/MW-day.[11] For 2012, governmental aggregation initiatives approved before or as a result of the November 2011 elections would be awarded additional allotments at the $146/MW-day capacity price, while the additional aggregation load would be included within the 31% set-aside level for 2013 and the 41% set-aside level for 2014.[12]

Like the Stipulation, the Application includes numerous riders. Chief among them is the RSR, a non-bypassable rider.[13] The RSR is designed to replace the generation revenue AEP Ohio expects to lose because of increased shopping caused by the "discounted" capacity offered in the Modified ESP.[14] Thus the amount collected through the rider would increase as shopping increases.[15] The RSR is meant to bolster the Companies' non-fuel generation-related revenues during the term of the Modified ESP, to help the Companies meet both their generation-related revenue target of $929 million per year and their target of an annual 10.5% return on equity ("ROE").[16]

A hold-over rider from the former Stipulation is the Generation Resource Rider ("GRR"), a proposed non-bypassable rider designed to collect costs associated with "renewable and alternative capacity additions, as well as, more traditional capacity

[10] Id.

[11] Id.

[12] Id.

[13] See AEP Ohio Ex. No. 100 at 10. (Application).

[14] See AEP Ohio Ex. No. 116 at 13. (Allen).

[15] See Tr. Vol. V at 1427 (Allen) (if AEP Ohio's connected load goes down, the RSR increases); see also AEP Ohio Ex. No. 116 at Exhibit WAA-6. (Allen).

[16] See AEP Ohio Ex. No. 116 at Exhibit WAA-6. (Allen).

constructed or financed by the Company and approved by the Commission."[17] The charge would be in place for the life of the facility.[18] As in the rejected Stipulation, the GRR is proposed -- at least initially -- as a placeholder rider, with the proposed Turning Point solar project being "the first capacity resource addition to be included in the GRR, if approved."[19] In order to give proper consideration to the Application, the Commission directed AEP Ohio to supplement its Application with "information related to any projected rate impacts by customer class, as well as any projected costs that are currently known to be associated with the creation of the Turning Point facility * * *."[20]

Other riders proposed in the Application include an Alternative Energy Rider[21] and a Distribution Investment Rider ("DIR").[22] AEP Ohio also proposed continuation of the Enhanced Service Reliability Rider ("ESRR")[23] and the gridSMART Rider,[24] with modifications to the existing Transmission Cost Recovery Rider ("TCRR"), the Energy Efficiency/Peak Demand Reduction Rider and the Economic Development Cost Recovery Rider ("EDR").[25] In addition, the Application also proposed continuing the bypassable Fuel Adjustment Clause as modified to remove renewable energy credits[26] and modifying and continuing interruptible service rates.[27]

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[17] AEP Ohio Ex. No. 100 at 8. (Application).

[18] Id.

[19] Id.

[20] Entry (April 25, 2012) ("April 25 Entry") at 3.

[21] See AEP Ohio Ex. No. 100 at 8. (Application).

[22] Id. at 12-13.

[23] Id. at 13.

[24] Id.

[25] Id. at 12.

[26] Id. at 8.

[27] Id. at 9.

Local public hearings on the Modified ESP were held in Canton, Columbus, Chillicothe and Lima during late April and early May 2012.[28] On May 17, 2012, the evidentiary hearing began, and concluded on June 15, 2012. More than 40 parties were granted intervention in this proceeding, and the testimony of almost 70 witnesses was taken. On the last day of the hearing, the Attorney Examiners set the briefing schedule, with initial briefs due June 29, 2012 and reply briefs due July 9, 2012.[29]

III. STANDARD OF REVIEW

The standard of review for ESP cases is found in R.C. 4928.143(C)(1), which states in pertinent part:

> [T]he commission by order shall approve or modify and approve an application filed under division (A) of this section if it finds that the electric security plan so approved, including its pricing and all other terms and conditions, including any deferrals and any future recovery of deferrals, is more favorable in the aggregate as compared to the expected results that would otherwise apply under section 4928.142 of the Revised Code. Additionally, if the commission so approves an application that contains a surcharge under division (B)(2)(b) or (c) of this section, the commission shall ensure that the benefits derived for any purpose for which the surcharge is established are reserved and made available to those that bear the surcharge. Otherwise, the commission by order shall disapprove the application.

In addition, R.C. 4905.22 mandates that every public utility furnish necessary and adequate service and facilities, and that all charges for any service must be just and reasonable.

[28] See Entry (April 13, 2012) at 3.

[29] Tr. Vol. XVII at 4959. (Allen).

IV. ARGUMENT

A. AEP Ohio Has the Burden of Proof in this Proceeding.

S.B. 221 contained far-reaching revisions to R.C. Chapter 4928 that changed the way electric distribution utilities ("EDUs") operate in the State of Ohio. Along with these changes, the General Assembly recognized that the burden of proof should remain with the utility, and not be shifted to the other parties.

R.C. 4928.143(C)(1) provides that the "burden of proof in the [ESP] proceeding shall be on the electric utility." That burden refers to not only proving the SSO meets the statutory test, but also extends to proving that the provisions in the ESP have a basis in law under R.C. 4928.143(B)(2)(b).[30]

On many issues the Companies have failed to meet this burden of proof. For instance, in determining whether the statutory test is met, the Companies failed to come forward with quantifiable expenses associated with the ESRR and the gridSMART rider. The Companies also do not quantify, for purposes of the statutory tests, the future costs to customers for the distribution deferrals -- retired meters for gridSMART, and storm damages expenses. Also, the Companies fail to show that it would even be lawful under R.C. 4928.143(B)(2)(b) to charge customers for the rate stability rider. The Companies have also neglected to provide an estimate of the impact of the Interruptible Power-Discretionary rider on the retail stability rider..

These are but a few examples of how the Companies failed to bear their burden of proof. AEP Ohio's failure is pandemic and permeates its application. Its failure to provide reliable information to support its Modified ESP provisions makes it difficult for

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[30] See *In re Columbus Southern Power Co.*, 128 Ohio St.3d 512, 2011-Ohio-1788, ¶32.

the Commission to carry out its responsibilities under the law. These responsibilities include making the determination whether the Modified ESP is more favorable in the aggregate than an MRO.

Rather than accept the insufficiencies of the Companies' case, the Commission should reject the Modified ESP on grounds that the Companies have failed to meet their burden of proof.

B. The Modified Electric Security Plan Is Less Favorable in the Aggregate than the Market Rate Offer, and Thus the PUCO Cannot Approve the Plan as Filed.

In S.B. 221, the General Assembly revised Chapter 4928 and introduced the concepts of an ESP and a MRO for providing a SSO to retail electric customers. R.C. 4928.143(C)(1) states:

> [T]he commission by order shall approve or modify and approve an application filed under division (A) of this section [i.e. the ESP] if it finds that the electric security plan so approved, including its pricing and all other terms and conditions, including any deferrals and any future recovery of deferrals, is more favorable in the aggregate as compared to the expected results that would otherwise apply under section 4928.142 of the Revised Code.

The "otherwise apply" portion of the quoted statute refers to providing generation service by a market means -- the MRO. This provision of the law requires that the expected price of the SSO generation under an electric security plan be compared to the expected price derived under a market rate offer. This requires a price comparison to determine what is better for customers.

Additionally, the statute requires the comparison to be made on an "aggregate" basis. That means that the comparison must consider "all other terms and conditions" of the Modified ESP plan. Such provisions may include quantifiable non-price benefits, as well as non-quantifiable provisions of the utility's electric security plan. This comparison has been referred to by the Commission and parties as the "statutory test."[31] Under R.C. 4928.143(C)(1) the utility has the burden of proving that the Modified ESP meets the statutory test -- it is more favorable in the aggregate for customers.

OCC Witness Hixon presented testimony comparing the proposed Modified ESP results with the expected results of an MRO.[32] Ms. Hixon concluded that the Modified ESP produces results that are less favorable in the aggregate than the expected MRO results.[33] Other intervenor witnesses came to the same conclusion.[34] The Companies' Modified ESP does not pass the statutory test. On this basis, the Commission cannot approve the Modified ESP because the Companies have failed to prove that the Modified ESP complies with R.C. 4928.143(C)(1).

1. The Price Test presented by the Companies cannot be relied upon by the PUCO to determine whether the Modified ESP meets the statutory test for protecting customers.

a. The Companies started out with the wrong SSO generation price for their comparison because they mistakenly assumed that the Modified ESP price and the MRO price are the same for the first five months of 2015.

OCC Witness Hixon, for purposes of the price test, accepted AEP Ohio witness Roush's "Market Comparable Generation Prices, Proposed" as the SSO generation rates

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[31] See *In the Matter of the Application of Columbus Southern Power Companies and the Ohio Power Companies 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. 11-346-EL-SSO, Opinion and Order (December 14, 2011) ("December 14 Order") at 27.

[32] OCC Ex. No. 114. (Hixon); 114A. (Hixon and Soliman errata).

[33] OCC Ex. No. 114 at 4. (Hixon).

[34] See FES Witness Schnitzer (FES Ex. 104 at 4-7); IEU Witness Murray (IEU Ex. 125 at 4); DERS Witness North (DERS Ex. 102 at 6); Staff Witness Fortney (Staff Ex. 10 at 6).

under the Modified ESP.[35] Ms. Hixon also accepted Mr. Roush's "Market Comparable Generation Prices, Current" as the most recent SSO generation prices.[36] To derive the MRO SSO generation price for comparison, Ms. Hixon took Mr. Roush's most recent SSO generation price and combined it with the bid price, based on the specific blending provision contained in R.C. 4928.143(D). That provision requires that an MRO SSO generation price must be a proportionate blend of the "most recent standard service offer price adjusted for costs of fuel, purchased power, supply and demand portfolio requirements and compliance with environmental laws and regulations and a competitively bid price."[37]

In the Companies' SSO price test, though, they concluded that the Modified ESP price and the MRO price are the same for the first five months of 2015 when 100% of the SSO is competitively bid. This assumption is not appropriate because under R.C. 4928.143(D) the "proportionate blend" must include the "most recent standard service offer price." The most recent standard service offer price is not equal to the MRO price. Similarly, DERS Witness North and IEU Witness Murray filed testimony pointing out the error in Ms. Thomas' approach.[38] The statute simply does not allow any other price to be utilized, regardless of how the Modified ESP is structured. The Commission has no discretion to ignore the clear words in the statute. As often noted, the Commission is a

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[35] OCC Ex. No. 114 at 6. (Hixon).

[36] Id. at 7.

[37] Id. at 6-7.

[38] See DERS Ex. No. 102 at 4-5. (North); IEU Ex. No. 125 at 74-78. (Murray).

creature of statute with no authority other than that expressly granted to it by the General Assembly.[39]

Thus, the Companies' SSO price test was flawed from the start. The Companies' test did not follow the law and use the "most recent standard service offer price" of $62.08 per MWh for the blending purposes.[40] Instead, the Companies used $74.34 per MWh for blending. The Companies' approach overstates the MRO SSO generation price. Because the MRO SSO generation price is overstated, it means that the comparison between the MRO and Modified ESP is skewed in favor of the Modified ESP. The Commission thus cannot rely upon this portion of the price comparison because it is flawed.

b. The Companies used an inappropriate capacity charge of $355.72/MW-Day in determining the bid price for the blended MRO SSO generation price.

In setting the bid price for the comparison between the Modified ESP and MRO, the Companies included a capacity component that they claim recognizes their fixed resource requirement ("FRR") obligations during the ESP period.[41] Companies' Witness Thomas' comparison assumed that the capacity component in the bid price would be $355.72/MW-day. This is the capacity rate the Companies are requesting in Case No.

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[39] *Columbus S. Power Co. v. Pub. Util. Comm.* (1993), 67 Ohio St. 3d 535, 620 N.E.2d 835; *Pike Natural Gas Co. v. Pub. Util. Comm.* (1981), 68 Ohio St. 2d 181, 22 Ohio Op. 3d 410, 429 N.E.2d 444; *Consumers' Counsel v. Pub. Util. Comm.* (1981), 67 Ohio St. 2d 153, 21 Ohio Op. 3d 96, 423 N.E.2d 820; and *Dayton Communications Corp. v. Pub. Util. Comm*. (1980), 64 Ohio St. 2d 302, 18 Ohio Op. 3d 478, 414 N.E.2d 1051.

[40] OCC Ex. No. 114 at Revised Schedule BEH-2B. (Hixon).

[41] OCC Ex. No. 114 at 9. (Hixon); AEP Ohio Ex. No. 114 at 10. (Thomas).

10-2929-EL-UNC, the Capacity Charge Case.[42] The Capacity Charge case is currently pending.

Nonetheless, the Companies presuppose the outcome of the Capacity Charge Case, when no PUCO decision has been made. In that case, the level of capacity charges was hotly debated. Intervenors presented proposals for capacity charges ranging from $20.01/MW-day (market-based price for 2012/2013) to $146.41/MW-day. OCC, along with others,[43] for instance, supported a capacity charge based on PJM's reliability pricing model ("RPM").[44] The Commission Staff, advocating for a cost-based approach, recommended a significantly lower charge ($146.41/MW-day) than that requested by the Company.[45]

But there has been no determination of what the appropriate capacity charge is for the Companies. Thus, as the Commission noted in its *Opinion and Order* in the first stage of this proceeding, the requested capacity price cannot be considered a meaningful number for purposes of conducting the statutory test.[46]

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[42] *In the Matter of the Commission Review of the Capacity Charges of Ohio Power Company and Columbus Southern Power Company*, Case No. 10-2929-EL-UNC.

[43] FirstEnergy Solutions, RESA, Constellation Energy Commodities Group, Inc., Exelon Energy Company, Inc., IGS, the Ohio Manufacturer's Association, National Federation of Independent Businesses, Buckeye Association of School Administrators, et al, and the Ohio Energy Group all submitted direct testimony in favor of RPM pricing. In addition, Industrial Energy Users-Ohio critiqued the Company's cost-based approach calling it "strategically asymmetrical, unbalanced, unjust and unreasonable." *AEP Ohio Capacity Charge Case*, Case No. 10-2929-El-UNC, IEU Ex. 101 at 18.

[44] See OCC Brief at 11-14 (May 23, 2012). .

[45] *AEP Ohio Capacity Charge Case*, Case No. 10-2929-El-UNC at Staff Ex. 103, Direct Testimony of Ralph Smith at 9 and 10. Note also that Staff Witness Emily Medine later revised the energy credit proposed by witness Harter and recommended a $146.41 merged CSP and OPCo capacity daily rate with energy credit and ancillary services receipts. See *AEP Ohio Capacity Charge Case*, Case No. 10-2929-El-UNC, Staff Ex. 105, Medine at ESM-4, page 1 of 1.

[46] *In the Matter of the Application of Columbus Southern Power Companies and the Ohio Power Companies 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. 11-346-EL-SSO, Opinion and Order at 31 (December 14, 2011).

If the Commission determines a different capacity charge (i.e. a lower capacity charge) is consistent with the proposals of all other opposing parties in that case -- then that is the meaningful number for purposes of the statutory test. The approved capacity charge from the Capacity Charge Case must be included as a component for the bid price to determine the blended MRO price for the statutory test.[47] And based on OCC's analysis, using a lower capacity charge will reduce the advantage of the ESP vis-à-vis the MRO, making it difficult for the Companies' Modified ESP to pass the statutory price test.[48]

Here's why. The capacity component of the expected bid price is the second largest component of the Companies' competitive benchmark price, or the generation price projected from a competitive bidding process.[49] Thus, just a single adjustment to recognize the actual results of the Capacity Charge Case will have a significant impact on the blended MRO price for the statutory test. This can be seen under the scenarios run by OCC Witness Hixon,[50] where she used the $145.79/MW-day capacity price that AEP Ohio proposed as a first tier capacity price in this case.[51] This would be consistent with the $146.41/MW-day level of capacity charge proposed as the PUCO Staff's alternative netted capacity price proposal in the Capacity Charge Case.[52]

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[47] OCC Ex. No. 114 at 10. (Hixon).

[48] The Companies' assumption of $355.72 MW-day capacity charge also impacts the Companies' quantification of other benefits of the Modified ESP, as will be discussed infra. If the Commission sets the capacity at a rate lower than that proposed by the Companies, the Companies will have overstated the other benefits of the Modified ESP.

[49] OCC Ex. No. 114 at 11-12. (Hixon).

[50] OCC Ex. No. 114A at Schedule BEH-2B. (Hixon).

[51] AEP Ohio Ex. No. 116 at 6. (Allen).

[52] Case No. 10-2929-EL-UNC, PUCO Staff Initial Brief at 65.

Under the SSO price comparison, if the Companies' proposed capacity component of $355.72/MW-day is used, the results of the SSO price comparison show the Modified ESP SSO price being **more favorable** for customers than the MRO SSO price by $28.1 million. But this is not a meaningful number for purposes of conducting the statutory test. If a lower, more reasonable capacity component is used, such as $145.79/MW-Day, the SSO price comparison changes to a result where the Modified ESP SSO price is **less favorable** for customers than the MRO SSO price by $17.5 million.[53]

Because the Companies have used their requested capacity price as part of the analysis, when the capacity price is not certain, the Commission should not use the Companies' ESP/MRO comparison as the foundation for their analysis. Rather the Commission should rerun the analysis, plugging in the actual capacity price that is derived from the Capacity Charge Case. Otherwise the Commission will be basing its analysis on a capacity charge that it has determined is meaningless.

c. The Companies' analysis applies the benefits and costs of the Modified ESP to the total connected load instead of the SSO load. AEP's error overstates the benefits of the Modified ESP for customers and is inconsistent with other assumptions made in the Companies' statutory analysis.

In the Companies' analysis, the results of the price test show that the expected SSO pricing under the Modified ESP is $256,022,505 less for customers than the expected SSO pricing under a MRO.[54] As part of this price test analysis, Ms. Thomas took the difference between the expected Modified ESP price and the expected MRO

[53] OCC Ex. No. 114 at 13. (Hixon).

[54] AEP Ohio Ex. No. 114 at Exhibit LJT-1, page 1 of 3. (Thomas).

price and multiplied that difference by AEP Ohio's connected load.[55] "Connected load" is the load associated with the electricity use of the Companies' distribution customers. Distribution customers include those who purchase their electricity from the Companies and those who have shopped to purchase electricity from an alternative supplier.

But the potential benefit, or cost, of the expected ESP will only be experienced by non-shopping customers. Customers either shop and are subject to MRO pricing, or they remain SSO customers and pay Modified ESP rates. Customers cannot do both at once -- shop and pay Modified ESP rates.[56] Thus, Ms. Thomas vastly overstated the number of customers that could benefit from the ESP and, as a result, greatly overstated the customer benefits she determined for the Modified ESP on Exhibit LJT-1. The Companies' analysis of the benefits of the Modified ESP is therefore deeply flawed. Rather, the analysis should only have applied the Modified ESP benefit to customers who would receive the benefit (being the SSO load), and not to total connected load.

Additionally, had the Companies' correctly applied the benefits of the Modified ESP to SSO load (and not to connected load) it would have been consistent in its application of the statutory test. For instance, in calculating the benefits of the Modified ESP (shown on LJT-1 as $989 million), the Companies made significant switching assumptions for customers over the term of the Modified ESP.[57] Despite the fact that the switching assumptions are an integral part of the Companies' analysis, they were ignored in this portion of the Companies' analysis. The Companies are inconsistent in their

[55] Tr. Vol. IV at 1261. (Thomas).

[56] See Tr. Vol. IV at 1261. Witness Thomas admitted that the $989 million figure was derived from shopping assumptions provided by Mr. Allen.

[57] See Tr. Vol. IV at 1261 (Witness Thomas admit that the $989 million figure was derived from shopping assumptions provided by Mr. Allen).

approach, making their price test analysis unreasonable and flawed. The Commission should, therefore, not rely upon the Companies' analysis to determine whether the Modified ESP meets the statutory test for benefiting customers.

OCC Witness Hixon, on the other hand, determined the Modified ESP benefit, but applied that benefit to the SSO load only, accepting the Companies' switching assumptions. This calculation is shown on Ms. Hixon's Revised Schedules BEH-2a and BEH-2b. Applying the corrected SSO Price Comparison to the SSO load only, results in a $17.5 million cost to customers for having the Modified ESP,[58] instead of an MRO. This means that SSO customers would pay $17.5 million more[59] for SSO generation service under the Modified ESP than under the MRO.

The Commission, in analyzing whether the proposed Modified ESP meets the statutory test, should not rely upon the Companies' price test results. The assumption that the benefits from the Modified ESP will flow to total connected load contradicts reality. Customers who shop will not get the benefits of the Modified ESP. Thus, benefits will only flow to a fraction of connected load, assuming that switching occurs according to the Companies' projections. When the benefits of the Modified ESP are applied only to customers comprising non-shopped load, the calculated benefit of the Modified ESP is greatly diminished. Applying the benefits solely to non-shopped load is consistent with the shopping assumptions made in other parts of the Companies' statutory test. The Commission should adopt this more reasoned approach when it is analyzing

[58] OCC Ex. No. 114 at Schedule BEH-2b. (Hixon).

[59] This cost resulting from the SSO Price comparison does not yet consider other Modified ESP costs to all customers that are separately identified on BEH-1 (e.g., RSR and GRR).

ESP/MRO comparisons, especially if it accepts the shopping assumptions the Companies have made.

2. The impact of other Modified ESP rates must be included in the ESP/MRO comparison. When these impacts are included, it reveals that the Modified ESP will impose additional costs on customers ranging from $638.9 million to $997.8 million, causing the ESP to be less favorable in the aggregate than the MRO.

Under R.C. 4928.143(C), the Commission, in performing the statutory test, must consider "all other terms and conditions, including any deferrals and future recovery of deferrals." This, as Ms. Hixon testified, means that the Commission must also consider the Companies' proposals to implement a RSR and a GRR.[60]

Although the Companies acknowledge these provisions as part of their Modified ESP, they do not properly value either of these charges (the RSR and the GRR) in their statutory test. In fact, OCC Witness Hixon determined that the Companies had significantly understated the costs of the Modified ESP rates by $638.9 to $997.8 million. Because the Companies improperly valued these provisions, their statutory test should not be relied upon by the PUCO as a foundation for its analysis of whether the test has been passed to benefit customers.

a. The value of the RSR should reflect the impact of Interruptible Power-Discretionary credits and the impact of the changes in capacity charges.

Under the statutory test the RSR is considered a term or condition of the Modified ESP. The RSR is a charge that the Companies designed to allow them to collect from

[60] Id. at 13.

customers non-fuel generation revenues that are lost during the Modified ESP term.[61] These non-fuel generation revenues could be "lost" by AEP Ohio when customers shop or move out of the Companies' service territory. The non-fuel generation revenues could also be lost due to other "non-shopping factors" such as reduced usage and changes in weather.[62]

The RSR is directly related to the Companies' proposed tiered capacity pricing.[63] Under the Modified ESP, any decrease in capacity charges below AEP Ohio's proposal of $355.72/MW-day will cause the RSR to increase. Consequently, increases in the RSR will increase the cost of the Modified ESP to customers, but not the cost of the MRO.

AEP Ohio Witness Allen estimates that RSR revenues of $284.1 million will need to be collected from customers during the term of the Modified ESP.[64] This revenue requirement flows from a target level of $929 million in annual non-fuel generation revenues, built upon a 10.5% return on equity.[65] As explained *infra*, OCC (and others) strongly oppose the imposition of an RSR on numerous grounds. But, for purposes of this discussion, OCC is focusing on valuing the RSR, assuming an RSR is permitted.

The Companies link the RSR to the Interruptible Power-Discretionary ("IRP-D") Rider. This has the effect of allowing much more than the proposed $284 million RSR rate increase. Under the Companies' proposal, they will be compensated for any increased interruptible credits given to customers under this revamped rider. The

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[61] OCC Ex. No. 114 at 13. (Hixon); OCC Ex. 111 at 7. (Duann). As explained in a later section of this brief, OCC opposes the RSR because it lacks any legal or regulatory basis, violates the law, and makes for bad public policy.

[62] See Tr. Vol. V at 1445-1449. (Allen).

[63] OCC will address how the linkage between the RSR and capacity pricing is inappropriate in a later section of this brief.

[64] AEP Ohio Ex. No. 116 at Exhibit WAA-6. (Allen).

[65] Id. at 14 and Exhibit WAA-6.

compensation will come straight from the Companies' customers in the form of increased RSR charges, over and above the $284 million.

And yet the Companies, in valuing the RSR, merely assign a value of $284 million as a cost of the RSR in the Modified ESP price comparison.[66] Conveniently, the Companies have not prepared a forecast of the impact of any proposed increase in the IRP-D credit on the RSR.[67] This is yet another example of the Companies not meeting their statutory burden of proof with any tangible evidence.

The Companies failed to assign a value to the RSR for the added cost associated with the IRP-D. This understates the cost of the Modified ESP. This is a flaw in the Companies' MRO/ESP analysis. Because the Companies' Modified ESP proposes the IRP-D rider as a term and condition of the Modified ESP, it must be considered when conducting the statutory test. The Companies should have included an estimated cost for the IRP-D, especially since the Companies have claimed the IRP-D is a benefit of the Modified ESP.[68]

Additionally, the Companies' analysis fails to account for the fact that if the Commission approves a lower capacity price in the Capacity Charge Case, then the RSR will increase. The increase to the RSR is directly linked to the difference between the PUCO-approved capacity price and the Companies' "fully embedded" capacity cost of $355.72/MW-Day. This is because the Companies have structured the RSR to compensate them for the "value" of capacity lost due to shopping. If the capacity is priced at less than the $355.72/MW-day, then there will be a corresponding increase in

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[66] AEP Ohio Ex. No. 114 at Exhibit LJT-1. (Thomas).

[67] OCC Ex. No. 114 at 14. (Hixon).

[68] AEP Ohio Ex. No. 119 at 7-8. (Dias).

the revenues to be collected under the RSR, because the capacity charge and the RSR are interrelated. OCC Witness Hixon, when using a $145.79/MW-day capacity rate, testified that the cost of the RSR to customers would increase from $284 to $643 million.[69]

Because the Companies failed to properly value the RSR in their statutory test, the statutory test is materially flawed. It substantially understates the value of the ESP in the statutory test. The Commission should not rely upon the Companies' ESP/MRO comparison for the basis of its analysis. Rather, it should rely on OCC's ESP /MRO comparison as presented by OCC Witness Hixon.

b. The costs customers would be charged for the GRR should be included in the ESP/MRO price comparison.[70]

Another reason the Commission should not rely upon the Companies' ESP/MRO analysis is because the Companies have failed to appropriately assign to the Modified ESP the cost of the GRR. The GRR is a non-bypassable rider that the Companies will use to charge customers for the cost of the proposed Turning Point Solar Project.[71] The Companies proposed the GRR as a "placeholder rider," and established it at a zero rate.[72] The Companies, through the testimony of witness Thomas, list the GRR as a "quantifiable benefit of the ESP" and assign it zero cost.[73] Witness Thomas testified that the GRR has no impact on the MRO/ESP comparison because the GRR would be available to the Companies under either an ESP or MRO.[74]

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[69] OCC Ex. No. 114 at 14. (Hixon); OCC Ex. 114A at Revised Schedule BEH-1. (Hixon Confidential),

[70] APJN does not join in this subsection – IV.B.2.b of the Residential Advocates Initial Post-Hearing Brief.

[71] OCC Ex. No. 114 at 14. (Hixon).

[72] Id.

[73] AEP Ohio Ex. No. 114 at Exhibit LJT-1, page 1 of 3. (Thomas).

[74] Id. at 8; AEP Ohio Ex. No. 115 at 2. (Thomas Supplemental).

Ms. Thomas assumes the GRR would be a provision allowable under a market rate offer. She offers no further explanation other than this opinion is based on advice of counsel.[75] And yet the Companies bear the burden of proof on this issue.[76] The Companies have failed to meet the burden of proof here.

Witness Thomas' premise that a GRR would be available to the Companies under either an ESP or MRO does not comport with R.C. 4928.142, the provision of the Revised Code that establishes a Market Rate offer.

Under R.C. 4928.142, the statutory provision applicable to a Market Rate Offer, a utility may, through a reconciliation mechanism or other recovery mechanism, collect costs incurred as a result of the competitive bidding or procuring generation service to provide the standard service offer.[77] This provision lists the costs as "the costs of energy and capacity and the costs of all other products and services procured as a result of the competitive bidding process." The GRR does not fit into these categories of costs.

While there are other provisions for the recovery of costs under an MRO, such as subsection (D) of the MRO statute, even those provisions do not provide for charging customers the GRR. Under R.C. 4928.142(D), the standard service offer price for unbid retail generation service shall be equal to the "utility's most recent standard service offer price, adjusted upward or downward, as the Commission determines reasonable, relative to the jurisdictional portion of any known and measurable changes" from certain costs. Although the costs listed in subsections (3) and (4) may include costs akin to those collected under the GRR, the costs must first meet a threshold condition: these costs must

[75] AEP Ohio Ex. No. 114 at 8-9. (Thomas).

[76] See R.C. 4928.143(C)(1).

[77] See R.C. 4928.142(C)(3).

have been included in the utility's most recent standard service offer. Because the Companies' most recent standard service offer did not include the costs of the GRR, the costs could not be included as part of the MRO, according to R.C. 4928.142(D). Thus, the cost of the GRR should be assigned to the Modified ESP, while no corresponding GRR costs can be assigned to the MRO.

Additionally, the Companies' assumption that the GRR will cause no costs to customers unrealistically and significantly understates the cost of the Modified ESP.[78] Indeed, the PUCO recently indicated that the GRR costs should be considered in evaluating an ESP. The Commission declared that "the inclusion of projected Turning Point solar project costs were an important consideration in the statutory test under Section 4928.143, Revised Code."[79]

AEP Ohio's own estimates for the Turning Point costs indicate a net revenue requirement **during the Modified ESP** of $8.4 million.[80] OCC witness Hixon, for purposes of the statutory test, accepted the $8.4 million net revenue requirement for purposes of the quantifiable benefits/costs during the ESP period.[81] However, Ms. Hixon noted that only considering estimated GRR costs **during the Modified ESP** period ignores the total cost of this provision of the Modified ESP. For this reason, Ms. Hixon considered, as future quantifiable costs of the Modified ESP, an additional $346 million in revenue requirements. The $346 million represents the remaining estimated revenue

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[78] OCC Ex. No. 114 at 15. (Hixon).

[79] April 25 Entry at 3.

[80] OCC Ex. No. 114 at 17. (Hixon); AEP Ohio Ex. 104 at Exhibit PJN-5. (Nelson Supplemental).

[81] OCC Ex. No. 114 at 17. (Hixon).

requirement for June 2015 through 2040, before credits for market capacity and energy requirements.[82]

Including $346 million in GRR costs is important in order to render an appropriate and accurate MRO/ESP comparison. The Companies are seeking approval of the GRR through the Modified ESP. The statutory test (R.C. 4928.143(C)(1)) requires the Commission to consider the Modified ESP "including its pricing and all other terms and conditions, including any deferrals and future recovery of deferrals." The law reflects that elements other than SSO generation pricing -- "all other terms and conditions" should be considered and that the ESP could affect customers in the future. The Commission should not ignore probable future costs to customers resulting from the terms and conditions of a proposed ESP.

Because the $346 million in GRR costs have not been included by the Companies in their MRO/ESP comparison, the Companies have presented a flawed comparison which greatly understates the cost of the Modified ESP. The Commission cannot rely upon the Companies' ESP/MRO comparison for purposes of the statutory test. The Commission should instead assign an $8.4 million cost to the GRR for the Modified ESP during the Modified ESP term, and should assign $346 million in GRR costs as future costs of the Modified ESP.

[82] OCC, through discovery (OCC Interrogatory No. 179, see OCC Ex. No. 114 at Attachment BEH-2), (Hixon) sought the Companies' estimate of capacity and energy revenues to be derived over the 25-year life of the project. The Companies indicated they had not estimated those revenues.

3. The Companies' analysis of "not readily quantifiable benefits" of the Modified ESP is flawed because it fails to recognize the costs associated with distribution related riders of the Modified ESP, including the DIR, ESRR, and gridSMART.

While the Companies are quick to claim "not readily quantifiable" benefits of the distribution related riders in the Modified ESP,[83] the Companies fail to consider that these very same provisions will impose additional costs on customers during the term of the Modified ESP. In particular, the Distribution Investment Rider, the Enhanced Service Reliability Rider, and the gridSMART rider all will impose additional costs on customers.[84] Failure to consider these costs in the MRO/ESP analysis means that the costs of the Companies' Modified ESP are again underestimated, making their analysis skewed and unreliable.

Under the Distribution Investment Rider, the distribution expenses will be collected on an accelerated basis, as compared to the collection which otherwise might occur through a distribution rate case.[85] The Companies themselves acknowledge that the DIR will reduce the current regulatory lag that exists in this regard.[86] The Commission has recognized this as well, characterizing the Companies' previously proposed DIR as "incentive ratemaking to accelerate recovery of the Companies' investment in distribution service."[87] This creates an additional cost to customers because customers will pay the Companies sooner.

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[83] AEP Ohio Ex. No. 114 at 6 and Exhibit LJT-1. (Thomas).

[84] OCC Ex. No. 114 at 18. (Hixon).

[85] Id. at 19.

[86] AEP Ohio Ex. No. 110 at 19. (Kirkpatrick).

[87] December 14 Order at 45.

To estimate the difference between revenue collected under the DIR and the revenue that would be collected under a distribution rate case, assumptions would have to be made on what increase the Companies would request, what the Commission would approve, and when the increase would be effective.[88] For this reason the estimates of the cost to customers of the DIR may not be readily quantifiable. But nonetheless they should be recognized as not readily quantifiable costs to customers of the Modified ESP.

Likewise, the ESRR and gridSMART rider, which the Companies list as not readily quantifiable benefits of the Modified ESP, will also impose additional costs on customers. Thus, the costs should be considered part of the not readily quantifiable costs of the Modified ESP. But they are not listed as a not readily quantifiable cost of the ESP.[89] Inexplicably, the Companies failed to come forward with estimates of the costs of these riders despite bearing the burden of proving the Modified ESP is more favorable than the MRO.[90] This has stymied any attempt by the intervenors to assign a cost to these riders. And it will prevent the Commission from accurately performing its analysis of the statutory test, where it must consider "all other terms and conditions."

Since the Companies are in the better position to estimate these costs, but chose not to, the Commission should accordingly reject the notion that the riders are a non-quantifiable benefit of the Modified ESP. Otherwise, an asymmetrical comparison will result where benefits are recognized and not the costs. Listing the benefits of the riders without recognizing their costs will understate the costs of the Modified ESP. This understatement will tend to make the MRO/ESP analysis flawed, favoring the Modified

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[88] OCC Ex. No. 114 at 19. (Hixon).

[89] See AEP Ohio Ex. No. 114 at Exhibit LJT-1, page 1 of 3. (Thomas).

[90] See R.C. 4928.143(C)(1).

ESP over the MRO. This is another reason the Commission cannot rely upon the Companies' MRO/ESP analysis.

4. The Companies fail to consider other provisions of the Modified ESP that will impose additional costs on customers, making their ESP/MRO analysis flawed. These provisions relate to the Companies' request to defer for future recovery two items – the net book value of retired meters related to gridSMART and the storm damage expenses.

The Companies have included provisions in their Modified ESP that will result in costs to customers, and yet they have not included these same costs in the ESP/MRO comparison. By failing to recognize these provisions as costs of the Modified ESP, the Companies have understated the cost of the Modified ESP, making their ESP/MRO comparison flawed.

The Companies have requested the PUCO grant them accounting authority to defer for future recovery two items -- the net book value of retired meters related to gridSMART and storm damage expenses. While the Companies are not seeking to collect these revenues immediately, their intent, in seeking authority to defer, is to establish the probability of future recovery from customers of these deferred costs and likely carrying costs on the deferrals.[91] Under R.C. 4928.143(C)(1), the statutory test requires the Commission to consider "all other terms and conditions, **including any deferrals and future recovery of deferrals."** This provision of the statute, thus, clearly envisions that the value of deferrals and future recovery of deferrals be considered by the Commission in the statutory test.

[91] OCC Ex. No. 114 at 20. (Hixon).

Yet, despite the statutory language, and their request to defer these expenses, the Companies have not quantified the resulting future costs to customers.[92] Although the actual amount of storm expenses that might be deferred under AEP Ohio's proposal is not known at this time, OCC witness Hixon provided some historical perspective on the Companies' storm damage costs that may be used as a predictor of future costs. Ms. Hixon testified that previously in this proceeding and in its recent distribution rate case, AEP Ohio provided information on the major storm expense the Companies incurred from 2005 through the first half of 2011.[93] Ms. Hixon compiled the data into the following chart, in order to provide insight as to the magnitude of major storm expense for AEP Ohio:[94]

Year	Major Storm Expense Million $'s
2005	11.8
2006	6.9
2007	1.8
2008	3.5
2009	21.7
2010	8.1
2011 (to July 5)	10.7
Source: PUCO Set #141-001, Attachment 1 Case Nos. 11-351-EL-AIR et al.	

The data shows that in five of the seven years, AEP Ohio incurred more than $5 million in major storm expense, with an average of $8.97 million per year in the six full years covered in the timeframe. This means that AEP Ohio is likely to accumulate a

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[92] See id. at 21, where Witness Hixon presents historic data on major storm expenses that the Companies have incurred since 2005. The average expense incurred over that period was $16.8 million. The Companies propose a baseline of $5 million and any amount that varies from the baseline will be deferred for future collection. Id.

[93] OCC Ex. No. 114 at 21. (Hixon).

[94] Id.

considerable amount of deferrals through the storm damage mechanism, which customers will ultimately be asked to pay for. This constitutes yet another area where the Companies have failed to meet the burden of proving that the Modified ESP passes the statutory test.[95]

The fact that the Companies have not included these deferrals and future recovery of deferrals as a cost of the Modified ESP makes the Companies' ESP/MRO comparison statutorily deficient. It cannot be relied upon by the Commission to determine if the Modified ESP is more favorable in the aggregate than the MRO.

The Companies are in a better position than others to estimate these costs, and yet they chose not to, despite bearing the burden of proof on this issue. As a consequence of the Companies' inability or unwillingness to quantify the costs associated with these riders, the Commission should reject the riders outright. Failing to recognize these missing costs enables the Companies to "game the system" by setting up future regulatory recovery (through the deferral of costs), and yet at the same time preclude the Commission from conducting the statutory test in a meaningful and statutorily sufficient manner. This is not permitted under the statute and the Commission should take steps to prevent such action by the Companies.

Moreover, as a policy matter, the Commission should be concerned with creating more deferrals, especially in light of the significant amount of deferrals already existing on the Companies' books. The creation of more deferrals and the potential for adding carrying costs on those deferrals will only add unnecessarily to the rate increases already being imposed on the Companies' customers and have the effect of making the ultimate

[95] See R.C. 4928.143(C)(1).

rates unaffordable. This is unreasonable and will impede the Commission in carrying out the policy of R.C. 4928.02(A) -- ensuring reasonably priced electric service is made available to consumers in the State of Ohio.

5. On a quantifiable basis, the Modified ESP is less favorable for customers than what is expected under an MRO. Thus, the Modified ESP fails to meet the statutory test of R.C. 4928.143(C), and cannot be approved, without modification, by the Commission.

OCC Witness Hixon concluded that the Modified ESP should be rejected by the Commission because it fails the statutory test.[96] Ms. Hixon's conclusion is shared by numerous other intervenors.[97] The Companies' Modified ESP is not more favorable in the aggregate as compared to the expected results that would otherwise apply under a market rate offer. The Modified ESP produces results that are less favorable in the aggregate because:

- On a quantifiable basis, the Modified ESP results in significant additional costs to customers over what is expected under an MRO. Even if one accepts the Companies' assumed capacity charge of $355.72/MW-day [98] (which OCC does not recommend), the Modified ESP imposes additional costs above the MRO totaling $610.8 million, as reflected on OCC Ex. 114A, at Revised Schedule BEH-1. These additional costs flow from recognizing the quantifiable costs of the RSR and the GRR (during the ESP term and into the future), both of which are "all other terms and conditions" of the ESP that the Commission must include when conducting the statutory test of R.C. 4928.143(C)(1).

- Additional not readily identifiable costs to customers will result from certain provisions of the Modified ESP including the DIR,

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[96] OCC Ex. No. 114 at 22. (Hixon).

[97] FES Witness Schnitzer (FES Ex. No. 104 at 4-7); IEU Witness Murray (IEU Ex. No. 125 at 4); DERS Witness North (DERS Ex. No, 102 at 6): Staff Witness Fortney (Staff Ex. No. 110 at 6).

[98] Using a $145.79/MW Day capacity price in the MRO/ESP comparison shows an even greater disparity between the ESP and MRO. Under such an analysis the ESP is quantifiably less favorable in the aggregate than the MRO by $1.0153 billion. See OCC Ex. No. 114A at Revised Schedule BEH-1. (Hixon and Soliman Errata).

> the ESRR, the gridSMART rider, the IRP-D, and the deferrals of storm expenses and retired meters, net book value. These costs will reduce the overall claimed benefits of the Modified ESP and must be considered by the PUCO in comparing the aggregate results of the Modified ESP to the expected results of an MRO. These provisions qualify as "all other terms and conditions, including any deferrals and any future recovery of deferrals." Accordingly the Commission must include the value of these provisions when conducting the statutory test of R.C. 4928.143(C)(1).

The Companies' Modified ESP not only fails the statutory test. It fails the statutory test by a lot. According to OCC, the gap between the Modified ESP and MRO is over $610 million.[99] This is a significant gap, and is above the $325 million gap the Commission found in the first phase of this proceeding, when the Commission was compelled to make modifications to the Companies' Modified ESP.[100] The Commission should determine here as well that the abject failure of the Modified ESP, by a gap of over $325 million, impels the Commission to make substantial modifications to the proposed ESP.

C. Discrete Modifications to the Companies' Modified ESP Are Needed in Order to Ensure that the Modified ESP Fulfills the State Policies of R.C. 4928.02.

Under R.C. 4928.02, there are 14 objectives listed for Ohio's electric policy -- objectives that have remained largely in place since 1999. These explicit statutory policies cannot be ignored.[101] In order to determine whether an ESP's "pricing and other terms and conditions, including any deferrals and any future recovery of deferrals, are

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[99] See OCC Ex. No. 114A at Revised Schedule BEH-1. (Hixon and Soliman Errata).

[100] See *In the Matter of the Application of Columbus Southern Power Companies and the Ohio Power Companies 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. 11-346-EL-SSO, Opinion and Order at 31 (December 14, 2011)(finding that the gap between the proposed ESP and MRO of over $325 million made it "necessary" to make modifications to the proposed ESP.)

[101] *Elyria Foundry v. Pub. Util. Comm* (2007), 114 Ohio St.3d 305.

more favorable in the aggregate as compared to the expected results that would otherwise apply under an MRO," the Commission must individually examine each part of the ESP, in light of the policy objectives of R.C. 4928.02.

The Commission's pronouncements in the *FirstEnergy MRO,* the *FirstEnergy ESP* cases, [102] and the Companies' first ESP Case ("*ESP I*") embrace this approach. In November 2008, the Commission, in analyzing FirstEnergy's application for a standard service offer through a MRO, emphasized the need to examine FirstEnergy's application in light of R.C. 4928.02:

> Chapter 4928 of the Revised Code provides a roadmap of regulation in which specific provisions were put forth to advance state policies of ensuring access to adequate, reliable, and reasonably priced electric service in the context of significant economic and environmental challenges. In reviewing the Companies' application for an MRO, the commission is aware of the challenges facing Ohioans and the electric power industry and will be guided by the policies of the state as established by the General Assembly in Section 4928.02, Revised Code, as amended by Amended Substitute Senate bill No. 221 (SB 221), effective July 31, 2008.
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> In determining whether an MRO meets the requirements of Section 4828.142(A) and (B), Revised Code the Commission must read those provisions together with the policies of this state as set forth in Section 4928.02, Revised Code. Accordingly, the policy provisions of Section 4928.02, Revised Code, will guide the

[102] *In the Matter of the Application of Ohio Edison Companies, the Cleveland Electric Illuminating Companies, and the Toledo Edison Companies for Approval of a Market Rate Offer to Conduct a Competitive Bidding Process for Standard Service Offer Electric Generation Supply, Accounting Modifications Associated with Reconciliation Mechanism, and Tariffs for Generation Service*, Case No. 08-936-EL-SSO, Opinion and Order (November 25, 2008) ("FirstEnergy MRO Order"); *In the Matter of the Application of Ohio Edison Companies, the Cleveland Electric Illuminating Companies, and the Toledo Edison Companies 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 (December 19, 2008) ("FirstEnergy ESP Order").

> Commission in its implementation of the statutory requirements of Section 4928.142(A) and (B), Revised Code.[103]

Moreover, despite arguments that R.C. 4928.02 is merely a redundant standard once the requirements of "more favorable in the aggregate" standard has been met, the Commission determined otherwise stating: "The Commission notes that Section 4928.06, Revised Code, makes the policy specified in Section 4928.02, Revised Code, more than a statement of general policy objectives. Section 4928.06(A), Revised Code, imposes on the Commission a specific duty to 'ensure the policy specified in section 4928.02 of the Revised Code is effectuated.'"[104]

The Commission also dismissed arguments that R.C. 4928.02 does not impose any obligations or duties upon utilities.[105] In doing so the Commission relied upon the Ohio Supreme Court ruling in *Elyria Foundry v. Pub. Util. Comm.*,[106] where the Court held that the Commission may not approve a rate plan that violates the policy provisions of R.C. 4928.02. Accordingly, the Commission held that an electric utility should be deemed to have met the "more favorable in the aggregate" standard "only to the extent that the electric utility's proposed MRO is consistent with the policies set forth in section 4928.02, Revised Code."[107]

Less than a month later, the Commission cemented its interpretation that each provision of the SSO application must be examined in light of the policy objectives of

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[103] *In the Matter of the Application of Ohio Edison Companies, the Cleveland Electric Illuminating Companies, and the Toledo Edison Companies for Approval of a Market Rate Offer to Conduct a Competitive Bidding Process for Standard Service Offer Electric Generation Supply, Accounting Modifications Associated with Reconciliation Mechanism, and Tariffs for Generation Service*, Case No. 08-936-EL-SSO, Opinion and Order (November 25, 2008) at 5.

[104] Id. at 13

[105] Id.

[106] *Elyria Foundry v. Pub. Util. Comm.* (2007), 114 Ohio St. 3d 305.

[107] *First Energy MRO*, Opinion and Order at 14.

R.C. 4928.02 in FirstEnergy's ESP application: "Chapter 4928 of the Revised Code provides an integrated system of regulation in which specific provisions were designed to advance state policies of ensuring access to adequate, reliable, and reasonably priced electric service in the context of significant economic and environmental challenges."[108] Rather than ignoring the state policies enumerated in R.C. 4928.02, in the *FirstEnergy ESP* case, the Commission embraced the policies in order to give meaning to R.C. 4928.143:

> The Commission believes that the state policy codified by the General Assembly in Chapter 4928, Revised Code, sets forth important objectives which the Commission must keep in mind when considering all cases filed pursuant to that chapter of the code. Therefore, in determining whether the ESP meets the requirements of Section 4928.143, Revised Code, the Commission takes into consideration the policy provisions of Section 4928.02, Revised Code, and we use these policies as a guide in our implementation of Section 4928.143, Revised Code.[109]

In the *FirstEnergy ESP* case, assertions were made that R.C. 4928.02 does not impose requirements on an ESP and the ESP should not be rejected or modified if it fails to satisfy the policies of the state.[110] Nonetheless, the Commission appropriately dismissed such arguments.

Indeed the Commission remained true to its words as can be seen throughout the *FirstEnergy ESP order*. For instance, in recognition of the need to ensure reasonably priced service (under R.C. 4928.02(A)), the Commission reduced the base generation rates of FirstEnergy -- "mindful of the significant economic difficulties facing residents

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[108]*First Energy ESP* Order at 8.

[109]Id. at 12.

[110]Id.

in Ohio at this time."[111] The Commission also eliminated other provisions in FirstEnergy's ESP plan that significantly increased costs to customers -- the deferred generation cost rider was eliminated, saving customers approximately $500 million in carrying costs. There the Commission concluded that this savings will help promote the competitiveness of Ohio in the global economy, a state policy enumerated in R.C. 4928.02(N).[112] In evaluating the distribution service improvement rider, although the Commission noted that the rider was permissible under R.C. 4929.143(B)(2)(h), it nonetheless found that the "sound policy goals" of R.C. 4928.02 required the rider to be limited to "prudently incurred costs."[113] Since FirstEnergy's rider was not cost based, the Commission found it should not be approved unless it is shown "to comply with both the intent and scope of the statute (R.C. 4928.02)." With respect to FirstEnergy's capital improvement program for its distribution system, the Commission ordered FirstEnergy to work to develop a program that "advances state policy."[114]

In the Companies' *ESP I Order*,[115] the Commission cited its holding in the FirstEnergy ESP case, and indicated its belief that "the state policy codified by the General Assembly in Chapter 4928, Revised Code, sets forth important objectives which the Commission must keep in mind when considering all cases filed pursuant to that chapter of the code."[116] It further opined that in determining whether the ESP meets the

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[111]Id. at 17.

[112]Id. at 25.

[113]Id. at 41.

[114]Id at 41-42.

[115] *In the Matter of the Application of the Columbus Southern Power Companies for Approval of its Security Plan; an Amendment to its Corporate Separation Plan; and the Sale or Transfer of Certain Generating Assets,* Case Nos. 08-917-EL-SSO, Opinion and Order (March 18, 2009).

[116] Id at 12-13.

requirements of R.C. 4928.143, it would consider the policy provisions of R.C. 4928.02 and use the policies to guide it in implementing R.C. 4928.143.[117]

Indeed, the Commission specifically relied upon the policies of R.C. 4928.02 when it modified portions of the Companies' ESP. For instance, in light of the then "current economic conditions" faced by customers, the Commission eliminated the Companies' proposed automatic increases in the non-FAC portion of the generation rates.[118] The Commission also rejected a proposed Regulatory Asset Rider on the grounds that the Companies failed to demonstrate the rider fulfills the requirements of SB 221 or advances the state policy.[119]

Consistent with this established precedent, and in order to ensure that the rates paid by AEP Ohio customers are reasonable, the Commission should take a similarly broad and well reasoned approach that considers each aspect of the Modified ESP in light of whether it furthers the policy objectives of R.C. 4928.02, including ensuring "reasonably priced electric retail service." This is the approach urged by OCC for implementing S.B. 221 in the fair way that the General Assembly intended for customers.

The Commission has authority to modify the Companies' proposed Modified ESP under R.C. 4928.143. Indeed the Commission has expressly ruled that its authority to modify a utility's ESP is not dependent upon its finding that the Modified ESP is not more favorable than the expected results of an MRO.[120] Rather the Commission aptly described its statutory authority as including the authority to make modifications to the

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[117] Id.

[118] Id. at 30.

[119] Id. at 41.

[120] See AEP ESP 1 Order at 72.

Modified ESP that are supported by the record in the case.[121] And in this case, modifications are recommended to transform the Modified ESP into a rate plan that serves the public interest and promotes the policies of the state. The Residential Consumer Advocates request that the Commission exercise that authority and make the following modifications to the ESP, as supported by the record in this case.

1. The Rate Stability Rider

The RSR is a non-bypassable charge intended to guarantee that the Companies collect a set level of non-fuel generation revenue during each year of the Modified ESP.[122] That level of revenue is $929 million per year, and is based on a return on equity of 10.5%. As structured the RSR is intended to make the Companies "whole" primarily for lost revenue from "discounted" capacity offered to Competitive Retail Electric Service ("CRES") providers, and lost revenues associated with the early auctions under the Modified ESP.[123]

The Companies recognize that the customers should receive some offset to the RSR for the fact that shopping will enable energy to be freed up and sold off-system.[124] The Companies propose a $3/MWH credit to account for the margins from off-system sales and apply that credit to the actual shopping load in 2011 (4,935 GWh).[125] The $3/MWH credit is also applied to the assumed shopping load for the remainder of the ESP term.[126]

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[121] Id.

[122] OCC Ex. No. 114 at 7-8. (Hixon).

[123] Tr. Vol. I at 195-197 (Powers).

[124] AEP Ohio Ex. No. 116 at 13. (Allen).

[125] FES Ex. No. 109.

[126] OCC Ex. No. 111 at 7-8. (Duann).

Under the Companies' proposed RSR, accepting all assumptions the Companies have made with respect to shopping levels and capacity pricing,[127] the RSR will collect $284 million from customers over the term of the ESP.[128] Even though the $284 million RSR collection is a projected collection, it may turn out to be higher under a number of scenarios including: if the SSO customer load is lower than currently projected; if there is a milder winter and customer usage is reduced from 2011 levels; or if there is a severe economic downturn.[129]

Moreover, it is important to note that the $284 million revenue requirement associated with the RSR does not consider the effect of the Rider Interruptible Power-Discretionary credit. If the IRP-D credit increases, the base generation revenues would be decreased and the Companies will collect the lost revenues attributable to the increased credits through the RSR. This will cause even more than $284 million to be collected.[130] Furthermore, the Companies have indicated that if the RSR is approved they would be willing to increase the IRP-D credit from its current levels (that varies by voltage level and service territory) to $8.21 per kW-month.[131] After the targeted RSR revenue is calculated, the rates for different classes are developed based on a

[127] See OCC Ex. No. 114 at Revised Schedule BEH-1, (Hixon) that if the capacity charge is $145.79/MW-day, instead of the Companies' assumed $355/MW-day, the RSR increases to collect $643 million from customers.

[128] AEP Ohio Ex. No. 116 at WAA-6. (Allen).

[129] OCC Ex. No. 111 at 9. (Duann).

[130] OCC Ex. No. 111 at 10. (Duann); AEP Ohio Ex. 111 at 9. (Roush).

[131] The Company proposed Rider IRP-D in which the Generation Demand Credit of $8.21 per kW month will apply to participating customers at secondary, primary, subtransmission, and transmission voltage levels in both CSP and OP service territories. See AEP Ohio Ex. No. 111 at Original Sheet 427-5, attached to Company Ex. No. 111. (Roush).

methodology that allocates costs based on the class' average contribution to AEP Ohio's load during PJM's highest five peak loads.[132]

a. The Commission should reject the proposed Retail Stability Rider because it has no legal basis, is inconsistent with regulatory practices and policies under the law, and fails to benefit customers or advance the state policies.

i) There is No Legal Basis for the Rate Stability Rider

OCC Witness Duann testified that several of the provisions of the Companies' Modified ESP violate important regulatory principles and practices and impose an unjust and unfair financial burden on customers.[133] One of these provisions is the Retail Stability Rider. Witness Duann recommended that the RSR be rejected in its entirety.[134]

One reason the Commission must reject the RSR is because the Companies have failed to prove[135] that the RSR is a permissible provision of an ESP under R.C. 4928.143(B)(2). The Ohio Supreme Court recently determined that if a provision of an electric security plan does not fit within one of the categories listed following R.C. 4928.143(B)(2), it is not authorized by statute.[136]

While the Companies appear to argue that the RSR is authorized under R.C. 4928.143(B)(2)(d),[137] this argument fails. Witness Dias attempts to explain this concept

[132] OCC Witness Ibrahim recommended, that if the RSR is adopted, it should be allocated on a different basis than the coincident peak basis. Dr. Ibrahim testified that the RSR should be allocated to the different classes based on the relative share of each customer in shopped kWhs as the Company attributes the RSR to shopping. See OCC Ex. No. 110 at 9-10. (Ibrahim).

[133] OCC Ex. No. 111 at 4. (Duann).

[134] Id.

[135] Under R.C. 4928.143(C)(1), the burden of proof rests squarely upon the Companies, not the intervenors.

[136] See *In re: Application of Columbus Southern Power Co.*, 2011-Ohio-1788 at ¶ 32.

[137] See OCC Ex. No. 111 at 11, (Duann) citing to AEP Ohio's response to OCC Interrogatory No. 3-055.

when he discusses the RSR as the enabling provision of the Modified ESP which allows other "rate stabilizing" provisions to be included as part of the Modified ESP.[138]

But, the fact is that the proposed RSR does not provide rate stability at all. The amount of the RSR to be collected each year will vary significantly in response to the extent of customer shopping. OCC Witness Duann has correctly indicated that the RSR "will lead to higher electricity rates and financial uncertainty to all native load customers."[139] This shows that the RSR itself will NOT stabilize or provide certainty. R.C. 4928.143(B)(2)(d) requires that the "terms, conditions, or charges" themselves must "have the effect of stabilizing or providing certainty regarding retail electric rate service."

Moreover, the RSR is not one of the categories of "terms, conditions, or charges" allowed under R.C. 4928.143(B)(2)(d). The RSR is not related to "limitations on customer shopping for retail electric generation service," "bypassability," "standby, back-up, or supplemental power service," "default service," "carrying costs," "amortization periods" or "accounting or deferrals." Thus, even if it arguably had the effect of stabilizing or providing certainty, it does not qualify as one of the "terms, conditions, or charges" listed in R.C. 4928.143(B)(2)(d).

The Companies have failed to prove some legal basis for the RSR. That is no surprise, as the law does not allow for an RSR. The Commission must reject the RSR, consistent with the holding of the Supreme Court of Ohio in the ESP I appeal.[140]

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[138] AEP Ohio Ex. No. 119 at 2-3. (Dias Supplemental).

[139] OCC Ex. No. 111 at 10. (Duann).

[140] See *In re: Application of Columbus Southern Power Co.*, 2011-Ohio-1788 at ¶ 32.

ii) It would be inconsistent with regulatory principles and policies under the law to approve the RSR.

OCC Witness Duann testified that the RSR is inconsistent with two long-established regulatory principles and practices.[141] First, the RSR is inconsistent with the regulatory principle that a utility should be afforded an opportunity, not a guarantee, of earnings.[142] Under the RSR, the Companies are guaranteed annual non-fuel generation revenues at a pre-determined level ($929 million). That target of non-fuel generation revenues was reached by building into the formula a 10.5% return on equity. OCC Witness Duann testified that he is not aware of any electric distribution utility in Ohio that collects a charge guaranteeing itself non-fuel generation revenue over an extended period of time.[143]

Second, the RSR violates the regulatory principle that costs are to be paid by the cost causer and subsidies from one customer group to another should be avoided, unless there is a showing that the subsidy is in the public interest.[144] In this regard, the Companies have not demonstrated that such a subsidy is in the public interest and needed to achieve specific public policy goals.

Witness Duann testified that the RSR will result in cost shifting to the SSO customers from other parties, and in particular from AEP Ohio and its unregulated Genco. In particular, requiring SSO customers to pay through the RSR for the lost

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[141] OCC Ex. No. 111 at 12. (Duann).

[142] See *Bluefield Water Works v. West Virginia*, 262 U.S. 679, 692-93 (1923); *FPC v. Hope Natural Gas*, 320 U.S. 591, 603 (1944).

[143] OCC Ex. No. 111 at 13. (Duann).

[144] Id.

revenues caused by shopping customers is unreasonable and unfair. This is because SSO customers are not causing the lost revenues in the first place.[145]

Not only does this violate cost causation principles, but the RSR runs afoul of the policy provisions of R.C. 4928.02(H), which prohibit anti-competitive subsidies. R.C. 4928.02(H) requires the PUCO to ensure effective competition by avoiding anti-competitive subsidies flowing from a non-competitive retail service (SSO generation native load) to a competitive retail service. OCC Witness Duann testified that AEP Ohio's SSO customers are being asked to subsidize other parties (AEP Ohio, shopping customers, and possibly CRES providers) for the shortfall between non-fuel generation revenue actually collected and the $929 million annual revenue target set by AEP Ohio.[146] Additionally, under the RSR proposed by the Companies, the revenues collected will be passed along to the Companies' new unregulated generation subsidiary, AEP Genco. This kind of subsidization appears to be inconsistent with the state policy of R.C. 4928.02(H).

iii) The benefits to customers from the RSR are illusory.

The Companies admit that the RSR is a benefit to the Companies in exchange for a range of so-called "benefits" to customers under the Modified ESP.[147] The Companies describe the benefits to customers as the "discount" in capacity cost; no changes to the generation rate; and the Companies bearing the going forward risk of environmental compliance -- shouldering incremental environmental compliance costs above the level of

[145] Id. at 17.

[146] OCC Ex. No. 111 at 11. (Duann).

[147] See AEP Ohio Ex. No. 101 at 18. (Powers).

the current charges.[148] Additionally, according to the testimony of the Companies' Witness Dias, the delay of the PIRR and a unified FAC rate are other benefits of the RSR.[149]

As explained by OCC Witness Duann, characterizing these Modified ESP provisions as "benefits" to customers is at best questionable, and more likely illusory.[150] The offering of a capacity price to CRES providers that is below the Companies' claimed estimated embedded capacity cost of $355.72/MW-day, is not a benefit. The "discount" contained in the Tier 1 ($145.79/MW-day) and Tier 2 ($255/MW-day)[151] assumes that the Companies' estimate is the true cost of capacity, and that the PUCO will accept that estimate and adopt it as the state compensation mechanism in the Capacity Charge Case. As explained *infra*, the Tier 1 and Tier 2 "discounts" are actually higher prices than the current and expected capacity prices under the default capacity pricing mechanism, PJM's RPM. And as OCC and others argued in the Capacity Charge Case, the state compensation mechanism for the Companies is RPM pricing.[152]

Similarly, the benefit to customers of keeping base generation rates at the current level is dubious when the auction price of generation service or prices of electricity supplied by CRES providers has generally declined and is expected to decline further over the next few years. Companies' Witness Allen in fact testified there were significant reductions in forward energy prices in the PJM markets recently.[153] In fact,

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[148] Id.

[149] AEP Ohio Ex. No. 119 at 3. (Dias Supplemental).

[150] OCC Ex. No. 111 at 14-16. (Duann).

[151] AEP Ohio Ex. No. 116 at 6. (Allen).

[152] OCC Ex. No. 111 at 15. (Duann).

[153] OCC Ex. No. 111 at 15. (Duann).; AEP Ohio Ex. No. 116 at 4. (Allen).

the PUCO has when reviewing other utilities ESP applications, ordered a reduction in proposed base generation rates to account for declines in energy prices.[154]

Continuing the current level of environmental investment carrying charges is not likely to significantly reduce costs or create a benefit to customers. The Companies' savings claim is dependent on the assumption that the Commission would approve collection of environmental carrying charges, as it did in the Companies' ESP I case. There is no present indication that this will be the case.[155] Additionally, the Companies have substantial control over the timing and magnitude of such investments and these investments will only be shouldered by the Companies as long as the Companies own the generating units. Under the Companies' proposed corporate separation plan, the generating units will be transferred to AEP Genco, who will then take on the environmental compliance responsibilities.[156] So any so-called benefit, if it is to accrue, will occur over a relatively short period of time, such as the next two years or until corporate separation is approved and the generating units are transferred.

As explained *infra*, the delay of the PIRR is not a benefit to customers. To the contrary, delaying the PIRR will significantly increase the total costs of the PIRR that customers will have to pay under the Companies' Modified ESP. OCC Witness Duann

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[154] *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 16 (December 19, 2008)(ordering a reduction in proposed base generation rates of approximately 10%, with additional reductions thereafter, in order to reflect the market decline between the date of the filing of the application and the hearing.).

[155] OCC Ex. No. 111 at 15. (Duann).

[156] AEP Ohio Ex. No. 103 at 5. (Nelson).; Tr. Vol. II at 674-675. (Nelson).

testified that a one-year delay of the PIRR will cost the Companies' customers $64.5 million.[157]

In conjunction with the delay of the PIRR, the Companies have proposed to delay the unification of the FAC.[158] According to Witness Roush merging the FAC rate at the same time the PIRR is implemented on a merged basis limits the impact on customers in both the OP and CSP service territories.[159] This so called benefit will dissipate if the Commission adopts the recommendations from OCC (and others)[160] that the PIRR not be delayed. Additionally the delay of a unified FAC is neutral in terms of the overall revenue impact on the Companies' customers as a whole.[161]

b. AEP Ohio's SSO customers should not be required to pay the RSR.

OCC Witness Duann testified that the RSR is driven by the level of shopping within the Companies' service territory and the level of the capacity prices set by the Commission.[162] As more customers switch to CRES providers, the higher the RSR rises, assuming there is a difference between the capacity price set in the Capacity Charge Case and the tiered capacity prices proposed by the Companies. The SSO customers do not create the claimed need for the RSR in the first place; nor do they contribute to any increase in required RSR collection.[163] The SSO customers are not the cause of the RSR cost and thus, should not be asked to bear the associated costs. Hence it is both

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[157] See OCC Ex. No. 111 at 20. (Duann).

[158] AEP Ohio Ex. No. 111 at 5-6. (Roush).

[159] Id.

[160] Staff Ex. No. 09 at 4-5. (Turkenton).

[161] OCC Ex. No. 111 at 16. (Duann).

[162] Id. at 17.

[163] Id.

unreasonable and unfair to require SSO customer to pay, through the RSR, for the "lost revenues" they do not cause in the first place.[164]

Moreover, SSO customers are already paying AEP Ohio's estimated full embedded capacity cost of $355.72/MW-day.[165] As such SSO customers pay, through the proposed base generation rate, and will continue to pay an "undiscounted" capacity price that is higher than Tier 1 and Tier 2 capacity cost charged to CRES providers and presumably paid by shopping customers. Thus, there is no justification for having a rate mechanism (the RSR) that will collect additional charges from SSO customers to compensate the Companies for the revenues lost due to customers switching.

On a fundamental basis, the RSR is a significant rate increase to all customers. The RSR revenues that could be collected under the Modified ESP plan are substantial. The Companies have identified the cost of the RSR as $284 million. But, because the RSR is linked to the ultimate capacity price the PUCO approves and linked to the IRP-D credits, the RSR could mushroom significantly beyond this amount -- approaching a billion dollars to be paid by customers, as testified to by OCC Witness Hixon.[166] Even at a level of $284 million, PUCO approval is likely to make it difficult for PUCO to carry out the policy of R.C. 4928.02(A) -- ensuring that reasonably priced retail electric service is available to consumers in the State of Ohio.

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[164] Id.

[165] See AEP Ohio Ex. No. 116 at 9. (Allen).

[166] See OCC Ex. No. 114 at 14, 14A at Schedule BEH-1, (Hixon) testimony of OCC Witness Hixon that alternate capacity assumptions of less than $333.72/MW-day could triple the cost of the RSR.

c. If the Commission approves the Retail Stability Rider despite the law and evidence against doing so, it should modify the rider by increasing the shopping credit for off-system sales, decoupling the linkage with the IRP-D, and allocating the rider based on the customers' class share of switched KWs.

For the reasons stated above, the Commission should reject the RSR in its entirety. If however, the Commission adopts the RSR, it should modify it. Modifications should be made so that RSR does not impose such significant increases in customers' rates, and is allocated in a manner consistent with the principles of cost causation.

i) The Commission should allocate the RSR based on the customer classes' respective shares of customers leaving AEP for competitive suppliers , meaning the residential class should pay at most 8 percent and not 41.55 percent of the charges.

The Companies designed the RSR as a non-bypassable charge that would vary by customer class, based on the metered kWh use of each customer.[167] The Companies allocated the RSR to customer classes based on the class' average contribution to AEP Ohio's load during PJM's five highest peak loads ("5CP").[168] Since residential 5CP demand share is 41.55%, the Companies propose to collect $39.3 million annually from residential customers.[169]

OCC Witness Ibrahim recommended that the rider be allocated in proportion to each customer class' relative share of switched KWh sales, instead of being based on the

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[167] OCC Ex. No. 110 at 6. (Duann).

[168] Id.

[169] Id.

class' contribution to peak load.[170] Mr. Ibrahim testified that the approach advocated by the Companies is not fair, just, or reasonable. Additionally, it contradicts one of the main regulatory principles in cost allocation, namely, cost causality.[171]

The Companies' rationale for the RSR is to mitigate the financial impact from the "discounted" capacity provided to CRES providers. CRES providers in turn provide service to retail customers who choose them to supply generation service, in lieu of receiving SSO service from AEP Ohio. Basically, the Companies want to be made whole, by customers, for the Companies' losses from competition.

The cost causers -- those imposing the cost of "discounted capacity" -- are the retail customers who shop and receive the discount capacity. If none of the AEP customer classes were shopping, the Companies would not have proposed the RSR. But as proposed the RSR is quite simply the measure of generation revenues lost to competition. The costs of the RSR, thus, belong to the cost causers -- the shopping, non-SSO customers.

Allocating the costs of the rider to the cost causers can be done and should be done. OCC Witness Ibrahim recommended that the costs be allocated on the basis of each customer class' share of kWh sales resulting from customers that switched from AEP to competitive suppliers.[172] The residential customer class share of the Companies' total switched kWh sales is 8%.[173] Thus, following cost causality principles, the residential customer class would be responsible for 8% of the yearly RSR or $7.57

[170] OCC Ex. No. 110 at 8-9. (Ibrahim).

[171] Id.

[172] OCC Ex. No. 110 at 9-10. (Duann).

[173] Id.

million, instead of $39.3 million. This share would then be divided among members of the residential class, by their metered kWh sales. Under this approach, the Companies would recalculate the class' relative shares of switched kWh sales under the Companies' proposed periodic adjustment process. The allocation of the RSR recommended by OCC will assist in keeping residential customer rates at a lower and more reasonable level. OCC Witness Ibrahim has estimated that under his proposed cost allocation, residential customer increases can be reduced from an average of 6% to around 3%.[174]

ii) The shopping credit for off-system sales should be increased or tied to the actual margins realized so that customers are given a rate-reducing benefit from off-system sales commensurate with magnitude of the revenues expected from the sales.

Companies' Witness Nelson testified that as more customers shop, energy is freed up to be sold in the market as off-system sales ("OSS").[175] In the Companies' ESP I, all of the profits from off-system sales were kept by the Companies, including those profits derived from energy freed up by customer shopping. For AEP Ohio, there is no active sharing mechanism, whereby customers pay less for base rates or fuel costs through a crediting of profits from off-system sales.[176] Nor are off-system sales recognized as part of the significantly excessive earnings test ("SEET").

Under the Modified ESP, the Companies recognize that if customers have to pay a charge (RSR) for the costs of shopping ("discounted capacity) they should be given some credit for the profits the Companies earn when the freed up energy is sold into the

[174] OCC Ex. No. 110 at 24-26. (Ibrahim).

[175] Tr. Vol. II at 677. (Nelson).

[176] Tr. Vol. XVII at 4773-4774. (Allen).

market. The Companies offer to credit the RSR in the amount of $3/MWH for the profit margin on off-system[177] sales by AEP Ohio for energy freed up from shopping.

The derivation of the $3/MWH credit is quite a tale. Originally, in response to OCC discovery, the Companies claimed that the credit was merely part of an overall package proposed in the stipulation presented to the Commission in September 2011.[178] The Companies' original explanation, however, is not found in the Rebuttal Testimony Mr. Allen submitted. Rather, in an attempt to bolster its validity, Mr. Allen goes through detailed iterations to show how the $3/MWH is appropriate.

The Companies, however, failed to supplement responses to the OCC discovery to correct what, with the filing of rebuttal testimony, appeared to be either a mistake or was information that did not exist and subsequently came into existence.[179] During the cross-examination, Mr. Allen identifies his May 7, 2012 deposition as the epiphanic point related to the development of the $3 value.[180] There, Mr. Allen described the thought process one might go through to determine the reasonableness of the $3/MWH credit for shopped load.[181] Mr. Allen testified at the evidentiary hearing that he came up with the $3 in developing the RSR, and could not say "[w]hether I did a formal thought in my head of what the math would be or I just did the math subconsciously."[182]

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[177] AEP Ohio Ex. No. 116 at 13. (Allen).

[178] Ormet Exs. Nos. 110, 111, Tr. XVII 4910-4912. (Allen).

[179] Under Ohio Adm. Code 4901-1-16 (D), the Companies had a duty to supplement the discovery, and yet did not. OCC (and Ormet) objected (and moved to strike) Mr. Allen's testimony on the RSR in this regard, but that was overruled. Tr. Vol. VIII at 4951-4956. Rather the Attorney Examiner ruled that, in light of the issues raised, it would give Mr. Allen's discussion of the RSR the weight deemed to be appropriate. Tr. Vol. VIII at 4956. Given the facts, very little weight should be accorded to this portion of Mr. Allen's testimony.

[180] Tr. Vol. XVII at 4913-4914. (Allen).

[181] Id.

[182] Id. at 4915.

This credit serves to reduce the amount of the RSR that the Companies propose to collect from customers so it appears to benefit customer.[183] But, for customers, AEP's $3/MWH credit is a mere pittance of the margins expected to be earned by the Companies on such off-system sales. OEG Witness Kollen also testified that this extremely low energy margin is substantially below energy pricing projections used by AEP in other regulatory jurisdictions.[184]

Specifically, the energy margin of $3/MWH is substantially below the margins projected by Companies Witness Sever, in his pro-forma AEP Ohio financial projections,[185] shown on OJS-2. In his rebuttal testimony Witness Allen attempts to justify the $3/MWh shopping credit by using future year estimates, and adjusting downward rather than accepting Mr. Sever's AEP Ohio specific projections. Witness Allen's downward adjustments, however, are not appropriate.

For example, Witness Allen reduces the off-system sales margin to account for the fact that not all shopping equates to off-system sales.[186] He reduces the margin by a range of 50% to 80%.[187] But in response to OCC discovery,[188] the Companies indicated that in 2011 80.2%, not 50%, of shopped load was converted to off-system sales. Thus, based on the Companies' own numbers, use of a 50% assumption is not appropriate.

[183] Id. at 4766.

[184] OEG Ex. No. 101 at 15 and Exhibit LK-2. (Kollen).

[185] Mr. Sever's energy margins are AEP Ohio specific margins, as opposed to AEP East margins. Thus, Mr. Sever's AEP Ohio margins need not be reduced by 40% (the member load ratio share) to arrive at an AEP Ohio share.

[186] AEP Ohio Ex. No. 151 at 6. (Allen Rebuttal).

[187] Id.

[188] FES Ex. No. 109.

Doing so unreasonably reduces the shopping credit calculation and reduces the benefit owed to customers.

Witness Allen also makes another downward adjustment to energy margin that is not appropriate. Mr. Allen uses the Member Load Ratio ("MLR") from the AEP Pool Agreement to further reduce the energy margin for OSS.[189] Witness Allen points out that the MLR language in the Pool Agreement means that AEP Ohio only gets to keep 40% of the OSS margins attributable to lost sales due to shopping.[190] Unfortunately, he failed to consider two crucial points in his calculation using the MLR. First, when the Pool Agreement ends, AEP Ohio will keep 100% of margins from off-system sales, not 40%. And second, Witness Allen points out in his direct testimony that until the Pool Agreement ends, AEP Ohio is receiving compensation through the pool from other members for the OSS margins. So in effect, AEP Ohio is trading OSS margins for other benefits. Given these two facts, reliance on the MLR is questionable.

Through cross-examination it was established that for 2012, using the same methodology employed by Mr. Allen in his schedule WAA- 2, energy margins projected for total off-system sales was $11.57/MWH.[191] For 2013, using the same methodology employed by Mr. Allen in his schedule WAA-2, Mr. Sever's energy margins projected for off-system sales was $12.28/MWH.[192]

These AEP Ohio-specific off-system sales margins, used for purposes of the "unchallenged" AEP Ohio pro forma financial forecast, represent a more reasonable

[189] AEP Ohio Ex. No. 151 at 5-6. (Allen Rebuttal).

[190] Id.

[191] Tr. XVII at 4796-4800. (Allen).

[192] Id. at 4803-4805.

projection of the energy margins for off-system sales, than does the $3 credit. Moreover, these are AEP Ohio-specific margins that need not be adjusted for the AEP Ohio MLR share of off-system sales.

If one were to use these ($11.57 to 12.28/MWh) more realistic energy margins as a basis for the energy credit to the RSR, the RSR would be reduced to a negative number. In other words, there would be no need for the RSR and refunds would be made to customers.[193] This analysis shows that profits from OSS -- if fully credited for freed up energy associated with shopping -- would eliminate the need for an RSR and provide for a refund to customers.

If, however, the Commission determines that some level of RSR is appropriate, a finding which OCC does not advocate, then it should set the level of the RSR, using a larger, more realistic shopping credit than $3/MWh but less than $12/MWh. Based on available data, a conservative shopping credit, at a minimum, could be set using the actual off-system sales margin for 2011 of $11.73/MWh[194] and reducing it by 19.8% to account for the lost sales due to shopping that do not result in off-system sales. A reduction of 19.8% of the $11.73/MWh margin results in a shopping credit of $9.40/MWh.

Alternatively, the Commission could order the actual profit margins from freed up energy from shopping load be credited to the RSR. In other words, a credit would be created from tracking the actual energy freed up and actual energy sold. This would eliminate the guess work in assigning an estimated profit margin to energy sales freed up by shopping load. No assumptions would need to be made as to whether the freed up

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[193] Id. at 4806-4809.

[194] Companies Ex. No. 151 at 5. (Allen Rebuttal).

energy results in 50% of the energy being sold or 80% of the energy being sold. No assumptions would need to be made about the GWh sold, or of the percentages of shopped load. The information could be tracked, recorded, and credits applied.

iii) The Commission should not permit the lost revenues from IRP-D credits to be collected through the RSR.

The Companies have proposed changes to their Interruptible Service offerings in their Modified ESP. As part of the changes, the Companies propose to restructure Schedule Interruptible Power-Discretionary rate schedule ("IRP-D"). The Companies indicate that upon approval of the RSR, they are willing to increase the IRP-D credit for eligible customers regardless of their voltage level and service territory. Mr. Roush testified that, if this part of the Modified ESP is approved, the increased level of credit would reduce the non-fuel base generation revenues and "would be reflected in the RSR."[195] What this means is that the decrease in non-fuel base generation revenues would have to be picked up through the RSR, causing the revenues collected under the RSR to increase, and imposing higher charges on the Companies' customers .

OCC Witness Ibrahim testified that the Commission should not permit the Companies to reduce the base generation revenues by the credit offered to IRP-D customers.[196] Additionally, he testified that any possible changes to the IRP-D credit, such as the increase to $8.21 per kW-month, should not result in changes to the retail stability rider.[197]

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[195] AEP Ohio Ex. No. 111 at 9. (Roush).

[196] OCC Ex. No. 110 at 11. (Ibrahim).

[197] Id.

Mr. Ibrahim explained that the direct and primary beneficiaries of the IRP-D tariff are those customers who have no less than 1MW of interruptible capacity and participate in the discretionary program.[198] These beneficiaries are the eligible customers that have sufficient capacity for interruption of no less than 1,000 kW (i.e. customers served at secondary, primary, subtransmission, and transmission voltage) that will receive a demand credit to apply to their monthly interruptible demand. Other customers, including residential customers, are not eligible to participate in this program. According to Mr. Ibrahim, non-participating customers should not be responsible for making AEP whole for the revenues forgone under the IRP-D credits, nor should they be responsible for increases in the IRP-D credit.[199] Otherwise, subsidization is occurring, which is generally eschewed from the regulatory perspective unless the subsidization can be shown to promote the public interest. Here the Companies failed to show how this subsidization is justified and in the public interest.

Mr. Ibrahim's approach is in line with the rationale that the cost causer should generally be responsible for the costs. Indeed, the PUCO recently embraced the principles of cost causation in the FirstEnergy All-Electric Case when it determined that residential customer class alone should be responsible for revenue shortfalls resulting from discounts granted to residential all-electric customers.[200] There the Commission determined no legitimate reason had been presented to justify recovery from all customer

[198] Id. at 12.

[199] OCC Ex. No. 110 at 12. (Ibrahim).

[200] *In the Matter of the Application of Ohio Edison Companies, the Cleveland Electric Illuminating Companies, the Toledo Edison Companies for Approval of a New Rider and Revision of an Existing Rider*, Case No. 10-176-EL-ATA, Opinion and Order (May 25, 2011) at 26.

classes.[201] The same rationale applies here. The Companies have offered no legitimate reason why recovery of the revenue deficiency from shopping customers should come from other customer classes.

Moreover, to the extent that the IRP-D unnecessarily adds to increased rates for electric service, it will impede the Commission's ability to carry out its duty, under R.C. 4928.06, to ensure that the state policy provisions of R.C. 4928.02 are carried out. As discussed earlier, R.C. 4928.02(A) requires that reasonably priced electric service be made available to customers in this state. Creating the need for a higher RSR, which will add to the customers bills, is just another provision of the Modified ESP that will impair the Commission's ability to keep the SSO rates at a reasonable and affordable level.

2. The Commission Should Require AEP Ohio to Continue Funding for the Neighbor to Neighbor Program.

AEP Ohio's Neighbor to Neighbor program provides valuable and much needed bill assistance to customers struggling to pay their monthly electric bills, many of whom literally will have their lights go off without such assistance. Through the Partnership with Ohio ("PWO") fund, AEP Ohio has provided approximately $2 million per year to the Neighbor to Neighbor program over the course of the first ESP. No one can seriously contend in this economy that the need for a Neighbor to Neighbor program or some other type of bill assistance program has diminished, or will go away in the near term. Customers are still suffering from the economic downturn and it is not clear yet whether the end is truly in sight.

[201] Id.

The Company, Staff and the Commission have all opined on the PWO fund and universally they have found that PWO is a significant benefit of an ESP.[202] Moreover, the PWO serves two important state statutory policy objectives: ensuring the availability of reasonably priced service pursuant to R.C. 4928.02(A) and protecting at-risk populations under R.C. 4928.02(L).

In AEP Ohio's first ESP, the Commission directed that the Companies commit a specific dollar amount to -- at least $15 million over the three years -- to "low-income, at-risk customer programs."[203] The Commission also directed that the funding come from shareholder dollars,[204] and not from customers.

In the original application in this case, AEP Ohio proposed not only continuing the Partnership With Ohio, but increasing the funding from $5 million per year to $6 million per year.[205] Unfortunately, the Partnership with Ohio did not find its way into the Companies' proposed Modified ESP. When AEP Ohio witness Dias was asked repeatedly on cross-examination as to why the Modified Application contained no provision for the PWO, he was at a loss to provide any explanation regarding its absence.[206]

If the Commission approves or modifies this new Application, it should require AEP Ohio to fund the PWO at its current level ($5 million per year) -- if not the amount proposed in AEP Ohio's original application ($6 million per year) -- with at least $2

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[202] For example, in the ESP 1 Order, the Commission called the PWO fund "a key component" of AEP Ohio's economic development proposal. ESP 1 Order at 48.

[203] Id.

[204] Id.

[205] See Tr. Vol. VI at 1921.

[206] See Tr. Vol. VI at 1927-1931.

million specified for the Neighbor to Neighbor fund. If, however, the Commission does not require full funding of the PWO, the Commission should at least direct AEP Ohio to fund the Neighbor to Neighbor program, at the funding level recommended by the Residential Consumer Advocates. The Commission should also direct that the funding come from shareholder dollars, as it did in the ESP 1 Order.

Residential low-income customers are still feeling the effects of the worst economic period since the Great Depression. The combination of still higher rates, coupled with no bill assistance when low-income customers face default and shut-off, promises to have devastating consequences for many families in AEP Ohio's service territory.

3. The Phase in Recovery Rider should be Modified so that it does not impose unreasonable and unnecessary costs upon customers and so that it does not impede the Commission in ensuring reasonably priced retail electric service is available to customers in the State.

The PIRR is a rider that the Companies are seeking to collect for deferrals created under the Companies' phase-in rates set in *ESP I.* The most recently available PIRR balance (as of March 31, 2012) shows that the deferrals have ballooned to $549 million. Of the $549 million, a truly staggering $136 million represents financing costs on the principle that customers will be asked to pay.[207] This carrying-cost figure is all the more inexplicable to customers at a time when they cannot earn much more than zero percent on their bank account savings.

These deferrals were created when the PUCO authorized the Companies to phase-in "any authorized increases' under the ESP I so as to not exceed the PUCO specified rate

[207] See OCC Ex. No. 111 at Attachment DJD-D, page 2 of 2. (Duann).

caps.[208] The capping or limiting of the increases was intended to make the increases more affordable (in the short term) to customers. Any and all revenue increases above the capped rates were to be collected from customers later, just not in 2009-2011. These increases were not forgotten or forgiven, but were set aside or deferred for later collection scheduled for 2012 through 2018.

The Companies received accounting authority from the PUCO to defer the rate increases. The deferrals created under the three-year phase-in were authorized to be booked as "regulatory assets" for accounting purposes. The Companies were also given accounting authority to book a financing or carrying charge on the deferrals, beginning in 2009. The PUCO in the *ESP I Order* directed the Companies to collect the deferrals and carrying costs through an unavoidable surcharge, but did not approve a specific mechanism that was to collect the unavoidable surcharge.

In September 2011, the Companies filed an application seeking PUCO approval of a mechanism to collect the deferrals.[209] The collection mechanism was labeled a "Phase-In Recovery Rider" and the Companies requested that it become effective with the first billing cycle of January 2012.

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[208] The Commission ordered a cap for CSP of 7% for 2009, 6% for 2010, and 6% for 2011. For OP, the Commission adopted a cap of 8% for 2009, 7% for 2010, and 8% for 2011. See *In the Matter of the Application of Columbus Southern Power Companies for Approval of its Electric Security Plan; an Amendment to its Corporate Separation Plan; and the Sale or Transfer of Certain Generation Assets*, Case Nos. 08-917-EL-AIR et al, Opinion and Order at 22 (March 18, 2009) (*ESP 1 Order*).

[209] *In the Matter of the Application of Columbus Southern Power Companies for Approval of a Mechanism to Recover Deferred Fuel Costs Ordered Under Section 4928.144, Ohio Revised Code*, Case Nos. 11-4920-EL-RDR, Application (September 1, 2011) ("PIRR proceeding").

On October 3, 2011, the PUCO approved the Companies' second electric security plan, and ordered tariffs to be filed to implement its order.[210] Rates under the new tariffs would begin starting January 1, 2012. As part of the tariffs that were implemented on January 1, 2013, there was a "phase in recovery rider" that began collecting the deferred ESP 1 charges from all customers, except residential customers.[211]

On February 23, 2012, the PUCO rejected the Companies' second electric security plan and ordered the Companies to replace the ESP 2 rates (which had been in effect for six weeks) with rates from their previous electric security plan.[212] On February 28, 2012, the Companies proposed as part of continued rates, a phase-in recovery rider to collect its ESP 1 deferred fuel costs.

The Residential Consumer Advocates opposed such collection, as did numerous other parties. The Residential Consumer Advocates and other parties argued that including a phase-in recovery rider was improper because no specific recovery mechanism -- other than "an un-avoidable surcharge" -- had been authorized in the ESP I order. In its motion, the Residential Consumer Advocates requested that the PUCO reject the tariffs seeking to implement a rider to collect the deferrals. The Residential Consumer Advocates also filed to protect customers from paying the deferral rider by requesting a stay or alternatively seeking to collect the rider subject to refund.

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[210] *In the Matter of the Application of Columbus Southern Power Companies and Ohio Power Companies for Authority to Establish a Standard Service Offer Pursuant to §4928.143, Ohio Rev. Code, in the Form of an Electric Security Plan*, Case No. 11-346-EL-SSO et al., Opinion and Order (December 14, 2011).

[211] As part of the PUCO's December 14 Order in this proceeding, the PUCO adopted provisions of a Joint Stipulation that the collection of the phase in recovery rider for residential customers would be delayed for twelve months if certain conditions were met. Id. at 59, adopting provisions of the Joint Stipulation at 26-27.

[212] *In the Matter of the Application of Columbus Southern Power Companies and Ohio Power Companies for Authority to Establish a Standard Service Offer Pursuant to §4928.143, Ohio Rev. Code, in the Form of an Electric Security Plan*, Case. No. 11-346-EL-SSO et al., Entry on Rehearing (February 23, 2012).

On March 7, 2011, the Commission, in approving the Companies' "continued" rate tariffs, ruled that the continued rates should not include the phase-in deferrals.[213] Instead the Commission ruled stated that it would address this issue in other cases -- Case Nos. 11-4920-EL-RDR and 11-4921-EL-RDR. On March 14, 2012, the PUCO issued an Entry in those cases seeking comments and reply comments on the Companies' rider applications.[214] In comments filed on April 2, 2012, OCC opposed the collection of the rider on grounds, *inter alia*, that the deferrals identified were overvalued and should be reduced by the Provider of Last Resort ("POLR") revenues collected from customers from April 2009 through May 2011. The PUCO has not issued a substantive ruling in that case as of the filing of this brief. Yet, consistent with the Attorney Examiner's ruling in this proceeding,[215] the Commission intends to address PIRR issues other than the Companies' proposed modifications, in the PIRR rider docket.

Thus, at the present time, the terms and conditions proposed by AEP for the PIRR are pending before the Commission in Case No. 11-4920-EL-RDR et al.[216] In its Modified ESP, though, the Companies have proposed changes that affect how the PIRR will be implemented. The Companies propose to delay implementing the PIRR for one

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[213] *In the Matter of the Application of Columbus Southern Power Companies and Ohio Power Companies for Authority to Establish a Standard Service Offer Pursuant to §4928.143, Ohio Rev. Code, in the Form of an Electric Security Plan*, Case No. 11-346-EL-SSO et al, Entry at ¶14 (March 7, 2011).

[214] *In the Matter of the Application of Columbus Southern Power Companies for Approval of a Mechanism to Recover Deferred Fuel Costs Ordered Under Section 4928.144, Ohio Revised Code,* Case Nos. 11-4920-EL-RDR et al., Entry (March 14, 2012).

[215] See Tr. 2738-2740, striking portions of OCC Witness Duann's testimony on the PIRR on grounds that it related instead to the primary PIRR case, Case No. 11-4920-EL RDR et al.

[216] *In the Matter of the Application of Columbus Southern Power company for Approval of a Mechanism to Recover Deferred Fuel Costs Ordered Under Ohio Revised Code 4928.144*, Case No. 11-4920-EL-RDR et al.

year, with collection to begin June 1, 2013.[217] Collection would continue until the balance of the PIRR is fully amortized, which is expected to occur by December 21, 2018. The Companies also propose a unified PIRR rate when amortization starts, meaning that customers of both OP and CSP will pay one rate. Additionally, the Companies submit that the deferral balance will continue to accrue an 11.26% Weighted Average Cost of Capital ("WAAC") during the delay period.[218] The Companies also request that the Commission suspend the procedural schedule of the PIRR proceeding.[219]

a. The collection of the PIRR should not be delayed until June 2013, because delay means that customers will pay even more of the high financing charges for what the PUCO has allowed AEP to earn on the PIRR capital.

OCC Witness Duann testified that delaying the PIRR is unnecessary and will allow the Companies to accrue a large amount of additional carrying charges at a very high weighted average cost of capital rate.[220] Staff Witness Turkenton comes to this conclusion as well, and does not support the Companies' proposal to delay the PIRR.[221] Both OCC and Staff recommend instead that the collection start as soon as the Commission order is final.[222]

Mr. Duann estimated that a one-year delay in collecting the PIRR would increase the deferral balance that customers would pay by $64.5 million; while Ms. Turkenton

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[217] AEP Ohio Ex. No. 118 at 10. (Dias).

[218] AEP Ohio Ex. No. 100 at 15. (Application).

[219] Id.; AEP Ohio Ex. No. 111 at 6. (Roush).

[220] OCC Ex. No. 111 at 20. (Duann).

[221] Staff Ex. No. 109 at 4-8. (Turkenton).

[222] OCC Ex. No. 111 at 21 (Duann).; Staff Ex. 109 at 5. (Turkenton).

testified that the increase would be larger and closer to $71 million.[223] The additional carrying costs -- whether $71 or $64 million -- can be avoided by implementing the PIRR rather than delaying it. Collecting the PIRR now, instead of later, is a way to minimize the cost of the PIRR to customers and is in keeping with the policy of the state, under R.C. 4928.02(A), to ensure reasonably priced electric service.[224]

Additionally, as noted by Witness Duann, there is no justification to ask customers to pay for the cost of the delay. Delaying the PIRR does not make the charges go away; it only causes additional charges, in the form of financing charges. Although the delay will lessen the increase in customers' rates in the first year of the Modified ESP, customers will pay significantly more in the long run. Customers of AEP Ohio need to pay less for electricity, and not pay another $60 million or more for a one-year delay in charges. They are already being asked to pay for over $500 million in deferrals in the PIRR proceeding. Allowing more costs to pile up for later collection will not advance the state policy of ensuring reasonably priced electric service.[225]

Additionally, asking customers to pay higher financing charges (i.e., WACC) for the additional deferral period is unreasonable and inconsistent with this state policy. The delay in collection has been initiated by the Companies because it is advantageous to them. During this period of recession, earning an 11.26% return on investment (the

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[223] Id. at 20; Id. at 4.

[224] Cf. *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 17 (December 19, 2008)(concluding that the creation of deferrals in the short term provided benefits, but the need to recovery the deferred rates and carrying charges has the potential to damage Ohio's competitiveness in the global economy, another policy of the State under R.C. 4928.02(N)).

[225] See R.C. 4928.012(A); OCC Ex. No. 111 at 21. (Duann).

WACC requested) creates an extraordinary opportunity for the Companies, to the detriment of customers.

b. If the PIRR is delayed, the Companies should not accrue carrying costs on the PIRR during the one-year delay, so customers are protected against paying even more money for financing charges.

Both Staff Witness Turkenton and OCC Witness Duann testified that the Commission should reject the Companies' proposal to accrue carrying charges based on the Companies' WACC during the one-year delay of the PIRR.[226] Both witnesses testify that the delay was initiated by AEP and not its customers.[227] OCC Witness Duann concluded that it is unreasonable and inconsistent with state policy (R.C. 4928.02)(A)) for the Companies to charge customers to finance the delay, let alone at the high WACC interest rate (11.26%) they propose. Similarly, Witness Turkenton recommends that customers should not pay additional carrying cost for a deferred liability "simply because the Companies elect to delay collections that were supposed to begin January 1, 2012."[228]

Additionally, OCC Witness Duann testified that if the Commission allows the Companies to delay implementing the PIRR and accrue carrying charges during the delay period, it should only permit accruals at the long term cost of debt, not WACC. Mr. Duann and Ms. Turkenton testify that the current fuel adjustment clause costs for serving the Companies' customers are no longer being deferred as of January 1, 2012.[229] In other words the Companies are collecting their full fuel costs from customers through the non-capped FAC rates. With the direct pass through of fuel costs, there is more certainty that

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[226] OCC Ex. No. 111 at 22. (Duann).; Staff Ex. No. 109 at 6. (Turkenton).

[227] Id.; Id. at 5.

[228] Staff Ex. No. 109 at 7. (Turkenton).

[229] OCC Ex. No. 111 at 22. (Duann); Staff Ex. No. 109 at 6. (Turkenton).

the amortization (collection) of the FAC deferral balance will start shortly. The added certainty equates to a lower risk of non-collection. This should translate into a lower interest rate, during this specific accrual period. This lower interest rate should be based on the Companies' long term cost of debt, not the much higher WACC of 11.26%.

i) The amortization period for collecting the PIRR should be shortened.

OCC Witness Duann testified that a shorter amortization period than recommended by the Companies, for collecting the PIRR, would cost customers less.[230] A shorter amortization period would mean that customers would be paying off the deferrals sooner, and thus forgoing carrying costs. The savings to customers (thru the avoidance of additional carrying costs) will depend on what amortization period is chosen. For example, OCC witness Duann testified that under a five-year amortization period, customers would forgo paying $74.7 million in total carrying charges.[231]

OCC Witness Duann testified that using a shorter amortization period than that proposed by the Companies will reduce the costs of carrying charges that customers will pay. A shorter timeframe for collection may mean that Companies' customers would pay a slightly higher rider to get rid of the unamortized balance quicker. But while there would be higher monthly charges under a shorter schedule, the overall costs to consumers would be less as consumers would be paying millions of dollars less in carrying charges. This should assist the PUCO in carrying out its duty to ensure reasonably priced electric rates, consistent with the state policy espoused in R.C. 4928.02(A). Additionally,

[230] OCC Ex. No. 111 at 27-28. (Duann).

[231] Id. at 28.

reducing the deferrals and carrying costs was a regulatory objective recognized by the Commission when it initially approved the Companies' phase-in plan in ESP 1.[232]

The *ESP I Order* did not require that the phase-in recovery rider must be in effect for the entire seven-year period -- 2012 through 2018. Although the *ESP I Order* established a 2012 to 2018 time frame for collecting deferrals, that timeframe was qualified by the phrase "*as necessary* to recover the actual fuel expenses incurred plus carrying costs."[233] The Order thus provides only that the Rider exist as long "as necessary" to collect deferred fuel costs. The Commission is not required to set a collection schedule that goes the full period.

Adjusting the collection period can be done by the Commission, through its general accounting authority, set forth in R.C. 4905.13, as well as through its ongoing authority under R.C. 4928.144 to ensure that only a "just and reasonable" phase-in be implemented. For instance, the PUCO has in the past adjusted deferrals by changing the allocation factors used by the utility, despite the fact that the allocation factor was different than that used in the utility's deferral accounting.[234] More recently, the Commission ordered a crediting of these very same phase-in deferrals in the Companies' 2009 fuel audit case.[235]

With the authority to act, and the responsibility to ensure reasonably priced electric service, the PUCO should act. It should order the amortization period of the

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[232] *ESP I Order* at 23.

[233] Id.

[234] See, e.g., *In the Matter of the Application of Ohio Edison Companies for Authority to Change Certain of its Filed Schedules Fixing Rates and Charges for Electric Service*, Case No. 89-1001-EL-AIR, Opinion and Order (Aug. 16, 1990) at 65-71; affirmed by Entry on Rehearing (October 11, 1990).

[235] *In the Matter of the Fuel Adjustment Clauses for Columbus Southern Power Companies and Ohio Power Companies*, Case No. 09-872-EL-FAC, Opinion and Order (January 23, 2012).

PIRR be shortened to a five-year or shorter amortization period, as recommended by OCC Witness Duann.

ii) The amortization of the FAC deferral balance should be adjusted to account for the accumulated deferred income tax effect, to protect customers from paying financing charges on capital that investors did not supply.

Accumulated Deferred Income Tax ("ADIT") is a non-investor supplied fund.[236] The accumulated deferred income tax associated with the ability to deduct fuel expenses was created during the period that the fuel expenses were being deferred.[237] During that period the Companies deducted the entire fuel expense incurred from its taxable income, and thus, reduced its taxable income. This, in turn reduced the Companies' tax obligation.[238] The tax savings reduced the amount of money the Companies needed to finance the deferrals.

Thus, ADIT is a cost-free source of funds provided by the federal and state governments and is available to the Companies to finance the deferred fuel costs.[239] OCC witness Mr. Soliman concluded that utility customers therefore should not pay carrying charges to AEP Ohio on a source of funds that has no cost to the Companies. This conclusion was shared by several other witnesses in this proceeding, including Staff Witness Turkenton and IEU Witness Bowser.[240]

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[236] Id.

[237] OCC Ex. No. 115 at 4. (Soliman).

[238] Id.

[239] Id.

[240] See Staff Ex. No. 109 at 8. (Turkenton); IEU Ex. No. 129 at 4. (Bowser).

This recommendation is in keeping with the way these and other non-investor supplied funds are treated in Ohio regulatory matters. The Ohio Supreme Court has consistently ruled that utilities are not entitled to earn a return (from customers) on funds the utilities have not provided.[241] For instance, the Court has required customer deposits to be deducted from rate base for this very reason.[242] The PUCO has applied this reasoning to numerous rate base items and in particular to accumulated deferred taxes.[243] The PUCO has typically deducted accumulated deferred taxes from rate base so that investors do not earn a return on funds they did not supply.

While the Residential Consumer Advocates may agree that there are some parts of this proceeding that are not based on cost of service ratemaking, the FAC, as set forth in S.B. 221 and as proposed by the Companies is based on costs. Expenditures collected from customers under the fuel adjustment clause are explicitly for actual costs incurred, with a dollar-for-dollar recovery of those costs. The FAC is to operate as a traditional fuel clause to collect costs. Thus, arguments can and should be made that traditional cost

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[241] *Cincinnati v. Pub. Util. Comm.*, 161 Ohio St. 395, 406 (1954) (ruling that customer contributions in the form of accruals for the payment of taxes, deposits to secure the payment of customers' bills, and collection of rents to be paid at future dates should be used to off-set rate base.); *Office of Consumers' Counsel v. Pub. Util. Comm.*, 58 Ohio St.2d 108, 114 (1979) (customer deposits which will be constant with reasonable certainty into the foreseeable future and which are available for investment should be an offset to rate base)

[242] Id.

[243] See, e.g., *In the Matter of Ohio Edison Companies for Authority to Change Certain of its Filed Schedules Fixing Rates and Charges for Electric Service,* Case No. 89-1001-EL-AIR Opinion and Order (August 16, 1990) at 79-80; *In the Matter of the Application of the Cleveland Electric Illuminating Companies for Authority to Amend and Increase Certain of its Filed Schedules Fixing Rates and Charges for Electric Service,* Case No. 85-675-EL-AIR, Opinion and Order (June 24, 1986) at 71-74.

of service principles apply to the FAC, including those which recognize that the actual federal tax expenses to be charged to customers should be on a net of tax basis.[244] Moreover, nothing in the law prohibits the Commission from using its discretion to consider the reasonableness of costs based on cost of service principles.

Notably, the Commission ruled on this very issue in the *FirstEnergy SSO case*. There the Commission found that the calculation of carrying charges on a net of tax basis is in accordance with "sound ratemaking theory," as well as Commission precedent.[245] The Commission should stand by its decision in the *First Energy SSO case* and rule here that the FAC deferrals should be on a net of tax basis. Staff Witness Turkenton made this recommendation as well.[246]

Although there are two ways to address this issue, OCC Witness Soliman recommended that the Commission direct the Companies to calculate carrying charges net of ADIT by reducing the unamortized deferred fuel balance by the unamortized ADIT balance before applying the carrying charge rate during the amortization or recovery

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[244] See, e.g., *In the Matter of the Application of the Cleveland Electric Illuminating Companies for Authority to Amend and Increase Certain of its Filed Schedules Fixing Rates and Charges for Electric Service,* Case No. 81-1378-EL-AIR, Opinion and Order (January 5, 1983) at 42 (establishing Quarto coal cost deferrals on a net of tax basis); *In the Matter of the Application of the Monongahela Power Companies for Authority to Modify Current Accounting Procedures to Defer Expenditures and Net Lost Revenues Associated with the Implementation of Various Cost-Effective Demand Side Management Options*, Case No. 93-2043-EL-AAM, Entry (November 3, 1994) at 4, 1994 Ohio PUC LEXIS 907 (deferred taxes should be provided for carrying charges on a net of tax basis); *In the Matter of the Application of the Cincinnati Gas and Electric Companies and Columbus Southern Power Companies for Authority to Capitalize and Defer Interest Expense on Certain Capitalized and Deferred Costs Related to the Wm. H. Zimmer Generating Station Investment and Operating Costs*, Case No. 90-2017-EL-AAM, Entry (January 10, 1992) at 6, 1992 Ohio PUC LEXIS 48 (permitting the accrual of carrying charges on deferred expenses using an uncompounded embedded interest cost net of tax*); In the Matter of the East Ohio Gas Companies Application for Authority to Modify its Accounting Procedures to Accumulate Post In-Service Carrying Charges and to Defer and Subsequently Amortize Depreciation and Other Expenses Associated with the Protection of Gas Pipelines*, Case No. 92-555-GA-AAM, Entry (April 30, 1992) at 2, 1992 Ohio PUC LEXIS 329 (permitting deferred taxes on depreciation and other deferred expenses at net of tax rates).

[245] *FirstEnergy SSO*, Opinion and Order at 58, citing *FirstEnergy Distribution Rate Case* Staff Ex. 16 at 8, 12; *In re Cleveland Electric Illuminating Co.*, Case No. 88-205-EL-AAM, Entry (February 17, 1988); *In re Cleveland Electric Illuminating Co.*, Case No. 92-713-EL-AAM, Entry (December 17, 1992).

[246] Staff Ex. No. 109 at 8. (Turkenton).

period.[247] Thus, the Commission should modify this portion of the Companies' Modified ESP, in this regard. Doing so will assist the Commission in carrying out its responsibilities under the laws of Ohio, to ensure reasonably priced electric service is made available to customers.[248]

iii) The interest rate used to calculate the carrying charges during the amortization period should be based on the Companies' long term cost of debt, to protect customers from paying for high financing charges.

On the phase-in recovery deferrals, AEP Ohio proposes that it be paid a carrying cost based on the weighted cost of capital or 11.15% during the period of amortization -- when the deferred costs are being collected from customers.[249] This interest rate is not reasonable, especially in this period of economic recession when customers struggle to make ends meet. Accepting the interest rate of 11.15 % on the deferred phase-in charges jeopardizes the ability of the PUCO to ensure reasonably priced electric rates to customers in this State -- a policy of the State, under R.C. 4928.02. As noted in the testimony of OCC Witness Williams,[250] the affordability of the current rates is an issue for almost 20% of the Companies' customers. Increases coming from the ESP will only exacerbate the problems these customers face. Carrying costs at the Companies' weighted average cost of capital would result in excessive payments by these and other customers.

It is well established precedent that utilities are allowed to earn a return on plant investment that is used and useful, but carrying costs are another matter, especially the

[247] OCC Ex. No. 115 at 5. (Soliman).

[248] See R.C. 4928.02(A).

[249] See OCC Ex. No. 111 at 18-20. (Duann).

[250] OCC Ex. No. 113 at 5-7. (Williams).

carrying cost for any fuel cost deferral. Fuel cost deferral is basically an accounting cost recovery mechanism. It is used primarily to recover costs incurred in procuring fuel and fuel-related items, and not to yield a return for shareholders.

Moreover, as OCC Witness Duann testified, the use of a lower interest rate appropriately reflects the fact that once the deferral collection has begun, the risk of non-collection is significantly lessened.[251] Lower risk means that there should be a lower financing cost of the deferrals, such as long term debt. OCC Witness Duann testified that the interest rate used in calculating the carrying charge during the amortization period should be no higher than the Companies' current cost of long-term debt, or 5.34%.[252] Use of long term cost of debt for carrying charges once collection of the deferrals has begun is appropriate.[253] Staff Witness Turkenton supports this recommendation as well.[254]

Use of debt, long or short term, to calculate carrying charges on deferred expenses is consistent with practices used by other Ohio electric distribution utilities[255] and consistent with rulings by the Commission.[256] For instance, the cost of debt was used in the past when the Companies filed for accounting treatment that would create deferrals of

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[251] OCC Ex. No. 111 at 27. (Duann).

[252] Id.

[253] See, e.g., *In the Matter of the Application of Ohio Edison Companies, the Cleveland Electric Illuminating Companies and Toledo Edison Companies for Approval of a New Rider and Revision of an Existing Rider*, Case No. 10-176-EL-ATA, Opinion and Order (May 25, 2011) at 24.

[254] See Staff Ex. . No. 109 at 8. (Turkenton).

[255] See *In the Matter of the Application of Columbus Southern Companies and Ohio Power Companies to Adjust Each Company's Transmission Cost Recovery Rider*, Case No. 08-1202-EL-UNC, Staff Audit Finding (December 8, 2008) at 3.

[256] See for example, *In the Matter of the Application of Columbus Southern Companies and Ohio Power Companies to Adjust Each Companies' Transmission Cost Recovery Rider*, Case No. 08-1202-EL-UNC, Finding and Order (December 17, 2008) at 4 (where the Commission adopted the Staff's Audit finding recommending carrying costs at interest only).

their alleged storm damage expenses.[257] The Companies asked for carrying charges based on their weighted average cost of debt. The Commission rejected the Companies' request and instead held that carrying charges on the deferrals should be based on the actual cost of debt.[258]

4. Corporate Separation

On September 30, 2011, AEP Ohio -- as OP -- filed an Application seeking approval of an amendment to its corporate separation plan.[259] The Application sought to implement structural separation. This was a fundamental change from the functional separation that existed under the previously approved corporate separation plan. OCC and others filed comments and reply comments in that proceeding.

On December 14, 2011, the Commission issued an order in the present case, modifying but adopting the Stipulation that had been reached in September 2011. Among other things, the Commission determined that, subject to approval of the Companies' corporate separation plan, OP and CSP should divest their competitive generating assets to a separate competitive retail generation subsidiary. On January 23, 2012 the Commission issued a Finding and Order modifying and approving OP's application to amend its corporate separation plan.[260]

On February 27, 2012, OP filed a motion requesting that its corporate separation application be dismissed in light of the Commission's February 23, 2012 Entry on

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[257] See *In the Matter of the Application of Columbus Southern Power Companies and Ohio Power Companies for Authority to Modify Their Accounting Procedure for Certain Storm-Related Services Restoration C*osts, Case No. 08-1301-EL-AAM, Application (December 15, 2008).

[258] Id, Finding and Order (December 19, 2008) at 3.

[259] *In the Matter of the Application of Ohio Power company for Approval of an Amendment to its Corporate Separation Plan*, Case No. 11-5333-EL-UNC, Application (September 30, 2011).

[260] Id., Opinion and Order (January 23, 2012).

Rehearing rejecting the ESP Stipulation. The PUCO, by a March 14, 2012 Entry on Rehearing, dismissed the Companies' Application (and also denied OCC and IEU's Application for Rehearing).

On March 30, 2012, OP filed another Application seeking approval of an amended corporate separation plan.[261] Its Application was filed concurrently with its Modified ESP. Its filed plan appears to be no different than the earlier filing in September 2011, where it sought, among other things, to transfer assets at net book value. Mr. Nelson confirms this in his filed testimony.[262] On May 29, 2012, by Attorney Examiner Entry, the Company's Application was suspended to allow the PUCO to fully evaluate the proposed amendments.[263]

Even though the Application is to be approved in a separate case, the Companies' Modified ESP filing is contingent upon receiving approval of the corporate separation plan, which cannot be done in the instant case. This creates an evidentiary problem for the Companies, as the record in this case does not contain the Application for corporate separation and no party has moved to consolidate the two proceedings. With no record in the present proceeding, the Commission cannot rule upon the corporate separation issues[264] which are a condition precedent to the offering of the Modified ESP. Thus, the Commission cannot here render an opinion on the corporate separation plan.

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[261] *In the Matter of the Application of Ohio Power company* for Approval of Full Legal Corporate Separation and Amendment to its Corporate Separation Plan, Case No. 12-1126-EL-UNC, Application (March 30, 2012).

[262] AEP Ohio Ex. No. 103 at 5. (Nelson).

[263] Case No. 12-1126-EL-UNC, Entry (May 29, 2012).

[264] See R.C. 4903.09, which requires the PUCO to show the facts in the record upon which the order is based. *MCI Telecommunications Corp. v. Pub. Util. Comm*., (1987) 32 Ohio St.3d 306.

Beyond this fundamental procedural problem, the substance of the corporate separation plan -- the transfer of the generating assets at net book value -- is objectionable. It is objectionable because the transfer appears to be inconsistent with the objectives of the controlling statute, R.C. 4928.17.

R.C. 4928.17(A) sets out three primary objectives for corporate separation plans. These objectives are:

- To provide for competitive retail electric service (or the non-electric product or service) through a fully separate affiliate, with separate accounting requirements and a Code of Conduct as ordered by the PUCO;

- To satisfy the public interest in preventing the abuse of market power; and

- To ensure no undue preference or advantage is extended to any affiliate, division or part of the business engaged in supplying competitive retail electric service (or non-electric product or service).[265]

The Companies' plan must address these objectives. The PUCO has also adopted enabling rules that apply, *inter alia*, to R.C. 4928.17. Under the Commission's rules there are certain

[265] See also R.C. 4928.02(G), which specifies that the policy of the state includes ensuring effective competition by avoiding anti-competitive subsides flowing from non-competitive service to competitive retail electric service.

restrictions[266] detailed in Ohio Adm. Code 4901:1-37-04(C) that seek to eliminate the exposure to the electric utility based on actions of a competitive business. They also require the competitive businesses to obtain financial arrangements that better reflect their business risks. Such rules are also consistent with the prohibition under R.C. 4928.02(G) on ensuring effective competition by avoiding anticompetitive subsidies between the regulated and unregulated electric service.

R.C. 4928.17, in numerous subsections, refers to the "competitive advantage and abuse of market" that the law seeks to prevent through the filing of a corporate separation plan. In subsection (A)(2), the Commission is tasked with evaluating a corporate separation plan to determine if it "satisfies the public interest in preventing unfair competitive advantage and preventing the abuse of market power." Additionally, the Commission must determine under subsection (A)(3) whether the plan is sufficient to ensure that the utility will not extend any "undue preference or advantage" to its affiliate. Section (B) of the statute requires the PUCO to adopt rules regarding corporate separation that include limitations on affiliate practices "to prevent unfair competitive advantage."

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[266] The restrictions are as follows:

1) Any indebtedness incurred by an affiliate shall be without recourse to the electric utility.
2) An electric utility shall not enter into any agreement with terms under which the electric utility is obligated to commit funds to maintain the financial viability of an affiliate.
3) An electric utility shall not make any investment in an affiliate under any circumstances in which the electric utility would be liable for the debts and/or liabilities of the affiliate incurred as a result of actions or omissions of an affiliate.
4) An electric utility shall not issue any security for the purpose of financing the acquisition, ownership, or operation of an affiliate.
5) An electric utility shall not assume any obligation or liability as a guarantor, endorser, surety or otherwise with respect to any security of an affiliate.
6) An electric utility shall not pledge, mortgage or use as collateral any assets of the electric utility of the benefit of an affiliate.

R.C. 4928.02(H) also conveys this theme, but uses slightly different terminology. It establishes, as one of the state policies, ensuring effective competition by avoiding anticompetitive subsidies flowing from a non-competitive retail service to a competitive retail service. This is one of the state policies the PUCO must ensure is effectuated under R.C. 4928.06.

When an affiliate receives property from an electric utility, the electric utility should show that it has been properly compensated for such property. If the electric utility has not been properly compensated, i.e., the compensation is too low, the affiliate receives a competitive advantage, which is unlawful under R.C. 4928.17(B) and R.C. 4928.02(H).

Transfer at net book value, as proposed by the Companies, instead of market value, is likely to result in compensation that is too low, and in subsidies flowing from the customers of the utility to the unregulated affiliate. This is not in the public interest as it threatens the development of a competitive generation market, a key component of S.B. 221. This is contrary to the policy of the state to ensure the diversity of electricity supply and suppliers.[267]

Arguments can be made that the asset transfer at book value would deny the Companies' customers their appropriate share of any market premiums associated with the portfolio of generating units. Customers may be entitled to a share in the corresponding asset market premiums obtained by the utility for the generating units that are divested. It is these generating units that customers have been charged a return on and of for many, many years.

[267] See R.C. 4928.02(C).

The evidence from this proceeding tends to support the notion that there are market premiums associated with these generating units. In this proceeding, Mr. Nelson testified that the transfer of the generating units to the Genco would be approximately 8,900 MW in capacity.[268] This capacity would be primarily coal and natural gas resources.[269] Mr. Nelson testified that once corporate separation is approved, there will be a contract between the EDU and the Genco to provide SSO energy and capacity.[270] There will at times be excess energy that the Genco has after supplying the SSO and this excess energy would be available for the SSO to sell on the market.[271] Indeed, if the connected load figures shown on LJT-1 are accurate, there will be quite a bit of excess energy that the Genco can sell on the market.

The net book value of the generating assets to be transferred as of September 30, 2011, was estimated to be approximately $6 billion. [272] Although the Companies have resisted producing evidence of the market value of the assets,[273] in the course of this proceeding evidence was adduced showing a cash flow study for the generating units of AEP East.[274] The evidence shows that for the AEP East fleet when the total cash flows of the assets were compared to the total book value of the fleet, over thirty years, it

[268] Tr. Vol. II at 661, 664. (Nelson).

[269] Id. at 664-665.

[270] Id. at 666.

[271] Id.

[272] See OCC Ex. No. 105.

[273] See, e.g., Case No. 12-1126-EL-UNC, Application (March 30, 2012).

[274] OCC Ex. No. 104.

generated a positive cash flow value of $22 billion.[275] A portion of the cash flow generation is attributable to AEP Ohio generating assets.[276]

What this record evidence shows is that the generating assets may have significant value above net book value that the Commission should consider when ruling upon the Companies' corporate separation plan in the 12-1126 docket. OCC and others should be given the opportunity there to fully explore the market value of the generating units. The market value of the units is something the Commission should duly consider in determining whether the transfer of generating assets at net book value serves the public interest. Only then when it has considered the evidence in conjunction with the directives under R.C. 4928.17, et al., can the Commission make a determination of whether to approve the Companies' corporate separation plan. Doing so now in this docket is premature.

5. AEP Ohio's two-tiered capacity pricing plan is flawed and the Companies overstate the benefit associated with the plan.

a. The Commission should reject the Companies' two-tiered capacity pricing plan because there is no valid basis for the plan and there is a real potential for harm to competition.

According to AEP Ohio, its capacity pricing plan is rooted in its obligation as a FRR entity under PJM. AEP Ohio states that, through May 31, 2015, the AEP East companies must continue to provide capacity for all the loads that were submitted to PJM as FRR.[277] The Companies contend that the FRR obligation includes AEP Ohio's load for its SSO customers, as well as the shopping load served by CRES suppliers in AEP

[275] Tr. Vol. III at 851. (Mitchell).

[276] Id. at 856-857; see also IEU Ex. No. 121 (confidential).

[277] AEP Ohio Ex. No. 103 at 10. (Nelson).

Ohio's service territory.[278] AEP Ohio will become a PJM RPM entity on June 1, 2015.[279]

During its final years as an FRR entity, AEP Ohio proposes a two-tiered capacity pricing plan. The first tier would be priced at $146/MW-day,[280] which is considerably higher than the RPM rates that will be in effect during the term of the ESP.[281] This capacity rate would be available to approximately 21% of each customer class through December 31, 2012, approximately 31% of each customer class during 2013 and approximately 41% of each class from January 1, 2014 through May 31, 2015.[282] Any capacity purchased after these thresholds are met would be offered at $255/MW-day.[283] For 2012, governmental aggregation initiatives approved before or as a result of the November 2011 elections would be awarded as additional allotments of the $146/MW-day capacity price, while the additional aggregation load would be included within the 31% set-aside level for 2013 and the 41% set-aside level for 2014.[284]

AEP Ohio has not offered any cost basis or market basis for its proposed tiered prices. Instead, the Companies simply assert that these proposals were developed as part of a stipulation package offer which AEP Ohio considers to be reasonable.[285]

Whether the two-tiered capacity pricing scheme proposed by AEP Ohio is reasonable cannot be determined at this time, because it is uncertain whether such prices

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[278] Id.

[279] Id. at 9.

[280] See AEP Ohio Ex. No. 101 at 15. (Powers).

[281] See IEU Exs. Nos. 125 (Murray Public) and 126 (Murray Confidential) at 38.

[282] AEP Ohio Ex. No. 101 at 15. (Powers).

[283] Id.

[284] Id.

[285] See OCC Ex. No. 117 at 17. (Wallach).

represent a discount on the actual cost of capacity for the Companies' generation assets. As OCC witness Wallach noted in his testimony, one witness in the Capacity Charge Case estimated the actual cost of AEP Ohio's capacity at about $79/MW-day.[286] Thus, the pricing the Companies propose for both Tier 1 and Tier 2 capacity in this proceeding could be well above cost, not a discount on cost as alleged by AEP Ohio.

What is known, however, is that the plan will likely harm competition because of the potential for confusion among CRES suppliers and customers concerning the prices to be charged. FES witness Banks detailed the problems inherent in the two-tiered scheme. First, because customers can join the queue only after they have signed a contract with a CRES provider, they will not know at the time they sign the contract whether they fall under the cap and will receive Tier 1 capacity prices, or instead will receive the higher Tier 2 price.[287]

Second, AEP Ohio may needlessly invoke the minimum stay provision under certain circumstances. A customer who does not fall under the cap, and thus will have to pay the higher Tier 2 price, may back out of the contract and seeks to return to AEP Ohio's SSO without ever having taken service from the CRES provider. In that instance, AEP Ohio could deem the customer subject to any applicable minimum stay and block the customer from shopping when the caps incrementally increase the following year.[288]

Third, the proposed "Cap Tracking System" will not be operational for 60 more days after an order approving the Modified ESP. Thus, while the caps are being filled,

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[286] Id. at 18, citing Direct Testimony of Jonathan A. Lesser on behalf of FirstEnergy Solutions Corporation in Case No. 10-2929-EL-UNC, April 4, 2012, at 7.

[287] FES Ex. No. 105 at 9-10. (Banks).

[288] Id. at 10.

CRES providers and customers will have no ready means of knowing where the caps stand and whether there is any likelihood that they will fall under the cap.[289]

AEP Ohio witness Allen attempted to refute the notion that confusion surrounding the two-tiered system is not an impediment to shopping. In his rebuttal testimony, Mr. Allen presented data showing the increase in shopping in AEP Ohio's service territory since the two-tiered scheme was put forth in the September 7, 2011 Stipulation.[290] Mr. Allen, however, ignored two facts. First, the amount of residential shopping has not yet reached 21%, and thus residential customers have not been subjected to Tier 2 pricing, only the lower Tier 1 capacity prices.[291] Thus, many residential customers may not even know there is a two-tiered system in place.[292]

Second, the commercial class and industrial classes are already over the 21% shopping threshold and thus are subject only to the Tier 2 pricing. They, too, are faced with only one price for capacity.

The Commission should reject AEP Ohio's proposed pricing and quantity limits for both Tier 1 and Tier 2 capacity. Instead, **all** capacity sales should be priced at a single rate. The Residential Consumer Advocates urge the Commission to set AEP Ohio's capacity price at the RPM market-based price. RPM prices for capacity represent the true market value of capacity and takes into consideration market risks. Cost-based capacity prices do not. RPM-priced capacity also provides the most efficient market prices, which avoid creating any distortions to the capacity market. If, however, the Commission finds

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[289] Id.

[290] AEP Ohio Ex. No. 151 at 10. (Allen Rebuttal).

[291] See Tr. Vol. XVII at 4815-4816. (Allen).

[292] See id. at 4818.

that AEP Ohio is entitled to recover embedded costs, then the Commission should also include an energy credit that recognizes the Companies' margins from off-system sales. Such a credit would protect customers from paying twice for those costs.

b. AEP Ohio overstates the benefit of the two-tiered capacity pricing, for purposes of whether the ESP is more favorable than an MRO.

AEP Ohio claims there is a benefit associated with the two-tiered capacity pricing scheme, for purposes of its position that its ESP is more favorable in the aggregate than an MRO. The alleged benefit -- $989 million over the term of the Modified ESP, according to the Companies -- is calculated as the difference between all CRES providers paying the capacity price of $355/MW-Day the Companies proposed in the 10-2929 case, and all CRES providers paying $146/MW-Day for capacity up to the proposed Tier 1 threshold and $255/MW-Day for capacity over the threshold.[293] That claimed benefit is overstated.

AEP Ohio's claim is based on the premise that the Commission would approve the $355/MW-Day price for capacity. But that premise is faulty, especially in light of the Commission setting interim capacity prices in the 10-2929 case at $146/MW-Day for the first 21% of load and $255MW-Day for load above 21%.[294] If the PUCO approves a capacity charge that is less than the $355 level in Case No. 10-2929, then AEP's claimed benefit is commensurately reduced.

AEP Ohio's claimed benefit for the ESP/MRO test is overstated for another reason. AEP Ohio makes assumptions regarding shopping that seem to be over-inflated, and thus overstate the benefit of the two-tiered capacity charge. The Companies'

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[293] Tr. Vol. V at 1366-1367. (Allen).

[294] See Case No. 10-2929, Entry (March 7, 2012) at 17 (granting interim relief).

calculation of the benefit from the two-tiered capacity price structure assumes that shopping will increase "to 65% of load for residential customers, 80% of load for commercial customers and 90% of load for industrial customers (excluding a single large customer) by the end of 2012 and remains at those levels through May of 2015."[295] This seems unrealistic, especially for the residential class; residential shopping is only at 14% as of June 1, 2012.[296] The benefit of the two-tiered capacity charge is not as great as the Companies claim.[297]

6. AEP Ohio has not justified the need to charge customers the Generation Resource Rider.[298]

In its Modified ESP, AEP Ohio proposed a new non-bypassable GRR to collect from customers the cost of new generation resources, including renewable capacity that the Companies own or operate for the benefit of Ohio customers.[299] The GRR is designed to collect costs of renewable and alternative capacity additions, as well as "more traditional capacity" constructed or financed by the Companies and approved by the Commission. The Companies assert that they do not expect there will be any additional projects included in the rider during the Modified ESP, with the exception of the proposed Turning Point solar generating facility.

The GRR is offered as a "placeholder" rider, with no dollar figure associated with the rider. However, AEP Ohio has -- at the direction of the Commission[300] -- provided information related to the projected rate impacts of the GRR by customer class and

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[295] AEP Ohio Ex. No. 116 at 5. (Allen).

[296] See AEP Ohio Ex. No. 151 at 10. (Allen Rebuttal).

[297] Tr. Vol. V. at 1370. (Allen).

[298] APJN does not join in this subsection of the Residential Advocates Initial Post-Hearing Brief.

[299] AEP Ex. No. 103 at 20. (Nelson).

[300] See April 25 Entry.

projected costs currently known to be associated with the creation of the Turning Point facility. AEP Ohio has the burden of proof to explain and justify the GRR, but has not met this burden.

R.C. 4928.143(B)(2)(b) allows EDUs to collect, on a non-bypassable basis, a reasonable allowance for construction work in progress on an electric generating facility. The Commission must first determine “in the proceeding” that there is need for the facility based on the EDU’s resource planning projections, and the facility’s construction must be sourced through a competitive bid process. R.C. 4928.143(B)(2)(c) also requires that the new generation projects must be “used and useful” and “dedicated to Ohio consumers.” AEP Ohio has not demonstrated a need for the facility, or that it was constructed through a competitive bidding process, or that it is used and useful, or that the generation from the facility will be dedicated to Ohio consumers. AEP Ohio has not made the showings required by R.C. 4928.143(B)(2)(b) or (c). Because AEP Ohio has not made the showing required by Ohio law for collection of the cost of construction of the Turning Point facility, the Commission cannot lawfully approve the GRR in this proceeding.

However, if the Commission nonetheless is able to lawfully approve the GRR, it should require AEP Ohio to collect the rider from the different customer classes through a per-kWh charge. As this charge is dedicated to collect costs associated with the Turning Point solar project, these costs are associated with a predominantly energy resource. As discussed by OCC witness Ibrahim, costs associated with energy resources should be collected in terms of a per kWh basis; this is an established practice in Ohio and consistent with R.C. 4928.64(c)(2)(a).[301]

7. The Commission should reject the Pool Termination rider or modify it to ensure that customers benefit from off-system sales to AEP Ohio's Pool partners.

AEP Ohio is proposing a Pool Termination rider to begin if and when it is needed to collect lost revenues as part of the Companies' move to competitive markets. The Companies state that the rider would be needed only if the Commission does not approve the Corporate Separation plan "as filed"[302] and the transfer of the Amos and Mitchell generating units.[303]

In the Modified ESP, AEP Ohio proposes to bear up to $35 million in pool termination "costs."[304] AEP Ohio will not seek to collect the first $35 million from customers under the Modified ESP. The $35 million figure is arbitrary and represents an overall AEP Ohio revenue target rather than a substantiated reason why the Companies should be made whole on lost revenues above $35 million.

The Companies propose that the rider should be non-bypassable. The Companies will compare the lost AEP Pool capacity revenue to increases in net revenue related to wholesale transactions or decreases in generation asset costs that result from the AEP Pool termination.[305] AEP Ohio plans to make this comparison against the actual AEP

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[301] OCC Ex. No. 110 at 20-21. (Ibrahim).

[302] AEP Ohio Ex. No. 103 at 22. (Nelson).

[303] Id.

[304] See id. at 23.

[305] Id. at 22-23.

Pool capacity revenue from the most recent twelve-month period preceding the effective date of the termination of the AEP Pool.[306]

There is no legal basis to include a pool termination provision in a utility's ESP. This rider is aimed at guaranteeing a level of revenue for AEP Ohio; such a guarantee is not part of the General Assembly's plan for competitive generation service. There is no provision under R.C. 4928.143(B)(2) which authorizes such a charge.

Further, there is no Commission precedent for the Pool Termination rider, because transactions within the AEP Pool have been disregarded for purposes associated with the Companies' ESP. In AEP Ohio's first ESP, the Commission decided -- and the Supreme Court of Ohio affirmed -- that revenue or sales margins from the opportunity sale of capacity and energy by AEP Ohio to other AEP Pool members would not be used to reduce AEP Ohio's FAC costs to be collected from customers.[307] The Commission also determined that sales margins from off-system sales need not be included in determining whether AEP Ohio meets the significantly excessive earnings test.[308]

It would be unfair and unreasonable to require customers to compensate AEP Ohio for revenues from off-system sales, when such revenues were not used to reduce the ESP rates. AEP Ohio's customers should not have to guarantee the Companies' earnings.

Moreover, the Pool Termination rider seemingly is one-sided in favor of the Companies. AEP Ohio does not mention what will happen if, after termination of the

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[306] Id. at 23.

[307] *In the Matter of the Application of Columbus Southern Power Company for Approval of an 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 et al., Opinion and Order (March 18, 2009) at 17.

[308] *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Administration of the Significantly Excessive Earnings Test under Section 4928.143(F), Revised Code, and Rule 4901:1-35-10, Ohio Administrative Code*, Case No. 10-1261-EL-UNC, Opinion and Order (January 11, 2011) at 29. This case is on appeal to the Supreme Court of Ohio.

AEP Pool, the Companies can find new or additional revenue that exceeds the sales margin received from other AEP Pool members in the past. Thus the rider apparently guarantees AEP a minimum level of off-system sales margin, but customers do not benefit from any additional sales margins that may exceed the alleged “lost revenues.” The rate mechanism is unfair to customers.

The rider also contravenes several State policy objectives. One such objective is for the Commission to ensure the availability of reasonably priced electric service. Allowing AEP Ohio to collect these additional revenues from customers will impede the attainment of this objective.

It is also a State policy to ensure effective competition by avoiding “anti-competitive subsidies.” The guarantee of revenues to AEP Ohio for earnings lost when the AEP pool is terminated could be an anti-competitive subsidy. Customers of AEP would be subsidizing AEP Ohio’s competitive wholesale service with funds collected from retail customers.

All this points to the need for the Commission to either reject the Pool Termination rider, or to modify it so that customers will receive the benefits from the Companies’ off-system sales.

8. AEP Ohio has not justified its proposal to collect up to $365 million from customers through the Distribution Investment Rider.

The Companies have proposed a three year $365.7 million Distribution Investment Rider (“DIR”) as part of the Modified ESP.[309] Consumers who budget for purchases of even $365 might find it difficult to believe that their public utilities would

[309] AEP Ohio Ex. No.116 at 11. (Allen).; AEP Ex. No. 110 at 11. (Kirkpatrick).

propose a mechanism for collecting $365 million with very little detail on the specifics of how the money will be spent.[310] Instead of a cost-benefit analysis to justify or support this massive spending program,[311] the Companies have only made claims of benefits.[312]

The Companies averred that the failure of their aging infrastructure is a primary cause of customer outages and reliability issues.[313] Company witness Kirkpatrick argued that the DIR would enable the Companies to take a more proactive approach of replacing equipment that has a likelihood of failure instead of waiting for the equipment to actually fail, which would improve system reliability.[314] He also noted that the Companies were concerned that some of the aging infrastructure does not support gridSMART technology.[315]

As an example, Mr. Kirkpatrick identified distribution substation circuit breakers as the type of equipment that the Companies would proactively replace.[316] The Companies argued that they need the DIR, because current funding levels are insufficient to keep up with the replacement of failed equipment as facilities continue to age.[317]

Rather than seeking rate increases in a distribution rate case with the thorough review entailed in that process -- including prudency -- the Companies seek a rider that would increase customer rates and reduce the risks faced by the Companies and their shareholders. Moreover, it appears as if the need for the $365.7 million DIR program is

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[310] See Staff Ex. No. 106 at 10. (Baker).

[311] Id. at 20.

[312] AEP Ohio Ex. No. 116 at 12. (Allen).

[313] AEP Ohio Ex. No. 110 at 12. (Kirkpatrick).

[314] Id.

[315] Id..

[316] Id. at 16.

[317] Id. at 18-19.

contingent on the Companies receiving more immediate cost recovery through the DIR Rider rather than through the Companies budget process and rate cases. When this contingency is added to the lack of detail in the DIR, it raises a question of just how much the DIR is actually needed, instead of just being wanted.

As support for the proposed DIR, Mr. Kirkpatrick noted that 71% of residential customers and 73% of commercial customers indicated that their service reliability expectations would remain the same over the next five years.[318] He added that another 19% of residential and 20% of commercial customers believed that future reliability expectations would increase and thus the DIR was consistent with the future reliability concerns of customers.[319] This is similar to the argument presented in the First Phase of the Companies ESP.[320] The only difference is that Mr. Kirkpatrick is now presenting the testimony instead of Mr. Hamrock. In both phases, the Companies have argued that the DIR complies with the statutory requirements of R.C. 4928.143(B)(2)(h) because of the Companies' spin on the customer survey results. However, in relying on the same survey results, the Companies have repeated the mistake they made in the prior first phase of the ESP.

The Companies focused on only part of the survey results while ignoring the complete results. Mr. Kirkpatrick focused on the 71% of residential customers and 73% of commercial customers who do not believe that their future reliability expectation will increase in the next five years as supporting the need for more funding. Mr. Kirkpatrick

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[318] AEP Ohio Ex. No. 110 at 19. (Kirkpatrick).

[319] Id.

[320] See AEP Ex. No.19 at 4 (October 21, 2011). (Rebuttal Testimony of Joseph Hamrock).

added these customers to the minority of 19% of residential customers and 20% of commercial customers who do expect an improvement in system reliability.

In making this argument, Mr. Kirkpatrick ignores the "flip side" of his argument which would take the same 71% of residential customers and 73% of commercial customers who do not believe that their future reliability expectations will change and add them to the remaining residential and commercial customers who actually anticipate a reduction in future reliability expectations and conclude that a similar majority are content with the status quo. In fact Staff witness Pete Baker reached this very conclusion when he stated "[T]he survey results indicated that a high percentage of OPC customers both residential and commercial were satisfied overall with the service reliability provided by OPC."[321]

Mr. Baker also noted that "[M]ost of OPC's reliability measures showed worse performance in 2011 [compared to 2010]."[322] He added that the CSP service territory also missed the Customer Average Interruption Duration Index ("CAIDI") standards in 2011 by 4.25 minutes or 3 percent.[323] Based on the survey results and the worse reliability measures for CSP in 2011, Mr. Baker noted that "**Staff recommends the Commission find that OPC's expectations are not currently in alignment with those of its customers**."[324] By reaching this conclusion and making this recommendation, Staff is essentially noting that the Companies failed to met the statutory requirements

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[321] Staff Ex. No. 106 at 7. (Baker).

[322] Id.

[323] Id. at 9.

[324] Staff Ex. No. 106 at 9. (Emphasis added). (Baker).

spelled out in R.C. 4928.143 (B)(2)(h) which requires the PUCO to ensure that the customers' and the Companies expectations are aligned.

In contrast to the Staff findings, Mr. Kirkpatrick cites to 71% of residential customers and 73% of commercial customers who do not anticipate any changes to their future reliability expectations.[325] He also cites to 19% of residential customers and 20% of commercial customers who believe that their future reliability expectations will increase.[326] However those two categories together do not add up to 100%. What Mr. Kirkpatrick does not address is the remaining 10%[327] of residential customers and 7%[328] of commercial customers who presumably expect their future reliability expectations to decrease in the next five years. The Company may have ignored these customers, the PUCO should not.

A more accurate conclusion regarding the customer survey results is that -- at best -- they are inconclusive regarding any expectation for reliability improvements. To the extent that the vast majority of customers support the status quo, the Company cannot meet the statutory requirements to ensure that "customers' and the electric distribution utility's expectations are aligned and that the electric distribution utility is placing sufficient emphasis on and dedicating sufficient resources to the reliability of its distribution system, because the majority of customers are content with the status quo or expect no improvement in reliability."[329]

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[325] AEP Ohio Ex. No. 110 at 12. (Kirkpatrick).

[326] Id.

[327] 100% - (71% + 19%) = 10%.

[328] 100% - (73% + 20%) = 7%.

[329] R.C. 4928.143.(B)(2)(h).

Staff witness Baker also raised concerns that the proposed "DIR is not sufficiently defined."[330] Although Mr. Kirkpatrick identified the type of equipment that the Companies would target to proactively replace under the DIR, the Company failed to provide significant important details about its plans. In fact, Mr. Baker identified four categories of information that Mr. Kirkpatrick failed to include in his testimony:

> 1. The quantity of these assets OPC plans to install during each year of the [Modified] ESP;
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> 2. The planed cost for each asset class;
>
> 3. The incremental amount of cost above previous levels; and
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> 4. The quantified improvement in reliability performance estimated to result from the incremental expenditures.[331]

Without this information, the Companies are essentially asking for a DIR that would be equivalent to a $365.7 million check that customers would have to pay without knowing whether these hundreds of million of dollars will provide customers with any real quantifiable reliability benefits commensurate with the cost. It would be completely unreasonable for the PUCO to approve this level of spending without some assurance that the spending will produce benefits that justify their cost.

The lack of information is even more alarming when it is more closely examined. For example, the Companies proposed a program but did not quantify the number of assets that they plan to proactively replace or the cost associated with those replacements. Without any program goals or objectives related to specific assets or planned costs for each asset class, there can be very little analysis done at the end of the program to determine if the spending matched what was projected. Without any detail beforehand,

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[330] Staff Ex. No. 106 at 10. (Baker).

[331] Id.

the Companies can arbitrarily change their mind regarding what type of equipment to purchase or replace, and customers would have very little -- if any recourse. Customers should have some understanding of the magnitude of such a program before they are asked to pay for it and informed only after-the-fact.

The Companies also failed to estimate the incremental amount of the cost above previous levels, so there is no understanding of whether the program would actually attempt to improve reliability by doing more than had previously been done. We do not know if the DIR would simply replace prior maintenance programs, and whether the planned spending is equal to -- let alone greater than -- recent equivalent spending levels. In fact, because we lack the specifics regarding proposed DIR spending, the Companies could actually spend fewer dollars in some equipment categories and yet customers would experience significant rate increase without any insurance or proof that service quality or reliability was improved. Moreover, as acknowledged by Mr. Kirkpatrick the Companies capital plans already include funding for substation circuit breakers.[332]

Finally and perhaps most importantly, Mr. Baker noted that there was no quantified improvement in reliability performance estimated to result from the incremental expenditures. In other words, the Company failed to include any type of cost-benefit analysis to determine if spending potentially hundreds of millions of dollars would actually produce any quantifiable reliability benefits for the customers that would be paying for the program. Such a cost-benefit analysis should be an absolute threshold requirement before a DIR is even contemplated. It would be folly to spend hundreds of

[332] Tr. Vol. IV at 1021. (Kirkpatrick).

millions of dollars only to see no quantifiable or recognizable difference in service quality or reliability.

As proposed, the DIR also fails to meet the requirements of R.C. 4928.143(B)(2)(h) because the DIR does not decouple revenues from sales and does not focus on distribution infrastructure modernization. Instead, Companies witness Kirkpatrick stressed the system reliability improvements under the DIR.[333] When the Companies' failure to include any means to measure the alleged system reliability improvements touted by Mr. Kirkpatrick in the Application is added to the fact that the interests of the Companies and their customers are **not** aligned, the DIR fails the statutory requirements of R.C. 4928.143(B)(2)(h).

The absence of this information demonstrates the Companies' failure to meet their burden of proof regarding the DIR. R.C. 4928.143(C)(2) states, "The burden of proof in the proceeding shall be on the electric distribution utility." The Companies cannot meet this burden of proof regarding the DIR without information like the items identified as missing by Staff witness Baker. Moreover, without a cost-benefit analysis there can be no finding that expenditures are reasonable and result in reasonably priced electric service.[334]

AEP Ohio witness Mr. Allen touted the benefit of the DIR over base distribution rate cases by arguing that the DIR would delay the need for distribution rate cases, and

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[333] AEP Ohio Ex. No. 110 at 11. (Kirkpatrick).

[334] R.C. 4928. *In the Matter of the Application of Columbus Southern Power Company for Approval of an 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, Opinion and Order (March 18, 2009) at 30-34, and 40-41. *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 (December 19, 2008) at 40-41.

that the Companies would not seek such a rate case with an effective date any earlier than June 1, 2015.[335] Thus, the allegation that, in exchange for $365.7 million in immediate additional costs, customers get the future benefit of no distribution rate case until June of 2015. Essentially, AEP Ohio's premise is that customers should pay more up front to delay some spending that could occur later. But in reality, delaying the spending until later (in distribution rate cases where there is thorough review) could cost customers less (or much less) than the upfront spending (under the limited review of a DIR). In light of the magnitude of the DIR program the customer benefit seems minimal if any at all.

Mr. Allen also noted that the DIR would encourage investment that could improve reliability.[336] Thus, Mr. Allen seemed to be testifying that the investment is needed and will be made only if the Companies can recover those costs through a rider. If the Companies' willingness to make the DIR investment is limited to being able to recover those costs through a rider, then it raises a question as to whether the need for the spending actually exists. It appears that the scrutiny, uncertainty and regulatory lag associated with a distribution rate case, may be impacting the actual need for the DIR program spending. This connection between the need for the spending and recovery for a rider should cause the PUCO to more closely scrutinize the DIR. Moreover, when this issue is taken in consideration with the problems identified by Staff,[337] the PUCO should reject the DIR.

Finally, with regard to the DIR, as noted below in OCC's discussion of rate affordability in this Brief, the PUCO is required to consider basic affordability of rates

[335] AEP Ohio Ex. No. 116 at 12. (Allen).

[336] Id.

[337] Staff Ex. No. 106. (Baker).

from a Modified ESP on customers, as well as the impact of an ESP on at-risk or low income customers.[338] To that end, the inclusion of a three-year $365.7 million DIR program would only add to the burden faced by a significant number of the Companies' customers under the current rates. When the lack of detail included in the Modified ESP is added to the lack of a basic cost-benefit analysis, it is clear that the DIR would only burden customers with additional costs without any quantifiable or measurable benefits in reliability.

In the event that the PUCO were to support a DIR despite the many problems associated with the proposal, then the Commission should require that the shortcomings noted by Staff are sufficiently addressed. Moreover, the PUCO should ensure that any DIR spending is not duplicative of other Company spending.

9. AEP Ohio has not justified the need to expand the gridSMART program, especially prior to completion of the gridSMART pilot project.

To the extent that the Company proposed including gridSMART costs in the DIR, there are numerous concerns that need to be addressed before the Companies are authorized to go forward. The Staff recommended that no additional gridSMART costs be authorized prior to a thorough evaluation of the Phase I Pilot project which will not be completed until December 31, 2013.[339] Therefore, it would be premature to implement a DIR to recover additional gridSMART costs before knowing that the gridSMART costs already spent to date provided a benefit for customers. Staff witness Cleaver explained that any request to expand gridSMART at this time was premature because:

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[338] R.C. 4928.02(A) and (L).

[339] Staff Ex. No. 107 at 7. (Cleaver).

> In addition to the fact that **the Phase I Pilot has not been completed, neither** the **total costs nor the benefits** of a system wide deployment of smart grid throughout the AEP Ohio service territory have been clearly defined. Furthermore, the enhanced scope due to the ARRA funding requirements has added both complexity and uncertainty to the project.[340]

Mr. Cleaver added that the Companies recognized these concerns and noted that they needed "additional time to study the benefits and customer acceptance of CES, smart appliances, and in-home technologies to support real time pricing."[341] Staff witness Greg Scheck echoed these concerns regarding gridSMART expansion, "The Staff and the Commission will not know until that time, [March 31, 2014] whether Phase 1 in its totality has been a success or not based on the metrics agreed to with the USDOE and any further Staff evaluation and analysis."[342]

Despite this need for information and analysis, noted above, and an acknowledged need to justify gridSMART costs, Mr. Kirkpatrick noted that the Companies plan to go forward with elements of gridSMART in the normal course of business.[343] This expansion plan flies in the face of sound business principles of reviewing the success and failure of the pilot project before going forward with expansion and therefore should be rejected by the Commission.

10. If the Commission approves the storm damage rider, any carrying charges should not be calculated using the Companies' Weighted Average Cost of Capital.

In addition to not quantifying the future costs to customers for storm expenses, discussed above in the ESP/MRO comparison section, AEP Ohio also does not specify

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[340] Staff Ex. No. 107 at 9. (Cleaver). (Emphasis added).

[341] Id. at 10.

[342] Staff Ex. No. 105 at 5. (Scheck).

[343] AEP Companies Ex. No. 110 at 10. (Kirkpatrick).

the carrying charge rate for these deferrals. Any carrying charges should not be calculated using the Companies' WACC because the storm damage mechanism would not include capital costs incurred as a result of a major storm.[344] Instead, such capital costs "would become a component of the DIR or would be included in rate base in the next distribution rate case."[345]

Thus, it would be more appropriate to use a lower rate -- such as the Companies' cost of long-term debt -- to calculate carrying charges on any deferrals from the storm damage mechanism. The Commission's Order in this proceeding should specify that AEP Ohio use a lower carrying charge rate on any deferrals from the storm damage mechanism.

11. Allocation of the Economic Development Cost Recovery Rider should be based on customers' share of total revenues, not only distribution revenues.

In its Modified ESP, AEP Ohio proposed to consolidate some riders into a single set of rates for both the CSP and OP rate zones.[346] One of those riders is the non-bypassable EDR, which is applied to customers' base distribution rates.[347] The EDR is designed to collect from customers the revenues (known as the delta revenues) that AEP Ohio forgoes as a result of offering its economic development programs and initiatives to

[344] See AEP Ohio Ex. No. 110 at 21. (Kirkpatrick).

[345] Id.

[346] AEP Ohio Ex. No. 111 at 3. (Roush). Other riders to be consolidated are the Transmission Cost Recovery Rider and gridSMART Rider.

[347] See id. at Exhibit DMR-5, Proposed Tariff Sheet No. 482-1.

mercantile customers,[348] with discounts totaling $80.4 million ($46.4 million in the OP rate zone and $34.0 million in the CSP rate zone).[349]

Under the Companies' allocation methodology, residential customers pay a disproportionate share of AEP Ohio's forgone revenues related to its economic development discounts and initiatives. Ohio Adm. Code 4901:1-38-08(A)(4), which addresses revenue collection, states:

> The amount of the revenue recovery rider shall be spread to all customers in proportion to the **current revenue distribution** between and among classes, subject to change, alteration, or modification by the commission. (Emphasis added.)

AEP Ohio, however, allocates collection of delta revenues based on just a single portion of service -- distribution. This allocation method is unfair to residential customers, who are served at the lowest voltage level among all other AEP Ohio customers and thus assume a larger share of the distribution service cost.

The base distribution revenues for CSP are approximately $339 million, of which $222 million -- 65.4% -- is the residential customers' share.[350] For OP, the base distribution revenues are approximately $325 million, with residential customers' share at $188 million -- 58% of the allocation.[351] On a consolidated basis, AEP Ohio's residential customers will pay 61.7% of the Companies' delta revenues.

Thus, a disproportionate share of delta revenues is collected from residential customers. The Commission should order that AEP Ohio allocate the collection of delta

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[348] See AEP Ohio Ex. No. 101 at 7. (Powers).

[349] See *In the Matter of the Application of Ohio Power Company to Adjust Its Economic Development Cost Recovery Rider Pursuant to Rule 4901:1-38-08(A)(5), Ohio Administrative Code,* Case No. 12-688-EL-RDR, Application (February 22, 2012) at Schedules 1 and 2.

[350] See OCC Ex. No. 110 at 15, n.26. (Ibrahim).

[351] See id. at 15, n.27.

revenues to all customers in proportion to the current **total** revenue -- distribution, transmission, and generation -- between and among classes. This would meet the standard in Ohio Adm. Code 4901:1-38-08(A)(4).

The Residential Consumer Advocates' recommendation is consistent with the practices followed by Dayton Power and Light Company ("DP&L"). In its recent (March 20, 2012) application, DP&L updated its Economic Development Rider, and allocated the delta revenues for DP&L's various economic development initiatives based on customers' share contribution to its total revenues, not just distribution revenues.[352] The Commission should adopt this approach for AEP Ohio.

AEP Ohio's revenues include more than just the distribution revenues that it uses for determining the collection of delta revenues from customers. Consistent with Ohio Adm. Code 4901:1-38-08(A)(4), all revenues, not just distribution revenues, should be used to determine the collection of AEP Ohio's delta revenues from among the customer classes.

12. The interim auctions proposed by the Companies would result in higher prices for residential customers, and therefore the Commission should adopt a different approach to produce reasonably priced service.

In its Modified ESP, AEP Ohio has proposed to hold interim auctions to meet its SSO load requirements during the first five months of 2015. The Companies' proposal, however, would result in SSO rates that are even further above fully competitive market prices than would be the case if the Companies continued to price SSO energy at actual fuel costs. Such rates would be unreasonable.

[352] See id. at 18, n.31.

AEP Ohio proposes to continue to meet the capacity obligation and energy requirements associated with SSO load under its Pool Agreement, until transfer of the Companies' generating assets, associated fuel contracts, and power-supply contracts to a generation affiliate, and termination of the Pool Agreement on January 1, 2014. For 2014, AEP Ohio proposes to meet its SSO capacity obligation and energy requirements through purchases of capacity and energy (along with ancillary services) from its generation affiliate. From January 1 through May 31, 2015, the Companies would continue to purchase capacity from the generation affiliate, but would procure energy for SSO load through an auction process.

From June 1, 2012 through December 31, 2013, SSO customers would pay for power supply at the base generation rate plus actual fuel and other variable costs recovered through the FAC. For 2014, SSO power supply from the generation affiliate would continue to be priced at the base generation rate plus actual costs to be collected through the FAC. For the first five months of 2015, capacity purchases from the generation affiliate would be priced at $255/MW-Day, while energy procured through the SSO energy auction would be priced at the auction-clearing price.[353]

AEP Ohio elected to self-supply its capacity obligations under the FRR option of the RPM market. The FRR obligation to self-supply will continue after the proposed transfer of the Companies' generation assets and contracts to the generation affiliate on January 1, 2014, and will terminate on May 31, 2015.

AEP Ohio proposes to discontinue energy purchases from its generation affiliate in order to introduce competition in the provision of SSO power supply, and to instead

[353] AEP Ohio Ex. No. 103 at 7. (Nelson).

procure SSO energy supply through an auction process. According to Mr. Powers, "the auction-based process will provide an opportunity for competitive suppliers and marketers to bid for AEP Ohio's SSO load."[354]

But this opportunity for competitive energy supply is likely to come at the expense of reasonable rates for SSO customers. Based on AEP Ohio's price projections, SSO customers will pay higher prices for generation service under the Companies' interim auction proposal than if AEP Ohio were to continue purchasing energy from its affiliate in the first five months of 2015.

If the Companies were to continue purchasing capacity at the base generation rate proposed by the Companies and energy at cost from its generation affiliate, the SSO generation rate for the period January 1 through May 31 of 2015 would be about $62/MWh.[355] On the other hand, purchasing capacity at $255/MW-day and energy at the expected market price prevailing during the first five months of 2015, as under the Company's proposal, would result in an SSO generation rate of about $67/MWh.[356] In other words, by AEP Ohio's own estimates, the generation rate paid by SSO customers during the first five months of 2015 under the Companies' proposal would likely be about 8.5% higher than if AEP Ohio were to continue purchasing both energy and capacity at cost from its generation affiliate.[357] The difference may be even greater; OCC witness Wallach estimates a competitive market price for full-requirements SSO supply (i.e.,

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[354] AEP Ohio Ex. No. 101 at 20. (Powers).

[355] AEP Ohio Ex. No. 111 at Exhibit DMR-2. (Roush)

[356] See OCC Ex. No. 117 at 11. (Wallach).

[357] Id.

capacity and energy) of about $60/MWh for the first five months of 2015.[358] The Companies' projected SSO rate of $67/MWh would be about 12% higher than Mr. Wallach's estimate of the competitive market price for the first five months of 2015.[359]

AEP Ohio's proposal does not ensure that reasonably priced electric retail service will be available to the Companies' customers. In order to help ensure that AEP Ohio's customers receive reasonably priced retail electric service, the Commission should require that the SSO agreement between AEP Ohio and its generation affiliate continue to price capacity at the base generation rate and energy at the actual cost of fuel and ancillary services from January 1 through May 31 of 2015. Alternatively, for the period from January 1 through May 31, 2015, AEP Ohio should purchase SSO capacity from its generation affiliate at the prevailing RPM market price. Either alternative would likely result in more reasonably priced electric service than would be the case under the AEP Ohio's proposal.

13. The Commission should either reject AEP Ohio's proposed shopping credit as an alternative to its two-tiered capacity price or modify the credit as suggested by OCC witness Wallach.

AEP Ohio's primary proposal for pricing of capacity charges is two-tiered capacity pricing scheme and implementation of the RSR. As an alternative, AEP Ohio offers to charge CRES providers $355.72/MW-Day while AEP Ohio is an FRR entity (during the period between June 1, 2012 and December 31, 2014), but provide a $10/MWh shopping credit for SSO customers who switch to a CRES provider.[360] AEP

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[358] Id.

[359] Id.

[360] See AEP Ohio Ex. No. 116 at 15-16. (Allen)

Ohio apparently conducted no specific analysis in developing the shopping credit.[361] The $10/MWh value was selected simply because it would provide a $10 per month credit to a residential customer with usage of 1,000 kWh per month.[362]

The proposed shopping credit would be available on a first come, first served basis by customer class, and would be applicable to shopping load up to a limit of 20% of SSO load per customer class from June 1, 2012 through May 1, 2013, 30% of SSO load per customer class from June 1, 2013 through May 31, 2014, and 40% of SSO load per customer class from June 1, 2014 through December 31, 2014.[363] AEP Ohio also proposes to cap the shopping credits at a total of $350 million over the period June 1, 2012 through December 31, 2014.[364]

There has been some criticism of this shopping credit approach. RESA witness Ringenbach, for example, faulted the credit because it does not bring customers to an RPM-based capacity price, and because the first come, first served approach would be confusing to customers.[365] RESA suggests that if the capacity cost is so high that it will prohibit shopping, "change the capacity cost rather than apply a credit."[366]

The Residential Consumer Advocates agree with RESA that the shopping credit proposed by AEP Ohio as an alternative to the two-tiered pricing plan serves no useful purpose. Because the base charge of $355.72/MW-Day is considerably higher than RPM

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[361] See Tr. Vol. V at 1437-1438. (Allen).

[362] See OCC Ex. No. 117 at 19 and Attachment 1. (Wallach).

[363] AEP Ohio Ex. No. 116 at 16. (Allen).

[364] Id.

[365] RESA Ex. No. 102 at 11. (Ringenbach).

[366] Id.

prices and even the two-tiered capacity charge, the proposed alternative provides little incentive for customers to shop. The Commission should reject the proposal.

If, however, the Commission moves forward with the proposed shopping credit, which the Residential Consumer Advocates do not recommend, the credit should be allowed only under limited circumstances. As OCC witness Wallach testified, the credit may be offered to shopping customers "only to the extent that such switching increases the Company's operating margins and to the extent that such operating margins are not already reflected in the price paid by competitive retail suppliers for purchases of FRR capacity from AEP Ohio."[367] The margins should be credited either to CRES providers through the price charged for capacity or to switching customers through a shopping credit, but not both.[368]

In addition, Mr. Wallach testified that AEP Ohio should provide a shopping credit only if the capacity price approved in the Capacity Charge Case is set at the full embedded cost of capacity and the credit reflects the expected margin from wholesale energy sales from the Companies' generating resources freed up by the migration of SSO customers to CRES providers.[369] A shopping credit would not be appropriate, however, if the capacity price approved in the Capacity Charge Case reflects an offset for the expected market value of energy associated with FRR capacity. In this case, the sales margin would already be captured in the price paid by competitive retail suppliers for FRR capacity.[370]

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[367] OCC Ex. No. 117 at 18. (Wallach)

[368] Id.

[369] Id. at 19.

[370] Id.

In addition, AEP Ohio's proposal to cap the total amount for such credits would not be appropriate if the shopping credit were set at the expected sales margin.[371] In such an instance, there would be no benefit to customers for shopping because the shopping credit would equal the additional margins attributable to those customers' decisions to shop. By capping the amount available for shopping credits, AEP Ohio would retain any operating profits from customer switching in excess of the payment cap.[372]

Again, the Commission should reject AEP Ohio's proposed alternative capacity plan. But if it does not reject the plan, the Commission should modify it as recommended by OCC witness Wallach.

As proposed, the Modified ESP will increase the average rate for residential customers for the period June 2012 to May 2013 by an average of 6%.[373] This percentage increase in rates is greater than the increase for any other customer class. The Commission can mitigate this unreasonable increase by rejecting the RSR or ordering the Companies to collect the RSR in a rider calculated to follow cost causality principles. An RSR that is calculated based on cost causality would reduce the average rate increase to a more reasonable 3% average.[374]

D. Bill Impact on Customers

The State policies for the provision of competitive retail electric service set forth in R.C. 4928.02 spell out a number of objectives, including to:

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[371] See id. at 19-20.

[372] Id. at 20.

[373] OCC Ex. No. 110 at 25. (Ibrahim); AEP Ohio Ex. No. 111 at Ex. DMR-1. (Roush).

[374] OCC Ex. No. 110. (Ibrahim).

> Ensure the availability to consumers of adequate, reliable, safe, efficient, nondiscriminatory, and **reasonably priced retail electric service.**[375]

It is important to recognize that this is the first policy provision listed in the statute and is from the perspective of customers, the most important consideration in the State policy.[376] Thus the price that customers pay for electric service and the affordability of that service are key considerations for the PUCO.

The Companies, however, are not focused on this policy. Rather, they stress that customers should be responsible for keeping the Companies financially whole.[377] But R.C. 4928.02 does state such an alleged responsibility for customers to serve as protection for utility finances.

Thus, when the Commission considers the merits of the Companies' Modified ESP, the Commission must consider the impact and implications of the Modified ESP on customers. Although the Companies paid lip service to how the Modified ESP meets this state policy goal,[378] in reality, the focus of the Companies Modified ESP is to maintain the financial well being of the Companies and their shareholders regardless of the negative impact on customers. For instance, residential customers -- the most likely to

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[375] R.C. 4928.02(A). (Emphasis added).

[376] *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 (December 19, 2008) at 17 where the Commission noted the significant economic difficulties facing residential customers; at 18 where the Commission eliminated commitments for generation and environmental reclamation; and at 25 where the Commission rejected the Deferred Generation Cost Rider due ton its negative impact on Ohio's economy. See also *In the Matter of the Application of Columbus Southern Power Company for Approval of an 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, Opinion and Order (March 18, 2009) at 30, where the Commission eliminated the inclusion of automatic non-FAC portion of generation rates.

[377] AEP Ohio Ex. No. 101 at 5. (Powers).

[378] AEP Ohio Ex. No. 118 at 4. (Dias).

experience difficulties paying their electric bills-- will get stuck with an extraordinarily large and unreasonable allocation of the RSR charge under the Companies' Modified ESP. This rate impact will only exacerbate the difficulties many residential customers are already having paying their current electric bills.

In addition to the more general policy guideline, R.C. 4928.02 also requires the State -- in this case through the PUCO to:

> **Protect at-risk populations**, including, but not limited to, when considering the implementation of any new advanced energy or renewable energy resource;[379]

Therefore, the Commission must pay particular attention to the impact of the Modified ESP on the Companies at-risk customers, such as low-income residential customers. When evaluating the impact of the Modified ESP on customers and low-income customers, a good starting point is the impact of current rates on customers -- before the Modified ESP proposed increases would be put in place.

OCC Witness Williams provided testimony on the impact of the current rates on at-risk or low-income customers in the Companies service territories in 2011. He testified that approximately 243,025 customers or up to 20% of the Companies' total customers are significantly negatively impacted by the current rates.[380] Mr. Williams noted that approximately 79,560 (6.2%) of the Companies' customers were actually disconnected for non-payment in 2011.[381] These customers faced disconnection as a last resort because they could not pay their current electric bills.

[379] R.C. 4928.02(L). (Emphasis added).

[380] Id.

[381] OCC Ex. No. 113 at 6. (Williams); Tr. Vol. XI at 3206. (Williams).

The Companies did not dispute these numbers, although they questioned whether the disconnection statistics for 2011 could include customers that were disconnected more than one time during the year.[382] In response to that argument, Mr. Williams noted that there is an additional and significant cost for customers associated with disconnection and reconnection, and that at-risk or low-income customers do not have the financial resources to face disconnection more than once in a year, unless their financial condition was such that they had no other option.[383] Thus, despite the Companies' assertions to the contrary, a significant number of customers had their electric service disconnected in 2011 because of problems paying their bills.

In addition to these levels of disconnections, another approximately 112,395 (8.8%) of the Companies' customers participated in the Percentage of Income Payment Plan ("PIPP") Plus plan under the current rate structure in 2011.[384] In order to participate on the PIPP Plus program, a customer must be certified as a low-income customer having an income at or below 150% of the federal poverty guidelines.[385] Thus PIPP Plus customers are by definition already at-risk under the current rate structure. There can be no dispute that PIPP Plus customers participate in the PIPP Plus program not because they want to, but instead they participate in the program because they are having significant difficulties paying their bills under the current rate structure. Moreover, while PIPP Plus customers pay a percentage of their income for electric service, they remain financially responsible for the entire bill. Therefore, even if their actual payment does

[382] Tr. Vol. XI at 3213. (Williams).

[383] Tr. Vol. XI at 3220. (Williams).

[384] OCC Ex. No. 113 at 6. (Williams).

[385] See Department of Development eligibility rules at Ohio Admin. Code 122.5-3-02(B)(1).

not increase if there is a Modified ESP rate increase, the PIPP Plus customers' ultimate financial responsibility would increase. For these at-risk customers, any Modified ESP rate increase will make an already tenuous position even more difficult.

Finally, Mr. Williams noted that another approximately 51,270 (4.0%) of the Companies' customers participate in some type of payment plan in order to be able to afford their electric service and avoid disconnection in 2011.[386] These customers are also negatively impacted by the Companies current rates, and are pursuing payment plans in an attempt to keep their electric service affordable.

In evaluating theses numbers the Commission should keep in mind that the statistics used by Mr. Williams is information that Electric Distribution Utilities ("EDU's"), including the Companies themselves, provide to the PUCO Staff who in turn make the information available to OCC upon request.[387] Having one in five residential customers experience difficulty in paying their bills under the current rate does not paint a pleasant picture for the Companies' customers, both now and in the future if and when any additional rate increases from the proposed Modified ESP are implemented.

The Companies projected an increase of 6.21% for CSP customers and 5.64% for OP customers[388] as a result of the Modified ESP. This increase is for the first year of the Modified ESP and will grow even larger in years 2 and 3 and have the ultimate effect of negatively impacting customer bills and forcing even more residential customers into one of the three at-risk categories discussed by Mr. Williams.

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[386] OCC Ex. No. 113 at 6. (Williams).

[387] Tr. Vol. XI at 3206. (Williams).

[388] AEP Companies' Ex. No. 111 at Ex. DRM-1, page 1 of 2 and 2 of 2. (Roush).

It is also worth noting that the docket in this case contains over 234 letters and correspondence from customers, groups of customers, businesses, community leaders, school officials and others all opposing the Modified ESP and the rate increases it would impose. These customers filed letters opposing the proposed Modified ESP rate increases because they fear that they will end up paying higher rates than presently in place.

In addition to the statistics that Mr. Williams cited, he also noted, that according to the Companies' own Customer Perception Survey, only 58% of customers gave the current rates a positive rating.[389] That means that 42% of the Companies' customers view the current rates negatively. Even if the 42% of customers who view the Companies' current rates negatively include all of the customers who had their service disconnected, participated in the PIPP Plus or another payment plan, then an additional 22% of the Companies' customers also view rates negatively.

On the other hand, if not all of those customers are included in the 42%, then that percentage of other customers view the current rates negatively becomes even larger. Then the question for the PUCO must be how many of the customers that view the current rates negatively eventually may fall into the category of being disconnected, a PIPP Plus participant or payment plan participant as the result of any increase from the Modified ESP. Moreover, when this 42% is taken together with the 20% of customers that are having difficulty paying their current rates it is clear that affordability of basic electric service is an issue for a significant number of customers -- before any increase from the Modified ESP is considered.

[389] OCC Ex. No. 113 at 7. (Williams).

In addition to the evidence presented by Mr. Williams, the City of Hillsboro presented the testimony of Mayor Drew Hastings who described the affordability of the current rates as well as the impact on affordability of any potential Modified ESP increases.[390] In addition to negatively impacting the City through potentially higher electric rates for traffic signals and street lighting, the Mayor described the trickle down implications of any rate increase, wherein the City and businesses within the City may be forced to pass through cost increases to residential customers.[391] This trickle down phenomena demonstrates that any projected impact of electric rate increases on residential customers significantly understates the actual cost increases that residential customers will experience.

These basic affordability concerns are not unique to residential customers, as numerous commercial and industrial customers also testified on the negative impact of the current rates and any potential Modified ESP rate increase. Among these witnesses were: Richard Walters of the Lima Refining Company,[392] John Siefker of the Whirlpool Corporation,[393] Bradley Belden of Belden Brick,[394] David W. Johnson of Summitville Tiles,[395] Ed Forshey of AMG Vandium,[396] John Burke of OSCO Industries,[397] R. Reed Fraley on behalf of the Ohio Hospital Association "OHA"),[398] and Roger Geiger on

[390] City of Hillsboro Ex. No. 101. (Hastings).

[391] Id. at 3-4.

[392] OMAEG Ex. No. 105A. (Walters Redacted).

[393] OMAEG Ex. No. 103A. (Siefker Redacted).

[394] OMAEG Ex. No. 104A. (Belden Redacted).

[395] OMAEG Ex. No. 106A. (Johnson Redacted).

[396] OMAEG Ex. No. 101A. (Forshey Redacted).

[397] OMAEG Ex. No. 102A. (Burke Redacted).

[398] OHA Ex. No. 101. (Fraley).

behalf of NFIB/Ohio,[399] all of whom described the negative impacts on their businesses from any electric rate increase resulting from the Modified ESP case.

Although individually, none of these witnesses represented an entity as large as the AEP Companies, when taken in the aggregate they represent a significant portion of Ohio's economy that cannot be ignored. These witnesses described the difficulty faced by their companies under the current rates, as well as if they were to face a Modified ESP rate increase.

Such testimony stands in stark contrast to the Companies' tales of possible woe and financial hardship if the PUCO were to deny its revenue requests.[400] However the Companies' proposed Modified ESP did not address the negative impact on these numerous commercial and industrial customers from their goal of protecting the Companies and their shareholders from any financial harm. Among the issues raised by these witnesses were: potential loss of current employees,[401] inability to make capital investments,[402] and the inability to expand or hire additional employees.[403] All of these negative impacts should be considered by the PUCO and weighed against any harm claimed by the Company.

In cross-examination many of these same commercial and industrial customer witnesses explained that in the event they could not mitigate any rate increase from the Modified ESP, they would be forced to pass along any increase to their customers -- who

[399] NFIBO Ex. No. 101. (Geiger).

[400] See e.g. Companies' Ex. No. 101 at 10, 17 and 18. (Powers).

[401] OMAEG Ex. No. 103A at 6. (Siefker Redacted); OMAEG Ex. No. 104A at 6. (Belden Redacted.; OMAEG Ex. No. 105A at 6 (Walters Redacted).; OMAEG Ex. No. 106A at 6 (David W. Johnson Redacted.; OHA Ex. No. 101 at 3 (Fraley).

[402] OMAEG Ex. No. 104A at 6 (Belden Redacted).; OMAEG Ex. No. 105A at 6 (Walters Redacted).; OMAEG Ex. No. 106A at 6 (David W. Johnson Redacted).

[403] OMAEG Ex. No. 103A at 6. (Siefker Redacted).

in many cases would be residential customers.[404] Thus residential customers would face the double whammy of a potential direct first year Modified ESP rate increase of 6.21% for CSP customers and 5.64% for OP customers[405] plus an additional undetermined indirect Modified ESP rate increase from higher costs charged to commercial and industrial customers.

Residential customers then also face the inevitable negative impact from schools and hospitals having to pay higher energy costs. Although there are limits to the ability of schools and hospitals to pass along electric rate increases, it is axiomatic that to the extent both schools and hospitals are unable to otherwise mitigate any Modified ESP rate increase, residential customers -- who fund schools through taxes and levies, and pay for hospital medical costs -- will eventually foot the bill for those electric rate increases.

V. CONCLUSION

Under the Companies' Modified ESP the Commission must resolve a myriad of issues. Fundamentally, the Commission must determine if the transition to competition, outlined in the Modified ESP, is reasonable and supportable under Chapter 4928 of the Ohio Revised Code. The Commission must determine whether the Companies' Modified ESP passes the statutory test, i.e. whether "the pricing and other terms and conditions, including any deferrals" is more favorable in the aggregate than a market rate offer. The Commission in its analysis must also individually examine each part of the Modified ESP in light of the policy objectives of R.C. 4928.02. Indeed, under R.C. 4928.06(A), the

[404] Tr. Vol. XIII at 3563. (Forshey); Tr. Vol. XIII at 3606. (Siefker); Tr. Vol. XIII at 3623. (Belden); Tr. Vol. XV at 4219. (David W. Johnson).

[405] AEP Companies Ex. No. 111 at Ex. DRM-1, page 1 of 2 and 2 of 2. (Roush).

Commission has a duty to ensure these policies are effectuated under the Companies' SSO.

The overwhelming evidence adduced at the evidentiary hearing shows that the Companies' Modified ESP does not pass the statutory test. Because of this, the Commission should reject the Modified ESP or modify and approve the ESP. The Commission can also modify the ESP even if it determines that the statutory test is met, so long as the modifications are supported by the record.

The Residential Consumer Advocates recommend extensive modifications to the Companies' ESP. These modifications include, but are not limited to, rejecting the rate stability rider (which could impose increases up to $1 billion on customers), rejecting excessive carrying costs on deferrals, and rejecting riders which will unnecessarily add costs onto customers' bills. In light of the likely rate increases to residential customers under new SSO rates, the Residential Consumer Advocates support shareholder funded bill payment assistance to low income customers.

The modifications proposed by the Residential Consumer Advocates are intended to assure that the base generation rates of residential customers are reasonably priced, consistent with this policy objective under R.C. 4928.02(A). While a great deal of emphasis has been placed on the benefits of competition, to date, very few residential customers have elected to shop. Under the Companies' Modified ESP, during the term of the ESP, the great majority of residential customers may not receive the benefit of market rates. Thus, for residential customers, reasonably priced electric service should be the end goal. The Residential Consumer Advocates urge the Commission to focus as well on this end goal—ensuring reasonably priced electric service for customers within the State, in keeping with R.C. 4928.02(A).

Respectfully submitted,

BRUCE J. WESTON
CONSUMERS' COUNSEL

/s/ Maureen R. Grady
Maureen R. Grady, Counsel of Record
Terry L. Etter
Joseph P. Serio
Assistant Consumers' Counsel

Office of the Ohio Consumers' Counsel
10 West Broad Street, Suite 1800
Columbus, Ohio 43215-3485
(614) 466-9567 – Grady
(614) 466-7964 – Etter
(614) 466-9565 – Serio
grady@occ.state.oh.us
etter@occ.state.oh.us
serio@occ.state.oh.us

/s/ Michael R. Smalz

Michael R. Smalz
Joseph V. Maskovyak
Ohio Poverty Law Center
555 Buttles Avenue
Columbus, Ohio 43215
Telephone: 614-221-7201
msmalz@ohiopovertylaw.org
jmaskovyak@ohiopovertylaw.org

On Behalf of the Appalachian Peace and Justice Network

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing Initial Post-Hearing Brief has been served electronically upon those persons listed below this 29th day of June 2012.

/s/ Maureen R. Grady___________
Maureen R. Grady
Assistant Consumers' Counsel

PARTIES SERVED

Werner.margard@puc.state.oh.us
John.jones@puc.state.oh.us
lmcalister@bricker.com
tsiwo@bricker.com
MWarnock@bricker.com
stnourse@aep.com
mjsatterwhite@aep.com
tobrien@bricker.com
fdarr@mwncmh.com
joliker@mwncmh.com
ghummel@mwncmh.com
ricks@ohanet.org
msmalz@ohiopovertylaw.org
jmaskovyak@ohiopovertylaw.org
Philip.sineneng@thompsonhine.com
Dorothy.corbett@duke-energy.com
Elizabeth.watts@duke-energy.com
myurick@taftlaw.com
dconway@porterwright.com
cmoore@porterwright.com
haydenm@firstenergycorp.com
mkurtz@BKLlawfirm.com
dboehm@BKLlawfirm.com
emma.hand@snrdenton.com
doug.bonner@snrdenton.com
dan.barnowski@snrdenton.com
JLang@Calfee.com
lmcbride@calfee.com
talexander@calfee.com
ssolberg@eimerstahl.com

jejadwin@aep.com
mhpetricoff@vorys.com
smhoward@vorys.com
mjsettineri@vorys.com
wmassey@cov.com
henryeckhart@aol.com
jesse.rodriguez@exeloncorp.com
sandy.grace@exeloncorp.com
kpkreider@kmklaw.com
dmeyer@kmklaw.com
holly@raysmithlaw.com
BarthRoyer@aol.com
Gary.A.Jeffries@dom.com
gthomas@gtpowergroup.com
laurac@chappelleconsulting.net
Christopher.miller@icemiller.com
Gregory.dunn@icemiller.com
Asim.Haque@icemiller.com
sjsmith@szd.com
tsantarelli@elpc.org
nolan@theoec.org
trent@theoec.org
cathy@theoec.org
ned.ford@fuse.net
gpoulos@enernoc.com
sfisk@nrdc.org
zkravitz@taftlaw.com
aehaedt@jonesday.com
dakutik@jonesday.com
callwein@wamenergylaw.com
Terrance.Mebane@ThompsonHine.com

aaragona@eimerstahl.com
dstahl@eimerstahl.com
whitt@whitt-sturtevant.com
thompson@whitt-sturtevant.com
vparisi@igsenergy.com
mswhite@igsenergy.com
kaelber@buckleyking.com
walter@buckleyking.com
judi.sobecki@dplinc.com
randall.griffin@dplinc.com
Carolyn.Flahive@ThompsonHine.com
Stephanie.Chmiel@ThompsonHine.com
rjhart@hahnlaw.com
rremington@hahnlaw.com
djmichalski@hahnlaw.com
jhummer@uaoh.net
tlindsey@uaoh.net
ssalamido@cloppertlaw.com
arthur.beeman@snrdenton.com
bpbarger@bcslawyers.com
cendsley@ofbf.org
dane.stinson@baileycavalieri.com
jmclark@vectren.com
sbruce@oada.com
rsugarman@keglerbrown.com
matt@matthewcoxlaw.com
mchristensen@columbuslaw.org
toddm@wamenergylaw.com
rburke@cpv.com
bkelly@cpv.com
eisenstatl@dicksteinshapiro.com
lehfeldtr@dicksteinshapiro.com
kinderr@dicksteinshapiro.com
kwatson@cloppertlaw.com
Thomas.millar@snrdenton.com
James.rubin@snrdenton.com
yalami@aep.com
greta.see@puc.state.oh.us
Jonathan.tauber@puc.state.oh.us