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, Revised 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

JOINT APPLICATION FOR REHEARING AND MEMORANDUM IN SUPPORT OF THE OMA ENERGY GROUP AND THE OHIO HOSPITAL ASSOCIATION

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On behalf of The Ohio Hospital Association

BEFORE
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JOINT APPLICATION FOR REHEARING

Pursuant to Section Ohio Revised Code Section ("R.C.") 4903.10 and Ohio Administrative ("OAC") Rule 4901-1-35, the OMA Energy Group ("OMAEG") and the Ohio Hospital Association ("OHA", collectively, "OMAEG/OHA") respectfully submit this Application for Rehearing of the August 8, 2012 Opinion and Order ("August 8 Order") issued by the Public Utilities Commission of Ohio ("Commission") modifying and approving AEP-Ohio's electric security plan ("ESP"). The Commission's August 8 Order is unreasonable and unlawful in the following respects:

A. The Commission's finding that the ESP, as modified, including the pricing and all other terms and conditions, deferrals and future recovery of the deferrals, and quantitative and qualitative benefits, is more favorable in the aggregate than the expected results of a market rate offer ("MRO") is unreasonable and unlawful.

B. The Commission's decision to permit AEP-Ohio to defer the difference between $189 per megawatt-day ("MW-D") and the PJM reliability pricing model ("RPM") auction price for capacity was unreasonable and unlawful.

C. The Commission's decision to authorize the Retail Stability Rider ("RSR") was unjust and unreasonable.

D. The Commission's total bill cap at 12% is unreasonably vague.

As discussed in greater detail in the Memorandum in Support attached hereto, OMAEG/OHA respectfully request that the Commission grant this Application for Rehearing and clarify and modify its August 8, Order in accordance with this Application for Rehearing.

Respectfully submitted,

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On behalf of The Ohio Hospital Association

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MEMORANDUM IN SUPPORT

I. INTRODUCTION

On March 30, 2012, AEP-Ohio filed a revised ESP proposal and supporting witness testimony. AEP-Ohio's proposal is a complex plan that establishes the pricing for SSO customers, but also establishes the cost of capacity for all customers, whether shopping or not, and changes the structure of AEP-Ohio to enable the transition to a "wires only" entity by 2015.

The proposed ESP is linked to a related case regarding the state compensation mechanism that sets the wholesale price that AEP-Ohio may charge competitive retail electric service ("CRES") providers for its capacity. *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* ("10-2929 Case"). In that case, on November 1, 2010, AEP Electric Power Service Corporation, on behalf of OP (and, at the time, CSP too), filed an application before the Federal Energy Regulatory Commission ("FERC") seeking authority to change the basis for compensation for

capacity costs from the PJM Reliability Pricing Model ("RPM") auction result to a cost-based mechanism.[1] In response to AEP-Ohio's FERC application, on December 8, 2010, the Commission issued an Entry preventing AEP-Ohio from changing the mechanism by expressly adopting as the state compensation mechanism for the Companies the current capacity charges established by the PJM RPM auction. However, on July 2, 2012, the Commission issued an Order on the merits of AEP-Ohio's request to charge CRES providers its fully embedded capacity costs and set a state compensation mechanism that will remain in place until June 1, 2015. The Commission found that the state compensation mechanism should be cost-based and, thus, AEP-Ohio is entitled to recover its cost of capacity, which the Commission determined is $188.88/MW-D. July 2 Order at 22. However, in order to encourage shopping, the Commission also found that AEP-Ohio is permitted to recover from CRES providers only the PJM RPM price, which is currently about $20/MW-D. *Id.* at 23. Nonetheless, to stabilize AEP-Ohio's transition to market and the SSO price, the Commission authorized AEP-Ohio to defer the difference between $188.88/MW-D and the prevailing PJM RPM prices for future recovery plus carrying costs. *Id.* at 23. The Commission stated that this total deferred amount is dependent on the number of customers who shop, or switch to a CRES provider, and would be addressed in AEP-Ohio's ESP case.

The Commission reached a substantive decision on this ESP case on August 8, 2012. The Commission found, in part, that although the ESP is less favorable than the expected results of an MRO by $386 million over the three year ESP period, because

[1] *See,* FERC Docket No. ER11-1995 et al. At the direction of FERC, AEP-Ohio refiled its application in FERC Docket No. ER11-2183 on November 24, 2010, (hereinafter, "*FERC Case*").

AEP-Ohio is transitioning to market faster than what the Commission could otherwise order under law, the ESP is better in the aggregate than an MRO. The Commission also increased and approved the RSR but stabilized it compared to AEP-Ohio's proposed RSR design; authorized AEP-Ohio to begin recovering $1 per megawatt-hour ("MWh") of the delta between the PJM RPM auction price and AEP-Ohio's cost of capacity; increased the percent of SSO load that AEP-Ohio must procure energy for through a competitive auction process and accelerated the start time for the energy-only auction; and, approved AEP-Ohio's proposal to create a placeholder rider to recover costs associated with the termination of the AEP East Pooling Agreement. Also, the Commission instituted a cap on customer rate increases at 12 percent over the current ESP rates for the entire term of the ESP.

The Commission's decision to approve the ESP when it is not more favorable in the aggregate than the expected results of an MRO is unreasonable and unlawful. Accordingly, for this reason alone, OMAEG/OHA urge the Commission to reverse its decision. In the alternative, the Commission's approval of particular components of the ESP, as described herein, is unreasonable and unlawful and should be reversed for the reasons set forth herein.

II. ARGUMENT

A. The Commission erred in finding the ESP is more favorable in the aggregate than the expected results of an MRO.

In order to approve an ESP, Section 4928.143(C)(1), Revised Code, requires the Commission to find that the ESP "including its pricing and all other terms and conditions, including any deferrals and any future recovery deferrals, is more favorable in the aggregate as compared to the expected results that would otherwise apply" under

a market rate offer ("MRO") plan. In other words, the Commission must conduct a balancing test to determine whether the ESP as proposed, or with Commission modification, is superior to the expected results of an MRO. The Commission conducted its balancing test but erred by: 1) failing to accurately reflect the total costs of the ESP; 2) finding that an expeditious transition to market outweighs the costs of the ESP; and 3) approving the ESP in spite of AEP-Ohio failing to meet its burden of proof and a lack of record evidence upon which it based its determination.

The result of these errors is that the Commission erroneously held that the ESP is more favorable in the aggregate than the expected results of an MRO and approved the ESP.

1. The Commission erred by understating the cost of the ESP.

The Commission cannot approve an ESP unless it finds that the ESP is more favorable in the aggregate than the expected results of an MRO. Section 4928.143(C)(1), Revised Code. After the Commission added the quantifiable costs of the Generation Resource Rider ("GRR"), $8 million, and the RSR at $388 million to the ESP, the $9.8 million benefit resulted in the ESP being less favorable than the expected results of an MRO by $386 million over the term of the ESP. Order at 73. However, the Commission has understated the cost of the ESP.

Also, the Commission's use of $188.88/MW-D for the competitive benchmark price rather than market prices is unjust and unreasonable and understates the cost of the ESP.

The Commission stated, "RPM prices are consistent with the state compensation mechanism…." Order at 74. However, the Commission held that the PJM RPM price is not appropriate to use as the capacity component of the competitive benchmark test, as

suggested by most parties, including Commission Staff. *Id.* Rather, the Commission responded to arguments that the PJM RPM price for capacity should have been used as the competitive benchmark price by stating that AEP-Ohio, as a fixed resource requirement ("FRR") entity, would be supplying capacity for its customers throughout the term of the ESP, even under an MRO. Order at 74. The Commission's point is irrelevant at best.

Duke Energy Ohio ("DEO") is also an FRR entity and is using the PJM RPM price as the charge to CRES providers for capacity to serve Ohio customers.[2] While DEO does not have the same Pooling Agreement in place as AEP-Ohio, as noted above, the record demonstrates that "AEP Ohio and the Pool members have the ability to terminate the Pool Agreement as of 2013." FES Ex. 105 at 20. Thus, there is no basis for using something other than the market price in the competitive benchmark test other than it would make the ESP even less favorable than the expected results of an MRO.

Additionally, the Commission stated that the period for comparison of the ESP to an MRO should be limited to June 1, 2013 through May 31, 2015, because AEP-Ohio would need sufficient time to develop an MRO and hold auctions before the MRO price could go into effect. Order at 74. To support its conclusion, the Commission cites to testimony of FirstEnergy Solutions ("FES") witness Banks' testimony. Order at 74. The Commission incorrectly states that Mr. Banks testified that a June 1, 2013 start date would provide AEP-Ohio sufficient time to plan for auctions and to develop bidding rules

[2] In fact, the error of the Commission's decision to use something other than market prices has become evident through a recent application filed by DEO requesting an additional $257 million per year to recover the difference between the market price for capacity and DEO's cost of capacity. *See, In the Matter of the Application of Duke Energy Ohio, Inc., for the Establishment of a Charge Pursuant to Revised Code Section 4909.18*, Case No. 12-2400-EL-UNC, *et al.,* Application of Duke Energy Ohio, Inc. (August 29, 2012).

and the auction structure. *Id.* Mr. Banks' testimony related to a competitive bidding process ("CBP") within this ESP. FES Ex. 105 at 20. It did not address an MRO filed concurrently with the initial ESP filing in this case or otherwise. Moreover, Mr. Banks stated:

> AEP Ohio's customers deserve to receive the benefits of wholesale competition immediately. FES proposes the June 2013 start date, however, as a conservative proposal to which AEP Ohio cannot reasonably object. June 2013 would align the auction delivery period with the start of the PJM planning year. It would also provide AEP Ohio more than enough time to achieve full corporate separation and to plan for the auctions, including the development of bidding rules and auction structure. Moreover, to the extent that termination of the Pool Agreement is a precondition to AEP Ohio's participation in the auction -- and FES witness Frame confirms it is not, AEP Ohio and the other Pool members can terminate the Pool Agreement prior to June 2013. *Id.* at note 18.

This case was initially filed in January 2011. It is not clear why the Commission presumed that an MRO and all of the auction rules would not have been developed and ready for deployment until June 1, 2013, had it been filed at the same time for the same period. Rather, if the Commission used the same timeframes to compare the ESP to the expected results of an MRO, the ESP would have been even less favorable. Moreover, the two year window for comparison does not reflect the actual ESP period, and was not based upon any record evidence.

Finally, the Commission conceded that it did not include costs of distribution related riders (like the Distribution Investment Recovery Rider, gridSmart, and the Enhanced Service Reliability Rider) but argued that the benefits of these riders outweigh the costs. *Id.* at 76. The Commission concluded that the riders support reliability improvements and an opportunity to utilize efficiency programs and would be mitigated by the increase in the percentages and acceleration of the energy-only

auctions. *Id.* at 76. There is no record evidence that demonstrates that the benefits can or will outweigh the costs of these riders.

Had the Commission used a market price for the competitive benchmark, the full term of the ESP to compare the MRO, and reflected the costs of the distribution riders, the ESP would have been even less favorable than the expected results of an MRO.

2. The Commission erred in finding that an expeditious transition to market outweighs the costs of the ESP.

In spite of finding that the ESP is less favorable than the MRO by $386 million, the Commission concluded that the ESP, in the aggregate, is more favorable than the expected results of the MRO. Order at 76. In order to reach its conclusion, the Commission held that the "most significant of the non-quantifiable benefits is the fact that in just under two and a half years, AEP-Ohio will be delivering and pricing energy at market prices, which is significantly earlier than what would otherwise occur under an MRO option." *Id.* at 76. The Commission's finding that AEP-Ohio's transition to market outweighs the $386 million (at a minimum) cost of the ESP is unjust, unreasonable and unlawful.

First, there is no record evidence that demonstrates that going to market in the timeframe required by the Commission's Order will provide any benefits to either AEP-Ohio or its customers. OMAEG/OHA reluctantly supported transitioning to market more quickly than permitted by an MRO in order to capture the currently low PJM RPM capacity prices. However, the Commission's Order blocks customers' access to the low market prices by requiring all customers to pay AEP-Ohio the difference between the PJM RPM capacity price and AEP-Ohio's cost of capacity.

Moreover, not only does the Commission's Order fail to provide customer access to the low PJM RPM capacity pricing, it also piles on additional costs for the speed of the transition to market, which was not fast enough to tap into the historic low capacity prices.

The Commission stated, "while the RSR and the inclusion of the deferral within the RSR are the most significant costs associated with the modified ESP, but for the RSR it would be impossible for AEP-Ohio to completely participate in full energy and capacity based auctions beginning in June 1, 2015." Order at 76. As the Commission alluded, it would only be impossible for AEP-Ohio to transition to market without the RSR because the Commission cannot force AEP-Ohio to do so as "the decision to move towards competitive market pricing is voluntary under the statute…." *Id.* Stated differently, customers will have to pay AEP-Ohio the RSR in order for the Commission to achieve the end of competition by June 1, 2015.

In other words, the most significant of the non-quantifiable benefits (the fact that AEP-Ohio will be delivering and pricing energy at market prices in just under two and a half years), which has not been demonstrated to benefit customers, comes with the RSR as a price tag. For this reason, an expeditious transition to market is completely illusory at best. It should be given no value in the balancing test required by statute.

The Commission appears to believe that competition is the end that it has been directed to achieve, regardless of the cost to customers. It is not. Regardless of when AEP-Ohio makes the full transition to market, it should be a smooth one with the ultimate goal of ensuring the availability to consumers of adequate, reliable, safe,

efficient, nondiscriminatory, and reasonably priced retail electric service. Section 4928.02, Revised Code.

OMAEG/OHA agree that Amended Substitute Senate Bill 3 ("SB 3") began to pave "the way for electric utilities to transition towards market-based pricing, and provide consumers with the ability to choose their electric generation supplier." Order at 76. OMAEG/OHA also agree that the ultimate outcome intended by SB 3 is for competitive markets to dictate the price of electric generation service.

Amended Substitute Senate Bill 221 provided for two options for SSO service. In order for the Commission to approve an ESP, it must be more favorable in the aggregate than the expected results of an MRO. In other words, the purpose of an ESP is to provide an alternative to market based pricing when the alternative, with all of its components, can provide customers a better option than what the market can provide. If the market can do better than an ESP, the Commission cannot approve an ESP. SB 221 was a customer protection and a way to make sure both that customers are protected from a still developing market and that customers get the benefit of market prices when the markets are properly functioning. Under either market-based pricing or the ESP alternative, the goal is to provide reasonably priced electricity.

While the Commission clearly has significant discretion under Section 4928.143, Revised Code, to determine whether an ESP is more favorable in the aggregate than the expected results of an MRO, the Commission has unreasonably and unlawfully sacrificed reasonably priced retail electric service for at least six years (depending on the repayment terms of the deferred capacity costs) in exchange for a more expeditious transition to market pricing.

Without providing the savings that going to market expeditiously could have provided, the customer benefits of going to market during the term of this ESP do not outweigh the significant costs. Because the ESP is less favorable than the expected results of an MRO by *at least* $386 million and the most significant of the non-quantifiable benefits is actually not a benefit at all, the Commission should reverse its decision and reject AEP-Ohio's modified ESP.

3. The Commission erred in approving the ESP in spite of AEP-Ohio failing to meet its burden of proof and a lack of record evidence upon which it based its determination.

AEP-Ohio has the burden of proving that the ESP is more favorable than an MRO. Section 4928.143(C)(1), Revised Code. AEP-Ohio did not meet its burden. As the Commission agreed that the AEP-Ohio did not meet its burden of proof, the Commission relied on extra-record evidence and conclusions unsupported by the record to unreasonably and unlawfully modify and approve the ESP.

Specifically, the Commission held that "AEP Ohio made multiple errors in conducting the statutory test…" and "[t]he way AEP-Ohio calculated its statutory price test precludes us from accurately determining the results that would otherwise apply under a market rate offer, as it begins its analysis on June 1,2012." Order at 73. Nonetheless, and in order to salvage the ESP, rather than concluding that AEP-Ohio failed to meet its burden of demonstrating that the ESP is more favorable than the expected results of the MRO, the Commission determined that the errors and flawed methodology were "correctible." Order at 73.

Although Section 4928.143(C)(1), Revised Code, gives the Commission the authority to modify the ESP, the Commission cannot also undertake the burden of creating new, extra-record evidence in order to prove that the ESP is more favorable in

the aggregate than the expected results of an MRO, particularly after finding that AEP-Ohio's evidence was flawed and insufficient to even determine whether the ESP could pass the statutory balancing test. However, that is precisely what the Commission has done.

As described above, the Commission modified both the methodology and the inputs to determine the statutory price test. To reach its conclusion, the Commission conducted its own analysis, but did not "show its work," merely describing how it derived its end result.[3]

For example, the Commission found that AEP-Ohio erred by using $355.72/MW-D for the capacity component of the competitive benchmark price. Order at 74. Instead, the Commission used $188.88/MW-D, which is the amount that the Commission found to be AEP-Ohio's cost of capacity. Order at 74. The Commission's ruling on the state compensation mechanism and its determination that AEP-Ohio's cost of capacity was $188.88/MW-D was not part of this case and was not available until the hearing had concluded and the opportunity to present evidence was closed. 10-2929 Case, Opinion and Order (July 2, 2012).[4]

Nonetheless, realizing the impact of the Commission's decision on the capacity cost case, several parties included an analysis in their reply briefs using $188.88/MW-D to demonstrate the impact of the Commission's capacity cost case on the ESP.

[3] Section 4903.09, Revised Code, requires that, in all contested cases heard by the Commission, the Commission shall file findings of fact and written opinions setting forth the reasons prompting the decisions arrived at, based upon said findings of fact.

[4] As the Commission notes in its Findings of Fact and Conclusions of Law, the evidentiary hearing on this case was called on May 17, 2012, and concluded on June 15, 2012. Initial and reply briefs were due on June 29, 2012 and July 9, 2012, respectively. Thus, the parties had only two days after the 10-2929 Order was issued to include any information at all in this case through reply briefs.

After making the modifications to the methodology and inputs to the statutory price test, the Commission apparently re-ran a calculation using the $188.88/MW-D capacity price that resulted in a demonstration that the ESP is more favorable than the MRO by $9.8 million. Order at 75. While it is not clear how the Commission applied the inputs that it determined were appropriate, the Commission's conclusion does not match that of any other party, including AEP-Ohio, as no other party conducted the same analysis using the same inputs. In fact, the Commission noted that Staff "calculated the average rates under AEP-Ohio's modified ESP and compared them to the results that would occur under an MRO on RPM price capacity, $146.41, and $255…." Order at 73. Staff witness, Mr. Fortney concluded that under all three scenarios the modified ESP is less favorable, not including the non-quantifiable benefits. *Id.* (citing Staff Ex. 110 at 3-7). "Similarly, FES revised Mr. Fortney's statutory price test using the $188.88 price of capacity and concluded an MRO would be less expensive by $277 million." *Id.* (citing FES Reply Br. At B-l). Even by AEP-Ohio's calculation, using $188.88/MW-D as the capacity price and including the 5% energy auction, the MRO is more favorable by $2.6 million and $12.6 million without considering the impact of the 5% energy-only auction. Ohio Power Reply Brief at 98, Appendix B-2.

Section 4903.09, Revised Code, requires the Commission to make a complete record of all of the proceedings and to file findings of fact and written opinions setting forth the reasons prompting the decisions arrived at, based upon said findings of fact. In *Tongren v. PUC*, 85 Ohio St. 3d 87 (1999), the Ohio Supreme Court described the requirements of complying with Section 4903.09, Revised Code. The Court stated that

while strict compliance with the terms of Section 4909.09, Revised Code, is not required, a Commission order must provide "in sufficient detail, the facts in the record upon which the order is based, and the reasoning followed by the PUCO in reaching its conclusion." *Id.* at 89 (citing *Commercial Motor Freight, Inc. v. Pub. Util. Comm.,* 156 Ohio St. 360, 363-364 (1951)). Further, the Court noted that it has addressed the question of what constitutes adequate factual support for Commission orders in a number of cases. "Suffice it to say, some factual support for commission determinations must exist ***in the record*****,** an obligation which the commission itself has recognized in its orders." *Id.* (emphasis added, internal citations omitted). *See also, Ideal Transp. Co. v. Pub. Util. Comm.*, 42 Ohio St. 2d 195 (1975).[5]

However, instead of relying on the record evidence, the Commission relied upon extra-record evidence by using the $188.88/MW-D capacity cost and created its own extra-record evidence through an analysis that is not verifiable or supported by any party or any record evidence to reach its conclusion that the ESP is more favorable than the MRO by $9.8 million. Such a process is contrary to law and is unjust and unreasonable.

Section 4903.13, Revised Code, provides that "[a] final order made by the public utilities commission shall be reversed, vacated, or modified by the supreme court on appeal, if, upon consideration of the record, such court is of the opinion that such order

[5] In *Ideal,* the Court set forth the law:

"1. Where an opinion and order of the Public Utilities Commission fails to state specific findings of fact, supported by the record, and fails to state the reasons upon which the conclusions in the commission's opinion and order were based, such order fails to comply with the requirements of R.C. 4903.09, and is, therefore, unlawful.

2. The Public Utilities Commission must base its decision in each case upon the record before it."

was unlawful or unreasonable." In this case, although there is a lengthy and complicated record, AEP-Ohio failed to provide sufficient evidence to demonstrate that the ESP is more favorable than an MRO and the Commission failed to meet the requirements of Section 4903.09, Revised Code, by relying on extra-record evidence or otherwise not providing an adequate record for the evidence upon which its decision was based. The prejudicial effect of the order on OMAEG/OHA is that their members, like all AEP-Ohio customers, will pay at least $386 million more for electric service than permitted by Ohio law.

Commissioner Roberto issued a lone dissent that simply said that the non-quantifiable benefits cannot overcome a $386 million deficit and, thus, she does not believe that the ESP is more favorable in the aggregate than the expected results of an MRO. For this reason and as described above, the Commission should reverse its decision or, at the very least, explain to customers why an expeditious transition is worth over $386 million to them.

B. The Commission's decision to permit AEP-Ohio to defer the difference between $189 per megawatt-day ("MW-D") and the PJM reliability pricing model ("RPM") auction price for capacity was unreasonable and unlawful.

AEP-Ohio proposed a two-tiered capacity cost approach (even if it was successful in obtaining authorization for a $355/MW-D capacity charge in the 10-2929 case) if the total ESP package and the corporate separation case were adopted without modification. As noted above, the Commission held in the 10-2929 Case that AEP-Ohio's fully embedded capacity costs are $189/MW-D but AEP-Ohio may only recover the PJM RPM price from CRES providers for shopping customers. However, in the 10-2929 Case, AEP-Ohio was authorized to defer the difference between the prevailing

PJM RPM price and $189/MW-D for future recovery. Accordingly, in this case, the Commission rejected AEP-Ohio's two-tiered capacity cost approach. Order at 49-51. The Commission also noted that, as the deferral amount is necessarily based upon actual customer shopping, the full amount of the deferral will not be known until the end of the ESP period (May 31, 2015). Order at 36. Nonetheless, the Commission held that AEP-Ohio should begin recovering the deferral through the RSR immediately. *Id.* The Commission directed AEP-Ohio to begin recovering the deferral through the RSR at a recovery amount of $1.00/MWh for the term of the ESP. *Id*. At the conclusion of the ESP term, the Commission will determine the deferral amount and make adjustments based upon AEP-Ohio's actual shopping statistics. *Id.* If there is still a balance on May 31, 2015, it will be amortized and recovered over three years. *Id.*

The Commission's decision to authorize AEP-Ohio to recover part and defer for future recovery the balance of the delta between the prevailing PJM RPM price and $189/MW-D is unreasonable and unlawful.

1. The Commission exceeded its jurisdiction by authorizing recovery and deferrals for future recovery of wholesale costs from retail customers.

In the 10-2929 Case, the Commission held that capacity service is a wholesale service – not retail. Specifically, the Commission stated:

> The electric service in question (i.e., capacity service) is provided by AEP-Ohio for CRES providers, with CRES providers compensating the Company in return for its FRR capacity obligations. **Such capacity service is not provided directly by AEP-Ohio to retail customers.** (AEP-Ohio Ex. 101 at 11; Tr. I at 63.) Although the capacity service benefits shopping customers in due course, they are initially one step removed from the transaction, which is more appropriately characterized as an intrastate wholesale matter between AEP-Ohio and each CRES provider operating in the Company's service territory.… We agree that the provision of capacity for CRES providers by AEP-Ohio, pursuant to the

> Company's FRR capacity obligations, is not a retail electric service as defined by Ohio law. 10-2929 Case, Order at 12 (July 2, 2012).

The Commission relied on its general supervisory authority and ratemaking authority in Sections 4905.04 through 4905.05, and Chapter 4909, Revised Code, to determine that the Commission has jurisdiction to establish a state compensation mechanism and that it should be cost-based. The Commission noted that those chapters require that the Commission use traditional rate base/rate of return regulation to approve rates that are based on cost, with the ultimate objective of approving a charge that is just and reasonable consistent with R.C. 4905.22. *Id.* at 22.

In spite of the Commission's determination that capacity for shopping customers is not a retail service provided by AEP-Ohio to retail customers, the Commission unreasonably and unlawfully permitted AEP-Ohio to recover its wholesale capacity costs from retail customers on a nonbypassable basis. Order at 51-52. The Commission argued that it may order any just and reasonable phase-in of any rate or price established under Sections 4928.141, 4928.142 or 4928.143, Revised Code, including carrying charges. Section 4928.141, Revised Code, requires electric distribution utilities, like AEP-Ohio, to provide consumers "a standard service offer of all competitive **retail** electric services necessary to maintain essential electric service to consumers, including a firm supply of electric generation service." (emphasis added).

The Commission is talking out of both sides of its mouth on this and cannot have it both ways. The capacity cost to CRES providers for shopping customers is either a wholesale cost or a retail cost. If it is a wholesale cost, the Commission has general supervisory authority and ratemaking authority pursuant to Sections 4905.04 through 4905.05, and Chapter 4909, Revised Code, to permit AEP-Ohio to recover its cost after

complying with the rate making process requirements. However, the Commission does not have authority to authorize deferrals under its general supervisory and ratemaking authority. *Columbus S. Power Co. v. Public Utils. Comm'n* (1993) 67 Ohio St. 3d 535, 620 N.E.2d 835, 1993 Ohio LEXIS 2265). Moreover, the Commission did not comply with the ratemaking requirements prior to approval of the capacity charge if it is wholesale.

If this is a retail cost, it is generation related and, thus, a competitive service that is not authorized to be included in an ESP pursuant to Section 4928.143(B)(2), Revised Code. The Commission's only deferral authority under Section 4928.144, Revised Code, pertains to "any just and reasonable phase-in of any electric distribution utility rate or price **established under sections 4928.141 to 4928.143 of the Revised Code….**" Section 4928.144, Revised Code (emphasis added). This capacity delta was not established under Sections 4928.141 to 4928.143, Revised Code, if it is a "wholesale service that is not provided directly by AEP-Ohio to retail customers," as the Commission asserted. It simply cannot be both wholesale and retail. Therefore, the Commission erred in finding it is both to the detriment of all AEP-Ohio ratepayers. OMAEG/OHA strongly recommend that the Commission reverse its authorization to recover in part, and defer for future recovery the balance of the capacity cost delta created by the Commission as it is unreasonable and unlawful.

2. Capacity costs should not be recovered from customers on an energy-basis.

While OMAEG/OHA believe that that the RSR should be eliminated entirely, at a minimum, the Commission should modify the cost recovery allocation. The Commission authorized AEP-Ohio to begin charging all customers on a nonbypassable basis $1/MWh for the deferred capacity costs through the RSR. Order at 36-37. The Commission also directed the RSR to recover charges per kWh by customer class. *Id.* at 37. Capacity is demand related and should be recovered based upon demand, not energy. Tr. Vol. VII at 2266. *See, Electric Utility Cost Allocation Manual, National Association of Regulatory Utility Commissioners,* "Embedded Cost Methods for Allocating Production Costs." OMAEG/OHA respectfully request that the capacity-related portion of the RSR be recovered based on demand to more appropriately reflect the cost of the service.

3. The Commission erred in not reducing the base generation rate to reflect the lower capacity cost.

If the Commission permits AEP-Ohio to recover its full capacity costs from retail shopping customers pursuant to Sections 4928.141 to 4928.143, Revised Code, then it should fully comply with those sections and require that AEP-Ohio provide consumers, on a comparable and *nondiscriminatory basis* within its certified territory, a standard service offer of all competitive retail electric services necessary to maintain essential electric service to consumers, including a firm supply of electric generation service. Section 4928.141, Revised Code. In order to do that, the Commission should reduce AEP-Ohio's base generation rates to reflect its holding that AEP-Ohio's capacity costs are $188.88/MW-D.

Although there is no explicit capacity charge in the SSO rates, AEP-Ohio has argued that its SSO capacity costs are equivalent to $355/MW-D.[6] By comparison, the Commission held that the cost of capacity that AEP-Ohio may collect from shopping customers is $188.88/MW-D. Thus, by approving a non-fuel base generation rate freeze for SSO customers, charging CRES providers $188.88/MW-D, and recovering the delta between $188.88/MW-D and the prevailing PJM RPM rate from all retail customers, the Commission has erred by permitting AEP-Ohio to charge discriminatory rates for capacity to the detriment of SSO customers.

The Commission should ensure comparable and nondiscriminatory charges for capacity to retail customers by reducing the SSO rate to reflect the Commission's holding that AEP-Ohio's cost of capacity is $188.88/MW-D.

C. The Commission's decision to authorize the RSR was unjust and unreasonable.

AEP-Ohio's ESP proposal included the RSR to stabilize AEP-Ohio's earnings essentially by replacing a portion of AEP-Ohio's lost generation revenues resulting from customers shopping at "discounted" capacity pricing. Company Ex. 116 at 13, Tr. Vol.

[6] AEP-Ohio has the burden of proof and could have conducted a new cost of service study to prove up its claims. AEP-Ohio did not. Rather, AEP-Ohio witness Allen attempted to make a comparison of the revenue received from CRES providers for capacity priced at $355/MW-D with the revenue received from SSO customers for base generation rates and concluded that the price that AEP-Ohio is charging SSO customers for capacity is equivalent to $355/MW-D. Tr. Vol. V at 1438. *See also,* IEU Ex. 125 at KMM-14.

XVII at 4583.[7] The RSR AEP-Ohio proposed was designed to collect $284.1 million over the ESP period. Company Ex. 116 at WAA-6. While the RSR did not guarantee that AEP-Ohio would hit its ROE target of 10.5%, the goal of the RSR was to stabilize earnings by adjusting up or down depending on movement of other components of the ESP regardless of sales. For example, if AEP-Ohio's load goes down, for any reason, the RSR would increase. Tr. Vol. V at 1427.

The Commission made several modifications to the RSR and approved it. Order at 31-38. Ultimately, the Commission increased the total amount for recovery from AEP-Ohio's proposal but found that the RSR should not serve as a decoupling mechanism. Thus, the RSR target amount will be static. *Id.* AEP-Ohio's proposed amount was targeted to recover $284.1 million over the three year term. The Commission's Order increased the amount to $508 million over the same term. The Commission directed AEP-Ohio to begin recovering an RSR amount of $2.50/MWh through May 31, 2014 and $3.00/MWh between June 1, 2014 and May 31, 2015. Order at 36. The Commission's approval of the RSR is unreasonable and unlawful.

1. The RSR is unreasonable and unnecessary, especially if AEP-Ohio is authorized to recover its fully embedded cost of capacity.

The Commission held that the RSR is statutorily justified under Section 4928.143(B)(2)(d), Revised Code, which permits an ESP to include terms, conditions or

[7] Specifically, AEP witness Allen started with AEP-Ohio's 2011 return on equity ("ROE") of 12.06% and then determined that a ROE target of 10.5% is reasonable for the ESP period. Company Ex. 116 at 14. AEP witness Allen then backed into an earnings number that would produce the target ROE of 10.5%. To do this, Mr. Allen totaled the base generation revenue, the Environmental Investment Carrying cost Rider ("EICCR") revenue, the revenue AEP-Ohio receives from CRES providers for capacity, and a $3/MWh credit for shopped load related to possible energy margins for 2011. Then, Mr. Allen estimated the projected revenue over the ESP period from the same categories used to develop the 2011 baseline. The difference between the anticipated revenue and the total revenue that would produce a 10.5% ROE is the RSR amount.

charges that have the effect of stabilizing retail electric service or provide certainty regarding retail electric service. In other words, the Commission accepted AEP-Ohio's threat that without the RSR, AEP-Ohio would be unable to freeze base generation rates and allow customers to shop for generation. The Commission stated that it understands that the nonbypassable charge will result in additional costs to customers but the effects are mitigated by the stabilization of non-fuel base generation rates and the promise that AEP-Ohio will base SSO prices on auction results in less than three years. Order at 31-32. As already described above, there is no record evidence that a more expeditious transition to market than otherwise permitted under an MRO outweighs the cost of the ESP. The record also demonstrates that it is not that AEP-Ohio cannot freeze base generation rates and allow customers to shop for generation without the RSR and transition to market. It is that they will not do so and cannot be required to do so under Ohio law.

AEP-Ohio has been authorized to recover its full capacity costs from all retail customers for the entire term of the ESP. While OMAEG/OHA do not agree that AEP-Ohio should recover anything more than the prevailing PJM RPM price for its capacity, if the Commission upholds its capacity cost recovery decision, the RSR becomes unnecessary and nothing more than an exorbitant payment to transition to market faster than otherwise permitted by Ohio law. Customers should not have to pay AEP-Ohio a premium to implement the Commission's policy decisions.

2. The Commission's increase of the total amount to be recovered through the RSR was unreasonable.

The Commission held that it is not appropriate to provide a guaranteed return to AEP-Ohio through the RSR. Order at 32. Rather, it is more appropriate to establish a

revenue target that will allow AEP-Ohio the opportunity to earn a reasonable rate of return between 7% and 11%. *Id.* at 33. The Commission found that a total revenue target of $826 million, rather than AEP-Ohio's proposed target of $929 million, more appropriately reflected the opportunity to earn a reasonable rate of return. *Id.* However, the Commission also found that AEP-Ohio's shopping estimates, upon which the RSR was based, were too high. *Id.* at 34. The Commission reduced the shopping estimates to 52% in 2012, 62% in 2013 and 72% in 2015. When the shopping assumptions and the revenue target are modified, the effect is to actually increase the RSR amount as follows:

	Planning Year 2012/13		**Planning Year 2013/14**		**Planning Year 2014/15**		**AEP Total**	**PUCO Total**
	AEP	**PUCO**	**AEP**	**PUCO**	**AEP**	**PUCO**	**AEP**	**PUCO**
Retail Non-Fuel Generation Revenues	$403	$528	$310	$419	$182	$308	$895	$1,255
CRES Capacity Revenues	$391	$32	$413	$65	$400	$344	$1,204	$441
Credit for Shopped Load	$91	$75	$103	$89	$120	$104	$314	$268
Subtotal	$885	$636	$826	$574	$792	$757	$2,503	$1,967
Revenue Target	$929	$826	$929	$826	$929	$826		
Retail Stability Rider Amount	$44	$189	$103	$251	$137	$68	**$284**	**$508**

While OMAEG/OHA believe that the Commission should reject the RSR altogether as unnecessary, OMAEG/OHA agree that making the target revenue static is an improvement over AEP-Ohio's proposal. Nonetheless, nearly doubling the revenue amount is unjust, unreasonable and will harm all AEP-Ohio customers. *See, for example,* OMAEG Exs. 101-106.

For these reasons, the Commission should reverse its decision and reject the RSR proposal altogether.

D. The Commission must clarify the customer rate impact cap.

In order to mitigate any customer rate changes, the Commission instituted a cap on customer rate increases at 12 percent over the current ESP rates for the entire term of the ESP. Order at 70. While OMAEG/OHA appreciate the Commission's attempt to be sensitive to the impact on customers of the ESP, it is not clear how the 12 percent will be calculated and applied, and the cap simply pushes the present costs of an unlawful ESP to the future. OMAEG/OHA respectfully request that the Commission provide clarity on how the cap should be calculated. For example, the Commission stated that the cap is to be determined not by overall customer rate classes, but on an individual customer by customer basis. *Id.* How can shopping customers make such a determination? Is the determination made on a monthly basis, annual or over the term of the ESP? Is AEP-Ohio required to show on a bill the calculation of the difference? What if, but for shopping, a customer's ESP rate would exceed 12%? In other words, is generation removed from the determination? Additionally, the Commission stated that the cap does not include any changes that arise as a result of past proceedings, including the distribution rate case, or subsequent proceedings (like the Pool Termination Rider). *Id.* Is the PIRR amount included or excluded? Any amounts that exceed the 12% cap will be deferred for future recovery. *Id.* AEP-Ohio must file a detailed accounting of its deferral impact created by the 12% cap on May 31, 2013, at which time the Commission will determine whether to adjust the 12% cap. What information should AEP-Ohio file? How will the Commission allocate the deferral cost recovery?

While OMAEG/OHA is certainly not advocating that the Commission reverse this decision, additional clarity would be useful to customers.

III. CONCLUSION

For the reasons set forth herein, the OMAEG/OHA respectfully request that the Commission grant rehearing and grant the relief requested by the OMEG/OHA.

Respectfully submitted,

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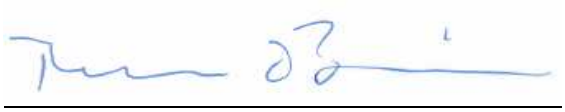

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On behalf of The Ohio Hospital Association

CERTIFICATE OF SERVICE

The undersigned hereby certifies that a copy of the foregoing Application for Rehearing and Memorandum in Support was served upon the parties of record listed below this 7th day of September 2012 *via* email transmission.

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