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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

INDUSTRIAL ENERGY USERS-OHIO'S APPLICATION FOR REHEARING OF THE AUGUST 8, 2012 OPINION AND ORDER AND MEMORANDUM IN SUPPORT

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Pursuant to Section 4903.10, Revised Code, and Rule 4901:1-35, Ohio Administrative Code ("OAC"), Industrial Energy Users-Ohio ("IEU-Ohio") respectfully submits this Application for Rehearing which is directed at the Opinion and Order ("ESP II Order")[1] issued by the Public Utilities Commission of Ohio ("Commission") on August 8, 2012. The ESP II Order authorizes AEP-Ohio[2] to significantly increase electric bills for shopping and non-shopping customers and insulates AEP-Ohio's competitive

[1] Hereinafter "ESP II Order" shall refer to the August 8, 2012 Opinion and Order in the instant proceedings, and "*ESP II Case*" shall refer to the cases identified above (Case Nos. 11-346-EL-SSO, *et al.*).

[2] Ohio Power Company ("OP") merged with Columbus Southern Power Company ("CSP"). The merged company is referred to herein as "AEP-Ohio."

generation business from the discipline of the electric market through a new Electric Security Plan ("ESP").

As a result of the many significant errors made in the ESP II Order modifying and approving the March 30, 2012 application for a modified ESP ("Modified ESP"), AEP-Ohio's shopping and non-shopping customers will pay substantially higher electric prices for years to come. These increases begin at a time when wholesale electricity prices are relatively low. Thus, the above-market increases work to deprive AEP-Ohio customers of their customer choice dividend while increasing the dividends AEP-Ohio will make available to its parent. The ESP II Order subordinates the interests of customers to provide AEP-Ohio's competitive generation business with more time to transition to a competitive electric market even though Ohio law states that the time for such a transition ended long ago. Thus, the ESP II Order provides AEP-Ohio with the means to secure an illegitimate end.

The ESP II Order is unlawful and unreasonable in the following respects:

1. The ESP II Order is unlawful and unreasonable because the as-approved Modified ESP, including its pricing and all other terms and conditions, including any deferrals and any future recovery of deferrals, is not more favorable in the aggregate as compared to the expected results that would otherwise apply under Section 4928.142, Revised Code.[3]

   A. The ESP II Order is unlawful and unreasonable because it uses $188.88/megawatt-day ("MW-day") as the price for the capacity component for generation supply associated with the MRO SSO, thereby overstating the MRO SSO pricing as compared to the as-approved Modified ESP SSO.

   B. The ESP II Order is unlawful and unreasonable because it disregards the costs of the as-approved Modified ESP for over 25% of the ESP term.

[3] This Section allows a utility to fulfill its standard service offer ("SSO") obligation through a market rate offer ("MRO").

C. The ESP II Order is unlawful and unreasonable because it does not include the full cost of the Generation Resource Rider ("GRR") as part of the quantitative costs in its application of the ESP versus MRO test, thereby understating the cost of the as-approved Modified ESP.

D. The ESP II Order is unlawful and unreasonable because it does not include known costs for the Pool Termination Rider ("PTR"), Retail Stability Rider ("RSR"), and Capacity Shopping Tax[4] as part of the quantitative costs of the as-approved Modified ESP for purposes of applying the ESP versus MRO test, thereby understating the cost of the as-approved Modified ESP.

E. The ESP II Order is unlawful and unreasonable because it does not include or address the effect of known costs of the energy-only auctions and the "quicker" move to a competitive bid process ("CBP") based SSO for purposes of conducting the ESP versus MRO test.

2. The ESP II Order is unlawful and unreasonable because it approves an ESP by introducing subjective and speculative "qualitative benefits" into the ESP versus MRO test, thereby evading compliance with Section 4903.09, Revised Code.

3. The ESP II Order is unlawful and unreasonable because the non-bypassable RSR, Capacity Shopping Tax, and the PTR cannot be lawfully included in an ESP SSO.

A. The ESP II Order is unlawful and unreasonable because it authorizes non-bypassable generation-related riders which are not included on the list of permissive ESP provisions contained in Section 4928.143(B)(2), Revised Code.

B. The ESP II Order is unlawful and unreasonable because it concludes that the RSR can be authorized under Section 4928.143(B)(2)(d), Revised Code. The RSR does not have the effect of stabilizing or providing certainty regarding retail electric service.

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[4] As used throughout this pleading, "Capacity Shopping Tax" refers to the non-bypassable rider that will collect the balance of the $188.88/MW-day capacity price that is not collected from competitive retail electric service ("CRES") providers through "RPM-Based Pricing" or through the $1/megawatt hour ("MWh") portion of the RSR. As used herein, this deferred balance to be collected through the Capacity Shopping Tax is referred to as the "Capacity Deferral." Throughout this Application for Rehearing and Memorandum in Support, the PJM Interconnection, LLC ("PJM") Reliability Pricing Model ("RPM") capacity pricing method and resulting prices are referred to as the "RPM Pricing method" and the "RPM-Based Price," respectively.

C. The ESP II Order is unlawful and unreasonable because the PTR cannot be authorized under Section 4928.143(B)(2)(h), Revised Code. The PTR has no relationship to AEP-Ohio's distribution service.

D. The ESP II Order is unlawful and unreasonable because it concludes that the Capacity Deferral and the Capacity Shopping Tax can be authorized under Section 4928.144, Revised Code. These items do not arise from rates or prices authorized under Sections 4928.141 to 4928.143, Revised Code, and therefore the Commission's authority in Section 4928.144, Revised Code, is unavailable.

4. The ESP II Order is unlawful and unreasonable because it authorizes AEP-Ohio to increase SSO prices so as to collect above-market generation-related revenue through the non-bypassable RSR, Capacity Shopping Tax, and the PTR, thereby providing AEP-Ohio with the ability to collect transition revenue or its equivalent at a time when Ohio law commands that AEP-Ohio's generation business be fully on its own in the competitive market. By allowing AEP-Ohio to collect transition revenue, the Commission unreasonably and unlawfully ignored the statutory bar against such collection. The ESP II Order is similarly unreasonable and unlawful because it permits AEP-Ohio to evade its Commission-approved settlement obligation to forego such collection and to not impose lost generation-related revenue charges on shopping customers.

5. The ESP II Order is unlawful and unreasonable because it assumes that the Commission may invent and apply a cost-based ratemaking methodology for purposes of authorizing a significant increase in the price for generation capacity service. It is similarly unlawful and unreasonable because it authorizes AEP-Ohio to defer the uncollected portion of this significant increase in the price for generation capacity service and then, after the term of the ESP, collect such portion plus interest charges through non-bypassable charges applicable to shopping and non-shopping customers.

6. The ESP II Order is unlawful and unreasonable because it functions to permit AEP-Ohio, an electric distribution utility ("EDU"), to evade statutory corporate separation requirements that call for strict separation between competitive and non-competitive lines of business and services and because it approves an SSO which insulates AEP-Ohio's competitive generation business from the discipline of the electricity market. The RSR, Capacity Shopping Tax, and PTR all function to allow AEP-Ohio, the EDU, to evade such corporate separation requirements, collect above-market generation-related revenue and insulate AEP-Ohio's competitive generation business from the discipline of the electricity market. Following

AEP-Ohio's proposed and untimely transfer of its generating assets to an affiliate, AEP Generation Resources Company ("Genco"), these three riders will further violate such corporate separation requirements by allowing AEP-Ohio to collect, on a non-bypassable basis, above-market generation-related revenue and remit such revenue to Genco thereby insulating Genco's competitive generation business from the discipline of the electricity market.

7. The ESP II Order is unlawful and unreasonable because it fails to promote the State policy contained in Section 4928.02, Revised Code. As the Commission found in the Capacity Order,[5] market-based pricing promotes the policies contained in Section 4928.02, Revised Code, by incenting shopping, promoting true competition, and by placing EDUs and CRES providers on a level playing field. Despite finding that market-based pricing promotes State policy, the ESP II Order authorizes AEP-Ohio to collect above-market pricing for generation-related services through the RSR, PTR, Capacity Shopping Tax, and the GRR.

8. The ESP II Order is unlawful and unreasonable because it fails to recognize that the rates and charges applicable to non-shopping customers also are providing AEP-Ohio with compensation for generation capacity service, it ignores or disregards the fact that AEP-Ohio has maintained that non-shopping customers are, on average, paying nearly twice the $188.88/MW-day price, and it fails to establish a mechanism to credit such excess compensation obtained from non-shopping customers against any deferred balance the ESP II Order, in combination with the Capacity Order, work to create by comparing RPM-Based Pricing to the $188.88/MW-day price. The non-symmetrical and arbitrary bias embedded in these Orders' description of how the Capacity Deferral shall be computed guarantees that AEP-Ohio shall collect, in the aggregate, total revenue for generation capacity service substantially in excess of the revenue produced by using the $188.88/MW-day price to determine generating capacity service compensation for shopping and non-shopping customers.

9. The ESP II Order is unlawful and unreasonable inasmuch as the Commission failed to adopt the uncontested recommendation of IEU-Ohio witness Kevin Murray contained at page 49 of IEU-Ohio Exhibit 125 which, if adopted, would provide much needed transparency to the process AEP-Ohio used to derive the billing determinants for generation capacity service.

[5] Hereinafter "Capacity Order" shall refer to the July 2, 2012 Opinion and Order in *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 and "Capacity Case" shall refer to the docket above (Case No. 10-2929-EL-UNC).

10. The ESP II Order is unlawful and unreasonable because the GRR cannot be lawfully approved under Section 4928.143(B)(2)(c), Revised Code.

A. The ESP II Order is unlawful and unreasonable because it authorizes AEP-Ohio to establish the GRR to recover the cost of compliance with Section 4928.64, Revised Code (renewable energy resource requirements), through a non-bypassable charge in violation of Ohio law. Section 4928.64(E), Revised Code, states that all costs incurred by an EDU to comply with such requirements shall be bypassable by any consumer that has exercised its choice of supplier under Section 4928.03, Revised Code. The ESP II Order is also unlawful and unreasonable because the Commission violated Section 4903.09, Revised Code, by failing to address this issue raised on brief by IEU-Ohio; the Ohio Supreme Court has held that the failure to address all material matters brought to the Commission's attention is a reversible error.

B. The ESP II Order is unlawful and unreasonable because the Commission failed to make the findings required by Section 4928.143(B)(2)(c), Revised Code, to support its authorization of the GRR.

11. The ESP II Order is unlawful and unreasonable because it authorized the Phase-In Recovery Rider ("PIRR") without allowing IEU-Ohio an opportunity to present testimony or to introduce exhibits regarding the effect of accumulated deferred income taxes ("ADIT") on the carrying charges in the PIRR, trespassing on IEU-Ohio's due process rights.[6] Generally accepted accounting principles, regulatory principles, Court precedent, and Commission precedent all support an offset to account for ADIT.

A. The ESP II Order is unlawful and unreasonable because IEU-Ohio was denied the opportunity to present evidence regarding the effect of ADIT on the calculation of carrying charges in the PIRR in violation of due process.

B. The ESP II Order is unlawful and unreasonable because it fails to direct AEP-Ohio to calculate the PIRR's carrying charges on deferred balances adjusted for ADIT in accordance with generally accepted accounting principles, regulatory principles, Court precedent, and Commission precedent. The ESP II Order's failure to require an ADIT adjustment permits AEP-Ohio to accrue carrying charges on overstated balances; thereby requiring customers to overcompensate AEP-Ohio.

[6] *Vectren Energy Delivery of Ohio, Inc. v. Pub Util. Comm.*, 113 Ohio St.3d 180, 192 (2007).

12. The ESP II Order is unlawful and unreasonable because, without authority to do so under Section 4928.143, Revised Code, the ESP II Order conditionally approves a transfer of generating assets without making the findings required by Sections 4928.17 and 4928.02, Revised Code, and Rule 4901:1-37, OAC, and without netting the above-book market value of AEP-Ohio's generating assets against the transition revenue which the ESP II Order authorizes AEP-Ohio to collect on a non-bypassable basis during and after the term of the as-approved Modified ESP.

13. The ESP II Order is unlawful and unreasonable because it fails to sustain objections to the admission of testimony where the testimony improperly relied upon settlement agreements from other proceedings for the purpose of addressing contested issues in the *ESP II Case*.

As discussed in the attached Memorandum in Support, IEU-Ohio respectfully requests that the Commission grant this Application for Rehearing, terminate any authority that may permit AEP-Ohio to bill or collect compensation based on the as-approved Modified ESP, and issue such orders as are necessary to continue the provisions, terms, and conditions of AEP-Ohio's most recent SSO until a subsequent SSO is lawfully authorized pursuant to Section 4928.142 or 4928.143, Revised Code. The Commission's restoration of the most recent SSO must require that AEP-Ohio's compensation for generation capacity service available to CRES providers be determined based on the capacity valuation and pricing method that is part of PJM's RPM. Further, IEU-Ohio requests that the order granting rehearing direct that any revenue increase collected by AEP-Ohio pursuant to the ESP II Order or pursuant to the Stipulation and Recommendation ("Stipulation ESP"), filed September 7, 2011 that was approved and then rejected on February 23, 2012, be refunded.

Respectfully submitted,

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MEMORANDUM IN SUPPORT

I. INTRODUCTION

Throughout the *ESP II Case*, AEP-Ohio's misguided proposals to increase default generation supply prices, extract above-market revenue for generation capacity service available to CRES providers, and block shopping opportunities have placed seriously contested legal, policy, and practical questions before the Commission. Initially these questions arose in the ESP application ("Application") filed by AEP-Ohio on January 27, 2011. The Commission's Staff ("Staff") and every other stakeholder opposed the Application because it contained unlawful and unreasonable proposals to increase SSO rates and block customer choice.[7] Eventually, the focus of the litigation

[7] IEU-Ohio filed a motion to dismiss without prejudice that identified several material procedural errors in AEP-Ohio's Applications. Motion to Dismiss and Memorandum in Support of Industrial Energy Users-Ohio (May 10, 2011) ("May 2011 Motion"). IEU-Ohio renewed that motion at the completion of AEP-Ohio's case-in-chief during the hearing on the Stipulation. Stipulation Tr. Vol. VI at 956-58. The Commission denied the motion in its Opinion and Order approving the Stipulation. Opinion and Order at 8 (Dec. 14, 2011).

shifted to proposals contained in the Stipulation ESP filed on September 7, 2011, but the main contested issues remained substantially the same.

On December 14, 2011, the Commission issued an Opinion and Order modifying and approving the contested Stipulation ESP. The Commission's approval, however, was short-lived. When customers opened their January 2012 bills and the Commission-approved Stipulation ESP's rate shock became evident, a public outcry inundated the Commission. On February 23, 2012, the Commission issued an Entry on Rehearing rejecting the Stipulation ESP because AEP-Ohio failed to demonstrate that the Stipulation ESP benefited ratepayers and was in the public interest.[8]

The February 23, 2012 Entry on Rehearing did not abate AEP-Ohio's ambitions to protect its generation revenue and block shopping. Instead, AEP-Ohio's focus shifted to the pursuit of an unlawful cost-based ratemaking methodology in the *Capacity Case* and a Modified ESP that was financially worse for customers than the Stipulation ESP.[9]

After additional months of discovery and another evidentiary hearing, the Commission issued the ESP II Order modifying and approving AEP-Ohio's Modified ESP. Because of the ESP II Order and the Capacity Order, AEP-Ohio has been authorized to significantly increase electricity prices applicable to shopping and non-shopping customers.

In the *Capacity Case*, the Commission unlawfully invented a cost-based ratemaking methodology and then applied that methodology to produce a significant

[8] Entry on Rehearing at 12 (Feb. 23, 2012).

[9] FirstEnergy Solutions Corp. ("FES") Ex. 104 at 37-43.

increase in AEP-Ohio's compensation for capacity available to CRES providers.[10] After the Commission unlawfully authorized AEP-Ohio to significantly increase its generation service capacity compensation through the application of a price of $188.88/MW-day, the Commission divided responsibility for this competitive service compensation between CRES providers and customers (shopping and non-shopping alike). The Commission limited the generation capacity service compensation responsibility of CRES providers to the much lower RPM-Based Price while condemning shopping and non-shopping customers to pick up the positive difference between $188.88/MW-day and the RPM-Based Price[11] through non-bypassable charges payable during the term of the Modified ESP and for three years after it ends. The practical effect of the Commission's decision in the *Capacity Case* and the *ESP II Case* is to insulate, at customers' expense, AEP-Ohio's competitive generation business from the discipline of market forces at a time when Ohio law requires AEP-Ohio's generation business to be fully on its own in the competitive market.[12]

In addition to authorizing AEP-Ohio to significantly increase its compensation for generation capacity service in the *Capacity Case* and *ESP II Case,* the Commission authorized AEP-Ohio to collect even more compensation for SSO service through additional non-bypassable riders. This incremental increase in compensation for SSO

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[10] The lawfulness and reasonableness of the Capacity Order is currently subject to several applications for rehearing. The Commission has granted rehearing to permit it additional time to consider the applications.

[11] This difference being the "Capacity Shopping Tax" or the above-market compensation for generation capacity service.

[12] Section 4928.38, Revised Code. This requirement was strengthened in Section 4928.141, Revised Code (enacted after Section 4928.38, Revised Code) by the General Assembly's termination of any future transition revenue collection opportunity.

service is not warranted since the Commission has no authority to approve any of the new generation-related non-bypassable riders as a part of an ESP, and its approval also violates corporate separation requirements.[13]

The ESP II Order goes through the motions required by the ESP versus MRO test and then wrongly concludes that the as-approved Modified ESP is more favorable in the aggregate than an MRO. But, the ESP II Order itself confirms that the as-approved Modified ESP is, in the aggregate, substantially worse than the expected results of an MRO-based SSO.

II. ESP VERSUS MRO TEST

AEP-Ohio had the burden of demonstrating that its Modified ESP satisfied the statutory requirement that the ESP SSO's pricing and all other terms and conditions, including any deferred amounts and the collection of those deferred amounts, are more favorable in the aggregate than an MRO SSO.[14] In its Modified ESP Application, AEP-Ohio claimed that the Commission should approve the Modified ESP because it satisfied the test by $960 million and provided several qualitative benefits.[15]

To support its claim, AEP-Ohio proposed that the Commission divide the statutory better-than test for approving an ESP into three steps.[16] The first step, the Price Test, consisted of a comparison of some of the provisions contributing to the Modified ESP price and an administratively-determined price of the MRO. In particular,

[13] The Application for the Modified ESP also requested Commission approval of AEP-Ohio's separate application to divest generating assets and to amend its corporate separation plan. As discussed below, those matters are not properly before the Commission in this proceeding.

[14] Section 4928.143(C)(1), Revised Code.

[15] AEP-Ohio Ex. 114 at LJT-1.

[16] Ohio Power Company's Initial Post-Hearing Brief at 127 (June 29, 2012) ("AEP-Ohio Initial Brief").

AEP-Ohio's version of the Price Test did not include the effects of the RSR. The second step presented the "other" quantifiable costs and benefits of the provisions of the ESP not addressed by the Price Test. To justify the Modified ESP, AEP-Ohio claimed that a proposed above-market capacity pricing scheme that increased capacity prices paid by CRES providers for capacity to serve shopping load was "discounted" as compared to a much higher and never-proven number and that the hypothetical discount provided a $989 million benefit.[17]

The third step presented the "qualitative benefits" (but not the costs) which AEP-Ohio attributed to its Modified ESP.[18]

In the ESP II Order, the Commission used a three-part test similar to that advanced by AEP-Ohio, but rejected AEP-Ohio's claim that it had demonstrated that the Modified ESP was more favorable because "AEP-Ohio made multiple errors in conducting the statutory test."[19] Having failed to find that AEP-Ohio had sustained its burden of proof to establish that the Modified ESP was lawful, the Commission then began its own search of the record to "correct" AEP-Ohio's errors.[20] During this search, the Commission substantially modified the input variables and their assigned value which AEP-Ohio used in its ESP versus MRO test. Based on the Commission's modifications, the ESP II Order identifies that the as-approved Modified ESP is financially worse than an MRO by $386 million.[21]

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[17] AEP-Ohio Ex. 116 at 8.

[18] AEP-Ohio Ex. 114, *passim.*

[19] ESP II Order at 73.

[20] *Id.*

[21] *Id.* at 75.

Despite finding that customers would pay several hundred million dollars more under the Commission's as-approved Modified ESP, the Commission nevertheless concluded that "in weighing the statutory price test which favors the modified ESP by $9.8 million [wrongly derived as discussed below], as well as the quantifiable costs and benefits associated with the modified ESP, and the non-quantifiable benefits, as we find the modified ESP, is more favorable in the aggregate than what would otherwise apply under an MRO [sic]."[22]

The revisions the Commission made to the Modified ESP and the ESP versus MRO test presented by AEP-Ohio were substantial. In the first step, the Commission's so-called Price Test, the Commission modified AEP-Ohio's calculation in two ways.

First, the Commission replaced the capacity price used by AEP-Ohio, $355/MW-day, with $188.88/MW-day, the capacity compensation the Commission authorized in the *Capacity Case*.[23] The Commission also decided to exclude the first nine months of the term of the as-approved Modified ESP in conducting the ESP versus MRO test stating that AEP-Ohio would be unable to conduct an auction for several months.[24] Based on the Commission's unreasonable and unlawful specifications for the Price Test, the ESP II Order concludes that the as-approved Modified ESP is $9.8 million more favorable than the MRO for the 2013-2014 and 2014-2015 PJM planning years (the last 24 months of the Modified ESP).[25] Of course, since the ESP II Order does not

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[22] *Id.* at 77.

[23] *Id.* at 74.

[24] *Id.*

[25] *Id.* at 75. The PJM planning year runs from June through May. Thus, the 2013-2014 planning year runs from June 2013 through May 2014.

use the full term of the as-approved Modified ESP, the $9.8 million "more favorable" conclusion offers a fictional account of the cost of the as-approved Modified ESP.

In the second step of the Commission's three-part approach to the ESP versus MRO test, the Commission again modified AEP-Ohio's ESP versus MRO test. The Commission removed AEP-Ohio's so-called "capacity discount" that AEP-Ohio had claimed in the Modified ESP Application.[26] Although AEP-Ohio's ESP versus MRO test included the full revenue effect of its proposed RSR, the ESP II Order's ESP versus MRO test omits the full impact of the non-bypassable RSR from the cost of the as-approved Modified ESP. The ESP II Order does not explain why the full amount of the non-bypassable RSR was not picked up in the Commission's ESP versus MRO test.[27] With a bit more tinkering to pick up $8 million associated with the illegally approved GRR as a cost of the as-approved Modified ESP,[28] the ESP II Order winds its way to the conclusion that the as-approved Modified ESP is worse than an MRO SSO by $386 million.[29]

The ESP versus MRO test applied by the Commission in the ESP II Order fails to recognize all of the quantifiable costs of the as-approved Modified ESP and is therefore unreasonable and unlawful. First, the ESP II Order understates the cost of the as-approved Modified ESP by the ignored portion of the RSR. Had the full effect of the RSR been recognized, the disadvantage of the as-approved Modified ESP would have

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[26] The Commission does not explicitly state that it removed the claimed "discount," but the Commission's conclusion that the Modified ESP fails the ESP versus MRO test impliedly supports that result. *Id.* at 75.

[27] *Id.* at 75 n.32.

[28] *Id.* The illegality of the GRR is discussed below.

[29] *Id.* at 75.

increased by $144 million (bringing the total disadvantage to $530 million as discussed below). Second, it also fails to include the full revenue effect of the Turning Point Solar Project ("Turning Point") over the life of the facility as part of the cost of the GRR included in the as-approved Modified ESP. Third, the ESP versus MRO test contained in the ESP II Order ignores the cost of two additional non-bypassable riders contained in the as-approved Modified ESP, the PTR and the Capacity Shopping Tax.[30]

In the third step, the ESP II Order resorts to qualitative judgments[31] regarding the as-approved Modified ESP and concludes that several qualitative benefits offset the (understated) $386 million by which the ESP II Order acknowledges that the as-approved Modified ESP flunks the ESP versus MRO test. The ESP II Order puts distribution-related benefits attributed to customer-paid distribution riders,[32] an expanded energy-only auction, and a claimed accelerated use of a CBP to set the default generation supply price relative to what would be available under an MRO in the Commission's qualitative benefits quiver.[33] But the ESP II Order is, qualitatively speaking, unreasonable and unlawful because it is very one-sided; it fails to recognize

[30] The details of the Capacity Shopping Tax are discussed below.

[31] Although qualitative benefits are, by definition, not subject to quantification, the test established by Ohio law obligates the Commission to articulate some proven rationale as to why the alleged qualitative benefits of an ESP outweigh its known costs. Otherwise, the Commission's ESP versus MRO analysis would, in every case, boil down to relying simply on the Commission's say-so and effectively put the Commission's decision and non-bypassable consequences beyond challenge or review. The statutory test is supposed to be beneficial to consumers and does not allow the Commission to, in substance, exercise unfettered discretion through a one-sided, back-door, qualitative analysis.

[32] The ESP II Order points to the ESP's distribution-related riders, such as the Enhanced Service Reliability Rider ("ESSR") and the gridSMART Rider. These riders, however, are also available to AEP-Ohio *via* a distribution rate case and thus would be available to AEP-Ohio under an MRO. Thus, the ESSR and the gridSMART Riders are not qualitative benefits of the as-approved Modified ESP.

[33] *Id.* at 75-76. These so-called qualitative benefits are a byproduct of AEP-Ohio's overdue transition to the competitive market and compliance with Ohio's corporate separation requirements. They can only be called benefits by ignoring the corporate separation that is otherwise required by Ohio law.

and include the costs of these so-called qualitative benefits in the ESP versus MRO test applied to the as-approved Modified ESP or objectively explain how these so-called qualitative benefits override the $386 million by which the ESP II Order finds that the as-approved Modified ESP fails the ESP versus MRO test.[34]

For the following reasons, the ESP II Order's application of the ESP versus MRO test and the finding that the as-approved Modified ESP is more favorable in the aggregate than the expected results of an MRO SSO are unlawful and unreasonable.

1. **The ESP II Order is unlawful and unreasonable because the as-approved Modified ESP, including its pricing and all other terms and conditions, including any deferrals and any future recovery of deferrals, is not more favorable in the aggregate as compared to the expected results that would otherwise apply under Section 4928.142, Revised Code.**

The ESP II Order unreasonably and unlawfully specifies and applies the statutory ESP versus MRO test to the as-approved Modified ESP. Once this unreasonable and unlawful specification and application are cured, the Commission must find that the as-approved Modified ESP fails the ESP versus MRO test. When the ESP II Order's findings and conclusions are corrected to account for all the costs of the as-approved Modified ESP, it quantitatively fails the ESP versus MRO test by $1.736 billion[35] and there are no offsetting qualitative benefits.

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[34] *Id.* at 77.

[35] The Commission identified that the as-approved Modified ESP was $386 million less favorable than an MRO. As demonstrated below, the as-approved ESP should include the full revenue effects of the RSR (an additional $144 million), the revenue effect of the PTR (an additional $410 million), the effect of the deferral of the deferred Capacity Shopping Tax (an additional $447 million as detailed in Attachment A), and the full revenue effect of the GRR that would account for the life of the generating facility ($349.2 million). If the ESP II Order is corrected for these amounts, the as-approved Modified ESP fails the ESP versus MRO test by $1.736 billion.

A. The ESP II Order is unlawful and unreasonable because it uses $188.88/megawatt-day ("MW-day") as the price for the capacity component for generation supply associated with the MRO SSO, thereby overstating the MRO SSO pricing as compared to the as-approved Modified ESP SSO.

The ESP II Order unreasonably and unlawfully assumes that the MRO SSO's generation supply price would compensate AEP-Ohio for generation capacity service based on a price of $188.88/MW-day, the amount authorized by the Commission in the *Capacity Case* as the "state compensation mechanism."[36] The ESP II Order reached this result based on its assumption that a state compensation mechanism price of $188.88/MW-day applies where all or part of the MRO generation supply is procured through a CBP.[37] It does not so apply. According to the ESP II Order, the $188.88/MW-day price is appropriate because AEP-Ohio is an FRR Entity and will be supplying capacity whether the customer is an SSO customer or the customer is taking service through a CRES provider.[38] The ESP II Order's use of a capacity price of $188.88/MW-day to identify the expected results of an MRO SSO is unlawful and unreasonable for several reasons.

The ESP II Order's assumption that the state compensation mechanism price of $188.88/MW-day (adopted in the *Capacity Case*) applies in the MRO context is incorrect. As demonstrated in this case (as well as in the *Capacity Case*), the state

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[36] ESP II Order at 74.

[37] AEP-Ohio technically is not a Fixed Resource Requirement ("FRR") Entity; American Electric Power Service Corporation ("AEPSC") is the signatory party of the Reliability Assurance Agreement ("RAA"). AEPSC is the agent of AEP-Ohio under the agreement. The RAA is contained IEU-Ohio exhibit 124 at KMM-15. Duke Energy Ohio, Inc.'s ("Duke") recent application in Case Nos. 12-2400-EL-UNC, *et al.* suggests that Duke will also seek advantage from this incorrect assumption as it pushes the Commission to provide to Duke what the Commission has rendered unto AEP-Ohio at customers' expense.

[38] ESP II Order at 74.

compensation mechanism under Section D.8 of Schedule 8.1 of the RAA deals only with generation capacity service compensation available from an alternative load serving entity or "LSE" (which in Ohio is a CRES provider) that is serving a retail customer.[39] Under the MRO option, the EDU procures an escalating portion of the SSO generation supply through a Commission-supervised CBP. The winning generation supply bidders in this MRO SSO process do not serve retail customers; they provide generation supply, including capacity, on a wholesale or sale for resale basis to the EDU (AEP-Ohio in this case) with the delivered total price of the generation supply determined through the CBP. Regardless of what role the state compensation mechanism might have for determining the price CRES providers pay AEP-Ohio for capacity when such CRES providers are serving retail customers, the state compensation mechanism has no role in establishing AEP-Ohio's compensation when the MRO generation supply is procured through a wholesale CBP. The demand served by the supply provided by the bidder is not "switched load," it is the demand of non-shopping customers (non-switched load). As a result, the wholesale generation supplier bidding in the MRO CBP is free to secure capacity by contract with AEP-Ohio, provide its own capacity, or enter into a bilateral transaction for capacity with a third party, and it is unreasonable to assume that a bidding wholesale supplier would pay above-market prices for capacity.[40] Indeed, the Commission's supervisory role with regard to this CBP process and statutory obligations would require the Commission to reject an above-market bid.

[39] Capacity Order at 23.

[40] IEU-Ohio Ex. 125 at 64.

The pricing under the RAA's state compensation mechanism simply does not apply to a wholesale supplier selected in the MRO's CBP process to meet all or part of the demand of the EDU's non-shopping customers. And by using $188.88/MW-day as the price for the capacity component of the MRO's default generation supply price, the ESP II Order significantly overstates the cost of the MRO's default generation supply. Indeed, the Commission's supervisory role with regard to this CBP process and statutory obligations would require the Commission to reject an above-market bid.

Even if a wholesale bidder in the MRO's default generation supply CBP was required to pay the same price for capacity as a CRES provider, the ESP II Order ignores the decision in the *Capacity Case* which holds that CRES providers pay the RPM-Based Price.[41] Thus, the use of the $188.88/MW-day price to establish the capacity component of the MRO default generation supply price is incorrect and unreasonable based on the reasoning contained in the ESP II Order.

Instead of assuming (wrongly) that the $188.88/MW-day price was proper to identify the capacity component of the cost of default generation supply in an MRO context and as a matter of sound decision-making, the Commission should have used actual CBP results to identify the expected generation supply price for the MRO. As Mr. Murray correctly concluded, "it is unreasonable to use administratively-determined price estimates to portray the MRO option in view of the actual CBP information that is readily available for at least a portion of the period covered by the Modified ESP."[42]

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[41] Capacity Order at 23.

[42] IEU-Ohio Ex. 125 at 58.

Moreover, the record includes detailed information to establish a generation supply price based on the actual CBP results for part of the Modified ESP term. In his application of the ESP versus MRO test, Mr. Murray divided the ESP term into two periods to account for the availability of relevant auction information to develop the competitive benchmark price.[43] For only the period of June 2012 to December 2014 and based on the same shopping assumptions used by AEP-Ohio, Mr. Murray estimated that the Modified ESP would fail the ESP versus MRO test by $330 million if the actual CBP results were relied upon to establish the competitive benchmark price.[44] Mr. Murray estimated the Modified ESP would fail the ESP versus MRO test for the period of January 2015 to May 2015 by another $77 million,[45] and this second calculation does not reflect the additional higher costs of the 5% energy-only auction, discussed below.[46]

Additionally and as discussed below and in IEU-Ohio's Post-Hearing Brief and Application for Rehearing in the *Capacity Case*,[47] the Commission has no authority to invent and apply the cost-based ratemaking methodology for purposes of increasing AEP-Ohio's compensation for generation capacity service. Therefore, it was unlawful and unreasonable to assume for purposes of the ESP versus MRO test that the capacity price component of the MRO's default generation supply would be dictated by

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[43] *Id.* at 65-69.

[44] *Id.* at 69-70 & Ex. KMM-20.

[45] *Id.* During his examination, Mr. Murray corrected Exhibit KMM-20 to reflect the ESP being less favorable than an MRO between January 2014 and May 2015 by $13.34/MWh, rather than $13.53/MWh.

[46] *Id.* at 72-74.

[47] *Capacity Case*, Post-Hearing Brief of Industrial Energy Users-Ohio (May 23, 2012) and Industrial Energy Users-Ohio's Application for Rehearing (Aug. 1, 2012).

the cost-based ratemaking methodology used in the *Capacity Case* to produce the $188.88/MW-day price.

Finally, by assuming an above-market $188.88/MW-day capacity price for purposes of portraying the expected results of the MRO, the ESP II Order also unreasonably and unlawfully assumes that AEP-Ohio would be entitled to collect above-market compensation for generation-related service provided to non-shopping customers through the MRO option. As discussed below and in IEU-Ohio's Application for Rehearing in the *Capacity Case*, this above-market compensation for generation-related service is "transition revenue" under Ohio law. Since the opportunity to collect transition revenue or its equivalent expired years ago and since AEP-Ohio agreed, in a Commission-approved settlement in AEP-Ohio's Electric Transition Plan ("ETP") proceedings,[48] to forego any recovery of generation-related transition revenue, the ESP II Order's use of the above-market $188.88/MW-day price is precluded by operation of Ohio law. The expected results of the MRO cannot, as a matter of law, include above-market compensation for generation-related service or be structured to provide AEP-Ohio's generation business with additional time to transition to a competitive market.

B. The ESP II Order is unlawful and unreasonable because it disregards the costs of the as-approved Modified ESP for over 25% of the ESP term.

The ESP II Order's quantitative analysis of the as-approved Modified ESP is improper because it ignores certain and quantifiable costs of the ESP. The ESP II Order states that it must "begin evaluating the statutory price test analysis

[48] *In the Matter of the Applications of Columbus Southern Power Company and Ohio Power Company for Approval of Their Electric Transition Plans and for Receipt of Transition Revenues*, Case Nos. 99-1729-EL-ETP, *et al.*, Opinion and Order (Sept. 28, 2000). The Opinion and Order is IEU-Ohio Ex. 104.

approximately ten months from the present" and, thus, is limited to a comparison of the ESP versus an MRO in the Commission's Price Test between June 1, 2013 and May 31, 2015.[49] The ESP II Order states this limitation results from the fact that AEP-Ohio's quantitative analysis was prepared as of June 2012 and the Order was not issued until August 2012. The ESP II Order further states that because FES witness Banks offered testimony that AEP-Ohio *could* participate in a 100% energy-only auction as of June 2013, then somehow an MRO could not be established until then.[50] This explanation defies logic, reason, and the statutory test required by Section 4928.143(C)(1), Revised Code. It also ignores the fact that AEP-Ohio and its affiliates have participated in CBPs associated with default generation pricing for other Ohio EDUs,[51] and AEP-Ohio, itself, has used CBPs to establish default generation supply pricing for its retail customers.[52]

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[49] ESP II Order at 74.

[50] *Id.*

[51] IEU-Ohio Ex. 125 at KMM-6 & 7.

[52] *See In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of their Plan to Provide Additional Options for Customer Participation in the Electric Market*, Case No. 06-1153-EL-UNC, Application (Sept. 22, 2006). *See also In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company For Approval of a Competitive Bidding Process for Standard Service Offer Electric Generation Supply, Accounting Modifications Associated With Reconciliation Mechanism and Phase In, and Tariffs for Generation Service*, Case Nos. 07-769-EL-ATA, *et al.*, Comments of Columbus Southern Power Company and Ohio Power Company at 5 (Sept. 5, 2007) (AEP-Ohio indicated that if a CBP were held to obtain SSO generation for AEP-Ohio's load, given AEP-Ohio's FRR status, AEP-Ohio would sell capacity to winning bidders at the RPM clearing price until such time as AEP-Ohio could terminate its FRR status); *In the Matter of the Transfer of Monongahela Power Company's Certified Territory in Ohio to the Columbus Southern Power Company*, Case No. 05-765-EL-UNC, Opinion and Order at 14-17 (Nov. 9, 2005) (the Commission authorized AEP-Ohio to conduct a Request for Proposals ("RFP") for the generation supply that AEP-Ohio said it needed to meet the default supply needs of the former Monongahela Power Company customers). AEP-Ohio has also been able to secure other forms of market-based compensation for the default generation supply costs associated with the load of Ormet Primary Aluminum Corp. and Ormet Aluminum Mill Products Corp. *Columbus Southern Power Company's and Ohio Power Company's Application to Set the 2007 Generation Market Price for Ormet's Hannibal Facilities*, Case No. 06-1504-EL-UNC, Finding and Order at 2-3 (June 27, 2007); *Columbus Southern Power Company's and Ohio Power Company's Application to Set the 2008 Generation Market*

Section 4928.143(C)(1), Revised Code, requires that the ESP, even as modified by the Commission and including all of its terms and conditions, be more favorable in the aggregate than the expected results of an MRO. By virtue of the ESP II Order, the as-approved Modified ESP is effective September 1, 2012 and runs until May 31, 2015 assuming AEP-Ohio does not reject the as-approved Modified ESP. There is no term or condition in the as-approved Modified ESP that would cause the effective date to be delayed until June 1, 2013. All of its costs must be considered, and ignoring over 25% of the costs of the ESP through delayed recognition of its actual start date is unreasonable and unlawful.

To the extent AEP-Ohio requires more time to prepare for the MRO's CBP, Ohio law provides that AEP-Ohio's current ESP, with limited adjustments, continues until a subsequent SSO is authorized.[53] Thus, at the very least, the current ESP rates that would remain in effect until June 2013 should be included in the projected costs of an MRO (if it actually would take that long for the CBP to be instituted, and there is no evidence to that effect). The ESP II Order's exclusion of the costs associated with over 25% of the term of the as-approved Modified ESP is unlawful and unreasonable.

Finally, the Commission's own experience with Duke belies the conclusion that it would take nine months to set up a proper full requirements auction. The Commission approved Duke's full-requirements auction process on November 22, 2011.[54] Duke

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Price for Ormet's Hannibal Facilities, PUCO Case No. 07-1317-EL-UNC, Columbus Southern Power Company's and Ohio Power Company's Ormet-Related 2008 Generation Market Price Submission at 1 (Dec. 27, 2007).

[53] Section 4928.143(C)(1), Revised Code.

[54] *In the Matter of Duke Energy Ohio, Inc. for Authority to Establish a Standard Service Offer Pursuant to Section 4928.143, Revised Code, in the Form of an Electric Security Plan, Accounting Modifications, and Tariffs for Generation Service*, Case No. 11-3549-EL-SSO, Opinion and Order (Nov. 22, 2011).

conducted the first full requirements auction on December 14, 2012.[55] Based on real world experience, it is nonsensical to conclude that it would take nine months to implement a full-requirements auction under the MRO alternative.

C. The ESP II Order is unlawful and unreasonable because it does not include the full cost of the Generation Resource Rider ("GRR") as part of the quantitative costs in its application of the ESP versus MRO test, thereby understating the cost of the as-approved Modified ESP.

The ESP II Order authorized the GRR to be included in the as-approved Modified ESP and set the initial non-bypassable GRR rate at zero.[56] As discussed below, the ESP II Order erred in authorizing the non-bypassable GRR. But, once authorized, the Commission is obligated to recognize the full cost of the GRR in conducting the ESP versus MRO test.

In its application of the ESP versus MRO test, the ESP II Order did assign some cost to the GRR. The ESP II Order assumed that Turning Point would be recovered as a "known" cost through the GRR during the term of the ESP and assigned $8 million to the Modified ESP for the GRR.[57] While $8 million represented a "known" ESP-related cost of the GRR during the term of the as-approved Modified ESP, the ESP II Order unlawfully and unreasonably understated the costs recoverable through the GRR by not accounting for the cost of Turning Point over the life of the facility.

By law, the Commission must consider "all the terms and conditions" of the as-approved Modified ESP.[58] A non-bypassable charge for a new generating plant cannot

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[55] *In the Matter of the Procurement of Standard Service Offer Generation for Customers of Duke Energy Ohio, Inc.*, Case No. 11-6000-EL-UNC, Finding and Order (Dec. 15, 2011).
[56] ESP II Order at 24-25.

[57] *Id.* at 75

[58] Section 4928.143(C)(1), Revised Code.

be authorized by the Commission as part of an MRO SSO.[59] When a non-bypassable generating plant-related charge is established as part of an ESP, customers become responsible for the non-bypassable charge "for the life of the facility,"[60] and this continuing responsibility to pay the surcharge is a term or condition of the as-approved Modified ESP. Based on the testimony of AEP-Ohio, the estimated life-of-facility revenue requirement for Turning Point is $357.2 million, leaving an unrecognized balance of $349.2 million.[61] Despite its assumption that Turning Point would be recovered from customers through the GRR, the ESP II Order fails to include the $349.2 million as a quantitative cost of the as-approved Modified ESP in the application of its ESP versus MRO test. By failing to include the full life-of-facility cost of Turning Point in the ESP versus MRO test, the ESP II Order is unreasonable and unlawful. Therefore, the Commission must grant rehearing and include the full cost of Turning Point, $357.2 million, as a cost of the as-approved Modified ESP.

D. The ESP II Order is unlawful and unreasonable because it does not include known costs for the Pool Termination Rider ("PTR"), Retail Stability Rider ("RSR"), and Capacity Shopping Tax as part of the quantitative costs of the as-approved Modified ESP for purposes of applying the ESP versus MRO test, thereby understating the cost of the as-approved Modified ESP.

The ESP II Order authorizes an ESP that includes the PTR, RSR, and the Capacity Shopping Tax. In its application of the ESP versus MRO test, however, the ESP II Order does not include the full costs of the RSR or any costs of the PTR or the Capacity Shopping Tax. As a result, the cost of the as-approved Modified ESP is

[59] Section 4928.142, Revised Code.

[60] Section 4928.143(B)(2)(c), Revised Code.

[61] Office of the Ohio Consumers' Counsel ("OCC") Ex. 114 at 17-18 (based on the supplemental testimony of AEP-Ohio witnesses Thomas, Nelson, and Roush).

unlawfully and unreasonably understated as compared to the expected results of the MRO. Under the MRO option, the RSR, PTR, and the Capacity Shopping Tax are not lawful.

The PTR is a generation-related non-bypassable rider designed to permit AEP-Ohio to recover "lost revenue in association with the termination of the Pool Agreement."[62] The ESP II Order set the initial PTR rate at zero.[63] As discussed below, the inclusion of the non-bypassable PTR in the as-approved Modified ESP is, as in the case of the GRR, unlawful and unreasonable. Nonetheless, once the ESP II Order authorized the inclusion of the PTR in the as-approved Modified ESP, the effect of the PTR must be included as a cost of the as-approved Modified ESP for purposes of conducting the ESP versus MRO test.

AEP-Ohio failed to offer any evidence on the cost customers will face through the PTR. FES, however, presented evidence that shows that the PTR's impact could be as much as $410 million for the period of January 1, 2014 to May 31, 2015.[64] Yet, the ESP II Order ignores this potential impact, thereby unreasonably and unlawfully ignoring "all the terms and conditions" of the as-approved Modified ESP for purposes of conducting the ESP versus MRO test.

The ESP II Order's application of the ESP versus MRO test also unreasonably and unlawfully fails to account for the two non-bypassable riders that make shopping and non-shopping customers responsible for the portion of the generation capacity

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[62] ESP II Order at 47. The Pool Agreement deals with generation-related relationships between AEP-Ohio and its affiliates.

[63] *Id.* at 49.

[64] FES Ex. 104 at 31.

service compensation that is driven by the $188.88/MW-day price and is not paid by CRES providers. In the Capacity Order, the Commission authorized AEP-Ohio to make accounting changes to defer the difference between the RPM-Based Price and the $188.88/MW-day price for capacity provided to CRES providers serving customers in the AEP-Ohio service territory, setting the stage for the decision in the *ESP II Case*.[65]

In the ESP II Order, the Commission authorized the RSR and held that $1/MWh of the RSR would be applied to begin to pay the RPM-Based Price/$188.88 difference created by the terms of the Capacity Order.[66] Under the ESP II Order, any remaining deferred balance is to be collected through the non-bypassable Capacity Shopping Tax rider that will begin after the term of the as-approved Modified ESP.[67] As discussed below, the authorizations of the RSR and the Capacity Shopping Tax are unlawful and unreasonable. However, since the ESP II Order authorized the inclusion of the RSR and the Capacity Shopping Tax in the as-approved Modified ESP, it is unreasonable and unlawful for the ESP II Order to not recognize the full costs of these non-bypassable riders for purposes of conducting the ESP versus MRO test.

First, the ESP II Order fails to include the full cost of the RSR in its version of the ESP versus MRO test. The as-approved RSR will generate $508 million over the term of the ESP.[68] When it assigned a value to the RSR in its version of the ESP versus MRO test, however, the ESP II Order removed $144 million of the $508 million indicating that the removal was related to the portion of the RSR initially dedicated to

[65] Capacity Order at 23.

[66] ESP II Order at 36.

[67] *Id.* at 52.

[68] ESP II Order at 35.

paying the Capacity Shopping Tax ($1/MWh).[69] The ESP II Order does not explain why it is appropriate to remove the $144 million from the cost of the RSR. Certainly, customers will see the RSR's full $508 million in their bills.[70]

Second, the ESP versus MRO test must include consideration of "any deferrals and any future recovery of deferrals."[71] Yet, the effect of the Capacity Shopping Tax is not recognized in the ESP versus MRO test identified in the ESP II Order. In total, the Capacity Shopping Tax balance resulting from the Commission's Capacity Order could amount to $447 million, based on the shopping projections adopted by the Commission in its calculation of the RSR and without any carrying charges.[72]

E. The ESP II Order is unlawful and unreasonable because it does not include or address the effect of known costs of the energy-only auctions and the "quicker" move to a competitive bid process ("CBP") based SSO for purposes of conducting the ESP versus MRO test.

The ESP II Order concludes that an expansion of the energy-only auctions is a qualitative benefit of the as-approved Modified ESP[73] because the costs of various distribution riders that the Commission continued and the Distribution Investment Rider ("DIR") "will be mitigated by the increase in [energy-only] auction percentages."[74] Additionally, the ESP II Order concludes that an additional significant qualitative benefit

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[69] *Id.* at 75 n.32.

[70] In fact, because of bill language changes approved on August 22, 2012, customers will see a line item detailing exactly how much they are paying in above-market RSR charges to AEP-Ohio. Entry at 1-2 (Aug. 22, 2012).

[71] Section 4928.143(C)(1), Revised Code.

[72] *See* Attachment A to this Memorandum in Support. *See* ESP II Order at 34 (Commission shopping assumptions).

[73] ESP II Order at 76.

[74] *Id.*

was the faster transition to a full CBP to establish the SSO default generation supply price than would be available under an MRO.[75] The ESP II Order's conclusions that the energy auctions and the quicker move to a CBP to establish the SSO's default generation supply price provide qualitative benefits are not supported by the record.

AEP-Ohio offered no evidence that the auctions would reduce or mitigate the impact of the as-approved Modified ESP. Notably, AEP-Ohio treated its proposal to conduct energy-only auctions as a "qualitative" benefit; it did not assign any quantitative value to the auctions.[76] On the other hand, IEU-Ohio provided testimony demonstrating that the energy-only auctions were likely to increase the cost of AEP-Ohio's Modified ESP due to the manner in which AEP-Ohio proposed to treat the results of the auctions in its Fuel Adjustment Clause ("FAC").

> AEP-Ohio indicated it plans to flow the costs of the 5% energy-only bid through the FAC and make no other changes to base SSO rates for distribution, transmission and generation. If that is the case, the only way that the limited energy-only SSO bid will not require an overall price increase to SSO customers is if the cleared bid price is lower than AEP-Ohio's FAC. The market price estimates presented in this case suggest that the results of the energy-only auction will likely be above the FAC rate and thereby increase the cost of the ESP as compared to the MRO and make the rates less stable and predictable as well.[77]

In addition to Mr. Murray's testimony, the administratively-determined competitive benchmark prices advanced by AEP-Ohio in support of its Modified ESP also indicate that the energy-only auctions will increase the SSO price (a quantitative

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[75] *Id.*

[76] AEP-Ohio Ex. 116, LJT-1.

[77] IEU-Ohio Ex. 125 at 72-73. Mr. Murray provided two separate demonstrations of the probable results of the auctions in his testimony. *Id.* at 73-74.

disadvantage).[78] Similarly, IEU-Ohio provided evidence, noted in the ESP II Order but then ignored without explanation,[79] that the energy and capacity auction used to set 2015-2016 ESP rates would, if considered individually and without regard to the other defects in the ESP versus MRO test as applied by the ESP II Order, result in an ESP that is less favorable than the MRO by $26 million (a quantitative disadvantage).[80]

Thus, the ESP II Order ignores the record evidence regarding the effect of the energy-only auctions, evidence confirmed by AEP-Ohio's competitive benchmark prices. That evidence shows that the energy-only auctions increase the cost of the as-approved Modified ESP. That same evidence shows that that customers will be quantitatively disadvantaged (relative to the MRO alternative) by accelerating complete reliance on a CBP to set the default generation supply price beginning with the first year after the term of the as-approved Modified ESP.

Furthermore, the ESP II Order's assumption that a move (faster or otherwise) to a CBP to set the default generation supply price will yield a qualitative benefit demonstrates that the ESP II Order is based on a fundamental misconception about the statutory outcomes required by Chapter 4928, Revised Code, including the policies and the priorities set forth therein.

As discussed more fully below (in the context of the illegally authorized RSR), the General Assembly has declared retail generation service to be a competitive service.[81]

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[78] *Id.* at 73-74.

[79] ESP II Order at 72.

[80] IEU-Ohio Ex. 125 at 70 & 79-80. Stated more plainly, accelerating the use of a CBP to set the default generation supply price will produce a higher cost for SSO customers when market prices are rising. By any reasonable definition, this produces a quantitative disadvantage not a qualitative advantage.

[81] Section 4928.03, Revised Code.

The SSO, whether based on an ESP or MRO, contains a default generation supply component for those customers not receiving competitive service from a CRES provider.[82] The goal, clearly expressed by the General Assembly, is to encourage customer choice through actions by individual customers having comparable and non-discriminatory access to a diverse group of CRES providers.[83] The goal includes a statutory scheme that specifically limits the role of the EDU to that of a default supplier of competitive service and prohibits an EDU from being directly engaged in the business of providing competitive services. Yet, the ESP II Order hobbles the ability of individual customers to meaningfully exercise their customer choice rights during the term of the as-approved Modified ESP so as to maybe, someday, produce a somewhat better, qualitatively speaking, default generation supply outcome. In other words, the ESP II Order wrongly elevates future qualitative goals regarding the default generation supply available from an EDU and the near-term success of AEP-Ohio's competitive generation business above the present goal of providing customers with meaningful access to the electricity market at a time when market prices are the lowest they have been in ten years. Fundamentally, the ESP II Order has embraced a mission statement that is different than the one given to the Commission by the General Assembly.

The ESP II Order unreasonably and unlawfully reverses the priorities clearly expressed in Ohio law. The Commission's role in setting the SSO's default generation supply price is specifically limited to the role provided by Sections 4928.141 through 4928.143, Revised Code. That role does not permit the Commission to subordinate the

[82] Section 4928.14, Revised Code.

[83] Section 4928.02(A), Revised Code.

customer choice rights of individual customers because the Commission wants to help an EDU and its generation business evade the discipline provided by customer choice or because the Commission believes that a future default generation supply option may be better, qualitatively speaking. So the fundamental premise of the ESP II Order (a premise that permits future qualitative benefits[84] associated with an unknown default generation supply option outcome to override a clear, near-term quantitative customer choice disadvantage) unreasonably and unlawfully conflicts with the driving purpose of Ohio's electric restructuring legislation contained in Chapter 4928, Revised Code.

Additionally, the ESP II Order unlawfully and unreasonably assumes that the as-approved Modified ESP will produce a qualitative "benefit" through some future default generation supply price outcome when that outcome is not within the control of the Commission. Chapter 4928, Revised Code, does not require AEP-Ohio to submit an ESP SSO that establishes default generation supply prices based on a capacity and energy auction, and if the Commission orders an auction-based SSO as part of some future ESP, AEP-Ohio may reject it,[85] at which point the Commission must issue an order to continue the provisions, terms, and conditions of the most recent SSO.[86] Further, AEP-Ohio's view of Section 4928.141(C)(1), Revised Code (as demonstrated in its tariff submission letter), is that the EDU never has to say "yes" to the Commission's version of the Modified ESP, but can say "no" and withdraw compliance with the ESP II

[84] As discussed above, establishing the SSO's default generation supply price by means of a CBP beginning in June 2015 produces, after the term of the as-approved Modified ESP, a disadvantage for non-shopping customers while hurting shopping and non-shopping customers in the meantime. There is no qualitative advantage. There is a quantitative disadvantage.

[85] Section 4928.143(C)(2)(a), Revised Code, permits an EDU to withdraw its ESP application, thereby terminating it, if the Commission modifies and approves the application.

[86] Section 4928.142(C)(2)(b), Revised Code.

Order at any time.[87] Thus, not only does the Commission lack authority to require AEP-Ohio to move to the auction-based SSO in 2015, AEP-Ohio's "commitment" in the Modified ESP can be revoked unilaterally and, according to AEP-Ohio, at any time. AEP-Ohio's assumed ability to terminate the as-approved Modified ESP is particularly relevant in this case because AEP-Ohio's commitment to an auction-based ESP SSO in 2015 was tied to numerous conditions, some of which (*e.g.*, adoption of AEP-Ohio's capacity pricing scheme and RSR) have already been rejected by the Commission.[88] Under these circumstances, it is unreasonable and unlawful for the ESP II Order to conclude that the as-approved Modified ESP provides a future qualitative benefit more powerful than the near-term quantitative disadvantage of the as-approved Modified ESP.

2. The ESP II Order is unlawful and unreasonable because it approves an ESP by introducing subjective and speculative "qualitative benefits" into the ESP versus MRO test, thereby evading compliance with Section 4903.09, Revised Code.

In a contested case, Section 4903.09, Revised Code, requires the Commission to issue "findings of fact and [a] written opinion[] setting forth the reasons prompting the decision[] arrived at, based on said findings of fact." As the Supreme Court has indicated, the Commission in assessing the record must explain its rationale, respond to

[87] Letter of Steven T. Nourse to Greta See at 2 (Aug. 16, 2012). In *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 Nos. 08-917-EL-SSO, et al. ("*ESP I Case*"), AEP-Ohio took the position that "[t]he right to withdraw an ESP application under §4928.143(C) (2), Ohio Rev. Code, contains no time restriction." *ESP I Case*, Columbus Southern Power Company's and Ohio Power Company's Memorandum Contra IEU-Ohio's Motion for Immediate Relief from Electric Rate Increases at 4 (Apr. 23, 2010).

[88] AEP-Ohio Ex. 101 at 4-5.

contrary positions, and support its decision with appropriate evidence.[89] "The commission cannot decide cases on subjective belief, wishful thinking, or folk wisdom."[90]

The ESP II Order "weighs" the various parts of AEP-Ohio's three-part approach to the ESP versus MRO test and eventually concludes that the as-approved Modified ESP is more favorable. Because the as-approved Modified ESP is substantially less favorable than the MRO on a quantitative basis, the ESP II Order assigns some indeterminate, but apparently significant, weight to over-the-horizon qualitative benefits attributed to the as-approved Modified ESP.

Although the ESP II Order identifies the qualitative benefits for which it has affection, the ESP II Order does not address the evidence that demonstrates that each of the alleged benefits carries an uncounted cost. The ESP II Order does not explain how the three qualitative "benefits" outweigh the $386 million by which the ESP II Order finds that the as-approved Modified ESP fails the ESP versus MRO test.[91]

Without an objective and articulated explanation of how each of the so-called qualitative benefits was weighted, the ESP II Order's subjective qualitative benefits test prevents the parties, the Supreme Court, and the public from assessing the validity of the Commission's decision. Section 4903.09, Revised Code, requires more than the

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[89] *In re Columbus Southern Power Co.*, 128 Ohio St.3d 512, 519 (2011).

[90] *Consumers' Counsel v. Pub. Util. Comm.*, 61 Ohio St.3d 396, 406 (1991) (*quoting Columbus v. Pub. Util. Comm.*, 58 Ohio St.2d 103, 104 (1979) (Brown, J., dissenting)).

[91] The unreasonableness of the subjective test is further demonstrated by the lack of objective means to measure the effect of corrections to the ESP II Order for the costs of the as-approved Modified ESP that were not addressed by the ESP II Order. There is no objective basis by which a party can determine that the quantitative costs of $1.736 billion are "outweighed" by the qualitative benefits.

"trust me" reasoning contained in the ESP II Order.[92] As a result, the ESP II Order's conclusion that the Modified ESP is more favorable in the aggregate based on "subjective belief" violates the requirements of Section 4903.09, Revised Code, that require the Commission to make findings of fact, to base its decisions based on those findings, explain its rationale, respond to contrary positions, and support its decision with appropriate evidence.

III. NON-BYPASSABLE GENERATION-RELATED RIDERS

The ESP II Order authorized five new non-bypassable generation-related riders under Section 4928.143, Revised Code: the RSR, the Capacity Shopping Tax, the PTR, the GRR, and the PIRR. As discussed below in this section and the following two sections, the portions of the ESP II Order authorizing these riders are unlawful and unreasonable for various reasons and, therefore, the Commission must grant rehearing to remedy these errors.

3. The ESP II Order is unlawful and unreasonable because the non-bypassable RSR, Capacity Shopping Tax, and the PTR cannot be lawfully included in an ESP SSO.

A. The ESP II Order is unlawful and unreasonable because it authorizes non-bypassable generation-related riders which are not included on the list of permissive ESP provisions contained in Section 4928.143(B)(2), Revised Code.

The Commission may authorize a provision of an ESP only if its fits within one of the provisions of Section 4928.143(B)(2), Revised Code.[93] Of the provisions in (B)(2), only divisions (b) and (c) allow for a generation-related non-bypassable charge.

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[92] *In re Columbus Southern Power Co.*, 128 Ohio St.3d 512 at 519.

[93] *Id.* at 519-20.

However, the RSR, the PTR, and the Capacity Shopping Tax were not authorized under divisions (b) or (c), nor could they be.

A non-bypassable charge under (B)(2)(b) or (c) is only available to recover costs associated with generating facilities under construction or constructed after 2009 that meet additional statutory requirements. The RSR, Capacity Shopping Tax, and PTR are not designed to recoup the costs of a generating facility under construction or newly built after 2009; no party has claimed as much. Therefore, there is no basis under Section 4928.143(B)(2), Revised Code, to approve the RSR, Capacity Shopping Tax, and the PTR as non-bypassable charges.

B. The ESP II Order is unlawful and unreasonable because it concludes that the RSR can be authorized under Section 4928.143(B)(2)(d), Revised Code. The RSR does not have the effect of stabilizing or providing certainty regarding retail electric service.

The ESP II Order is unlawful and unreasonable because the RSR cannot be authorized under Section 4928.143(B)(2)(d), Revised Code, since the RSR does not have the effect of stabilizing or providing certainty regarding retail electric service. That division provides that an ESP may include "[t]erms, conditions, or charges relating to limitations on customer shopping for retail electric generation service, bypassability, ... [and] default service ... as would have the effect of stabilizing or providing certainty regarding retail electric service." Retail electric service is defined by Section 4928.01(A)(27), Revised Code, to mean "any service involved in supplying or arranging for the supply of electricity to ultimate customers in this state." The terms "certainty" and "stabilizing," however, are not defined in Chapter 4928, Revised Code.

Because there is no statutory definition of "certainty" or "stabilizing," it is necessary to rely on the ordinary and appropriate dictionary meanings of the terms.[94] Under that standard, the ordinary and appropriate definition of "certainty" is that the subject is made more probable of occurrence.[95] "Stabilizing" denotes "to hold steady."[96] Because the burden of proof rested with AEP-Ohio to demonstrate that the charge is reasonable and lawful, AEP-Ohio was required to show that the RSR was necessary to make it probable that customers would receive retail electric service or to hold steady the provision of retail electric service.

The ESP II Order finds that the RSR meets the statutory requirements of Section 4928.143(B)(2)(d), Revised Code, because the RSR: (1) "ensures certainty regarding retail electric service;" and (2) "promotes stable retail electric service prices."[97] As discussed below, the record does not support the first finding, and the ESP II Order does not provide any analysis to support that finding. The second finding does not meet the statutory requirements and, in any event, the RSR does not promote stable prices. Despite its burden to demonstrate the reasonableness and lawfulness of the RSR, the testimony AEP-Ohio offered did not explain how the RSR would have the effect of making retail electric service more stable or certain. The only statement AEP-Ohio witness Allen offered relative to this statutory requirement appears to be the following

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[94] *Davis v. Davis*, 115 Ohio St.3d 180, 2007-Ohio-5049 at ¶ 14 (*quoting Sharp v. Union Carbide Corp.*, 38 Ohio St.3d 69, 70 (1988) ("[w]here a particular term employed in a statute is not defined, it will be accorded its plain, everyday meaning.")).

[95] Webster's Ninth New Collegiate Dictionary at 223 (1983).

[96] *Id.* at 1146.

[97] *See, e.g.*, ESP II Order at 31 (the RSR "promotes stable retail electric service prices ..." and the RSR allows a freeze of "non-fuel generation rate increase that might not otherwise occur absent the RSR").

question and answer taken from his direct testimony that offers only a conclusion without explanation:

> Q. Is there a reason that you are proposing a retail stability rider that focuses on revenues instead of earnings?
>
> A. Yes. There are several reasons: 1) it provides greater certainty and stability for customers and AEP Ohio ... .[98]

Mr. Allen's testimony merely contrasts the difference between an RSR that is focused on guaranteeing earnings and an RSR that is focused on guaranteeing revenue (including a specified earnings component). Saying that one illegal version of the RSR provides more stability and certainty than another is not responsive to the requirements of Section 4928.143(B)(2)(d), Revised Code. In addition, Mr. Allen acknowledged, both in his direct and rebuttal cross-examination that the EDU operates within the PJM system and the reliability of retail generation service is a function of PJM's control.[99] If AEP-Ohio did not have any generating facilities, PJM would still dispatch supply-side resources under its control to satisfy the needs of AEP-Ohio's customers.[100]

The only other testimony offered by AEP-Ohio applicable to the requirements of Section 4928.143(B)(2)(d), Revised Code, likewise fails to demonstrate how the RSR makes it probable that customers would receive retail electric service or would hold steady the provision of retail electric service. In his Supplemental Direct Testimony, Mr. Dias offered that the lack of the above-market RSR generation-related revenue might result in less investment, but provided no demonstration of any likely impact on

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[98] AEP-Ohio Ex. 114 at 15.

[99] Tr. Vol. V at 1495-96.

[100] *Id.* Section 4928.12, Revised Code, confirms that regional transmission entities such as PJM are responsible for maintaining reliability.

retail service.[101] He also did not assert that increasing rates by the introduction of the RSR would make things better. In fact, AEP-Ohio has admitted that it does not plan to make any new generation investment other than Turning Point during the term of the ESP.[102] As a result of AEP-Ohio's failure to demonstrate that the statutory requirements of Section 4928.143(B)(2)(d), Revised Code, are satisfied, the ESP II Order is unlawful and unreasonable.[103]

The holding that the RSR was authorized by Section 4928.142(B)(2)(d), Revised Code, is also inconsistent with the terms of the as-approved Modified ESP. Although the Commission found the RSR promoted "stable retail electric services prices" by freezing base generation rates, the base generation rates are but one part of AEP-Ohio's generation rates under the Modified ESP. As approved, the Modified ESP has ten generation or transmission-related riders besides the RSR that can and will fluctuate. These include the FAC, the Alternative Energy Rider ("AER"), the DIR, the gridSMART Rider, the Transmission Cost Recovery Rider ("TCRR"), the ESRR, the Energy Efficiency and Peak Demand Reduction Rider ("EE/PDR"), and the Economic Development Rider ("EDR").[104] Additionally, the Commission approved the GRR and the PTR that are initially set at zero but could eventually collect hundreds of millions of

[101] AEP-Ohio Ex. 119 at 5.

[102] Tr. Vol. I at 226-227. See also Tr. Vol. II at 564-65; Tr. Vol. VI at 1976-80. Additionally, there is no evidence that Turning Point will be operational during the term of the as-approved Modified ESP.

[103] ESP II Order at 31.

[104] *Id.* at 16-18, 42, 61-67.

dollars.[105] The structure of the as-approved Modified ESP and all of its moving parts preclude stability and certainty.

The ESP II Order also establishes a foundation for post-ESP riders so that shopping and non-shopping customers pick up the tab for the ESP II Order and Capacity Order liabilities not funded during the term of the as-approved Modified ESP. Further, the Commission indicated that it would adjust the RSR if shopping increased.[106] In fact, the only certainty or stability that the RSR offers is that, as one witness eloquently explained, it guarantees that AEP-Ohio never has a bad year.[107] Thus, the RSR in combination with frozen base generation rates do not promote "stable retail electric service prices" as the prices customers will see over the term of the ESP and, as a result of the deferral mechanisms, thereafter may and likely will vary dramatically. The ESP II Order confirms the electric bill instability produced by the as-approved Modified ESP by directing AEP-Ohio to impose a percentage limitation on the magnitude of some of the increases that ***each individual customer*** will see as a result of the as-approved Modified ESP. Ironically, the ESP II Order then makes customers responsible for a revenue shortfall created by this limitation through another future rider.[108]

The ESP II Order references three other justifications for the RSR, but none of these supports its decision that the RSR is authorized by Section 4928.143(B)(2)(d), Revised Code. The ESP II Order claims the RSR: (1) will provide AEP-Ohio with

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[105] *Id.* at 19-24, 47-49.

[106] *Id.* at 37-38.

[107] Tr. Vol. XIII at 3615.

[108] *See* ESP II Order at 70.

"financial integrity;"[109] (2) allows AEP-Ohio to transition to a market "in two years and nine months as opposed to five years;"[110] and (3) allows AEP-Ohio to offer a "reasonably priced SSO."[111] Because these three justifications do not make it more probable that customers would receive retail electric service or hold steady the provisions of retail electric service, they lend no support to the RSR's legality under Section 4928.143(B)(2)(d), Revised Code.

First, the financial integrity of an EDU's generation is, as a general matter, not relevant in an ESP proceeding. Since the end of AEP-Ohio's Market Development Period ("MDP") on December 31, 2005, AEP-Ohio's generation business has been required to be on its "own in the competitive market."[112] AEP-Ohio has previously argued, and the Commission has agreed, that AEP-Ohio's earnings for its generation business are not a relevant consideration when fixing its default SSO rates.[113]

> [W]ith the expiration of the MDP, generation rates are subject to the market (not the Commission's traditional cost-of-service rate regulation) .... We make this observation to point out that, under the statutory scheme, company earnings levels would not come into play for establishing generation rates–market tolerances would otherwise dictate, just as AEP argued.[114]

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[109] ESP II Order at 31 (The RSR "will provide AEP-Ohio with sufficient revenue to ensure it maintains its financial integrity as well as its ability to attract capital."); *id.* at 33 (The RSR will allow AEP-Ohio to "maintain its financial health."); *id.* at 37 (the RSR ensures "AEP-Ohio has sufficient funds to maintain its operations efficiently ... .").

[110] *Id.* at 36.

[111] *Id.* at 37 (The Commission claimed that the RSR provides shopping customers with a reasonably priced SSO offer should market prices increase and they wish to return to SSO service).

[112] Section 4928.38, Revised Code.

[113] IEU-Ohio Ex. 119 at 18.

[114] *Id.*

Thus, the financial integrity of AEP-Ohio's generation business is not a relevant or lawful justification for the RSR.

Second, the ESP II Order states that, as a package that includes the RSR, the as-approved Modified ESP allows AEP-Ohio to transition to a CBP to set its default SSO generation supply price in under three years instead of the five-year timeframe under an initial MRO application.[115] Even if this were a benefit (which, as discussed previously, it is not), there is no basis in Section 4928.143, Revised Code, or elsewhere in Ohio law for such a transition rider. Additionally, the offered justification is not accurate since the MRO statute allows the Commission "[b]eginning in the second year" of the MRO to "alter prospectively the proportions of the blend" if the Commission deems it necessary "to mitigate any effect of an abrupt or significant change" in SSO rates.[116] Thus, the CBP approved in the ESP II Order will not necessarily occur sooner than what would be possible under an MRO, and, in any event, the CBP set to occur in 33 months is likely to increase customers' rates, not benefit customers.

Finally, the ESP II Order states that the RSR allows AEP-Ohio to "keep[] a reasonably priced SSO offer on the table in the event market prices increase."[117] This statement ignores the fact that both AEP-Ohio and the Commission are obligated to a reasonable outcome as a matter of law regardless of whether the SSO is an ESP or MRO.

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[115] *See* ESP II Order at 36.

[116] Section 4928.142(A), Revised Code.

[117] ESP II Order at 37. Moreover, AEP-Ohio has also claimed that the RSR could be classified as a provider of last resort ("POLR") rider. AEP-Ohio Ex. 119 at 5.

Additionally, this circular reasoning essentially treats the RSR as a POLR charge. Unlike the POLR charge that the PUCO previously and illegally approved for AEP-Ohio, however, the RSR is not bypassable by a customer or a governmental aggregation program that agrees to return to SSO service at a market price.

The Supreme Court has described a POLR obligation as the "obligation to stand ready to accept returning customers" and defined POLR costs as "those costs incurred by [the utility] for risks associated with its legal obligation as the default provider, or electricity provider, of last resort, for customers who shop and then return to [the utility] for generation service."[118] The Commission has described the underlying POLR obligation as the requirement that an EDU "stand ready to provide SSO service to returning customers" which then allows customers to "return at any time" to the SSO,[119] and has defined POLR charges as "charges related to standby and default service, [which] provide certainty for both the [EDU] and [its] customers regarding retail electric service."[120]

Approval of the RSR as a POLR charge is not warranted in this case. The Supreme Court has admonished the Commission to consider carefully what costs it is attributing to POLR obligations.[121] Responding to the Supreme Court's direction, the Commission has required that there be a showing of cost to establish a POLR

[118] *In re Columbus Southern Power Co.*, 128 Ohio St.3d at 517-18.

[119] *ESP I Case*, Order on Remand at 18 (Oct. 3, 2011).

[120] *Id.*

[121] *In re Columbus Southern Power Co.*, 128 Ohio St.3d at 518. *See also, Indus. Energy Users-Ohio v. Pub. Util. Comm.*, 2008-Ohio-990 at ¶¶ 31-33.

charge.[122] AEP-Ohio did not demonstrate any costs that the RSR recovers; rather, the RSR is designed to supplement AEP-Ohio's generation-related revenue in a manner that provides AEP-Ohio a 9% return on equity based on its 2011 common equity capitalization. In other words, the RSR is designed to provide AEP-Ohio with revenue that it might not otherwise receive if customers shopped, *i.e.* "migrated", and left the SSO. It is a lost revenue charge, non-bypassable and payable by both shopping and non-shopping customers.

The Commission, however, has held that a POLR obligation relates only to the cost of returning customers, not migration risk. As the Commission explained, "migration risk is more properly regarded as a business risk faced by all retail suppliers as a result of competition rather than a risk resulting from an EDU's POLR obligation."[123] And, as already mentioned, the Commission has held that a POLR charge must be bypassable by customers agreeing to return to SSO service at market price.[124] Section 4928.20, Revised Code, also provides governmental aggregation program customers with the right to bypass such charges. Because the RSR compensates AEP-Ohio for revenue that is lost if customers migrate, and it does not allow customers to avoid the charge by agreeing to return to the SSO at market prices, the RSR violates Commission precedent, is unlawful and unreasonable.

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[122] *ESP I Case*, Order on Remand at 22 (company failed to demonstrate out-of-pocket cost of serving POLR obligation). If viewed as a stand-by charge, Section 4928.20, Revised Code, requires that the charge be bypassable for customers served by governmental aggregation programs upon election by the relevant unit of government.

[123] *Id.* at 31-32.

[124] *ESP I Case*, Opinion and Order at 40 (Mar. 18, 2009).

In summary, there is no legal or factual basis to support the RSR. The RSR does not meet the requirements of Section 4928.143(B)(2)(d), Revised Code. AEP-Ohio's generation business earnings are irrelevant when establishing default generation supply prices or considering an SSO. The RSR does not necessarily provide a faster-than MRO transition to full reliance on a CBP to establish the default generation supply price, and the ESP II Order's rush to a CBP is likely to increase non-shopping customers' bills relative to the pace of the MRO. Finally, the RSR is not a lawful POLR charge. Thus, the Commission must grant rehearing and reject the RSR as a part of the as-approved Modified ESP.

C. The ESP II Order is unlawful and unreasonable because the PTR cannot be authorized under Section 4928.143(B)(2)(h), Revised Code. The PTR has no relationship to AEP-Ohio's distribution service.

The ESP II Order approves the PTR pursuant to Section 4928.143(B)(2)(h), Revised Code, and states that:

> in the event AEP-Ohio seeks recovery under the PTR, AEP-Ohio must first demonstrate the extent to which the Pool Agreement benefitted Ohio ratepayers over the long-term and the extent to which the costs and/or revenues should be allocated to Ohio ratepayers. Further, AEP-Ohio must demonstrate to the Commission that any recovery it seeks under the PTR is based upon costs which were prudently incurred and are reasonable.[125]

The ESP II Order is unlawful and unreasonable because the PTR may not be approved under Section 4928.143(B)(2)(h), Revised Code. That Section can only be applied to approve distribution-related items. Specifically, that Section states:

> The plan may provide for or include ... Provisions regarding the utility's *distribution service*, including, without limitation and notwithstanding any provision of Title XLIX of the Revised Code to the contrary, provisions

[125] ESP II Order at 49.

> regarding single issue ratemaking, a revenue decoupling mechanism or any other incentive ratemaking, and provisions regarding *distribution infrastructure and modernization incentives* for the electric distribution utility. The latter may include a long-term energy delivery infrastructure modernization plan for that utility or any plan providing for the utility's recovery of costs, including lost revenue, shared savings, and avoided costs, and a just and reasonable rate of return on such infrastructure modernization. As part of its determination as to whether to allow in an electric distribution utility's electric security plan inclusion of any provision described in division (B)(2)(h) of this section, the commission shall examine *the reliability of the electric distribution utility's distribution system* and 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*. (Emphasis added.)

The scope of the above-quoted provision is not ambiguous; it does not provide a basis to authorize a generation-related rider. Moreover, the Commission has only relied upon the section to approve distribution-related items. For example, another portion of the ESP II Order states, "[a]s authorized by Section 4928.143(B)(2)(h), Revised Code, an ESP may include the recovery of capital cost for distribution infrastructure investment to improve reliability for customers."[126] Similarly, in *ESP I*, the Commission stated that "the Commission recognizes that Section 4928.143(B)(2)(h), Revised Code, authorizes the Companies to include in its ESP provisions regarding single-issue ratemaking for distribution infrastructure and modernization incentives."[127] The PTR, however, is put in place to recover lost generation-related revenue if AEP-Ohio makes the appropriate showing.[128] Because the PTR provides a home for a generation-related lost revenue charge, it cannot be lawfully approved under Section 4928.143(B)(2)(h), Revised Code.

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[126] *Id.* at 46.

[127] *ESP I Case*, Opinion and Order at 32 (Mar. 18, 2009).

[128] ESP II Order at 49.

D. The ESP II Order is unlawful and unreasonable because it concludes that the Capacity Deferral and the Capacity Shopping Tax can be authorized under Section 4928.144, Revised Code. These items do not arise from rates or prices authorized under Sections 4928.141 to 4928.143, Revised Code, and therefore the Commission's authority in Section 4928.144, Revised Code, is unavailable.

The Capacity Order invented and applied a cost-based ratemaking methodology to develop a price for capacity of $188.88/MW-day and authorized, under Sections 4905.04, 4905.05, and 4905.06, 4905.13 and Chapter 4909, Revised Code, AEP-Ohio to collect part of that price now (through RPM-Based Pricing) and part of that price through future rates.[129] The ESP II Order allows AEP-Ohio to collect part of the Capacity Order's $188.88/MW-day price through the RSR, and the remainder through the Capacity Shopping Tax authorized under Section 4928.144, Revised Code.[130]

Section 4928.144, Revised Code, however, grants the Commission authority to authorize a phase-in only of an EDU rate or price established in an ESP or MRO. Specifically, Section 4928.144, Revised Code, provides that the Commission:

> may authorize any just and reasonable phase-in of any electric distribution utility rate or price ***established under sections 4928.141 to 4928.143 of the Revised Code***, and inclusive of carrying charges, as the commission considers necessary to ensure rate or price stability for consumers. If the commission's order includes such a phase-in, the order also shall provide for the creation of regulatory assets pursuant to generally accepted accounting principles, by authorizing the deferral of incurred costs equal to the amount not collected, plus carrying charges on that amount. Further, the order shall authorize the collection of those deferrals through a nonbypassable surcharge on any such rate or price so established for the electric distribution utility by the commission. (Emphasis added.)

[129] Capacity Order at 23.

[130] ESP II Order at 52. Additionally, AEP-Ohio was authorized to collect part of the $188.88/MW-day price through RPM-Based Pricing charged to CRES providers.

As discussed above, the Commission authorized the $188.88/MW-day price for generation capacity service under its general supervisory jurisdiction contained in Sections 4905.04, 4905.05, and 4905.06, Revised Code, and, under Section 4905.13, Revised Code, authorized the accounting changes required to defer the difference between the RPM-Based Price charged to CRES providers and $188.88/MW-day. Because Section 4928.144, Revised Code, is not available when the rate or price is established under Sections 4905.04, 4905.05, and 4905.06, and 4905.13, Revised Code, the Commission is without authority to authorize a phase-in of the Capacity Shopping Tax and, therefore, the ESP II Order is unreasonable and unlawful.

Additionally, any use of phase-in authority under Section 4928.144, Revised Code, requires the Commission to identify, as part of the phase-in accounting, the "incurred costs" that are deferred for future collection. Neither AEP-Ohio nor the Commission has identified the "incurred cost" that the Commission must specify to lawfully proceed with the phase-in authority in Section 4928.144, Revised Code, even if such authority could be used. Absent the required identification of "incurred costs," there is no means proposed by AEP-Ohio or identified by the Commission to ensure that the deferral is necessary to compensate AEP-Ohio for "incurred costs." This point takes on added significance since the "cost" calculation, which is the foundation for the $188.88/MW-day state compensation mechanism, was based on a "formula rate" methodology that bears no relationship to AEP-Ohio's cost to meet its FRR obligation.[131] For these reasons, the ESP II Order is unlawful and unreasonable and rehearing should be granted.

[131] Capacity Order at 11 (AEP-Ohio's capacity cost calculation is based upon formulas).

4. The ESP II Order is unlawful and unreasonable because it authorizes AEP-Ohio to increase SSO prices so as to collect above-market generation-related revenue through the non-bypassable RSR, Capacity Shopping Tax, and the PTR, thereby providing AEP-Ohio with the ability to collect transition revenue or its equivalent at a time when Ohio law commands that AEP-Ohio's generation business be fully on its own in the competitive market. By allowing AEP-Ohio to collect transition revenue, the Commission unreasonably and unlawfully ignored the statutory bar against such collection. The ESP II Order is similarly unreasonable and unlawful because it permits AEP-Ohio to evade its Commission-approved settlement obligation to forego such collection and to not impose lost generation-related revenue charges on shopping customers.

AEP-Ohio has made it abundantly clear that it believes that it is entitled to a second bite at the "transition revenue" apple, through the RSR, Capacity Shopping Tax, and the PTR that hit shopping and non-shopping customers with the cost of satisfying AEP-Ohio's appetite. However, as demonstrated by IEU-Ohio through the testimony of its witnesses,[132] its initial and reply briefs,[133] and other pleadings before the Commission,[134] the Ohio Revised Code and the commitments AEP-Ohio made as part of a Commission-approved settlement in AEP-Ohio's ETP proceedings prohibit AEP-Ohio from collecting transition revenue.[135] In lieu of repeating all of the transition

[132] IEU-Ohio Ex. 124, *passim*; IEU-Ohio Ex. 125 at 3-4, 30-35.

[133] Initial Brief of IEU-Ohio at 22-36 (June 29, 2012); Reply Brief of IEU-Ohio at 21-23 (July 9, 2012).

[134] IEU-Ohio Reply Brief at 5-7 (Nov. 18, 2011); Application for Rehearing and Memorandum in Support of IEU-Ohio at 36-39 (Jan. 13, 2012); *Capacity Case*, IEU-Ohio Memorandum Contra Ohio Power Company's February 27, 2012 Motion for Relief and Request for Expedited Ruling at 15-16 (March 2, 2012); *Capacity Case*, IEU-Ohio Application for Rehearing of the March 7, 2012 Entry and Memorandum in Support at 18-20 (March 27, 2012); *Capacity Case*, IEU-Ohio Application for Rehearing of the May 30, 2012 Entry and Memorandum in Support at 12 (June 19, 2012); *Capacity Case*, IEU-Ohio Application for Rehearing of the July 2, 2012 Opinion and Order and Memorandum in Support at 34-36 (Aug. 1, 2012).

[135] Additionally, the Initial Brief of Buckeye Association of School Administrators, Ohio Association of School Business Officials, Ohio School Board Association, and Ohio School Council (June 29, 2012), The Kroger Company's Post Hearing Brief (June 26, 2012) and the Initial Brief By Duke Energy Commercial Asset Management, Inc. and Duke Retail Sales, LLC (June 29, 2012) support IEU-Ohio's arguments that AEP-Ohio is barred from collecting stranded costs. *See* ESP II Order at 28.

revenue/stranded costs discussion in IEU-Ohio's initial and reply briefs, IEU-Ohio hereby incorporates these arguments by reference and summarizes them below.[136]

Under Ohio law, AEP-Ohio had an opportunity to collect generation-related transition revenue while it prepared its competitive generation business for competition.[137] The "transition" period is over, and Ohio law now prohibits the collection of transition revenue.[138] AEP-Ohio does not dispute this.

> ***Under SB 3, all of these generation assets were subjected to market and EDUs therefore were given a temporary opportunity to recover stranded generation investments during a transition period. That transition period is over.*** EDUs can no longer recover stranded generation investments ... .[139]

Additionally, AEP-Ohio agreed to forgo collecting above-market transition revenue associated with its generation assets, promising it would not "impose any lost revenue charges (generation transition charges (GTC)) on any switching customer."[140] That commitment was reaffirmed and incorporated into AEP-Ohio's Rate Stabilization Plan ("RSP") which was effective into 2009.[141] Despite Ohio law and AEP-Ohio's previous commitments, it has sought and now obtained authority to collect additional transition

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[136] Initial Brief of IEU-Ohio at 22-36 (June 29, 2012); Reply Brief of IEU-Ohio at 21-23 (July 9, 2012).

[137] Sections 4928.37 to 4928.40, Revised Code.

[138] Section 4928.40, Revised Code.

[139] IEU-Ohio Ex. 124 at 14. The quote contained in the testimony of IEU-Ohio witness Hess was taken from a pleading AEP-Ohio filed with the Commission in March 2012. *Id.* (*quoting 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 at 7 (March 30, 2012) (emphasis added)).

[140] IEU-Ohio Ex. 124 at 13.

[141] *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of a Post-Market Development Period Rate Stabilization Plan*, Case No. 04-169-EL-UNC, Opinion and Order at 9 (Jan. 26, 2005) ("*RSP Proceeding*").

revenue in the *ESP II Case*, and the *Capacity Case*. The ESP II Order's approval of the RSR, Capacity Shopping Tax, and PTR delivers the apple to AEP-Ohio and provides a second "transition revenue" bite.

In particular, the above-market generation capacity service charges sought by AEP-Ohio and authorized in the ESP II Order through the RSR and Capacity Shopping Tax are based on the same assumptions as the transition revenue claim AEP-Ohio previously made and agreed to forgo in its ETP proceeding.[142] Both the revenue in the ETP proceeding and that collected as a result of the authorizations in the *Capacity Case* and the *ESP II Case* were based on AEP-Ohio's total net book value of its generation assets, and both included assumptions about the generation-related revenue that AEP-Ohio would be able to receive in the electric market (wholesale and retail).[143] As described by IEU-Ohio witness Hess:

> Regardless of the form or level of the capacity charge proposal, AEP-Ohio is persistently seeking another opportunity to collect transition revenue. The proposal which AEP-Ohio has put forward in this proceeding is designed to provide AEP-Ohio with generation-related revenue it says it will lose if customers shop and CRES suppliers pay a market-based capacity price.[144]

Although the ESP II Order rejects AEP-Ohio's two-tiered capacity proposal, the Order nonetheless approves collection of above-market generation-related revenue through the RSR, the Capacity Shopping Tax, and the PTR.[145] Thus, these new non-bypassable riders will allow AEP-Ohio to collect unlawful transition revenue, or its

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[142] IEU-Ohio Ex. 124 at 9-11.

[143] *Id.*

[144] *Id.* at 17.

[145] Capacity Order at 23, 33-35; ESP II Order at 36, 49-52.

equivalent, in violation of Ohio law and AEP-Ohio's Commission-approved ETP settlement.

The uncontested evidence shows that the RSR, the Capacity Shopping Tax, and the PTR are designed to replace generation-related revenue that AEP-Ohio claimed it could not recover in the market. As proposed, the RSR was designed to supplement AEP-Ohio's generation revenue stream to produce $826 million annually.[146] The differential used to calculate the RSR is based on the "lost" revenue associated with customer shopping.[147] As a means of providing AEP-Ohio with revenue it could not recover through its SSO rates and capacity charges to CRES providers, the RSR is nothing more than a prohibited transition revenue recovery mechanism.[148]

Likewise, the PTR, as AEP-Ohio witness Nelson explained, would recover "lost revenue" because "[t]he Capacity payments received by AEP Ohio cannot be mitigated by opportunity sales in the market alone" after the Pool Agreement is terminated.[149] To calculate the amount to be recovered through the PTR, AEP-Ohio would "compare the lost AEP Pool capacity revenue to increases in net revenue related to new wholesale transactions or decreases in generation asset costs that result from the AEP Pool termination."[150] AEP-Ohio proposes to then collect the "lost" revenue through the

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[146] *Id.* at 33.

[147] *See* ESP II Order at 34-35 (calculating the level of the RSR necessary to meet the $826 million revenue target as shopping increases and SSO revenues decrease).

[148] IEU-Ohio Ex. 124 at 23-25.

[149] AEP-Ohio Ex. 103 at 21.

[150] *Id.* at 22-23.

PTR.[151] Since the calculation is designed to ensure that AEP-Ohio can continue to recover generation-related revenue that is not recoverable in the market, the PTR is another mechanism to recover transition revenue.[152] Although the Commission required AEP-Ohio to satisfy certain conditions[153] prior to implementing the PTR to increase electric bills, those conditions do not change the fact that the PTR authorizes AEP-Ohio to recover transition revenue or its equivalent. Accordingly, the ESP II Order's conditions do not change the unlawful nature of the rider.

The Capacity Order and the ESP II Order have largely ignored the arguments of IEU-Ohio and other intervenors which demonstrate that AEP-Ohio's proposals are, in substance, simply another request for transition revenue. The Capacity Order entirely failed to address the issue, and the ESP II Order only contained the following two sentences addressing the argument:

> Further, we reject the claim that the RSR allows for the collection of inappropriate transition revenues or stranded costs that should have been collected prior to December 2010 pursuant to Senate Bill 3, as AEP-Ohio does not argue its ETP did not provide sufficient revenues, and, in light of events that occurred after the ETP proceedings, including AEP-Ohio's status as an FRR Entity, AEP-Ohio is able to recover its actual costs of capacity, pursuant to our decision in the Capacity Case. Therefore, anything over RPM auction capacity prices cannot be labeled as transition costs or stranded costs.[154]

The above-quoted statement, however, is factually incorrect and entirely illogical.

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[151] *Id.* at 22.

[152] IEU-Ohio Ex. 124 at 21-23.

[153] The ESP II Order states, "in the event AEP-Ohio seeks recovery under the PTR, AEP-Ohio must first demonstrate the extent to which the Pool Agreement benefitted Ohio ratepayers over the long-term and the extent to which the costs and/or revenues should be allocated to Ohio ratepayers. Further, AEP-Ohio must demonstrate to the Commission that any recovery it seeks under the PTR is based upon costs which were prudently incurred and are reasonable." ESP II Order at 49.

[154] *Id.* at 32.

First, AEP-Ohio has in fact claimed in the *ESP II Case* that its prior rates were insufficient;[155] however, this statement has absolutely nothing to do with whether the RSR allows AEP-Ohio to collect transition revenue. Second, AEP-Ohio is not an FRR Entity, AEPSC made an FRR Alternative election under the RAA for the combined pool of American Electric Power Co., Inc. ("AEP") operating companies in PJM, which includes AEP-Ohio.[156] Thus, the FRR Entity is AEPSC on behalf of all the AEP-East operating companies, and the footprint is the AEP-East region, not the AEP-Ohio service territory. AEP-Ohio does not dispute this fact.[157]

Additionally, whatever opportunities the RAA may provide an FRR Entity to charge above-market rates for generation capacity service again have absolutely nothing to do with whether the Commission may, ***under Ohio law***, approve a certain charge.[158] Ohio law provided each EDU with a time-limited opportunity to seek and obtain generation-related transition revenue associated with the transition to a competitive market. Before authorizing collection of any transition revenue, the Commission had to find that the costs were "prudently incurred," "legitimate, net, verifiable, and directly assignable or allocable to retail electric generation service provided to electric consumers in this state," "the costs are unrecoverable in a

[155] AEP-Ohio Ex. 101 at 7-9 (the Commission "acted to prevent utilities from collecting the higher market-based rates.").

[156] IEU-Ohio Ex. 125 at 23; AEP-Ohio. Ex. 103 at 9; *see also* Initial Brief of IEU-Ohio at 85 (June 29, 2012).

[157] "Through the PJM planning year 2014/2015 (PY14/15) AEP Ohio together with the other AEP East operating companies, APCo, I&M, KPCo, Kingsport Power Company and WPCo, have elected as a group (East System) to be under the FRR option in PJM. This requires the East System to provide its own capacity resources to meet its load obligations rather than rely on the PJM RPM market to provide capacity resources." AEP-Ohio. Ex. 103 at 9.

[158] *Tongren v. Pub. Util. Comm.*, 85 Ohio St.3d 87, 89 (1999).

competitive market" and the EDU "would otherwise be entitled an opportunity to recover the costs."[159] As described above, the RSR, Capacity Shopping Tax, and the PTR are designed to provide AEP-Ohio with generation-related revenue that it claims that it will not be able to collect in a competitive market. Those riders, therefore, are unlawful, regardless of what might be authorized under the RAA by a state regulatory agency with the proper jurisdictional authority.

As Mr. Hess's testimony demonstrates, the one-and-done opportunity to recover above-market generation revenue was through the ETP process.[160] The time for that recovery is long gone (and AEP-Ohio agrees).[161] Based on the unequivocal restriction on the Commission's authority, the ETP settlement, and the unrebutted testimony that the RSR, Capacity Shopping Tax, and the PTR collect above-market generation-related revenue, the ESP II Order unlawfully and unreasonably authorized these three provisions of the ESP.

The ESP II Order's authorization is also unreasonable and unlawful because it completely ignores AEP-Ohio's analysis that the cash flow available from the utilization of the generating fleet will be (assuming AEP-Ohio collects RPM-Based Pricing[162]), over the longer term, some $22 billion in excess of the cash flow level required to support the currently recorded generation asset book values.[163]

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[159] Section 4928.39, Revised Code.

[160] IEU-Ohio Ex. 124, *passim.*

[161] *Id.* at 14.

[162] IEU-Ohio Ex. 117.

[163] OCC and IEU-Ohio both introduced an internal analysis conducted by AEP that demonstrates that "the estimated generation cash flows are sufficient to recover the companies' generating assets." OCC Ex. 104 at 4; IEU-Ohio Ex. 124 at Exhibit KMM-23; *see also* IEU-Ohio Ex. 117. In fact, the document shows that even with an estimated $100 million per year in additional environmental expenditures from 2012-

5. The ESP II Order is unlawful and unreasonable because it assumes that the Commission may invent and apply a cost-based ratemaking methodology for purposes of authorizing a significant increase in the price for generation capacity service. It is similarly unlawful and unreasonable because it authorizes AEP-Ohio to defer the uncollected portion of this significant increase in the price for generation capacity service and then, after the term of the ESP, collect such portion plus interest charges through non-bypassable charges applicable to shopping and non-shopping customers.

Although the price AEP-Ohio is allowed to charge for generation capacity service is squarely in front of the Commission in the *Capacity Case* through IEU-Ohio's Application for Rehearing, as well as the Applications for Rehearing filed by several other parties, the ESP II Order has also injected the same contested issues into the *ESP II Case.*[164] As previously noted, the Capacity Order referred to the *ESP II Case* the determination of how the difference between the RPM-Based Price billed and collected from CRES providers for shopping load and $188.88/MW-day would be collected, and did so after the record in the *ESP II Case* closed.[165] The ESP II Order authorizes the RSR under Section 4928.143(B)(2)(d), Revised Code, and the Capacity Shopping Tax under Section 4928.144, Revised Code, to recover the difference between the $188.88/MW-day price and the RPM-Based Price.

In addition to the fact that the statutory timeframe for approving transition revenue has long since passed, the Commission is otherwise without authority to invent and apply a cost-based ratemaking methodology for purposes of substantially

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2014, AEP's generating function would generate positive cash flows more than $22 billion in excess of the asset book value. OCC Ex. 104 at 4. The AEP-Ohio specific cash flows are identified in a confidential exhibit. IEU-Ohio Ex. 121. IEU-Ohio also addressed the confidential AEP-Ohio specific cash flows in the confidential portion of its Initial Brief filed in this proceeding. Initial Brief of IEU-Ohio at 55 (June 29, 2012).

[164] ESP II Order at 36, 51-52.

[165] Capacity Order at 23.

increasing AEP-Ohio's compensation for generation capacity service. The Commission may only exercise that jurisdiction conferred upon it by the Ohio Revised Code.[166]

With the enactment of Amended Substitute Senate Bill 3 ("SB 3"), generation-related retail electric service became, and remains today, a competitive retail electric service.[167] The Ohio Supreme Court has held on several occasions that the generation component of retail electric service is not subject to the Commission's regulation:

> [i]t is well settled that the generation component of electric service is not subject to commission regulation. In *Constellation NewEnergy, Inc.*, 104 Ohio St.3d 530, 2004-Ohio-6767, 820 N.E.2d 885, ¶ 2, we stated that S.B. 3 'provided for restructuring Ohio's electric-utility industry to achieve retail competition with respect to the generation component of electric service.' R.C. 4928.03 specifies that retail electric-generation service is competitive and therefore not subject to commission regulation, and R.C. 4928.05 expressly removes competitive retail electric services from commission regulation.[168]

The definitions in Section 4928.01, Revised Code,[169] in combination with the declarations and limitations in Sections 4928.03 and 4928.05, Revised Code, likewise,

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[166] *Time Warner AxS v. Pub. Util. Comm.*, 75 Ohio St.3d 229, 234, 661 N.E. 2d 1097 (1996).

[167] "Beginning on the starting date of competitive retail electric service [January 1, 2001], *retail electric generation*, aggregation, power marketing, and power brokerage services supplied to consumers within the certified territory of an electric utility *are competitive retail electric services* that the consumers may obtain subject to this chapter from any supplier or suppliers." Section 4928.03, Revised Code (emphasis added).

[168] *Indus. Energy Users-Ohio v. Pub. Util. Comm.*, 117 Ohio St.3d 486, 2008-Ohio-990 at ¶20. The Court's use of "regulation" was in reference to the Commission's ability to use its traditional "cost-based" ratemaking authority. *Id.* at ¶19. That Court was effectively holding that in the context of competitive retail electric services, the Commission could only approve rates based on market prices, just as AEP-Ohio has claimed. IEU-Ohio Ex. 119 at 18.

[169] "'Retail electric service' means any service involved in supplying or arranging for the supply of electricity to ultimate consumers in this state, from the point of generation to the point of consumption. For the purposes of this chapter, retail electric service includes one or more of the following "service components": generation service, aggregation service, power marketing service, power brokerage service, transmission service, distribution service, ancillary service, metering service, and billing and collection service." Section 4928.01(A)(27), Revised Code.

"'Competitive retail electric service' means a component of retail electric service that is competitive as provided under division (B) of this section." Section 4928.01(A)(4), Revised Code.

make clear that the Commission may not lawfully supervise or regulate any service involved in supplying or arranging for the supply of electricity to ultimate consumers in Ohio, from the point of generation to the point of consumption, once that service is declared competitive, except under very narrowly defined circumstances. From these definitions and limitations, this conclusion holds irrespective of the force of federal preemption regarding sales for resale transactions[170] and regardless of whether the service is called wholesale or retail.

The definition of "retail electric service" includes *any service, i.e.*, generation, transmission, and distribution service, from the point of generation to the point of consumption.[171] Since January 1, 2001, the effective date of competitive retail electric service, generation service has been deemed competitive. Section 4928.03, Revised Code, provides:

> Beginning on the starting date of competitive retail electric service, retail electric generation, aggregation, power marketing, and power brokerage services supplied to consumers within the certified territory of an electric utility are competitive retail electric services[172] that the consumers may obtain subject to this chapter from any supplier or suppliers.

Because the General Assembly declared retail electric generation service competitive many years ago, that service (which by definition includes any generation

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[170] Of course, the Commission can exercise no authority except that authority that has been delegated to it by the General Assembly. To have any jurisdiction over wholesale services, the Commission would thus have to find some specific grant of authority by the General Assembly and this fundamental principle is true irrespective of the powers conveyed to the federal government. But the General Assembly could not lawfully delegate authority to the Commission to regulate or supervise wholesale electric transactions because the authority to regulate commerce among the states is reserved to the federal government. U.S. Const., Art. I, § 8, cl. 3.

[171] Section 4928.01(A)(27), Revised Code.

[172] The definition of "retail electric service" (in combination with the balance of Chapter 4928) also makes it clear that a service component or function is either competitive or non-competitive. Because non-competitive service components are defined to be everything except competitive service components or functions, a service component must either be competitive or non-competitive.

service from the point of generation to the point of consumption) is not subject to the Commission's supervision or regulation except as may be specifically permitted by Sections 4928.141 to 4928.144, Revised Code (which relate exclusively to the establishment of an SSO for *retail* electric customers), and Section 4905.06, Revised Code, as it provides for safety and reliability.[173] Additionally, Section 4928.05(A), Revised Code, precludes the Commission from regulating such a competitive service under Chapter 4909, Revised Code. Thus, the Commission is barred from using its supervisory powers or the regulatory authority in Chapters 4905, 4909, and 4928, Revised Code, except as specifically noted, to address pricing for any generation service from the point of generation to the point of consumption.

With respect to establishing rates for competitive retail electric services, the Commission's authority is limited to an EDU's SSO.[174] The Supreme Court has also held that concerns about the future do not empower the Commission to create remedies beyond those permitted by the law.[175] As the Commission held in its decision denying recovery of closure costs for the Sporn 5 generating facility:

> Pursuant to Sections 4928.03 and 4928.05(A)(1), Revised Code, retail electric generation service is a competitive retail electric service and, therefore, not subject to Commission regulation, except as otherwise provided in Chapter 4928, Revised Code. Just as the construction and maintenance of an electric generating facility are fundamental to the

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[173] Section 4928.05(A), Revised Code.

[174] "On and after the starting date of competitive retail electric service, *a competitive retail electric service supplied by an electric utility or electric services company shall not be subject to supervision and regulation ... by the public utilities commission under Chapters 4901. to 4909.*, 4933., 4935., and 4963. of the Revised Code, except sections 4905.10 and 4905.31, division (B) of section 4905.33, and sections 4905.35 and 4933.81 to 4933.90; except sections 4905.06, 4935.03, 4963.40, and 4963.41 of the Revised Code only to the extent related to service reliability and public safety; and except as otherwise provided in this chapter." Section 4928.05(A)(1), Revised Code (emphasis added).

[175] *Indus. Energy Users-Ohio v. Pub. Util. Comm.*, 117 Ohio St.3d 486, 2008-Ohio-990 at ¶ 23.

> generation component of electric service, we find that so too is the closure of an electric generating facility. Additionally, although there are exceptions in Section 4928.05(A)(1), Revised Code, that permit Commission regulation of competitive services in some circumstances, the enumerated statutory exceptions do not include Sections 4905.20 and 4905.21, Revised Code, which otherwise govern applications to abandon or close certain facilities.
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> OP also requests approval of a rider to collect the costs associated with the closure of Sporn Unit 5. As discussed above, Section 4928.05(A)(1), Revised Code, generally prohibits Commission regulation of retail electric generation service. However, that section expressly provides that it does not limit the Commission's authority under Sections 4928.141 to 4928.144, Revised Code.[176]

Despite the Commission's acknowledgement that it can only regulate retail electric service rates as part of an SSO, the Commission authorized AEP-Ohio to collect an above-market price for capacity under its general supervisory powers, and under Section 4905.13, Revised Code, authorized AEP-Ohio to defer for future collection the difference between RPM-Based Pricing and $188.88/MW-day in the Capacity Order.[177] It then compounded the Capacity Order's errors by unlawfully authorizing, in the ESP II Order, AEP-Ohio to recover this difference through the RSR and the Capacity Shopping Tax. Because the riders unlawfully authorized and guarantee above-market compensation for competitive generation-related service, they are unlawful and unreasonable.

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[176] *In the Matter of the Application of Ohio Power Company for Approval of the Shutdown of Unit 5 of the Philip Sporn Generating Station and to Establish a Plant Shutdown Rider,* Case No. 10-1454-EL-RDR, Finding and Order at 16-17 (Jan. 11, 2012) ("*Sporn Decision*").

[177] Capacity Order at 12-13, 23

6. The ESP II Order is unlawful and unreasonable because it functions to permit AEP-Ohio, an electric distribution utility ("EDU"), to evade statutory corporate separation requirements that call for strict separation between competitive and non-competitive lines of business and services and because it approves an SSO which insulates AEP-Ohio's competitive generation business from the discipline of the electricity market. The RSR, Capacity Shopping Tax, and PTR all function to allow AEP-Ohio, the EDU, to evade such corporate separation requirements, collect above-market generation-related revenue and insulate AEP-Ohio's competitive generation business from the discipline of the electricity market. Following AEP-Ohio's proposed and untimely transfer of its generating assets to an affiliate, AEP Generation Resources Company ("Genco"), these three riders will further violate such corporate separation requirements by allowing AEP-Ohio to collect, on a non-bypassable basis, above-market generation-related revenue and remit such revenue to Genco thereby insulating Genco's competitive generation business from the discipline of the electricity market.

Chapter 4928, Revised Code, and the rules the Commission has adopted to implement the corporate separation requirements are designed to assure that retail customers as well as CRES providers are not subjected to the EDU's discretion in ways that would allow the EDU to favor its or its affiliate's assets or competitive lines of business.[178] The ESP II Order violates the corporate separation requirements, which call for a strict separation between competitive and non-competitive services. The ESP II Order also violates the corporate separation requirements because it authorizes an SSO that functions to insulate AEP-Ohio's competitive generation business from the discipline of the electricity market. As Mr. Hess explains:

> Instead of being competitively neutral, AEP-Ohio, the EDU, is selectively advancing proposals to provide its generation business segment with financial and other benefits or preferences not available to any other supplier of generation service. Throughout this proceeding and in other cases, AEP-Ohio has often portrayed itself as competing with CRES suppliers even though AEP-Ohio, the EDU, can only provide generation

[178] *See, e.g.*, Section 4928.17, Revised Code; Rule 4901:1-16, OAC; Rule 4901:1-37, OAC; IEU-Ohio Ex. 124 at 26.

> supply when a customer is not served by a CRES supplier. AEP-Ohio has also asserted that the generation supply benefits of Ohio's customer choice must be delayed to allow AEP-Ohio to adjust its latest business model. The claim that AEP-Ohio needs additional time is irreconcilably inconsistent with the somewhat unique wires-transfer corporate separation plan approved by the Commission for AEP-Ohio. It is also my understanding that any competitive service provided by AEP-Ohio, the EDU, must be provided through a separate entity that is not benefitted by anything that AEP-Ohio, the EDU, does with regard to the provision of non-competitive services.
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> When AEP-Ohio's capacity charge, Pool Termination Provision and RSR proposals are considered in light of the role and purpose of the corporate separation requirements, I believe it is clear that the Modified ESP is essentially an attempt to bypass the corporate separation requirements for the benefit of AEP-Ohio's generation business segment and to the disadvantage of retail customers and CRES suppliers. Thus, the blueprint used by AEP-Ohio to assemble its Modified ESP ignores the building code established by the General Assembly and the Commission's rules.[179]

As a result of the ESP II Order, AEP-Ohio's corporate separation violations through the RSR, Capacity Shopping Tax, and the PTR will occur in two stages.

Before AEP-Ohio satisfies the full structural corporate separation requirement that has been part of Ohio law for more than a decade, AEP-Ohio will be providing its generation business preferential treatment[180] through the rates charged by the EDU function in its capacity as a default supplier of generation service. While AEP-Ohio continues to operate under functional corporate separation in accordance with Section 4928.17(C), Revised Code, its separation plan must provide "for ongoing compliance with the policy specified in section 4928.02 of the Revised Code." Section 4928.02(H), Revised Code, states that it is the policy of the State to ensure effective competition in the provision of retail electric service "by prohibiting the recovery of any generation-

[179] IEU-Ohio Ex. 124 at 30-31.

[180] Section 4928.17(A)(3), Revised Code, prohibits the extension of any undue preference to an affiliate, division, or part of its business.

related costs through distribution or transmission rates." The Commission has correctly concluded that a non-bypassable charge to recover generation-related costs would result in a subsidy of generation services through a rider that is collected from all distribution customers.[181] Despite this prohibition, the non-bypassable RSR, Capacity Shopping Tax, and PTR will allow AEP-Ohio to recover generation-related costs from all of its distribution customers at a point in time when AEP-Ohio's generation business is required to be a stand-alone, separate business, fully on its own in the competitive market.

After the transfer of generating assets and a delayed, eventual compliance with Ohio's corporate separation requirements, the ESP II Order allows AEP-Ohio to violate corporate separation requirements by permitting it to "pass through" the above-market SSO revenue collected through the RSR, Capacity Shopping Tax, and PTR to Genco, its competitive affiliate.[182] The transfer of above-market generation revenue to Genco provides Genco an undue preference in violation of Section 4928.17(A)(3), Revised Code, and provides Genco an unfair competitive advantage in violation of Section 4928.17(A)(2), Revised Code. Under this arrangement, AEP-Ohio, the EDU, will pass all generation-related revenue, including the RSR, Capacity Shopping Tax, and PTR revenue to Genco.[183] Because the competitive affiliate will receive the revenue AEP-Ohio has identified is necessary to make up for the "lost" generation-related revenue associated with shopping, these three generation-related non-bypassable riders

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[181] *Sporn Decision* at 19.

[182] AEP-Ohio. Ex. 104 at 6-8.

[183] *Id.* at 8.

improperly subsidize Genco's competitive generation function, effectively evade the corporate separation requirements and are unlawful and unreasonable.

7. The ESP II Order is unlawful and unreasonable because it fails to promote the State policy contained in Section 4928.02, Revised Code. As the Commission found in the Capacity Order,[184] market-based pricing promotes the policies contained in Section 4928.02, Revised Code, by incenting shopping, promoting true competition, and by placing EDUs and CRES providers on a level playing field. Despite finding that market-based pricing promotes State policy, the ESP II Order authorizes AEP-Ohio to collect above-market pricing for generation-related services through the RSR, PTR, Capacity Shopping Tax, and the GRR.

Section 4928.02, Revised Code, declares the State policies the Commission is obligated to effectuate pursuant to Section 4928.06, Revised Code. These policies generally support customer choice, reliance on market-based approaches to set prices for competitive services such as generation service, and strongly favor competition to discipline prices of competitive services. And the Commission has confirmed that "standard service offers must be consistent with state policy under Section 4928.02, Revised Code."[185]

> 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."
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[184] Hereinafter "Capacity Order" shall refer to the July 2, 2012 Opinion and Order in *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 and "Capacity Case" shall refer to the docket above (Case No. 10-2929-EL-UNC).

[185] *In the Matter of the Application of the Cincinnati Gas & Electric Company to Modify its Nonresidential Generation Rates to Provide for Market-Based Standard Service Offer Pricing and to Establish an Alternative Competitive-Bid Service Ration Option Subsequent to the Market Development Period*, Case Nos. 03-93-EL-ATA, *et al.*, Order on Remand at 37 (Oct. 24, 2007) (*citing Elyria Foundry Co. v. Pub. Util. Comm.*, 114 Ohio St.3d 305 (2007)).

> Moreover, we disagree with FirstEnergy's claim that Section 4928.02, Revised Code, does not impose any obligations or duties upon the Companies. The Ohio Supreme Court recently held that the Commission may not approve a rate plan which violates the policy provisions of Section 4928.02, Revised Code. *See Elyria Foundry v. Pub. Util. Comm.* (2007), 114 Ohio St. 3d 305. Accordingly, an electric utility should be deemed to have met the statutory requirements of Section 4928.142(A), Revised Code, only to the extent that the electric utility's proposed MRO is consistent with the policies set forth in Section 4928.02, Revised Code.[186]

As the Commission correctly determined, an SSO may only be approved if it complies with State policy; however the as-approved Modified ESP does not promote State policy.

In the Capacity Order, issued July 2, 2012, the Commission found that market-based pricing supports State policy. "RPM-based capacity pricing will stimulate true competition among suppliers in AEP-Ohio's service territory" and will "incent shopping."[187] The Commission also found that RPM-Based Pricing has "been used successfully throughout Ohio and the rest of the PJM region and puts electric utilities and CRES providers on a level playing field."[188] The Capacity Order did not find that an above-market capacity charge could comply with Section 4928.02, Revised Code, and the Commission's reasoning in that Order implicitly rejects the notion that above-market capacity pricing is compatible with Section 4928.02, Revised Code.[189]

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[186] *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Approval of a Market Rate Offer 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 at 13-14 (Nov. 25, 2008); *see also Elyria Foundry v. Public Util. Comm.*, 114 Ohio St. 3d.305 (2007).

[187] Capacity Order at 23.

[188] *Id.*

[189] As noted in IEU-Ohio's Application for Rehearing in the *Capacity Case*, the Commission did not comply with the State law or act within its jurisdictional scope of authority when it invented and applied a

Despite the State's policies and the Capacity Order's reaffirmation that market-based pricing complies with State policy, the ESP II Order authorizes AEP-Ohio to increase electric bills so that it can collect hundreds of millions of dollars in above-market, generation-related compensation through the RSR, PTR, Capacity Shopping Tax, and the GRR.[190] This outcome violates Ohio policy, the Commission's duty to effectuate that policy and conflicts with the Commission's findings in the Capacity Order. Therefore, the ESP II Order is unlawful and unreasonable.

8. **The ESP II Order is unlawful and unreasonable because it fails to recognize that the rates and charges applicable to non-shopping customers also are providing AEP-Ohio with compensation for generation capacity service, it ignores or disregards the fact that AEP-Ohio has maintained that non-shopping customers are, on average, paying nearly twice the $188.88/MW-day price, and it fails to establish a mechanism to credit such excess compensation obtained from non-shopping customers against any deferred balance the ESP II Order in combination with the Capacity Order work to create by comparing RPM-Based Pricing to the $188.88/MW-day price. The non-symmetrical and arbitrary bias embedded in these Orders' description of how the Capacity Deferral shall be computed guarantees that AEP-Ohio shall collect, in the aggregate, total revenue for generation capacity service substantially in excess of the revenue produced by using the $188.88/MW-day price to determine generating capacity service compensation for shopping and non-shopping customers.**

The ESP II Order is unlawful and unreasonable inasmuch as it fails to recognize that AEP-Ohio secures compensation for generation capacity service from non-

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cost-based ratemaking methodology to develop a $188.88/MW-day capacity price and referred a decision concerning the recovery of the difference between the price it permitted AEP-Ohio to bill and collect from CRES providers to the ESP II Order. In the ESP II Order, the Commission abandoned the State policy and authorized unlawful and shopping killing non-bypassable charges that will skew customer choice for years to come.

[190] *See* ESP II Order at 31-37, 70-77 (authorizing the RSR, which causes the ESP, based upon the Commission's own quantification, to be more expensive than the market-based MRO option by hundreds of millions of dollars); ESP II Order at 36, 52 (authorizing the Capacity Shopping Tax); ESP II Order at 49 (conditionally authorizing a yet-to-be-defined amount through the PTR). As Attachment A indicates, the Capacity Shopping Tax will collect an estimated $447 million.

shopping customers receiving default generation supply and from the generation capacity service pricing that applies in the case of shopping customers. In the case of non-shopping customers, AEP-Ohio claimed that it was receiving, on average and prior to the ESP II Order, generation capacity service compensation at a rate of $355/MW-day.[191] Thus, according to AEP-Ohio, its SSO customers are providing AEP-Ohio with significantly more compensation for generation capacity service than AEP-Ohio would be able to obtain if the Commission-specified $188.88/MW-day price governed compensation for generation capacity service from SSO customers. It is unreasonable and unlawful for the Commission to substantially increase AEP-Ohio's compensation for generation capacity service by authorizing a price of $188.88/MW-day in the case of shopping customers and then ignore the much higher level of generation capacity service compensation available to AEP-Ohio through its SSO for purposes of measuring the actual total generation capacity service compensation difference caused by limiting the compensation collected from CRES providers to RPM-Based Pricing. The analytical bias in the ESP II Order works to totally ignore excessive generation capacity service compensation available to AEP-Ohio through the SSO.

To eliminate this non-comparable, unreasonable and unlawful discrimination between generation capacity service compensation in the case of SSO customers and shopping customers and to avoid overstating the amount of the Capacity Deferral payable by shopping and non-shopping customers, the Commission must grant rehearing. More specifically, the Commission must modify the ESP II Order to credit the amount of generation service capacity compensation available from SSO customers

[191] Tr. Vol. V at 1438.

above the $188.88/MW-day price against the amount of the Capacity Deferral eligible for recovery through non-bypassable riders.

9. The ESP II Order is unlawful and unreasonable inasmuch as the Commission failed to adopt the uncontested recommendation of IEU-Ohio witness Kevin Murray contained at page 49 of IEU-Ohio Exhibit 125, which, if adopted, would provide much needed transparency to the process AEP-Ohio used to derive the billing determinants for generation capacity service.

The ESP II Order unlawfully and unreasonably failed to ensure that AEP-Ohio's generation capacity service charge will be billed in accordance with a customer's Peak Load Contribution ("PLC") factor that is the controlling billing determinant under the RAA.[192] Through its testimony and briefs, IEU-Ohio demonstrated the lack of transparency that currently exists with regard to the PLC billing determinant.[193] The means by which AEP-Ohio is specifying each customer's PLC has never been identified by AEP-Ohio. Despite the fact that no party challenged IEU-Ohio's testimony or briefs on this issue, the Commission failed to require AEP-Ohio to immediately disclose how it assigns a PLC value to each customer.

Instead, the ESP II Order directs AEP-Ohio to set up a meeting with the Ohio EDI Working Group ("OWEG")[194] within 30 days after the issuance of the ESP II Order to "develop an electronic system to provide CRES providers access to pertinent customer data, including but not limited to, PLC and [network service peak load] values and

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[192] The issue is material to the ultimate outcome of this case because, without disclosure of the means by which the PLC is disaggregated from AEP East down to AEP-Ohio and then down to each AEP-Ohio customer, it is not possible to test AEP-Ohio's specification of PLCs, determine whether Ohio customers are disproportionately covering the AEP East FRR capacity obligation, or determine whether certain customers or customer classes within AEP-Ohio's territory are unfairly being assigned their PLCs.

[193] IEU-Ohio Ex. 125 at 49; Initial Brief of IEU-Ohio at 91-92 (June 29, 2012); Reply Brief of IEU-Ohio at 5, 54 (July 9, 2012).

[194] EDI is defined as electronic data interchange. ESP II Order at 41.

historical usage and interval data no later than May 31, 2014."[195] Unfortunately, the ESP II Order will allow AEP-Ohio's PLC allocation process to remain a mystery for another two years.

The Commission must grant rehearing and require AEP-Ohio to publicly disclose the means by which the PLC is disaggregated from AEP-East down to AEP-Ohio and then down to each AEP-Ohio customer. This action is required regardless of the pricing method used to identify capacity charges because any capacity charge must be applied to the proper billing determinant. It is also important to note that this PLC specification requirement is critically important to the determination of how much revenue AEP-Ohio may eventually be able to collect for generation capacity service through the Capacity Shopping Tax since RPM-Based Pricing applies to the PLC. Calculating the difference between RPM-Based Pricing and $188.88/MW-day requires a transparent and proper identification of PLCs.

10. The ESP II Order is unlawful and unreasonable because the GRR cannot be lawfully approved under Section 4928.143(B)(2)(c), Revised Code.

The ESP II Order authorizes a non-bypassable GRR, at an initial rate of zero, pointing to Section 4928.143(B)(2)(c), Revised Code.[196] As discussed below, the ESP II Order's approval of the GRR is neither lawful nor reasonable.

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[195] *Id.*

[196] *Id.* at 24.

A. The ESP II Order is unlawful and unreasonable because it authorizes AEP-Ohio to establish the GRR to recover the cost of compliance with Section 4928.64, Revised Code (renewable energy resource requirements), through a non-bypassable charge in violation of Ohio law. Section 4928.64(E), Revised Code, states that all costs incurred by an EDU to comply with such requirements shall be bypassable by any consumer that has exercised its choice of supplier under Section 4928.03, Revised Code. The ESP II Order is also unlawful and unreasonable because the Commission violated Section 4903.09, Revised Code, by failing to address this issue raised on brief by IEU-Ohio; the Ohio Supreme Court has held that the failure to address all material matters brought to the Commission's attention is a reversible error.

The ESP II Order is unlawful and unreasonable in several respects. Although Section 4928.143(B)(2)(c), Revised Code, authorizes the Commission to approve a non-bypassable charge for a generating facility if certain requirements are satisfied, the Section cannot authorize a non-bypassable rider to recover the cost of compliance with renewable energy requirements. Specifically, Section 4928.143(B), Revised Code, states that the Commission cannot approve a provision of an ESP that is "contrary" to Section 4928.64(E), Revised Code.[197] Section 4928.64(E), Revised Code, states that "*[a]ll costs* incurred by an electric distribution utility in complying with the requirements of this section [renewable energy requirements] shall be bypassable by any consumer that has exercised choice of supplier under section 4928.03 of the Revised Code." (Emphasis added.) According to AEP-Ohio, the only project cost scheduled for collection through the GRR is related to Turning Point, a proposed 49.9 MW solar generating facility; the only purpose of the Turning Point project is to comply with renewable energy requirements.[198] Solar generating resources are defined as

[197] Section 4928.143(B), Revised Code.

[198] Tr. Vol. II at 704; Tr. Vol. VII at 2124.

renewable resources.[199] Accordingly, the GRR violates the statutory prohibition against recovering the cost of compliance with renewable energy requirements through a non-bypassable charge. Because the non-bypassable feature of the GRR is unlawful, the Commission must grant rehearing and reject the GRR or make it bypassable.

The ESP II Order is also unlawful and unreasonable because it fails to address this issue which was raised by IEU-Ohio during the evidentiary hearings preceding the ESP II Order and during the briefing process. It is reversible error if the Commission "initially failed to explain a material matter," that matter was again brought "to the commission's attention through an application for rehearing ... [and] the commission still failed to explain itself" on rehearing.[200] Because the Commission failed to address a contested and material matter with a reasoned explanation as required by Section 4903.09, Revised Code, the ESP II Order is unlawful and unreasonable.[201]

B. The ESP II Order is unlawful and unreasonable because the Commission failed to make the findings required by Section 4928.143(B)(2)(c), Revised Code, to support its authorization of the GRR.

Even if the Commission could approve a non-bypassable rider to recover the cost of compliance with renewable energy requirements, the ESP II Order is unlawful and unreasonable because it approves the GRR prior to and without satisfying the requirements contained in Section 4928.143(B)(2)(c), Revised Code. The ESP II Order states that it is not making any decision regarding the appropriateness of the costs of Turning Point, but nonetheless approves the GRR on the unrelated notion that the

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[199] Section 4928.01(A)(35), Revised Code.

[200] *In re Columbus Southern Power Company*, 128 Ohio St.3d at 526-27.

[201] *Id.*

Commission is "vested with the broad discretion to manage its dockets to avoid undue delay and duplication of effort."[202]

The ESP II Order's holding that it can approve the GRR now and position AEP-Ohio to satisfy the statutory conditions that must be met before the Commission can approve a non-bypassable cost-recovery mechanism in an ESP proceeding is unreasonable and unlawful. It also works to promote the very duplication of effort that the ESP II Order says the Commission may avoid by managing its dockets.

Section 4928.143(B)(2)(c), Revised Code, requires the EDU seeking the non-bypassable rider to demonstrate that the proposed generating facility is newly used and useful after January 1, 2009, and is sourced through a CBP subject to rules adopted by the Commission. No such non-bypassable surcharge mechanism shall be authorized by the Commission until there is first a determination in the ESP "... proceeding that there is a need for the facility based on resource planning projections submitted by the electric distribution utility." Section 4928.143(B)(2)(c), Revised Code, makes it clear that the need for the facility must be demonstrated in the ESP before the Commission has the authority to allow a non-bypassable cost recovery mechanism for a new generation facility to become part of an ESP. The reason for these requirements is obvious; equipping an EDU with the ability to recover the cost of a new generating facility through a non-bypassable charge works against the pro-competitive goals of Ohio law.

If the requirements of Section 4928.143(B)(2)(c), Revised Code, are met, the Commission is not required to—but may—approve a surcharge under that Section, in

[202] ESP II Order at 24.

which case the rider "shall cover all costs of the utility specified in the application, excluding costs recovered through a surcharge under division (B)(2)(b) of this section."

Whatever discretion the Commission may have to manage its dockets to avoid duplication, the plain meaning of Section 4928.143(B)(2)(c), Revised Code, precludes the Commission from approving a non-bypassable cost recovery mechanism under Section 4928.143(B)(2)(c), Revised Code, and then pushing the satisfaction of conditions precedent for the authorization of such a mechanism into other "dockets." Ohio law does not allow the Commission to evade the clear constraints on its authority expressed in Section 4928.143(B)(2)(c), Revised Code by kicking the required determinations into other dockets or through a piecemeal review process conducted outside the ESP in which the mechanism is proposed and approved.

The ESP II Order's reliance on *Duff v. Public Utilities Commission*[203] and *Toledo Coalition for Safe Energy v. Public Utilities Commission*[204] for the proposition that the Commission may ignore the statutory requirements in this proceeding is without merit.[205] In *Duff* and *Toledo*, the Court determined that Section 4901.13, Revised Code, provides the Commission with discretion to conduct its hearings. Section 4901.13, Revised Code, provides that "[t]he public utilities commission may adopt and publish rules to govern its proceedings and to regulate the mode and manner of all valuations, tests, audits, inspections, investigations, and hearings relating to parties before it." While the Commission may set its own rules with respect to the governance of its

[203] 56 Ohio St.2d 367, 379 (1978).

[204] 69 Ohio St.2d. 559, 560 (1982).

[205] ESP II Order at 24.

hearings, those rules cannot conflict with more specific statutory requirements that dictate how and when the Commission may exercise authority to increase electric bills or approve non-bypassable cost recovery mechanisms that create a launching pad for such increases.[206] Because Section 4928.143(B)(2)(c), Revised Code, requires that the identification of the facility, its sourcing through a CBP, the surcharge, and need must be presented and addressed in the ESP proceeding; the Commission does not have the discretion to permit AEP-Ohio to submit this information and satisfy these statutory requirements in separate proceedings.[207]

While the plain meaning of the statute is controlling, the requirement for full review of a request for a non-bypassable generation-related rider in an ESP is also consistent with the process the Commission must undertake when it reviews an ESP application. Under Section 4928.143(C)(1), Revised Code, the Commission must determine if the ESP is more favorable than an MRO. A non-bypassable placeholder cost recovery mechanism with unspecified costs prevents the Commission from making that determination in a manner that complies with the ESP versus MRO test because

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[206] *See Youngstown Sheet & Tube Co. v. Lindley*, 38 Ohio St.3d 232, 234 (1988).

[207] Section 4928.143(B)(2)(c), Revised Code. Section 4928.143(C)(1), Revised Code, states that an application containing a non-bypassable surcharge mechanism pursuant to Section 4928.143(B)(2)(b) or (c), Revised Code, must be denied unless the Commission first ensures "... that the benefits derived for any purpose for which the surcharge is established are reserved and made available to those that bear the surcharge." Since costs related to an EDU's compliance with Ohio's renewable energy portfolio requirements must be bypassable for customers who exercise their choice rights, there can be no benefit of the Turning Point facility for these customers. In the circumstances presented by the *ESP II Case*, the approval of a non-bypassable cost recovery mechanism as a host for costs related to Turning Point is also unlawful by the terms of Section 4928.143(C)(1), Revised Code. It is also important to note that Section 4928.20(K), Revised Code, obligates the Commission to encourage and promote large-scale governmental aggregation programs and, within the context of an ESP proceeding, to "... consider the effect on large-scale governmental aggregation of any nonbypassable generation charges, however collected, that would be established under that plan ..." Here again, the requirement that these required determinations be made in the ESP proceeding and not in some unidentified other "dockets" has been clearly written into Ohio law by the General Assembly. As with the other requirements that must be met before the Commission may authorize a non-bypassable cost recovery mechanism for generation-related costs, the ESP II Order unreasonably and unlawfully omits compliance with Ohio law.

the Commission will have no basis to determine whether the ESP as presented will satisfy the test during the term of the ESP.

11. The ESP II Order is unlawful and unreasonable because it authorized the Phase-In Recovery Rider ("PIRR") without allowing IEU-Ohio an opportunity to present testimony or to introduce exhibits regarding the effect of accumulated deferred income taxes ("ADIT") on the carrying charges in the PIRR trespassing on IEU-Ohio's due process rights.[208] Generally accepted accounting principles, regulatory principles, Court precedent, and Commission precedent all support an offset to account for ADIT.

The ESP II Order addresses only two issues with respect to the PIRR: (1) AEP-Ohio's request to delay implementation of the PIRR until 2013; and (2) AEP-Ohio's request to combine and average the PIRR rates[209] and collect the averaged PIRR from both CSP and OP customers. The Commission denied both requests.

Authorization of the PIRR, however, presented an additional issue that should have been addressed in either the *ESP II Case* or through an evidentiary hearing in the *PIRR Case*.[210] Specifically, IEU-Ohio sought Commission determinations addressing the calculation of carrying charges on the deferred balance adjusted to account for ADIT.[211] Through a combination of procedural errors, the Commission did not address this issue and trespassed on IEU-Ohio's due process rights as a result.

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[208] *Vectren Energy Delivery of Ohio, Inc. v. Pub Util. Comm.*, 113 Ohio St.3d 180, 192 (2007).

[209] There remains a deferred balance of approximately $7 million on the books of CSP. *In the Matter of the Application of Columbus Southern Power Company 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.*, Compliance Tariffs (Aug. 8, 2012) ("*PIRR Case*").

[210] IEU-Ohio has filed an Application for Rehearing in the *PIRR Case* raising issues regarding the treatment of the adjustment for ADIT.

[211] IEU-Ohio Ex. 129.

A. The ESP II Order is unlawful and unreasonable because IEU-Ohio was denied the opportunity to present evidence regarding the effect of ADIT on the calculation of carrying charges in the PIRR in violation of due process.

The Attorney Examiner, in the *ESP II Case*, determined that the Commission would only address the PIRR in the *ESP II Case* as it pertained to the two issues AEP-Ohio raised in the Modified ESP Application: delaying the implementation of the rider and spreading the costs of the rider to both CSP and OP customers.[212] The Attorney Examiner held that the remaining issues, which included ADIT, would be addressed in a separate docket,[213] the *PIRR Case*, and struck IEU-Ohio's testimony filed in the ESP II proceedings on that subject.[214] In the *PIRR Case*, however, the Commission approved AEP-Ohio's application without a hearing and without the development of an evidentiary record regarding the contested issues highlighted by the comments submitted in the separate *PIRR Case*.

The Commission's actions violate IEU-Ohio's due process rights. Due process in a Commission proceeding requires that a party is: (1) given "ample notice;" (2) "permitted to present evidence through the calling of its own witnesses;" (3) permitted to "cross-examin[e] the other parties' witnesses;" (4) permitted to "introduce exhibits;" (5) permitted to "argue its position through the filing of post hearing briefs;" and, (6) permitted to "challenge the PUCO's findings through an application for rehearing."[215] Failure to develop an appropriate record as a basis for the Commission's decision is

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[212] Tr. Vol. IX at 2738-39.

[213] *Id.*

[214] Tr. Vol. XIII at 3635-36 (Striking portions of IEU-Ohio Ex. 129).

[215] *Vectren Energy Delivery of Ohio, Inc. v. Pub Util. Comm.*, 113 Ohio St.3d 180, 192 (2007).

ground for reversal.[216] Likewise, the United States Supreme Court has held that parties have the right to a fair hearing,[217] and that "[t]he right to such a hearing is one of 'the rudiments of fair play.'"[218]

By granting the motion to strike IEU-Ohio's PIRR-related testimony in the *ESP II Case* and approving the PIRR in the *PIRR Case* without testimony or a hearing, the Commission has denied IEU-Ohio a meaningful opportunity to demonstrate that carrying charges should be calculated on a deferred balance adjusted for ADIT. As a result, the Commission has violated IEU-Ohio's due process rights and the statutory requirements governing the Commission's hearings. To remedy this violation, the Commission should either grant rehearing in the *ESP II Case* and allow the parties to address the proper ADIT adjustments to the balance eligible for amortization through the PIRR, or permit these issues to be addressed through an evidentiary hearing in the *PIRR Case* in which IEU-Ohio has also submitted an application for rehearing.

B. The ESP II Order is unlawful and unreasonable because it fails to direct AEP-Ohio to calculate the PIRR's carrying charges on deferred balances adjusted for ADIT in accordance with generally accepted accounting principles, regulatory principles, Court precedent, and Commission precedent. The ESP II Order's failure to require an ADIT adjustment permits AEP-Ohio to accrue carrying charges on overstated balances; thereby, requiring customers to overcompensate AEP-Ohio.

Pursuant to Section 4928.144, Revised Code, the Commission must ensure that the PIRR is just and reasonable, and the amounts deferred for collection through the PIRR comply with generally accepted accounting principles. Moreover, in ensuring that

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[216] *Tongren v. Pub. Util. Comm.*, 85 Ohio St.3d 87, 92-93 (1999).

[217] *West Ohio Gas Co. v. Pub. Util. Comm.*, 294 U.S. 63, 70 (1935).

[218] *Ohio Bell Tel. Co. v. Pub. Util. Comm.*, 301 U.S. 292, 304-305 (1937).

the PIRR is just and reasonable, the Commission must follow the policy and statutory requirements set forth under Chapter 4928, Revised Code.[219] Because Section 4928.144, Revised Code, may convert bypassable charges into future non-bypassable charges, the Commission must exercise the utmost caution to ensure that the phase-in is just and reasonable. The Commission's jurisdiction and supervision over the phase-in is ongoing.[220] On rehearing, the Commission must exercise its ongoing jurisdiction over the phase-in and direct AEP-Ohio to calculate carrying charges on deferred balances adjusted for ADIT to ensure that the PIRR complies with generally accepted accounting principles, State policy, and precedent, because the PIRR, as approved in the ESP II Order, is unlawful and unreasonable inasmuch as it requires customers to overcompensate AEP-Ohio.

The PIRR, as approved, fails to comply with generally accepted accounting principles because AEP-Ohio has been authorized to accrue carrying charges on deferred balances without an adjustment for ADIT. As Section 4928.144, Revised Code, states, the Commission may authorize the creation of regulatory assets, but such regulatory assets must comply with generally accepted accounting principles. CSP and OP record regulatory assets (deferred expenses) and regulatory liabilities (future revenue reductions or refunds) to reflect the economic effects of regulation by matching expenses with their recovery through regulated revenues and income with its passage

[219] Section 4928.02, Revised Code, states that it is the policy of this State to ensure the availability of reasonably priced electric service, and promote customer choice and competition. Section 4928.06(A), Revised Code, requires the Commission to ensure that the policy goals enumerated in Section 4928.02, Revised Code, are effectuated. Thus, the Commission must ensure that its actions and orders further the State policy goals enumerated in Section 4928.02, Revised Code.

[220] *PIRR Case*, Finding and Order at 17-18; *see also In re Application of Columbus S. Power Co.*, 129 Ohio St.3d 568, 569-70 (2011).

to customers through the reduction of regulated revenues. This treatment is required under generally accepted accounting principles, specifically under Financial Accounting Standards Board ("FASB") Accounting Standards Codification 980 (former FASB 71). The regulatory asset is capitalized on the asset side of the balance sheet, just like electric plant investment in traditional ratemaking.

Also in accordance with generally accepted accounting principles, there is a book to tax timing difference that results from deferring expenses. That book to tax accounting difference results in ADIT being recorded on the liability side of the balance sheet. Likewise, in traditional cost of service ratemaking for electric plant investment there may be book to timing differences created by differences in book and tax depreciation, which result in ADIT. The Commission's and Ohio Supreme Court's precedent dealing with capitalized assets where there is related ADIT supports the view that ADIT must be recognized in determining the amounts that are eligible to be recovered from customers.[221] The Commission, moreover, has recognized this regulatory principle in a different part of its ESP II Order, stating:

> We agree with Staff and Kroger that the DIR mechanism be revised to account for ADIT. The Commission finds that it is not appropriate to establish the DIR rate mechanism in a manner which provides the Company with the benefit of ratepayer supplied funds. Any benefit resulting from ADIT should be reflected in the DIR revenue requirement. Therefore, the Commission directs AEP-Ohio to adjust its DIR to reflect the ADIT offset.[222]

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[221] *Cincinnati v. Public Utilities Comm.*, 161 Ohio St. 395, 405-06 (1954); *Ohio Bell Telephone Co. v. Public Utilities Comm.*, 68 Ohio St.2d 193, 194 (1981); *Cleveland Electric Illuminating Company v. Public Utilities Comm.*, 12 Ohio St.2d 320, 323 (1984) (determining that the Commission's order is consistent with the principle that tax benefits must be passed through to customers).

[222] ESP II Order at 47.

Carrying charges are intended to compensate the utility for the cost of financing or delaying the recovery of an expense. Despite the fact that the tax benefit recognized in the ADIT offset means that AEP-Ohio does not finance the entire deferred amount, the ESP II Order authorized AEP-Ohio to accrue carrying charges on the total deferred amount. The consequence of the ESP II Order's neglect of the ADIT offset permits AEP-Ohio to accrue and then recover from customers carrying charges on unreasonably inflated balances. Moreover, it would allow AEP-Ohio to convert, through the phase-in structure, what would have otherwise been a bypassable charge into an inflated non-bypassable charge, which works against Ohio's policy objectives (customer choice and reasonable prices, for example).[223] Such a result is not just and reasonable, nor does it comply with generally accepted accounting principles, regulatory practices and principles, or precedent.

On rehearing, the Commission must direct AEP-Ohio to calculate carrying charges on deferred balances adjusted for ADIT. Because the Commission has ongoing jurisdiction to modify the phase-in, the Commission should direct AEP-Ohio to recalculate the carrying charges that have accrued on the deferred balances from the beginning of the phase-in to ensure that AEP-Ohio does not recover more than its actual costs from ratepayers. Alternatively, the Commission must permit these issues to be addressed through an evidentiary hearing in the *PIRR Case* in which IEU-Ohio has also submitted an application for rehearing.

[223] Section 4928.02, Revised Code.

IV. GENERATION ASSET DIVESTITURE

12. The ESP II Order is unlawful and unreasonable because, without authority to do so under Section 4928.143, Revised Code, the ESP II Order conditionally approves a transfer of generating assets without making the findings required by Sections 4928.17 and 4928.02, Revised Code, and Rule 4901:1-37, OAC, and without netting the above-book market value of AEP-Ohio's generating assets against the transition revenue which the ESP II Order authorizes AEP-Ohio to collect on a non-bypassable basis during and after the term of the as-approved Modified ESP.

Although AEP-Ohio filed testimony discussing its plan to transfer generation assets to Genco with its Modified ESP Application, it did not request approval of its corporate separation plan and such generation transfer in the Modified ESP proceeding. That request was filed in Case No. 12-1126-EL-UNC ("*Corporate Separation Case*") and AEP-Ohio stated in its Modified ESP Application that it requested such approvals to be made in the *Corporate Separation Case*.[224] Additionally, AEP-Ohio did not move to consolidate the *Corporate Separation Case* with the *ESP II Case*.[225] Because AEP-Ohio did not move to consolidate the *Corporate Separation Case*, the Commission stated that "the primary issues to be considered in this modified ESP proceeding is [*sic*] how the divestiture of the generation assets and the agreement between AEP-Ohio and [Genco] will impact SSO rates."[226]

Despite determining that the Commission's review was limited to the impact of the transfer on SSO rates, the ESP II Order then conditionally approved the generating asset transfer, stating, "the Commission finds that, subject to our approval of the

[224] AEP-Ohio Ex. 100 at 3-4.

[225] ESP II Order at 58-59.

[226] *Id.* at 59.

corporate separation plan, the electric distribution utility should divest its generation assets from its noncompetitive electric distribution utility assets by transfer to its separate competitive retail generation subsidiary, [Genco], as represented in this modified ESP."[227] The ESP II Order provided conditional approval of the transfer: (1) without determining whether the transfer is just, reasonable, and in the public interest; (2) without making specific findings regarding the effect of the generating asset transfer on customers or SSO rates; (3) without directing AEP-Ohio to offset the transition revenue collection opportunity (presented by the RSR, the Capacity Shopping Tax, the PTR and other mechanisms discussed herein and permitting AEP-Ohio to collect above-market compensation for generation-related functions) by the above-market value of the to-be-transferred generating assets; and (4) without requiring Genco or other AEP-Ohio affiliates to consent to jurisdiction under Section 4928.18, Revised Code. Because the conditional approval is beyond the scope of the issues the Commission said it would address in this proceeding and evades the requirements that must be satisfied prior to approval, conditional or otherwise, of any such transfer, the ESP II Order is unlawful and unreasonable; and the Commission must grant rehearing.

Initially, the ESP II Order's conditional approval of the generation asset transfer was unlawful because approval was not sought as part of the Modified ESP. As noted above, AEP-Ohio filed a separate application in the *Corporate Separation Case*, AEP-Ohio failed to move to consolidate the *Corporate Separation Case*,[228] and AEP-Ohio explicitly stated that it was not requesting approval of its corporate separation plan and

[227] *Id.* at 59.

[228] ESP II Order at 58.

divestiture in this proceeding.[229] Additionally, there is no basis for the Commission in a proceeding designated to establish an SSO to approve, conditionally or otherwise, a transfer of generation assets as a term of the Modified ESP under Section 4928.143, Revised Code.[230] As a result, the ESP II Order's conditional approval of the transfer of generation assets is beyond the Commission's legal authority.

Even if the matter was properly before the Commission, the ESP II Order contains none of the findings required by statute and Commission rules before any such Commission approval, conditional or otherwise, may be lawfully extended. It does not determine that the transfer is just, reasonable, and in the public interest,[231] consistent with Rule 4901:1-37, OAC,[232] and the State energy policy, as required by the Commission's rules.[233] The ESP II Order failed to determine whether AEP-Ohio had satisfied the requirements contained in Rule 4901:1-37-09, OAC,[234] which are intended

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[229] AEP-Ohio Ex. 100 at 3-4; ESP II Order at 57.

[230] For a related application of this principle in which the Commission sought to expand its authority to expand the terms of an ESP beyond those provided by Section 4928.143(B)(2), Revised Code, see *In re Columbus Southern Power Company*, 128 Ohio St.3d at 519-20.

[231] Rule 4901:1-37-09, OAC.

[232] Rule 4901:1-37-02, OAC, states :

> (A) The purpose of this chapter is to require all of the state's electric utilities to meet the same standards so a competitive advantage is not gained solely because of corporate affiliation.
>
> (B) This chapter is intended to create competitive equality, prevent unfair competitive advantage, prohibit the abuse of market power and effectuate the policy of the state of Ohio embodied in section 4928.02 of the Revised Code.

[233] Rule 4901:1-37-02, OAC.

[234] Rule 4901:1-37-09, OAC, requires:

> (B) An electric utility may apply for commission approval to sell or transfer its generating assets by filing an application to sell or transfer.
>
> (C) An application to sell or transfer generating assets shall, at a minimum:

to assist the Commission in determining whether the transfer is just, reasonable, and in the public interest.

In addition to failing to address the requirements for approval of a generation asset transfer, the ESP II Order did not address the likely effect of the transfer of assets on future SSO prices or future capacity prices, the same issue that the Commission itself identified in its Entry on Rehearing as so serious a concern that it could not find that the Stipulation was in the public interest.[235] Because the as-approved Modified ESP calls for the generation supply price of a future SSO to be established through a CBP, the price of capacity will impact suppliers' bids into the CBP.[236] The Commission previously determined that its "intent in approving the generation asset divestiture was based on our understanding that AEP-Ohio would place all of its current (as of September 7, 2011) generation assets into the 2015 base residual auction."[237] After that outcome was put into question by AEP-Ohio's Federal Energy Regulatory Commission ("FERC) filing to divest generating assets to affiliates subject to FRR Alternative requirements, the Commission, on rehearing, determined that "Parties have not met their burden of demonstrating that the Stipulation, as a package, benefits

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(1) Clearly set forth the object and purpose of the sale or transfer, and the terms and conditions of the same.

(2) Demonstrate how the sale or transfer will affect the current and future standard service offer established pursuant to section 4928.141 of the Revised Code.

(3) Demonstrate how the proposed sale or transfer will affect the public interest.

(4) State the fair market value and book value of all property to be transferred from the electric utility, and state how the fair market value was determined.

[235] Entry on Rehearing at 5-8 (Feb. 23, 2012).

[236] *See* Initial Brief of IEU-Ohio at 77 (June 29, 2012); Reply Brief of IEU-Ohio at 53 (July 9, 2012).

[237] Entry on Rehearing at 8 (Feb. 23, 2012).

ratepayers and the public interest" and rejected the Stipulation.[238] The concerns about the potential effect of AEP-Ohio's generation asset transfer plans upon future capacity prices that the Commission identified in the Entry on Rehearing have not been addressed by AEP-Ohio because its plans still indicate that it will withhold some generating assets (the Amos and Mitchell Units) from the RPM-related auction process. Yet, the Commission does not even mention this concern in the ESP II Order or address the requirement that AEP-Ohio must address the implications of its generation asset transfer plans on future SSO or RPM-Based Pricing of capacity. It is unreasonable and unlawful for the Commission to not address such implications and, on its own initiative, then proceed to grant conditional approval of the transfer planned by AEP-Ohio but not proposed in the ESP proceedings. Regardless, no amount of review can make the transfer as proposed — a transfer that withholds generation from the RPM's base residual auction — just, reasonable, and in the public interest. Accordingly, at a minimum, the Commission must condition the transfer on any subsequent owner of AEP-Ohio's generating units bidding such units into all future RPM auctions. As discussed further below, the Commission has the authority to enforce such a restriction pursuant to Section 4928.18, Revised Code.

Furthermore, approval of the transfer of assets is unlawful because AEP-Ohio has not complied with the requirement to provide the Commission with the net book and market value of its generating assets.[239] Without this information, it is impossible for the Commission to determine whether the transfer as proposed at net book value is just,

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[238] *Id.*

[239] Rule 4901:1-37-09(C)(4), OAC.

reasonable and in the public interest. The ESP II Order's authorization of AEP-Ohio's requests to collect transition revenue has further increased the necessity for a review of the market value of the to-be-transferred generating assets.[240] IEU-Ohio contests the lawfulness and reasonableness of these above-market transition revenue collection mechanisms for reasons explained in other parts of this rehearing request. But it is, in any event, unreasonable and unlawful for the ESP II Order to, on one hand, permit AEP-Ohio to collect above-market charges for generation-related services and, on the other hand, permit AEP-Ohio to avoid netting the above-book market value of any of its generating assets to determine the amount of any transition revenue recoverable from shopping and non-shopping customers as required by Section 4928.39, Revised Code. The problem is compounded because the ESP II Order then facilitates AEP-Ohio's efforts to then convey the above-book market value of such generating assets to an affiliate such as Genco and pass on to such affiliate the above-market revenue collected through the non-bypassable transition revenue collection mechanisms. The combination of results put in motion by the ESP II Order evades the discipline mandated by Ohio law upon the Commission's ability to authorize the collection of transition revenue assuming that the Commission is not otherwise barred from doing so for the reasons discussed herein.

The need for AEP-Ohio to comply with the requirement to provide a market valuation of the generation takes on special significance because of the evidence here. According to AEP-Ohio's internal analysis (the "Impairment Test Memo"), AEP-Ohio has

[240] ESP II Order at 26-38 (RSR); *id.* at 47-49 (PTR). While AEP-Ohio claims that these transition costs are not barred by SB 3, one thing remains clear regardless of the legality of AEP-Ohio's claim: the Commission authorized AEP-Ohio to collect generation-related transition revenue.

determined that the future cash flow from the AEP-East generating fleet for generation-related services[241] is billions of dollars more than the cash flow required to support the current book value of this generating fleet even assuming that compensation for generating capacity service is based on RPM-Based Prices.[242]

Before the Commission approves the transfer of generating assets and allows AEP-Ohio to flow hundreds of millions of dollars of non-bypassable generation-related charges to Genco, it must determine whether the transfer at net book value as proposed by AEP-Ohio is in the public interest, which is clearly affected by the imposition of non-bypassable generation-related charges that unlawfully provide AEP-Ohio with another opportunity to collect transition revenue. Because the Impairment Test Memo indicates that the market value of the generating fleet that includes AEP-Ohio's generating assets exceeds the book value, it is unreasonable and unlawful for the ESP II Order to not impose conditions on the transfer that require AEP-Ohio to net the above-book value of to-be-transferred generating assets against the transition revenue collection opportunity provided by the mechanisms discussed herein.

Finally, pursuant to Section 4928.18, Revised Code, the Commission has authority to exercise jurisdiction over AEP-Ohio's affiliates to enforce Section 4928.17, Revised Code, or any order issued pursuant to that section. The Commission, however, failed to require AEP-Ohio's affiliates to submit to Commission jurisdiction

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[241] OCC Ex. 104; IEU-Ohio Ex. 117.

[242] IEU-Ohio Ex. 120; OCC Ex. 104. The Impairment Test Memo states that the need for the analysis occurred because there was a "triggering" regulatory event: the United States Environmental Protection Agency's ("EPA") Cross-State Air Pollution Rule ("CSAPR") OCC Ex. 104 at 1. The analysis reduced projected cash flow by $100 million for 2012-2013 to account for the effects of the rule. *Id.* at 4. On August 21, 2012, however, the United States Court of Appeals for District of Columbia Circuit vacated CSAPR. *EME Homer City Generation v. EPA*, Case No. 11-1302, 2012 WL 3570721 (D.C. Cir. Aug. 21, 2012).

under Section 4928.18, Revised Code. To the extent the transfer occurs without such consent, any ability of the Commission to remedy subsequently discovered problems may be impaired by a preemption defense. Without assurances from AEP-Ohio's affiliates that they will consent to jurisdiction of the Commission, the transfer cannot be deemed just, reasonable, and in the public interest.

V. PROCEDURAL MATTERS

13. The ESP II Order is unlawful and unreasonable because it fails to sustain objections to the admission of testimony where the testimony improperly relied upon settlement agreements from other proceedings for the purpose of addressing contested issues in the *ESP II Case*.

On May 4, 2012, IEU-Ohio filed a Motion to Strike Ohio Power Company's Application and Supporting Testimony and Memorandum in Support. On May 11, 2012, IEU-Ohio filed a Motion to Strike Intervenor Testimony. In each, IEU-Ohio requested that the Commission strike portions of testimony that relied upon stipulations which contain provisions prohibiting reliance on them as precedent in other matters.[243] During the hearing, the Attorney Examiners denied the Motions to Strike.[244]

As a result of the Attorney Examiners' failure to grant the Motion to Strike, the testimony of several witnesses improperly relied on stipulations to support their recommendations. Exelon witness Fein claimed that the Duke ESP Stipulation[245]

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[243] Industrial Energy Users-Ohio's Motion to Strike Ohio Power Company's Application and Supporting Testimony and Memorandum in Support at 14-15 and Attachment 1 (May 4, 2012) ("Motion to Strike Company Testimony"); Motion to Strike Intervenor Testimony and Memorandum in Support of Industrial Energy Users-Ohio and Office of the Ohio Consumers' Counsel at 6-7 (May 11, 2012).

[244] Tr. Vol. I at 24-25; Tr. Vol. II at 447-448; Tr. Vol. IV at 1253.

[245] *In the Matter of the Application of Duke Energy Ohio for Authority to Establish a Standard Service Offer Pursuant to Section 4928.143, Revised Code, in the Form of an Electric Security Plan, Accounting Modifications and Tariffs for Generation Service*, Case Nos. 11-3549-EL-SSO, *et al.*, Stipulation and Recommendation at 2 (Oct. 24, 2011) ("Duke ESP Stipulation").

provides a basis for the RSR.[246] AEP-Ohio witness Powers used the Duke ESP Stipulation as evidence that non-bypassable riders in the Modified ESP are lawful.[247] AEP-Ohio witness Hawkins relied upon the AEP-Ohio Distribution Rate Case Stipulation[248] for evidence of AEP-Ohio's capital structure.[249] Each of those stipulations, however, expressly states that neither the stipulation nor any Commission order adopting it may be cited as precedent. IEU-Ohio raised the issue again in its Initial Brief, challenging the Attorney Examiners' decision to deny the Motion to Strike.

The ESP II Order affirmed the Attorney Examiners' decision, stating:

> The Commission finds that IEU's request to strike portions of the record should be denied. We acknowledge that individual components agreed to by parties in one proceeding should not be binding on the parties in other proceedings, but we find that references to other stipulations in this proceeding were limited in scope and did not create any prejudicial impact on parties that signed the stipulations. Consistent with our Finding and Order in Case No. 11-5333-EL-UNC, we also note that, while parties may agree not to be bound by the provisions contained within a stipulation, these limitations do not extend to the Commission.[250]

The ESP II Order's ruling is unreasonable and unlawful. Citations to stipulations that are "limited in scope" do not lessen the violation of the terms of such stipulations. Moreover, the Commission's determination that it is not

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[246] Exelon Ex. 101 at 9, 13.

[247] AEP-Ohio Ex. 101 at 6-7.

[248] *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company, Individually and, if Their Proposed Merger is Approved, as a Merged Company (collectively, AEP Ohio) for an Increase in Electric Distribution Rates*, Case Nos. 11-351-EL-AIR, *et al.*, Joint Stipulation & Recommendation (Nov. 23, 2011) ("Distribution Rate Case Stipulation").

[249] AEP-Ohio Ex. 102 at 4-5.

[250] ESP II Order at 10.

"bound by the provisions contained within a stipulation" is wrong. The Commission adopted each of the stipulations containing the following language:

> This Stipulation is submitted for purposes of these proceedings only, and *neither this Stipulation nor any Commission Order considering this Stipulation shall be deemed binding in any other proceeding nor shall this Stipulation or any such Order be offered or relied upon in any other proceedings*, except as necessary to enforce the terms of this Stipulation.[251]

The Commission orders adopting the stipulations did not modify this term; thus, the Commission agreed to enforce the prohibition against citation to and reliance upon the stipulations. However, the ESP II Order fails to do so.

The Commission has an interest in facilitating settlements. The quoted language is designed to facilitate the settlement process. By allowing parties to violate the terms of these stipulations in the *ESP II Case*, the Commission's interest in encouraging settlements in contested cases has been undermined and the failure has negatively affected the rights of parties such as IEU-Ohio. As a result, future settlements will be more difficult to achieve and, in the near term, the ESP II Order unreasonably and unlawfully prejudices the rights of parties such as IEU-Ohio to have contested issues resolved based on the evidence presented and the applicable law. Therefore, the failure to grant IEU-Ohio's Motions to Strike portions of testimony that relied upon such stipulations renders the ESP II Order unlawful and unreasonable and otherwise evades the Commission's obligation to address contested issues on the merits based on the evidence properly admissible and applicable law. Stipulations containing recommendations which are subsequently adopted by the Commission as a packaged resolution of any potentially contested issues are not properly included in testimony and

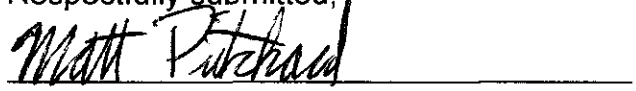
[251] *Duke ESP Stipulation* at 2 (emphasis added).

they may not be relied upon by the Commission to address or consider contested issues in these proceedings or any other.

VI. CONCLUSION

Based on the errors identified herein, considered both individually and combined, IEU-Ohio respectfully requests that the Commission grant this Application for Rehearing, terminate any authority that may permit AEP-Ohio to bill or collect compensation based on the as-approved Modified ESP, and issue such orders as are necessary to continue the provisions, terms, and conditions of AEP-Ohio's most recent SSO until a subsequent SSO is lawfully authorized pursuant to Section 4928.142 or 4928.143, Revised Code. The Commission's restoration of the most recent SSO must require that AEP-Ohio's compensation for generation capacity service available to CRES providers be based on the capacity valuation and pricing method that is part of PJM's RPM. Further, IEU-Ohio requests that the order granting rehearing direct that any revenue unlawfully collected by AEP-Ohio pursuant to the ESP II Order or pursuant to the Stipulation and Recommendation filed September 7, 2011 (that was approved and then rejected on February 23, 2012) be refunded.

Respectfully submitted,



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I hereby certify that a copy of the foregoing *Industrial Energy Users-Ohio's Application for Rehearing of the August 8, 2012 Opinion and Order and Memorandum in Support* was served upon the following parties of record this 7th day of September 2012, *via* electronic transmission, hand-delivery or first class U.S. mail, postage prepaid.

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Estimated Deferrals Related to Capacity Charges

Delivery Year	Cost-Based Capacity Charge in $/MW-Hour (a)	RPM Capacity Price in $/MW-Day	RPM-Capacity Charge in $/MW-Hour (b)	Estimated Wire Sales in MW-Hour (c)	Estimated % Shopping (d)	Shopped Load in MW-Hour	Estimated Revenue Shortage in $	$1.00/MWH against deferral (e)	Annual Deferral Without Carrying Charges (f)
2012/2013	$12.19	$20.01	$1.29	35,401,642.407	52.00%	18,408,854	$200,696,156	$35,401,642	$165,294,514
2013/2014	$12.19	$33.71	$2.18	48,260,877.259	62.00%	29,921,744	$299,746,733	$48,260,877	$251,485,856
2014/2015	$12.19	$153.89	$9.94	48,171,845.757	72.00%	34,683,729	$78,348,290	$48,171,846	$30,176,444
						Total	$578,791,180		$446,956,815

a) $12.19/MWH cost based capacity charge based on capacity cost of $188.88/MW-day and 64.54% load factor. $188.88/MW-day capacity cost per page 51 of PUCO Order dated August 8, 2012 in Case No. 11-346-EL-SSO, et al.

b) Based on RPM Capacity Price MW day and 64.54% load factor

c) MWH sales per Company witness Allen "Load Forecast" workpapers. 2012/2013 delivery year is September 2012 - May 2013.

d) Estimated shopping percentages per page 34 of PUCO Order dated August 8, 2012 in Case No. 11-346-EL-SSO, et al.

e) $1.00/MWh credit per page 36 of PUCO Order dated August 8, 2012 in Case No. 11-346-EL-SSO, et al.

f) Estimated deferral amounts do not include any carrying charges

ATTACHMENT A