

**BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO**

In the Matter of the Application of)
Ohio Power Company for Authority to)
Establish a Standard Service Offer) Case No. 13-2385-EL-SSO
Pursuant to §4928.143, Revised Code,)
in the Form of an Electric Security Plan.)

In the Matter of the Application of)
Ohio Power Company for Approval of) Case No. 13-2386-EL-AAM
Certain Accounting Authority.)

INITIAL BRIEF OF INDUSTRIAL ENERGY USERS-OHIO

Frank P. Darr (Counsel of Record)
(Reg. No. 0025469)
Matthew R. Pritchard (Reg. No. 0088070)
MCNEES WALLACE & NURICK LLC
21 East State Street, 17TH Floor
Columbus, OH 43215
Telephone: (614) 469-8000
Telecopier: (614) 469-4653
fdarr@mwncmh.com
(willing to accept service by e-mail)
mpritchard@mwncmh.com
(willing to accept service by e-mail)

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Attorneys for Industrial Energy Users-Ohio

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I. INTRODUCTION

In its Application, the Ohio Power Company (“AEP-Ohio”) seeks authorization of an Electric Security Plan (“ESP” or “proposed ESP” as appropriate) for the period of June 1, 2015 to May 31, 2018.¹ The Application proposes to provide energy and capacity under the standard service offer (“SSO”) through a competitive bidding process (“CBP”).² It also proposes several new nonbypassable riders. The most significant proposed nonbypassable rider is the Power Purchase Agreement Rider (“PPAR”), which would recover generation-related costs associated with AEP-Ohio’s retained interest in generation plants operated by Ohio Valley Electric Corporation (“OVEC”).³ The Application also proposes to classify some transmission costs as non-market-based and collect these costs from retail customers through a nonbypassable Basic

¹ AEP-Ohio Ex. 1 at 2. AEP-Ohio also seeks authority to terminate the ESP one year early unilaterally. *Id.* at 15.

² *Id.* at 7-8.

³ *Id.* at 8-9.

Transmission Cost Rider (“BTCR”).⁴ Additionally, AEP-Ohio proposes a Purchase of Receivables (“POR”) program that includes a nonbypassable Bad Debt Rider (“BDR”) to socialize the incremental bad debt costs in excess of amounts currently collected in distribution rates.⁵

To secure approval of its Application, AEP-Ohio argues that the proposed ESP satisfies the statutory requirement contained in R.C. 4928.143(C)(1), the “ESP v. MRO Test.” The Test requires AEP-Ohio to meet its burden of proof to show that the ESP is more favorable in the aggregate than a Market Rate Offer (“MRO”).⁶ AEP-Ohio claims that the proposed ESP is \$44.1 million quantitatively more favorable than an MRO and has several non-quantitative benefits.⁷

Based on the record produced by thirteen days of hearing, Industrial Energy Users-Ohio (“IEU-Ohio”) recommends that the Public Utilities Commission of Ohio (“Commission”) reject the PPAR because authorization would be both illegal and unreasonable. The Commission also should not authorize the unreasonable BTCR as proposed because it would send incorrect price signals to customers, reduce their ability to manage their total electric bills, and probably result in the double-billing of transmission costs from shopping customers. If the Commission, nonetheless, approves a nonbypassable BTCR, it also should provide a mechanism so that current shopping customers are not billed twice for transmission-related services, and the Commission should modify the proposed rider so that it provides efficient and

⁴ *Id.* at 12-13.

⁵ *Id.* at 14. As appropriate, the POR program refers to the combination of the POR and BDR proposed by AEP-Ohio.

⁶ *Id.* at 2.

⁷ AEP-Ohio Ex. 7 at 3-5.

transparent price signals. The Commission also should reject the POR program as filed because it is unreasonable. If the Commission does authorize a POR program, it should remove the BDR and modify the POR program to provide that AEP-Ohio will purchase accounts receivable at a discount.

Additionally, the Commission should not approve the proposed ESP as filed. Unless the Commission removes the objectionable riders (particularly the PPAR), the proposed ESP fails an objective, cost-based application of the ESP v. MRO Test.

II. THE COMMISSION SHOULD DENY AUTHORIZATION OF THE PPAR

AEP-Ohio has requested authorization of a PPAR as a nonbypassable rider that will operate as a credit or charge.⁸ The credit or charge will be estimated annually, at a time “near” the beginning of each planning year.⁹ The charge or credit would be based on an estimate of the revenue necessary to recover or credit the difference between what AEP-Ohio expects to realize through the liquidation of its “entitlement” to power from its 19% share of the OVEC generation units (“OVEC Entitlement”) and the costs AEP-Ohio is charged by OVEC.¹⁰ After the first year, the charge or credit will be further adjusted to account for under or over-recoveries of the PPAR relative to AEP-Ohio’s actual OVEC costs and revenue.¹¹ The amount of the over and under-recovery would include the cost of interest at AEP-Ohio’s weighted cost of debt.¹²

The OVEC Entitlement arises out of AEP-Ohio’s interest as a Sponsoring Company in two generation facilities that were constructed to provide electricity to the

⁸ AEP-Ohio Ex. 1 at 8-9.

⁹ Tr. Vol. I at 109-10.

¹⁰ AEP-Ohio Ex. 7 at Ex. WAA-1.

¹¹ *Id.* at 11.

¹² AEP-Ohio Ex. 13 at Ex. AEM-1 and AEP-Ohio Ex. 18 at 5.

Department of Energy for uranium enrichment in the 1950s.¹³ Under Article 5 of the Amended and Restated Inter-Company Power Agreement (“ICPA”), a Federal Energy Regulatory Commission (“FERC”)-approved contract, OVEC charges the Sponsoring Companies for the actual fixed and variable costs of operating the OVEC generation facilities including a return on equity.¹⁴ The cost-plus contract permits OVEC to charge the Sponsoring Companies for variable costs of energy production, fixed costs (for example, debt costs and fixed operation and maintenance expenses), and transmission charges assessed by PJM Interconnection, L.L.C. (“PJM”). Under Article 7 of the ICPA, Sponsoring Companies must also pay “Other Charges” such as replacement costs of plant, facility costs such as spare parts costs, post-agreement retirement benefit costs, and shut-down costs.¹⁵ Under Article 8, the Sponsoring Companies are obligated to pay all fixed (demand) costs, transmission charges, and Other Charges “whether or not any Available Power or Available Energy are supplied” by OVEC.¹⁶

The cost of power provided by OVEC under the ICPA to the Sponsoring Companies is sensitive to the total generation output of the plants. “In 2012, OVEC’s average power cost to the Sponsoring Companies was \$62.86 per megawatt-hour (“MWh”) compared with \$50.86 per MWh in 2011.”¹⁷ The difference in the cost was a function primarily of lower energy sales. “Mild weather, a soft energy market and low-cost natural gas generation were responsible for lower energy sales in 2012.”¹⁸

¹³ AEP-Ohio Ex. 7 at 8-9.

¹⁴ IEU-Ohio Ex 1B at KMM-2, pages 7-11.

¹⁵ *Id.* at KMM-2, pages 12-13.

¹⁶ *Id.* at KMM-2, page 14.

¹⁷ *Id.* at KMM-3, page 2.

¹⁸ *Id.*

The OVEC Entitlement is an asset that AEP-Ohio intended to transfer to its unregulated generation affiliate. In 2012, the Commission approved AEP-Ohio's request to divest its generation-related assets including the OVEC Entitlement by December 31, 2013.¹⁹ In late 2013, however, AEP-Ohio reported that it was unable to secure approval for the transfer of the OVEC Entitlement from an as-yet undisclosed Sponsoring Company or Companies.²⁰ AEP-Ohio then sought and received authority to retain the OVEC Entitlement "until the OVEC contractual entitlements can be transferred to AEP Genco or otherwise divested, or until otherwise ordered by the Commission."²¹ As a condition of its temporary retention of the OVEC Entitlement, the Commission ordered that AEP-Ohio liquidate its entitlement to energy and capacity in the PJM wholesale markets.²² Since the Commission's decision amending the order directing AEP-Ohio to divest the OVEC Entitlement on December 4, 2013, AEP-Ohio has not actively pursued disposition of the OVEC Entitlement, and it has no intention of exercising its rights to assign the OVEC Entitlement until the Commission rules on its application for the proposed ESP, including the PPAR.²³

The PPAR would not be utilized to provide physical generation supply to AEP-Ohio's customers. (AEP-Ohio also states that it will not bid its OVEC Entitlement into the SSO auctions to serve its default service customers to avoid affecting the bidding

¹⁹ *In the Matter of the Application of Ohio Power Company for Approval of an Amendment to its Corporate Separation Plan*, Case No. 12-1126-EL-UNC, Finding and Order at 5 & 24-25 (Oct. 17, 2012) ("*Corporate Separation Case*").

²⁰ AEP-Ohio does not remember which Sponsoring Company or Companies refused to approve the assignment of the OVEC Entitlement to AEP-Ohio's unregulated generation affiliate. See, e.g., Tr. Vol. I at 22-23.

²¹ *Corporate Separation Case*, Finding and Order at 9 (Dec. 4, 2013).

²² *Id.* at 8-9.

²³ Tr. Vol. I at 115; Tr. Vol. II at 577-78 & 590.

process adversely.²⁴) As a result, the capacity and energy from OVEC will not be used to limit shopping by customers or provide standby, backup, or supplemental power service, or default service.²⁵

Although the OVEC Entitlement will not be used to supply generation service to AEP-Ohio's customers, AEP-Ohio seeks to recover the costs not recovered by liquidating the capacity and energy in the PJM markets on the claim that the rider will operate as a "hedge" that has the effect of lowering the volatility of electric prices for customers.²⁶ According to AEP-Ohio, the "hedge" will be small. Its "best" estimate of the value of the hedge to customers over the term of the proposed ESP averages 7 cents per MWh (7¢/MWh).²⁷ As an AEP-Ohio witness conceded, AEP-Ohio's best estimate of the PPAR's anticipated effect on bills, the 7 cent solution, will not have an effect on residential customers' investment decisions.²⁸

AEP-Ohio also states that the effect of the PPAR is to allow AEP-Ohio to recover fully the costs it is billed by OVEC for the OVEC Entitlement.²⁹ Without the PPAR, any above-market cost of the OVEC Entitlement would be stranded with AEP-Ohio.³⁰

Other parties anticipate that the PPAR will be a significant cost to all customers. Their conclusions begin with the fact that AEP-Ohio's initial estimate indicated that the

²⁴ AEP-Ohio Ex. 7 at 10.

²⁵ Tr. Vol. II at 566-67.

²⁶ AEP-Ohio Ex. 7 at 10-11; Tr. Vol. II at 566.

²⁷ AEP-Ohio Ex. 8B.

²⁸ Tr. Vol. XIII at 3156.

²⁹ Tr. Vol. I at 29-30.

³⁰ As Dr. McDermott defined stranded costs, it is the amount of investment that the owner cannot recover through market prices. Tr. Vol. XIII at 3148-49. Without the PPAR, AEP-Ohio would not be able to recover the cost related to the OVEC Entitlement in the market if the OVEC costs exceeded the price AEP-Ohio could secure for capacity and energy.

PPAR would cost customers \$52 million over the term of the ESP.³¹ After correcting for unsupported assumptions AEP-Ohio made in its initial estimate of the PPAR rate impacts, IEU-Ohio and the Office of the Ohio Consumers' Counsel ("OCC") estimated that the actual cost of the PPAR would range from \$82 million to \$116 million over the term of the proposed ESP.³²

The Commission should not authorize the PPAR for several reasons. Initially, the rider is not authorized by a provision of R.C. 4928.143(B). Second, authorization of the PPAR would violate state energy policy. Third, the PPAR is barred by R.C. 4928.38 and the stipulation AEP-Ohio entered to resolve its electric transition plan ("ETP") application in 2000. Fourth, the Commission cannot authorize an adjustment in the wholesale compensation of AEP-Ohio under Ohio law. Fifth, authorization of the PPAR is preempted by the Federal Power Act ("FPA"). Finally, AEP-Ohio has not provided evidence supporting the reasonableness of the PPAR. In addition to failing to demonstrate that the PPAR will operate as an effective hedge, AEP-Ohio has the option of assigning its OVEC Entitlement to a third party in fulfillment of the Commission's directive to divest its interests in generation. Thus, there is no reason, as a matter of law, policy, or fact, for the Commission to authorize the PPAR.

A. The PPAR is not authorized by R.C. 4928.143(B)(1) or (2)

The Commission may authorize a term of the ESP only as provided by R.C. 4928.143(B).³³ As demonstrated by AEP-Ohio's testimony and admissions on cross-examination, the PPAR is not authorized by any provision of R.C. 4928.143(B)(1) or (2).

³¹ IEU-Ohio Ex. 1B at Ex. KMM-5.

³² IEU-Ohio Ex. 1B at 10-12; OCC Ex. 15A at 10-28.

³³ *In re Columbus S. Power Co.*, 128 Ohio St.3d 512 (2011).

R.C. 4928.143(B)(1) provides that an ESP must include “provisions relating to the supply and pricing of electric generation service.” As conceded by AEP-Ohio, the PPAR will have no effect on the supply of electric generation service. AEP-Ohio will secure a supply of electric generation service through the CBP for the ESP.³⁴ As further explained by AEP-Ohio, it will not bid the OVEC generation assets into the CBP.³⁵ Thus, the PPAR is not a provision related to the supply of electric generation service.

The PPAR also is not a provision related to the pricing of electric generation service. As Mr. Allen repeatedly stated during his cross-examination, the PPAR will not affect the price of generation service (although it will alter the total retail price the customer pays whether the customer takes generation service under the SSO or is shopping).³⁶ This assertion is consistent with the fact that the PPAR is proposed to be a nonbypassable rider. It will neither raise nor lower the price of generation service; rather it will operate in the same way as any other nonbypassable distribution or distribution-like rider (*e.g.*, the current Retail Stability Rider), increasing total bills of both ESP and shopping customers. As proposed, therefore, the PPAR does not relate to the pricing of electric generation service supplied under the ESP.

To authorize a rider under R.C. 4928.143(B)(1), the Commission must find that the cost to be recovered relates to the supply and pricing of electric generation service. Because the PPAR would not relate to either the supply or pricing of generation service, the Commission cannot authorize the PPAR as a provision of an ESP under R.C. 4928.143(B)(1).

³⁴ AEP-Ohio Ex. 1 at 7-8.

³⁵ AEP-Ohio Ex. 7 at 10.

³⁶ Tr. Vol. XIII at 3289-90.

R.C. 4928.143(B)(2)(a) through (i) identify the provisions the Commission may authorize in an ESP. None authorizes the inclusion of a PPAR.

R.C. 4928.143(B)(2)(a) provides for authorization of an automatic recovery mechanism for prudently incurred cost of fuel used to generate electricity supplied under the offer, the cost of purchased power supplied under the offer, the cost of emission allowances, and the cost of federally mandated carbon or energy taxes. The PPAR does not concern any costs of the ESP covered by this provision; as AEP-Ohio has made clear, the OVEC capacity and energy will not be contracted to serve the ESP. Accordingly, the Commission cannot authorize the PPAR under R.C. 4928.143(B)(2)(a).

R.C. 4928.143(B)(2)(b) and (c) provide for charges related to costs of construction work in progress commenced after January 1, 2009 or costs related to a generating facility which became newly used and useful after January 1, 2009 if other requirements are satisfied. The PPAR would recover costs for generation facilities that have been in service since the 1950s.³⁷ Thus, the Commission cannot authorize the PPAR under R.C. 4928.143(B)(2)(b) or (c).

R.C. 4928.143(B)(2)(d) provides for authorization of terms, conditions, or charges related to several items that have the effect of stabilizing or providing certainty regarding retail electric service. Other than being a charge, the PPAR does not meet any of the requirements of this division.

Under R.C. 4928.143(B)(2)(d), the charge must be related to limitations on customer shopping, bypassability, standby, backup, or supplemental power service, default service, carrying costs, amortization periods, or accounting or deferrals. AEP-

³⁷ AEP-Ohio Ex. 7 at 8-9.

Ohio states that the PPAR would not have the effect of limiting customer shopping.³⁸ During cross-examination, Mr. Allen also testified that AEP-Ohio would not use the OVEC generation for standby, backup, supplemental, or default service.³⁹ Additionally, the PPAR has no relationship to bypassability of generation-related costs (other than being nonbypassable), carrying costs, amortization periods, or accounting or deferrals. Therefore, the PPAR is not related to any of the kinds of services or accounting issues that may be addressed through a charge authorized under R.C. 4928.143(B)(2)(d).

Further, the PPAR is not proposed to stabilize retail electric service in either a physical or economic sense. In a physical sense, the PPAR will not expand the amount of generation service available to ESP customers. The power sold to nonshopping customers will be provided by successful CBP bidders. The OVEC Entitlement will not be bid into the auctions used to serve ESP customers. It also will not be used as a generation service to serve customers through a purchased power agreement, as is the case under the current ESP.⁴⁰ Thus, the PPAR will not have the effect of stabilizing or making more certain retail electric service in a physical sense.

Likewise, it will not have the effect of stabilizing or making more certain retail electric service in an economic sense; if anything, it will make prices less stable and more uncertain. As proposed, the PPAR will increase or decrease all customers' bills by some amount that is currently unknown.⁴¹ AEP-Ohio will provide the Commission an estimate of the PPAR "near" the start of the ESP planning year.⁴² That estimate will be

³⁸ AEP-Ohio Ex. 7 at 10.

³⁹ Tr. Vol. II at 566-67.

⁴⁰ See discussion below regarding the recovery of power purchase costs of OVEC under the current ESP.

⁴¹ Tr. Vol. XI at 2594.

⁴² Tr. Vol. I at 109-10.

in effect for twelve months. As the next twelve-month period nears, AEP-Ohio will provide a new estimate of the difference between the PJM revenue it expects to receive and the amounts it will be billed by OVEC and an estimate of the over or under-recovery based on the prior year's receipts from PJM and the costs billed by OVEC. As the actual costs of the OVEC generation move significantly up and down depending on multiple factors which are not predictable (such as weather, forced outages, and general economic conditions), the actual value of the PPAR in any planning year is itself unknowable.⁴³ As Dr. McDermott admitted during cross-examination, the design of the PPAR will inject additional volatility into the prices shopping and nonshopping customers will see in their electric bills if the Commission authorizes the PPAR.⁴⁴

Thus, AEP-Ohio has not demonstrated that the PPAR can be authorized under R.C. 4928.143(B)(2)(d). Of the three requirements that must be demonstrated to support authorization under this division, AEP-Ohio has shown only that the PPAR is a charge. It has not demonstrated that the charge addresses any of the subjects covered by this division or that the charge will stabilize or make more certain retail electric service. In fact, one of its witnesses concedes that the PPAR will inject more uncertainty into retail prices.

R.C. 4928.143(B)(2)(e) authorizes automatic increases and decreases in any component of the SSO price. The PPAR is proposed to be a nonbypassable charge designed to assure that AEP-Ohio is held harmless from the wholesale price risk of the OVEC Entitlement. By its terms, the rider does not increase or decrease automatically

⁴³ Tr. Vol. II at 544-49.

⁴⁴ Tr. Vol. XIII at 3141.

any component of the SSO price. Thus, R.C. 4928.143(B)(2)(e) does not provide a basis to authorize the PPAR.

R.C. 4928.143(B)(2)(f) provides for provisions related to the securitization of a phase-in and recovery of the electric distribution utility's ("EDU") cost of securitization. By its terms, the PPAR is unrelated to a securitization.

R.C. 4928.143(B)(2)(g) provides for provisions relating to transmission, ancillary, congestion, or any related service required for the SSO. As previously noted, the charge or credit provided by the PPAR is unrelated to the services required by the SSO. Thus, the PPAR will not be "required" for the SSO. Further, the charge or credit to customer bills resulting from the PPAR is unrelated to transmission, ancillary, congestion, or a related service; instead, the charge or credit is the difference between what AEP-Ohio is billed by OVEC and what AEP-Ohio recovers when it liquidates the capacity and energy associated with the OVEC Entitlement into the PJM markets. Accordingly, R.C. 4928.143(B)(2)(g) does not provide a basis to authorize the PPAR.

R.C. 4928.143(B)(2)(h) authorizes provisions related to the EDU's distribution service. By its terms, the PPAR is unrelated to the EDU's distribution service although AEP-Ohio has proposed that the credit or charge be assessed on a nonbypassable basis. Accordingly, the PPAR is not a provision that the Commission may authorize under R.C. 4928.143(B)(2)(h).

R.C. 4928.143(B)(2)(i) provides for provisions under which the EDU may implement economic development, job retention, and energy efficiency programs. AEP-Ohio indicated that OVEC has a positive economic effect on certain counties

surrounding the OVEC Ohio-based facilities,⁴⁵ but Mr. Vegas conceded that the regional benefits of the OVEC generation located in Ohio would not be affected if the Commission denied authorization of the PPAR.⁴⁶ Thus, the rider is unrelated to economic development or job retention. Additionally, AEP-Ohio specifically sought to continue an existing rider, the Economic Development Rider, which is designated to recover economic development and job retention costs.⁴⁷ Likewise, the rider does not recover costs associated with AEP-Ohio's compliance with mandated energy portfolio requirements. (AEP-Ohio sought the continuation of two specific riders, the Alternative Energy Rider and the Energy Efficiency and Peak Demand Reduction Rider, to recover the costs of implementing its programs to comply with state-mandated alternative energy, peak demand reduction, and energy efficiency requirements.⁴⁸) Accordingly, R.C. 4928.143(B)(2)(i) does not provide the Commission a basis to authorize the PPAR.

As this discussion demonstrates, the PPAR is not a provision authorized under R.C. 4928.143(B). Because it is not authorized by a specific provision, the Commission may not lawfully authorize the rider.⁴⁹

B. Authorization of the PPAR would violate R.C. 4928.02(H)

R.C. 4928.02(H) provides that it is the policy of the State to ensure effective competition in the provision of retail electric service by avoiding anticompetitive subsidies flowing from a noncompetitive retail electric service to a competitive retail electric service or a product or service other than retail electric service or vice versa.

⁴⁵ AEP-Ohio Ex. 7 at 9.

⁴⁶ Tr. Vol. I at 40.

⁴⁷ AEP-Ohio Ex. 1 at 13.

⁴⁸ *Id.* at 9 & 13

⁴⁹ *In re Columbus S. Power Co.*, 128 Ohio St.3d 512 (2011).

Additionally, R.C. 4928.02(H) prohibits the recovery of any generation-related costs through distribution or transmission rates.⁵⁰

Authorization of the PPAR would result in an anticompetitive subsidy to or from a noncompetitive retail electric service from or to a service other than retail electric service. As proposed, the PPAR would require all retail distribution customers to incur a charge or credit designed to collect the difference of AEP-Ohio's costs and wholesale revenue related to the OVEC Entitlement. When the difference is a charge, AEP-Ohio would recover the costs of the OVEC Entitlement that exceed the market prices for the entitlement, a subsidy to AEP-Ohio. When the difference is a credit (as unlikely as that may be), retail customers would receive a subsidy of any wholesale revenue from the OVEC Entitlement that exceeds AEP-Ohio's costs. "In either case, the result runs afoul of Ohio's pro-competitive policies and law."⁵¹

A rejection of the request to authorize the PPAR would be consistent with the Commission's application of R.C. 4928.02(H) when it dismissed AEP-Ohio's application to recover plant closure costs for the Sporn 5 Unit. To collect the closure costs, AEP-Ohio sought a nonbypassable charge.⁵² In its Finding and Order dismissing the application, the Commission concluded that no provision of R.C. 4928.143 authorized a rider to recover the plant closure costs and further held that "[a]pproval of such a charge

⁵⁰ *Elyria Foundry Co. v. Pub. Util. Comm'n of Ohio*, 114 Ohio St.3d 305 (2007).

⁵¹ IEU-Ohio Ex. 1B at 15.

⁵² *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 1-2 (Jan. 11, 2012).

would effectively allow [AEP-Ohio] to recover competitive, generation-related costs through its noncompetitive, distribution rates, in contravention of [R.C. 4928.02(H)].”⁵³

Authorization of the PPAR would trigger a violation similar to that presented by AEP-Ohio’s application to recover the closure costs of Sporn 5 through a nonbypassable rider. The PPAR would authorize AEP-Ohio to recover the difference of the generation-related costs that OVEC charges AEP-Ohio under the ICPA (even though those costs do not provide generation service to the customers of AEP-Ohio) and the wholesale capacity and energy revenues that AEP-Ohio receives from PJM. The recovery of the charge through a nonbypassable rider would result in a charge that is the same as a distribution charge; it would be applicable to all customers just as a distribution charge is. As a result, the recovery of the incremental energy and capacity costs related to the OVEC Entitlement through a nonbypassable charge would contravene the prohibition of the recovery of generation-related costs through a “distribution-like” rider contained in R.C. 4928.02(H).

C. Authorization of the PPAR would violate the prohibition of recovery of transition revenue or its equivalent contained in R.C. 4928.38 and AEP-Ohio’s ETP Stipulation

An EDU had a single opportunity to collect transition revenue from customers, but it was required to demonstrate it had transition costs. Further, the EDU had a limited period during which it could collect transition revenue. AEP-Ohio sought but gave up any claims it may have had to secure generation-related transition revenue through its settlement of its ETP. Nonetheless, AEP-Ohio is seeking to recover additional transition revenue through the PPAR when the revenues it recovers from

⁵³ *Id.* at 19.

PJM are less than the amounts it pays OVEC. Because AEP-Ohio has not presented a claim for transition revenue that complies with the statutory requirements, the time for such a claim has expired, and AEP-Ohio has stipulated that it will not seek generation-related transition revenue, the Commission cannot lawfully authorize the PPAR.

Amended Substitute Senate Bill 3 (“SB 3”) provided an EDU with a single opportunity to secure transition revenue. Within 90 days of adoption of SB 3, an EDU was required to file an ETP.⁵⁴ As part of that plan, it could request transition revenue.⁵⁵ Before authorizing collection of any transition revenue, the Commission had to find that the EDU had transition costs. The EDU was required to prove that the claimed transition costs were “prudently incurred,” “legitimate, net, verifiable, and directly assignable or allocable to retail electric generation service provided to electric consumers in this state,” and “unrecoverable in a competitive market,” and that the EDU “would otherwise be entitled an opportunity to recover the costs.”⁵⁶

If the Commission determined that the EDU had a legitimate claim to transition revenue, it could authorize the collection of transition revenue for a finite period. For certain transition cost recovery, the period was defined by the Market Development Period (“MDP”) that could not extend beyond 2005.⁵⁷ For transition costs identified as regulatory assets, the collection period could not extend beyond 2010.⁵⁸ R.C. 4928.141, enacted as part of Amended Substitute Senate Bill 221 (“SB 221”), precluded any further recovery of transition costs “effective on and after the date that the

⁵⁴ R.C. 4928.31(A).

⁵⁵ *Id.*

⁵⁶ R.C. 4928.39.

⁵⁷ *Id.*

⁵⁸ *Id.*

allowance is scheduled to end under the utility's rate plan."⁵⁹ The Commission cannot lawfully "authorize the receipt of transition revenues or any equivalent revenues by an electric utility except as expressly authorized in sections 4928.31 to 4928.40 of the Revised Code."⁶⁰ "With the termination of that approved revenue source, the utility [was to] be fully on its own in the competitive market."⁶¹

AEP-Ohio sought to recover transition revenue under SB 3 when it filed its ETP in 1999. The application was resolved by a stipulation ("ETP Stipulation"), and AEP-Ohio agreed to forgo collecting above-market transition revenue associated with its generation assets.⁶²

If the Commission authorizes the PPAR, AEP-Ohio would collect additional transition revenue or its equivalent when the PPAR is a charge to customers. The charge to customers would be based on the difference between what AEP-Ohio receives from PJM for wholesale power and capacity and the amounts billed to it by OVEC under the ICPA.⁶³ The PJM revenues are determined by the market-based prices established by the PJM tariffs. When the OVEC Entitlement costs exceed the market-based revenue, the difference is "the costs ... unrecoverable in a competitive market."⁶⁴ As Dr. McDermott explained in a different context, these above-market costs are "stranded" because AEP-Ohio's investment cannot be recovered through market

⁵⁹ R.C. 4928.141.

⁶⁰ R.C. 4928.38.

⁶¹ *Id.*

⁶² IEU-Ohio Ex. 1B at 16.

⁶³ *Id.*

⁶⁴ R.C. 4928.39(C).

prices.⁶⁵ AEP-Ohio would then recover these stranded costs through the PPAR. The PPAR, thus, would permit AEP-Ohio to recover transition revenue or its equivalent.

R.C. 4928.38 bars the Commission from authorizing transition revenue or its equivalent in two respects. First, the Commission may authorize the recovery of transition revenue only if AEP-Ohio complies with R.C. 4928.31 to 4928.40. In particular, R.C. 4928.39 and 4928.40 provided detailed requirements for the authorization of transition revenue, none of which AEP-Ohio sought to satisfy in its Application and related testimony. Second, the time by which the authorization of transition revenue or its equivalent may be authorized and collected has expired even if the evidence presented by AEP-Ohio were found to comply with the requirements of R.C. 4928.39 and 4928.40. The MDP ended no later than December 31, 2005. The period for recovery of regulatory assets ended no later than December 31, 2010. Thus, a claim for transition revenue is time-barred.

Likewise, the AEP-Ohio ETP Stipulation bars recovery of generation-related transition revenue. AEP-Ohio specifically agreed to forgo any further recovery of generation-related transition revenue when it entered the ETP Stipulation. Its Application in this case, however, seeks to recover above-market generation-related costs of OVEC through the PPAR. That request is barred by AEP-Ohio's prior agreement.

D. Authorization of the PPAR would exceed the Commission's jurisdiction under state law because it increases AEP-Ohio's compensation for wholesale electric services

⁶⁵ Tr. Vol. XIII at 3148-49.

By Commission order, AEP-Ohio will liquidate the OVEC Entitlement into the PJM wholesale markets. As a result, AEP-Ohio is not providing any of the capacity or energy associated with the OVEC Entitlement to its retail customers. The PPAR, if authorized, would then adjust AEP-Ohio's compensation from the OVEC Entitlement through either a charge or credit. Because the PPAR would adjust the compensation AEP-Ohio receives for wholesale electric service, the Commission has no authority to authorize the PPAR under state law.

The Commission's jurisdiction to regulate an EDU such as AEP-Ohio is governed by Chapters 4905, 4909, and 4928. For example, the Commission's jurisdiction under Chapter 4905 and 4909 is defined by R.C. 4905.02.⁶⁶ R.C. 4905.02 provides that a "public utility" includes every corporation, company, copartnership, person, or association, the lessees, trustees, or receivers of the foregoing, defined in section 4905.03 of the Revised Code." R.C. 4905.03 then provides a list of the types of public utilities subject to the Commission's jurisdiction:

As used in this chapter, any person, firm, copartnership, voluntary association, joint-stock association, company, or corporation, wherever organized or incorporated, is:

...
(C) An electric light company, when engaged in the business of supplying electricity for light, heat, or power purposes to consumers within this state, including supplying electric transmission service *for electricity delivered to consumers in this state*, but excluding a regional transmission organization approved by the federal energy regulatory commission. (Emphasis added.)

The same definition extends to the Commission's jurisdiction under Chapter 4928.⁶⁷ This definition specifically limits the Commission's jurisdiction over electric light

⁶⁶ See R.C. 4909.01(B).

⁶⁷ See, e.g., R.C. 4928.01(A)(6)& (7) & 4928.05(A) (defining the Commission's jurisdiction to supervise and regulate competitive and noncompetitive retail electric service supplied by an electric utility).

companies, including EDUs, to instances in which a retail service is being provided, *i.e.* electricity is being supplied “to consumers.” R.C. 4905.03(C) also exempts regional transmission organizations (“RTOs”), such as PJM, from the definition of an electric light company. By definition, therefore, the jurisdiction of the Commission does not extend to wholesale electric services.

The PPAR would operate to adjust AEP-Ohio’s compensation for wholesale electric services by increasing or decreasing the compensation it receives from PJM to match the costs AEP-Ohio is charged by OVEC. Because Ohio law limits the Commission’s jurisdiction to set charges for a service of an electric light company to electricity being supplied to consumers in Ohio, the Commission’s jurisdiction does not extend to establishing a charge or credit to adjust AEP-Ohio’s compensation for wholesale electric services. Accordingly, and in addition to the constitutional bar that prevents the Commission from authorizing the PPAR discussed in the next section, the Commission is without authority under Ohio law to authorize the PPAR.

E. Authorization of the PPAR is preempted by the Federal Power Act

Even if the Commission was authorized to adjust AEP-Ohio’s compensation for a wholesale service by Ohio law, Commission action increasing AEP-Ohio’s total compensation for a wholesale electric service is preempted by the FPA.

Under the Supremacy Clause of the United States Constitution, state legislation and regulating authority may be preempted: (1) if Congress, in enacting a federal statute, has expressed a clear intent to preempt state law; (2) if it is clear, despite the absence of explicit preemptive language, that Congress has intended, by legislating comprehensively, to occupy an entire field of regulation and has left no room for the

states to supplement the federal law; or (3) if compliance with both state and federal law is impossible or when compliance with state law stands as an obstacle to the accomplishment and execution of the full purposes and objectives of the federal policies embodied in the laws at issue.⁶⁸

Two recent federal district court decisions demonstrate that attempts by states to increase the compensation of a generation owner for wholesale capacity and energy services are preempted because they invade a field of regulation within the exclusive authority of FERC. In the first decision, *PPL Energyplus, LLC v. Nazarian*,⁶⁹ a federal district court in Maryland reviewed an order of the Maryland Public Service Commission ("Maryland Commission") that increased compensation for the provision of wholesale electric services of an entity that was seeking to construct a generation plant ("Generation Owner"). In the challenged order, the Maryland Commission directed the incumbent local electric utilities to enter into contracts with the Generation Owner. The contracts would have required the local electric utilities to pay the Generation Owner the difference between what the Generation Owner received for market-based sales of capacity and energy to PJM and a contract price established by the Maryland Commission based on the cost of construction and operation of the plant for twenty years. Any loss or gain that the local electric utilities incurred under the contracts ordered by the Maryland Commission was to be passed on to Maryland ratepayers by the local electric utilities.⁷⁰ The federal court concluded that the Maryland Commission's order fixed the monetary value of wholesale generation-related capacity and energy

⁶⁸ *Marketing Research Services, Inc. v. Pub. Util. Comm'n of Ohio*, 34 Ohio St.3d 52, 55 (1987).

⁶⁹ Case No. 1:12-cv-01286-MJG at 84-86, 2013 WL 5432346 *30 (D.MD Sept. 30, 2013) ("*PPL I*"), *aff'd*, *PPL Energy Plus, LLC et al. v. Nazarian*, Case No. 13-2419, Slip Op. (4th Cir. June 2, 2014).

⁷⁰ *Id.* at *33-*34.

services provided by the Generation Owner.⁷¹ As a result, the court held that the Maryland Commission's order was preempted because the Commission was without authority to establish the price for wholesale energy and capacity sales.⁷² Based on the Court's determination that FERC has exclusive authority in that field and has fixed the price for wholesale energy and capacity sales in the PJM markets as the market-based price produced by the auction processes approved by FERC and utilized by PJM, the Court declared the action of the Maryland Commission to be preempted.⁷³ In the opinion affirming the decision of the district court, the Fourth Circuit Court of Appeals agreed that the Maryland Commission was preempted because the field of wholesale energy prices was exclusively within the jurisdiction of FERC.⁷⁴

In *PPL Energy Plus, LLC, et al., v. Robert M. Hanna, et al.*,⁷⁵ a federal district court in New Jersey reached the same result, concluding that state legislation that attempted to encourage the construction of new generation plants by guaranteeing a price of capacity to the builder was preempted. In the New Jersey case, the state legislature passed legislation "to provide a transaction structure that would result in new power plants being constructed in the PJM territories that benefit New Jersey."⁷⁶ The law authorized the New Jersey Board of Public Utilities ("Board") to issue an SSO capacity agreement and directed the state's four EDUs to enter into contracts with

⁷¹ *Id.* at *34.

⁷² *Id.* at *35.

⁷³ *Id.* at *42.

⁷⁴ *PPL Energy Plus, LLC et al. v. Nazarian*, Case No. 13-2419, Slip Op. (4th Cir. June 2, 2014). It also found that the Maryland Commission's order was preempted because it conflicted with the accomplishment of federal policies. *Id.*, Slip Op. at 25.

⁷⁵ Civ. Action No. 11-745, 2013 WL 5603896 at *19 (D.N.J. Oct. 11, 2013) ("*PPL II*"),

⁷⁶ *Id.*

generators to pay any difference between the Reliability Pricing Model-Based Price and the development costs of the generators that the Board approved.⁷⁷ Like the Maryland federal court, the New Jersey federal court found that the New Jersey legislation was preempted because the FPA occupied the field of wholesale electricity sales, including the price at which electricity is sold at wholesale.⁷⁸ Based on its finding that the state law was preempted, the federal court declared the statute under which the Board had authorized above-market payments to the generator “null and void.”⁷⁹

An order approving the PPAR likewise would be preempted by federal law. Because AEP-Ohio is liquidating the OVEC Entitlement into the PJM markets, AEP-Ohio recovers FERC-approved wholesale capacity and energy revenues from PJM. If the PPAR is authorized, however, it is guaranteed to recover the costs of the OVEC Entitlement under the ICPA. Like the mechanisms the federal courts in Maryland and New Jersey held were preempted, the PPAR would make up the difference between the revenue that AEP-Ohio projects it will receive based on FERC-approved tariffs and the amounts it is billed by OVEC. (Also, like the Maryland Commission, the Commission would be authorizing AEP-Ohio to shift the revenue responsibility of the shortfall to customers from AEP-Ohio’s sole shareholder.) Through the same sort of mechanisms the Maryland and New Jersey courts held were preempted by the FPA, the PPAR would increase the compensation for wholesale generation-related capacity and energy services AEP-Ohio receives. Because wholesale electricity compensation is within the

⁷⁷ *Id.*

⁷⁸ *Id.* at *35.

⁷⁹ *Id.* at *38.

exclusive jurisdiction of FERC, however, the Commission is preempted from authorizing the PPAR.

F. The “hedge” is either, directionally, a potentially substantial cost or no benefit to customers and will fail to “hedge” the volatility of generation-related prices or charges resulting from other provisions of the proposed ESP

AEP-Ohio states repeatedly that the reason for authorizing the PPAR is that it will benefit customers as a hedge to the volatility of market-based prices for electricity.⁸⁰ Further, it claims that the PPAR will not have any negative effect on the generation market since the power will not be offered in the auctions.⁸¹ The record does not support any of these claims.

Although AEP-Ohio claims customers will see an \$8 million benefit if the PPAR is authorized, it is more likely that customers will incur a substantial cost in the range of \$82 million (AEP-Ohio’s initial estimate) to \$116 million (OCC’s estimate that corrects several errors in AEP-Ohio’s initial estimate) during term of the proposed ESP. Even if AEP-Ohio is correct that customers may realize an \$8 million benefit, the hedge will be 7¢/MWh over the entire term of the proposed ESP.⁸² At that insignificant level, the PPAR will not provide customers a hedge against market volatility.

More importantly, AEP-Ohio failed to demonstrate that customers will realize even the 7¢ benefit. The claim is based on the costs of OVEC generation being stable,⁸³ but OVEC costs can vary significantly from year to year. One recent report indicates that OVEC costs shifted 24% due to a change in output from 2011 to 2012,

⁸⁰ See, e.g., AEP-Ohio Ex. 7 at 11.

⁸¹ *Id.* at 10.

⁸² AEP-Ohio Ex. 8A.

⁸³ AEP-Ohio Ex. 7 at 8.

and output is a function of several factors including weather, general economic conditions, and lower energy prices.⁸⁴ AEP-Ohio concedes that it does not know how weather, economic conditions, or low power prices individually affect OVEC output.⁸⁵ On this record, AEP-Ohio cannot credibly claim that OVEC costs are relatively stable or could be expected to be so.

Further, the 7¢ solution on which AEP-Ohio relies is premised on OVEC cost reductions,⁸⁶ but those reductions are speculative. OVEC has not committed to those reductions, and AEP-Ohio makes no commitment to customers to flow-through the alleged customer benefit if OVEC fails to deliver the cost reductions.⁸⁷ Moreover, the cost reductions may have no effect on the costs charged to the OVEC Sponsoring Companies because other unrelated costs may increase.⁸⁸

Additionally, AEP-Ohio has a poor (and for customers unfavorable) recent record when it projects expected costs of its riders. In the 2012 and 2014 proceedings to adjust its rider to recover transmission costs, for example, it indicated that its prior projections were \$36 million and \$57 million too low.⁸⁹ After AEP-Ohio's recent failures

⁸⁴ IEU-Ohio Ex. 1B at Ex. KMM-3, page 2.

⁸⁵ Tr. Vol. II at 544-45.

⁸⁶ Tr. Vol. XI at 2603-04.

⁸⁷ Tr. Vol. II at 552.

⁸⁸ Tr. Vol. III at 749-50.

⁸⁹ See *In the Matter of the Application of Ohio Power Company to Update its Transmission Cost Recovery Rider*, Case No. 12-1046-EL-RDR, Application (June 15, 2012) (requesting a reconciliation adjustment of \$36 million); *In the Matter of the Application of Ohio Power Company to Update its Transmission Cost Recovery Rider Rates*, Case No. 14-1094-EL-UNC, Application (June 16, 2014) (identifying an under-recovery of \$57 million). AEP-Ohio's forecast of residential participation in shopping also missed the actual outcome by a substantial amount. Compare *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 Section 4928.143, Revised Code, in the Form of an Electric Security Plan*, Case Nos. 11-346-EL-SSO, et al., Opinion and Order at 34 (Aug 8, 2012) ("ESP II") (residential shopping estimated to be 65%) with AEP-Ohio Ex. 7 at 13 (residential shopping is 30%).

in estimating such things as transmission costs, it would be an act of faith for the Commission to accept future estimates of the “benefit” to customers of the PPAR.

Moreover, AEP-Ohio itself demonstrated little faith in its estimate that the ESP will provide a financial benefit to customers. At least one of the estimates was available to it when it filed its ESP (the one showing that the PPAR would result in a \$52 million cost to customers was prepared in August 2013, several months before AEP-Ohio filed the Application).⁹⁰ AEP-Ohio recognized that the cost of the rider would be unique to the ESP in the ESP v. MRO Test, but it did not include a value for the PPAR in the ESP side of the test.⁹¹ AEP-Ohio also did not provide a value for the PPAR in its bill comparisons.⁹² According to Mr. Roush, AEP-Ohio’s witness on the bill comparisons, Mr. Allen indicated that the value of the rider could be positive or negative and directed Mr. Roush to use a value of zero to account for the effects of the PPAR in preparing the bill comparisons.⁹³ Thus, it is apparent that AEP-Ohio was unwilling to stand behind its claim that the PPAR will provide a financial benefit to customers until Mr. Allen decided to recalculate the alleged benefits on the first day of the hearing and offer his revision on the second day of hearing.⁹⁴

In contrast to its late found reliance on the 7 cent solution, AEP-Ohio initially provided three projections. According to AEP-Ohio, a reason for choosing one projection over another is the vintage of the data; the one relied upon by AEP-Ohio for

⁹⁰ Tr. Vol. II at 494.

⁹¹ AEP-Ohio Ex. 7 at 5.

⁹² Tr. Vol. III at 930.

⁹³ Tr. Vol. III at 930.

⁹⁴ Tr. Vol. II at 484.

its 7 cent solution is based on more recently available information.⁹⁵ AEP-Ohio, however, concedes that each of the projections is “reasonable” and that each will be wrong.⁹⁶ If there is some direction to the projections, however, it is clear that in each instance the projections indicate in the near term that the PPAR would result in a charge to customers.⁹⁷ Only if the Commission takes a longer view do the projections begin to indicate that customers may see a benefit from the PPAR.⁹⁸

In addition to the fact that the PPAR will likely result in a substantial additional charge to consumers, the “hedging” effect of the PPAR, if any, may be offset by the over and under-recovery accounting that AEP-Ohio proposes to assure it does not face any price risk associated with the OVEC Entitlement. As proposed, AEP-Ohio will annually adjust the PPAR for prior under and over-recoveries of the charge or credit. Adjustments to the PPAR due to under or over-recoveries may be in either direction and could be greater or less than the charge or credit for the next year based on the estimate of the expected PJM revenues and OVEC costs. Whether large or small, however, the adjustments would be the result of the missed estimates from the prior year and have nothing to do with the price of generation service in the coming year. As a result, whatever hedge might be inherent in the design of the PPAR may be offset by under or over-recovery accounting.

Moreover, the hedge would not address the volatility in customer charges that would result from the collection of riders that would make up a customer’s total bill. The

⁹⁵ Tr. Vol. II at 498.

⁹⁶ Tr. Vol. I at 110.

⁹⁷ IEU-Ohio Ex. 1B at Ex. KMM-5, KMM-6, & KMM-7.

⁹⁸ See OEG Ex. 3 *passim*; Tr. Vol. XI at 2591.

proposed ESP contains up to 23 riders, many of them nonbypassable.⁹⁹ Most of those riders adjust for costs that are unrelated to the market prices of generation-related services.¹⁰⁰ With regard to a substantial portion of either a shopping and nonshopping customer's bill, therefore, the "hedge" is meaningless because the riders make the total bill volatile regardless of the effect of the "hedge" provided by the PPAR.

The record thus demonstrates that AEP-Ohio's claim that the PPAR will be a benefit to customers is wrong: either the 7 cent solution provides little benefit or hedge, or, more likely, the PPAR is a substantial cost to customers. Further, the PPAR will likely be ineffective because the design of the PPAR will account for historic over and under-recoveries. It will also be ineffective because the total customer bill is made up of up to 23 riders that inject additional volatility unrelated to generation-related costs or prices the PPAR is supposedly designed to hedge.

⁹⁹ AEP-Ohio Ex. 13 at Ex. AEM-1.

¹⁰⁰ Tr. Vol. I at 107-08.

G. The PPAR is not necessary to support AEP-Ohio's financial well-being and does not serve or advance market-based outcomes

In his testimony, Mr. Vegas stated that the proposed ESP “will provide for AEP Ohio’s financial stability as shown in the *pro forma* financial projections provided in witness Kyle’s workpapers, and is critical to AEP Ohio’s financial stability during the ESP III term.”¹⁰¹ The anticipated financial performance reflected in the *pro forma* financial statements, however, does not include any allowance for the PPAR because the rider would be earnings neutral for AEP-Ohio; it would permit AEP-Ohio to recover fully its cost of the OVEC Entitlement.¹⁰² AEP-Ohio, moreover, did not provide any evidence of the effect on its earnings if the Commission did not authorize the PPAR. As a result, AEP-Ohio has failed to demonstrate that the PPAR is required to support AEP-Ohio’s financial stability.

Even if the Commission did consider AEP-Ohio’s expected financial stability in the abstract (which is all the Commission can do since AEP-Ohio failed to indicate what effect an ESP without the PPAR would have on revenue or earnings), the Commission should also account for the fact that AEP-Ohio is performing exceptionally well as a wires company under ESP II. (Some care must be taken with this comparison of the effects of the ESP II financial results and those projected by AEP-Ohio under ESP III because AEP-Ohio is benefiting from the challenged Retail Stability Rider, a substantial portion of which goes to support a revenue target.¹⁰³) AEP-Ohio receives at least full

¹⁰¹ AEP-Ohio Ex. 2 at 3.

¹⁰² Tr. Vol. I at 84; Tr. Vol. IV at 1172-73.

¹⁰³ *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 Section 4928.143, Revised Code, in the Form of an Electric Security Plan*, Case Nos. 11-346-EL-SSO, *et al.*, Opinion and Order at 26-38 (Aug. 8, 2012) (“ESP II”).

cost recovery for the purchased power it receives from OVEC.¹⁰⁴ Because it receives full cost recovery of its OVEC purchased power agreement, the OVEC Entitlement currently is at least revenue neutral as well. (Because there is an indication that purchased power costs may be double-recovered, AEP-Ohio may be over-recovering its OVEC-related costs. That matter is currently under investigation in an AEP-Ohio fuel cost audit.) As a result of current approved rates, AEP-Ohio as a wires company secured a 13.1% return on equity from its regulated operations.¹⁰⁵ AEP-Ohio provided American Electric Power (“AEP”) 29% of its total system revenues.¹⁰⁶ Of the \$97 million in first quarter 2014 net income reported by AEP, AEP-Ohio contributed \$61 million.¹⁰⁷ Under current rates, AEP-Ohio has no fear of financial instability, and there is no evidence that its financial stability will be adversely affected if the Commission refuses to authorize the rider as noted above.

The Commission, moreover, should not consider authorizing the PPAR as a means of providing AEP-Ohio with financial stability. As of January 1, 2014, AEP-Ohio (but for the OVEC Entitlement) has divested its generation assets and is a wires

¹⁰⁴ *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.*, Opinion and Order at 14 (Mar. 18, 2009). As a result of the orders in the ESP II case, the Commission continued the existing fuel adjustment clause. *ESP II*, Opinion and Order at 16 (Aug. 8, 2012). In a proceeding to implement the orders requiring the blending of energy purchased at auction to serve the SSO, the Commission approved a provision in the fuel adjustment clause that permits AEP-Ohio to recover the OVEC demand costs. *In the Matter of the Application of Ohio Power Company to Establish a Competitive Bidding Process for Procurement of Energy to Support its Standard Service Offer*, Case No. 12-3254-EL-UNC, Opinion and Order at 15-16 (Nov. 13, 2013). There is an ongoing investigation as to whether AEP-Ohio may be double-recovering its demand-related costs associated with OVEC. *In the Matter of the Application of the Fuel Adjustment Clauses for Columbus Southern Power Company and Ohio Power Company and Related Matters*, Case No. 11-5906-EL-FAC, *et al.*, Entry (May 21, 2014) (appointment of auditor to review fuel adjustment clauses for double-recovery).

¹⁰⁵ Tr. Vol. I at 86; IEU-Ohio Ex. 3 at 4.

¹⁰⁶ Tr. Vol. I at 93.

¹⁰⁷ Tr. Vol. I at 91.

company.¹⁰⁸ As a wires company, it may seek to increase its distribution rates through the traditional rate making process if its return on investment in distribution assets is insufficient. It can seek relief through FERC if its transmission asset returns on investment are insufficient. As a wires company, therefore, AEP-Ohio has the opportunity to secure regulatory relief if it believes that its rates do not afford it a sufficient return on investment to satisfy its sole shareholder.

Furthermore, reliance on the Commission to protect an interest voluntarily retained by AEP-Ohio in the OVEC Entitlement (see discussion below regarding the choice AEP-Ohio has made to retain the OVEC Entitlement) is not supported by the provisions of Chapter 4928 discussed above, and it also makes no sense in light of the fact that the financial stability of AEP-Ohio's remaining "generation" business is no longer an issue the Commission should address in an ESP case. As the Staff succinctly explained:

Since AEP Ohio will no longer be in the business of selling electricity after May 31, 2015, Staff does not see a need for granting a PPA rider that is tied to electric generation. None of the MWs coming out of AEP Ohio's interests in the OVEC generation is being sold to AEP Ohio's distribution customers. It took over a decade for the Commission to transition the four Ohio EDUs to a fully competitive retail electricity market. Granting a PPA rider is a move in the opposite direction.¹⁰⁹

Yet, AEP-Ohio is seeking a Commission order imposing a regulatory solution, the PPAR, to protect AEP-Ohio from the wholesale price risk of the OVEC Entitlement that it voluntarily retains. In doing so, as Dr. McDermott made clear, AEP-Ohio is asking the Commission to decide for customers how important rate stability is and whether to keep

¹⁰⁸ Tr. Vol. I at 83-84.

¹⁰⁹ Staff Ex. 18 at 9.

the option open to buy additional price certainty for consumers.¹¹⁰ (Dr. McDermott's statement assumes that the PPAR works as a hedge. As discussed above, that assumption is unsupported.) The Commission, however, already has a clear directive from the General Assembly that customers should decide the level of market risk they are willing to absorb. It is the policy of the State to ensure the availability of unbundled and comparable retail electric service that provides consumers with the supplier, price, terms, conditions, and quality options they elect to meet their respective needs.¹¹¹ In keeping with that policy, it is not the Commission's job to substitute its judgment of "how important rate stability is for retail customers."

In particular, the one-size-fits-all (and applicable-to-all) solution offered by AEP-Ohio to address price stability is fundamentally inconsistent with the diversity of customer needs and expectations. As Dr. McDermott explained in his 2008 report for Compete Coalition, customers have varying degrees of risk tolerance and expectations. It is the market, not a "plain vanilla" regulatory solution, that provides the customer with choices to meet those expectations. If the customer wants a product that hedges price risk, competitive retail electric service ("CRES") providers are providing those products through fixed-price contracts and budget control products; if the customer is less risk averse, it can agree to contracts that track daily market prices.¹¹² As Dr. McDermott concluded, "those jurisdictions that continue to support and promote competitive retail electric markets will benefit from the innovation and ingenuity of different suppliers as they compete to provide customers with the products and services that are best suited

¹¹⁰ AEP-Ohio Ex. 32 at 10.

¹¹¹ R.C. 4928.02(A) & (B).

¹¹² IEU-Ohio Ex. 16 *passim*; Tr. Vol. XIII at 3160-63.

to those customers.”¹¹³ In contrast to the market-based solution that is responsive to customer needs, the PPAR, as Dr. McDermott explained, would be a regulatory solution imposed by the Commission on customers for a “service” (which appears to be nonexistent because of the design of AEP-Ohio’s proposed PPAR and other rates) the customer may not want or does not need.¹¹⁴ The PPAR, thus, is the antithesis of the sort of market solutions provided by competitive suppliers that offer customers products and services best suited to them.

The PPAR also is anticompetitive. Because the PPAR would guarantee that AEP-Ohio would never be at risk for prices that are lower than the costs charged it by OVEC, AEP-Ohio would be immune from market price risk.¹¹⁵ Further, AEP-Ohio would look to only its affiliated unregulated generation company as a source for any additional PPAs if it sought to expand the “hedge.”¹¹⁶ In contrast, competitors are facing and will face price risk daily and hourly and do not have a regulatory backstop that AEP-Ohio would have if the PPAR is approved. Contrary to AEP-Ohio’s repeated assertions,¹¹⁷ the PPAR would place unregulated generation providers at a competitive disadvantage.

Further, recent weather events such as the “Polar Vortex” and regulatory events such as the notice of rulemaking by the U.S. Environmental Protection Agency do not provide any justification for the authorization of the PPAR as a means of improving the reliability or reducing the volatility of generation service prices. It is PJM’s role to assure

¹¹³ IEU-Ohio Ex. 16 at 3. On the issue of risk management, Dr. LaCasse similarly suggested that the regulated utility is not well-suited to address management of market risk; she indicated that risk management is better left to CRES providers and auction bidders that understand and have resources directed toward risk management. Tr. Vol. IV at 1148-49.

¹¹⁴ Tr. Vol. XIII at 3092.

¹¹⁵ Tr. Vol. XI at 2598.

¹¹⁶ Tr. Vol. I at 110-11.

¹¹⁷ See, e.g., Tr. Vol. II at 566; AEP-Ohio Ex. 7 at 10.

the reliability of service for the thirteen state region in which AEP-Ohio operates.¹¹⁸ To the extent that reliability was recently at risk due to January 2014 weather events, PJM not only “survived the storm,” but is addressing the effects of adverse weather conditions on system reliability and volatility of prices.¹¹⁹ Likewise, markets will adapt to address the volatility caused by events such as what occurred in January 2014.¹²⁰ The recent rulemaking proceedings by the U.S. Environmental Protection Agency regarding carbon dioxide emissions also are irrelevant to the Commission’s decision concerning authorization of the PPAR. While carbon dioxide emission regulation may affect electric generation resources in the future, any rules that emerge from the announcement will take several years before they may affect generation resources in the PJM region, and alternatives may replace the current proposal.¹²¹ AEP-Ohio did not provide evidence that the proposed rules may have some affect on availability of generation resources during the proposed ESP.

AEP-Ohio’s PPAR, therefore, should not be authorized for several reasons. It frustrates competition, violates state policy, and will increase price risk for those customers that are seeking to reduce volatility. Further, there is no demonstration that the PPAR can or would have any effect on reliability. Rather than providing a non-quantifiable benefit to customers, the PPAR would be harmful to them.

H. AEP-Ohio can avoid the market risk of the OVEC Entitlement by assigning its interest to a third party

¹¹⁸ Tr. Vol. XI at 2592.

¹¹⁹ Tr. Vol. XI at 2594; IEU-Ohio Ex. 15.

¹²⁰ Tr. Vol. XIII at 3152; IEU-Ohio Ex. 14 *passim*.

¹²¹ Tr. Vol. XI at 2600-02.

After AEP-Ohio failed to secure consent to transfer the OVEC Entitlement to its unregulated competitive affiliate, the Commission stated that AEP-Ohio could retain the asset until the Commission directed otherwise.¹²² AEP-Ohio has taken the Commission's decision to permit it to retain the OVEC Entitlement as an opportunity to protect itself from wholesale price risk. AEP-Ohio has no intention of taking any steps to assign the OVEC Entitlement until the Commission acts on the ESP application.¹²³ Customers, however, should not be required to hold AEP-Ohio harmless from the wholesale price risk of the OVEC Entitlement when AEP-Ohio may assign its interest in OVEC to a third party.

Although AEP-Ohio was unable to secure consent to transfer the OVEC Entitlement, it has additional options to assign the OVEC Entitlement that do not require consent of the Sponsoring Companies. Under Section 9.182 of the ICPA, it may assign the OVEC Entitlement to a Permitted Assignee.¹²⁴ A Permitted Assignee includes another Sponsoring Party or its affiliate with credit ratings that are investment grade.¹²⁵ The other operating companies of AEP have the required credit ratings.¹²⁶ Thus, AEP-Ohio could assign its interest to another AEP operating company.

Under Section 9.183 of the ICPA, AEP-Ohio also could assign its OVEC Entitlement to a third party with an investment grade credit rating and without further action on the part of the Sponsoring Companies so long as it provides the Sponsoring

¹²² *Corporate Separation Case*, Finding and Order at 9 (Dec. 4, 2013).

¹²³ Tr. Vol. II at 590.

¹²⁴ IEU-Ohio Ex. 1B at Ex. KMM-2, page 20-21; Tr. Vol. II at 579.

¹²⁵ IEU-Ohio Ex. 1B at KMM-2, page 4.

¹²⁶ Tr. Vol. II at 580-82.

Companies a right of first refusal and secures approval of counsel for OVEC.¹²⁷ Securing OVEC counsel's approval should not be a problem as AEP-Ohio shares its in-house attorneys with OVEC.¹²⁸ Therefore, AEP-Ohio could also assign its interest to an appropriate third party and relieve customers of the consequences associated with the OVEC Entitlement.¹²⁹

I. The Commission should modify the proposed ESP by removing the PPAR from the proposed ESP

As noted previously, Dr. McDermott testified that the authorization of the PPAR presents the Commission with a policy decision. The Commission, however, is a creature of statute and must exercise its "policy making" within the bounds of Ohio law regardless of the policy outcomes it may wish to pursue.¹³⁰

As discussed above, authorization of the PPAR is unlawful for several reasons. Initially, no provision of R.C. 4928.143(B) provides for authorization of the PPAR. Additionally, the rider is prohibited because its authorization would result in an unlawful subsidy and the collection of transition revenue (when the value of the PPAR results in a charge). The authorization of the PPAR also is outside the jurisdiction of the Commission; the Commission is jurisdictionally barred by both state and federal law from increasing or decreasing the compensation of AEP-Ohio for the liquidation of its OVEC Entitlement in the wholesale power markets.

Additionally, the authorization of the PPAR would be unreasonable. The record demonstrates that the PPAR would not and could not operate as a hedge as AEP-Ohio

¹²⁷ IEU-Ohio Ex. 1B at Ex. KMM-2, page 21-23.

¹²⁸ Tr. Vol. II at 591.

¹²⁹ IEU-Ohio Ex. 1B at 14.

¹³⁰ *Ohio Consumers' Counsel v. Pub. Util. Comm'n of Ohio*, 67 Ohio St.2d 153, 166 (1981).

claims. Additionally, accepting the claims AEP-Ohio has made to support the likely effects of the PPAR would be an act of faith, not a decision based on any solid evidence in the record of this case. Further, the authorization of the PPAR would be a retreat from the Commission's recent effort to require AEP-Ohio to divest its generation assets and is unnecessary as AEP-Ohio may assign the OVEC Entitlement to a third party. Accordingly, the Commission should not authorize the PPAR.

III. THE COMMISSION SHOULD REJECT AEP-OHIO'S PROPOSED NONBYPASSABLE BTCR

AEP-Ohio proposes to modify the current method by which transmission service is provided and costs are collected in its certified distribution service area. Currently, AEP-Ohio provides transmission services to only SSO customers.¹³¹ AEP-Ohio proposes to classify some transmission service as non-market-based, to provide only non-market-based transmission services, to provide those services to both nonshopping and shopping customers, and to collect the costs of providing those services through the nonbypassable BTCR.¹³² Market-based transmission services will be part of the SSO auction product supplied by the SSO auction winners to nonshopping customers.¹³³ CRES providers would supply market-based transmission services for shopping customers.¹³⁴

¹³¹ IEU-Ohio Ex. 1B at 27.

¹³² AEP-Ohio Ex. 1 at 12-13; IEU-Ohio Ex. 1B at 28. "Non-market based transmission charges" are identified by AEP-Ohio as the following items: ID# 1100 Network Integration Transmission Service; ID# 1108 Transmission Enhancement; ID# 1320 Transmission Owner Scheduling, System Control and Dispatch Service; ID# 1330 Reactive Supply and Voltage Control from Generation and Other Source Service; ID# 1450 Load Reconciliation for Transmission Owner Scheduling, System Control and Dispatch Service; ID# 2130 Firm Point-to-Point Transmission Service; and ID# 2140 Non-Firm Point to-Point Transmission Service. AEP-Ohio Ex. 15 at Att. F (highlighted items); see, also, IEU-Ohio Ex. 10.

¹³³ IEU-Ohio Ex. 1B at 28.

¹³⁴ *Id.*

According to AEP-Ohio, several reasons support authorization of the BTCR.¹³⁵ Initially, AEP-Ohio claims that the proposed changes will align AEP-Ohio's transmission recovery mechanism with those of other EDUs, which will enable CRES providers and SSO suppliers to operate and provide offerings in a similar manner in different regions of the State.¹³⁶ Additionally, Mr. Vegas testifies the change will result in shopping customers paying actual non-market-based transmission costs, rather than estimated transmission costs.¹³⁷ Because AEP-Ohio's justifications are without merit, the Commission should reject AEP-Ohio's proposed BTCR.

Additionally, the proposed nonbypassable BTCR could disrupt the contractual relationships between shopping customers and their CRES providers in AEP-Ohio's territory. Finally, the proposed nonbypassable BTCR conflicts with state policies because it will not send customers efficient price signals and will reduce customers' ability to obtain transmission service on "price, terms, conditions, and quality options they elect to meet their respective needs."

A. The BTCR will not result in uniformity of transmission pricing terms across the State

AEP-Ohio offers that the BTCR should be approved because it will align the treatment of transmission service across the four EDUs' service areas.¹³⁸ AEP-Ohio also suggests that this uniformity will allow CRES providers to operate and provide offerings in a similar manner in different regions of the State.¹³⁹ AEP-Ohio's proposed

¹³⁵ AEP-Ohio Ex. 2 at 12.

¹³⁶ *Id.*

¹³⁷ *Id.*

¹³⁸ IEU-Ohio Ex. 1B at 29.

¹³⁹ *Id.*

BTCR, however, will vary from each of the nonbypassable transmission riders in place for the other three EDUs.¹⁴⁰ Additionally, the other three EDUs have nonbypassable transmission riders that vary from each other.¹⁴¹ Accordingly, there will not be uniformity no matter what AEP-Ohio proposes.

Further, the amount of shopping that exists in AEP-Ohio's territory, as well as the service areas of the other EDUs, suggests that CRES providers have no difficulty operating in Ohio and providing offers to customers across the State despite the current differences that exist among transmission rate tariffs of the EDUs.

Accordingly, the proposed BTCR should be rejected because AEP-Ohio's claim that it will achieve uniformity across the State is incorrect.

B. The BTCR could disrupt the contractual relationship between shopping customers and their CRES providers

AEP-Ohio's proposed changes to the collection of transmission costs also could disrupt the contractual relationships between AEP-Ohio's customers that are presently shopping (that constitute the majority of AEP-Ohio's distribution sales) and their CRES providers. As previously noted, shopping customers presently pay for transmission and ancillary services in the prices they pay to their CRES providers. If the Commission approves AEP-Ohio's proposed BTCR, shopping customers could be required to pay twice for non-market-based transmission and ancillary services.

AEP-Ohio has acknowledged that shopping customers may be double-billed for the same transmission costs.¹⁴² FirstEnergy Solutions Corp.'s ("FES") Mr. D'Allesandris

¹⁴⁰ IEU-Ohio Ex. 10; Tr. Vol. IV at 1056-60.

¹⁴¹ IEU-Ohio Ex. 10.

¹⁴² IEU-Ohio Ex. 1B at 30.

also testified that to the extent a customer has a current fixed-price contract with FES, the fixed-price contract will continue if the BTCR is authorized.¹⁴³ Thus, AEP-Ohio's claim that approval of the proposed BTCR will "come at no cost to customers"¹⁴⁴ is simply inaccurate.

If the Commission approves the BTCR, shopping customers may be double-billed for transmission service unless the CRES provider takes affirmative steps to credit these shopping customers' bills. Accordingly, the proposed BTCR should be rejected because some shopping customers may be billed twice for non-market-based transmission service.

C. The proposed BTCR conflicts with the state policy of providing customers with the ability to negotiate price, terms, and conditions of service that meet their respective needs

Ohio law supports leaving non-market-based transmission charges bypassable. R.C. 4928.02(B) provides that it is the policy of the State to "[e]nsure the availability of unbundled and comparable retail electric service that provides consumers with the supplier, price, terms, conditions, and quality options they elect to meet their respective needs." The proposed BTCR removes customers' ability to "elect" the price, terms, conditions, and quality options for non-market-based transmission service.

It is common practice for customers receiving service from a CRES provider to structure their contracts to treat transmission and ancillary services costs (*i.e.* the costs

¹⁴³ Tr. Vol. VI at 1390-92. Mr. Campbell testified that when FirstEnergy's distribution utilities became responsible for providing Network Integration Transmission Service ("NITS") service in Pennsylvania, a service that had been provided by the competitive suppliers, Constellation credited customers with fixed contracts to remove the NITS cost that would be recovered from the utility. Mr. Campbell further testified that he thinks it would be appropriate to do the same thing if the BTCR is approved, but indicated that Constellation had not yet agreed to do that, nor was he in a position to bind the company. Tr. Vol. VII at 1577-79.

¹⁴⁴ AEP-Ohio Ex. 2 at 11.

AEP-Ohio wants to collect through the BTCR) as either a cost reflected in a fixed-price offer or a pass-through cost.¹⁴⁵ Either approach may be viewed as beneficial from a customer standpoint.¹⁴⁶ Under a fixed-price approach, the CRES provider is assuming the transmission pricing risk, and this risk transfer can be valuable to the customer.¹⁴⁷ When transmission and ancillary services are treated as a pass-through cost, the pass-through provides customers with the ability to proactively manage their usage and reduce their energy usage and resulting electricity bill during times of peak demand.¹⁴⁸

Because the proposed BTCR conflicts with the state by reducing customer options, it should be rejected.

D. The BTCR does not provide customers with efficient price signals to reduce usage at times of peak demand

The BTCR also should be rejected because it will not send customers efficient price signals to reduce usage during times of peak demand. The inefficient price signals are a result of AEP-Ohio's proposal to assign costs to customer classes for some non-market-based transmission costs in a manner that differs from how the costs are assigned by PJM and to bill for costs in a manner that differs from how costs are assigned by PJM.

Of the five non-market-based cost categories listed on Exhibit AEM-3, attached to Ms. Moore's testimony, PJM bills all but Scheduling on a one coincident peak ("1 CP") basis.¹⁴⁹ Scheduling is billed on an energy basis to Load Serving Entities. AEP-

¹⁴⁵ IEU-Ohio Ex. 1B at 31.

¹⁴⁶ *Id.*

¹⁴⁷ *Id.*

¹⁴⁸ *Id.*

¹⁴⁹ Tr. Vol. IV at 1061-63.

Ohio proposes to allocate four of the five non-market-based cost categories to the rate schedules in the same manner as PJM bills the costs; however, AEP-Ohio plans to assign reactive supply costs to the rate classes on an energy basis.¹⁵⁰

After the charges are allocated to the rate schedules, AEP-Ohio plans to collect these costs through a combination of demand and energy charges.¹⁵¹ However, AEP-Ohio does not plan to use a demand-metered customer's individual contribution to the 1 CP as the demand billing determinant.¹⁵² Instead, AEP-Ohio plans to bill demand charges based upon a different demand-billing determinant, a customer's peak monthly demand (or through a demand ratchet).¹⁵³ A customer's monthly peak demand or demand ratchet will have little, if any, relationship to the single zonal coincident peak within the PJM zone. As a result, the BTCR would eliminate the demand response opportunity that is signaled to customers obtaining transmission service, directly or indirectly, through PJM.¹⁵⁴

In contrast to the proposed BTCR, current pricing options available through CRES providers allow customers to contract for transmission service as a portion of a fixed price of all services provided by the CRES provider or a pass-through.¹⁵⁵ For a customer interested in managing its demand-related costs, a pass-through sends a transparent pricing signal to the customer to reduce demand during peak load conditions and thereby reduce congestion that may otherwise result in higher prices or

¹⁵⁰ Tr. Vol. IV at 1064-65; AEP-Ohio Ex. 13 at AEM-3.

¹⁵¹ Tr. Vol. IV at 1066-67.

¹⁵² Tr. Vol. IV at 1067.

¹⁵³ Tr. Vol. IV at 1067; IEU-Ohio Ex. 1B at 32.

¹⁵⁴ IEU-Ohio Ex. 1B at 32.

¹⁵⁵ *Id.*

degradation in reliability.¹⁵⁶ As Mr. Wilson testified for Interstate Gas Supply, Inc. (“IGS”), rates based upon an individual customer’s contribution to the peak system demand send customers appropriate market signals to reduce usage during periods of peak demand on the electric grid.¹⁵⁷

Accordingly, the proposed nonbypassable BTCR should be rejected because it will not send efficient price signals to customers to reduce their usage during periods of peak demand on the transmission system.

E. The BTCR is not needed to advance the competitive marketplace

There are 69 CRES providers registered in AEP-Ohio’s service area, 46 of which are actively serving customers.¹⁵⁸ The competitive market is working in AEP-Ohio’s certified distribution service area without the need for the proposed nonbypassable BTCR. Thus, any claim that the rider is needed to advance the competitive marketplace is meritless.

F. If the Commission does not reject the BTCR for the foregoing reasons, it should at least modify the BTCR so that it ensures efficient price signals and does not result in double-billing

For the foregoing reasons, the Commission should reject the proposed BTCR. If the Commission does not reject the rider, it should order modifications of the BTCR to ensure that no customer is billed twice for the same service and so that the BTCR sends customers efficient price signals.

To avoid the potential for double-billing, the Commission should modify the proposed BTCR and allow any customer that can affirmatively demonstrate that its

¹⁵⁶ *Id.*

¹⁵⁷ IGS Ex. 3 at 4.

¹⁵⁸ Tr. Vol. III at 869. The transcript states that there are 46 “customers” that have one or more active customers. From the context, it is clear that the reference is to CRES providers.

CRES provider has not removed the non-market-based transmission service from its bills to opt-out of the BTCR (or receive a credit under the rider) until such time as the shopping customer is no longer paying the CRES provider for non-market-based transmission service. To address the problems of price transparency and efficiency, the Commission should direct AEP-Ohio to assign reactive supply costs to customer classes on a 1 CP basis. The Commission also should direct AEP-Ohio to use a 1 CP billing determinant for demand-metered customers.

IV. THE COMMISSION SHOULD REJECT THE POR PROGRAM; IF THE COMMISSION AUTHORIZES A POR, IT SHOULD ORDER THAT ACCOUNTS RECEIVABLE BE PURCHASED AT A DISCOUNT AND DENY AUTHORIZATION OF THE BDR

AEP-Ohio proposes to implement a POR program that includes a BDR. Under the POR program, AEP-Ohio would purchase CRES providers' commodity-related receivables without discount and without recourse.¹⁵⁹ According to Mr. Gabbard, the proposed POR program would encourage the entry of additional CRES providers, expand the use of budget and average monthly billing programs, and simplify customer contacts.¹⁶⁰ CRES providers would benefit from the improved cash flow certainty afforded by the purchase of receivables without discount or risk of recourse and reduced contact with customers and their billing issues.¹⁶¹ AEP-Ohio would benefit from simplified customer service processes associated with credit determinations and collections.¹⁶²

¹⁵⁹ AEP-Ohio Ex. 11 at 3-4 & 6-8; IEU-Ohio Ex. 2 at 3-5.

¹⁶⁰ AEP-Ohio Ex. 11 at 4-5.

¹⁶¹ *Id.* at 5-6.

¹⁶² *Id.* at 6.

In addition, AEP-Ohio is proposing that it be authorized to implement a BDR as part of the POR program. Through the nonbypassable BDR, AEP-Ohio would charge or credit the difference in bad debt expense in addition to or less than the bad debt expense embedded in current distribution rates (reduced by any revenue recovered through a proposed residential late payment charge).¹⁶³ AEP-Ohio argues that the Commission should authorize the BDR because other EDUs such as Duke Energy Ohio (“Duke”) have such a charge, that AEP-Ohio is at risk for under-recovery of bad debt expense, that the BDR will allow accurate and timely recovery of bad debt expense, and that a nonbypassable rider will prevent cross-subsidization.¹⁶⁴

The Commission should not authorize the POR and BDR proposed by AEP-Ohio because AEP-Ohio has failed to demonstrate the need or benefits of either. Further, approval of the BDR would result in two poor policy decisions: it would allow AEP-Ohio to breach the terms of the Stipulation it signed to resolve the prior Duke ESP case (“Duke Stipulation”) by using the Stipulation to support approval of the rider; and the rider creates a moral hazard because it frees CRES providers from market discipline by shifting the market risk (and resulting costs) of nonpayment for CRES to all customers. If the Commission approves a POR program, then the program should be based on a requirement that the accounts receivable be purchased at a discount. If the Commission approves a POR program modified to require that receivables be discounted, then there would not be a need for a BDR.

¹⁶³ *Id.* at 8-10.

¹⁶⁴ *Id.* at 8-9.

A. The POR program does not provide a quantitative or non-quantitative benefit to customers

AEP-Ohio concedes that customers and CRES providers will not receive a quantitative benefit if the Commission authorizes the POR program, but asserts that customers and CRES providers will realize non-quantitative benefits through increased CRES participation and access to billing alternatives.¹⁶⁵ The record does not support these claims.

Although it asserts that a POR program would lower a barrier to entry of additional CRES providers, AEP-Ohio could not demonstrate that any additional CRES provider would enter the AEP-Ohio service territory if the Commission authorized a POR program.¹⁶⁶ Further, AEP-Ohio could not point to any CRES provider not already serving customers that had contacted AEP-Ohio and requested a POR program.¹⁶⁷

AEP-Ohio's claim that it expects CRES provider participation to increase also is simplistic. The CRES provider's decision to enter a market is affected by many more factors than whether the EDU has a POR program. The CRES provider will consider the regulatory environment, existing market structure, EDU pricing of default service including nonbypassable riders, expected return on investment, and the long-term sustainability of entry (the last of which Mr. Bennett, testifying for CRES providers, described as a "large component" of the decision).¹⁶⁸ As only one of many issues, the POR program is an apparently minor factor affecting the decision to enter a particular service territory.

¹⁶⁵ AEP-Ohio Ex. 7 at 4-5; AEP-Ohio Ex. 11 at 4-5.

¹⁶⁶ Tr. Vol. III at 872.

¹⁶⁷ Tr. Vol. III at 873.

¹⁶⁸ Tr. Vol. XI at 2659-64.

Additionally, there does not appear to be a shortage of CRES providers making CRES offers or a lack in variety in the offers being made. Sixty-nine CRES providers are currently certified to serve the AEP-Ohio service territory; 46 are in contract with one or more customers.¹⁶⁹ The range of offers includes many that are for terms up to three years, and there are dozens more for periods of a few months to two years.¹⁷⁰ Further, the offers include fixed and variable pricing options.¹⁷¹

AEP-Ohio also failed to demonstrate that additional CRES provider entry will provide a benefit to customers. The Application did not attempt to quantify any potential price benefit to customers, and AEP-Ohio conceded that it could not anticipate the likely product offerings that CRES providers might make.¹⁷² Additionally, it testified that entry does not provide any guarantee of lower prices. According to AEP-Ohio, there is little support in the economic literature that additional entry will result in lower prices.¹⁷³

AEP-Ohio also asserts that customers would see an advantage if it prepared customer bills for those CRES providers participating in the POR program because the CRES customers could participate in average monthly and budget-billing programs.¹⁷⁴ If there is any benefit to such billing arrangements, there is no need for the Commission to impose a POR program. Large CRES providers could provide that billing service if

¹⁶⁹ Tr. Vol. III at 869.

¹⁷⁰ AEP-Ohio Ex. 33 at WAA-R3.

¹⁷¹ <http://energychoice.ohio.gov/ApplesToApplesCategory.aspx?Category=Electric>

¹⁷² Tr. Vol. III at 874.

¹⁷³ Tr. Vol. III at 876; Tr. Vol. XIII at 3151-52.

¹⁷⁴ AEP-Ohio Ex. 11 at 4.

customers see value to it, and the large CRES providers could subcontract similar billing services to other CRES providers.¹⁷⁵

AEP-Ohio and the Staff also assert that the POR program will improve the customer contact with the EDU and the CRES provider because it would focus the customer's contacts on the EDU for a variety of issues. AEP-Ohio provides no substantive support for these claims.¹⁷⁶ If there is a benefit to focusing customer contacts on one entity, it may make as much sense to permit customers to move their billing on a consolidated basis to the CRES provider. In fact, one intervenor sought explicit authorization of consolidated billing by CRES providers.¹⁷⁷

Finally, the benefits of a POR program would be limited to the residential class.¹⁷⁸ There is no evidence that CRES providers are not providing CRES to industrial and commercial customers due to the lack of a POR program.¹⁷⁹ (For other reasons reflecting concerns about the effect of large customers on the BDR, Staff recommends removing large commercial and industrial customers from the POR program and the BDR.¹⁸⁰) Whatever benefits a POR program might provide (and the record shows they are unlikely), they do not extend to commercial and industrial customers.

¹⁷⁵ Tr. Vol. II at 232-33; Tr. Vol. VII at 1652.

¹⁷⁶ IEU-Ohio Ex. 2 at 9.

¹⁷⁷ Direct Energy Ex. 1 at 6.

¹⁷⁸ IEU-Ohio Ex. 2 at 9.

¹⁷⁹ Tr. Vol. III at 869.

¹⁸⁰ Tr. Vol. VIII at 1893-95.

B. AEP-Ohio's reliance on the Duke Stipulation for authorization of the BDR is unwarranted and violates the terms of the Stipulation

As noted above, AEP-Ohio offers four reasons to support authorization of the BDR. AEP-Ohio's first reason for seeking a BDR is based on the logic that AEP-Ohio should have what Duke has. This "reasoning" is not an argument as to why bad debt expense of CRES providers should be socialized. In fact, Mr. Gabbard conceded that there was no value for customers if AEP-Ohio had a program including a BDR similar to that of Duke.¹⁸¹ Further, the claim is not based on any understanding of Duke's BDR; Mr. Gabbard admitted that he had only a limited familiarity with Duke's tariff.¹⁸² AEP-Ohio thus failed to demonstrate that what Duke secured under its Stipulation is what AEP-Ohio should be authorized to implement.

Additionally, AEP-Ohio's reliance on the Duke Stipulation violates the terms of an agreement that is binding on AEP-Ohio. Duke's BDR and POR program were authorized in a proceeding resolved by a Stipulation. The Stipulation provides that it was "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."¹⁸³ Counsel for AEP-Ohio signed the Stipulation without reservation on behalf of Ohio Power Company's predecessors, Columbus Southern Power Company and Ohio Power

¹⁸¹ Tr. Vol. III at 876.

¹⁸² Tr. Vol. III at 875-76.

¹⁸³ *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).

Company.¹⁸⁴ Thus, AEP-Ohio cannot lawfully rely on the Stipulation to support approval of the BDR (or the POR program).

C. The BDR will not enhance competition, but will unreasonably shift the market risk for bad debt to all customers of AEP-Ohio

While AEP-Ohio also indicates that a BDR will stimulate additional entry by CRES providers, there is no evidence that CRES providers are not making offers in the AEP-Ohio service territory because AEP-Ohio does not have a BDR tied to a POR program without a discount.¹⁸⁵ The current competitive environment also is not likely to change if the Commission does not approve a POR program and BDR.¹⁸⁶ Further, the alleged economic benefits of the BDR were not demonstrated.¹⁸⁷

The authorization of the POR program and BDR as proposed by AEP-Ohio, moreover, would be a bad policy choice. Because AEP-Ohio would purchase accounts receivable without a discount and collect any resulting bad debt expense through the BDR, the bad debt risk of CRES customers would be transferred from the CRES provider to AEP-Ohio and then to all customers. This mechanism, thus, removes the market discipline that encourages CRES providers to evaluate their customers and price their services appropriately.¹⁸⁸

¹⁸⁴ *Id.* at 48.

¹⁸⁵ IEU-Ohio Ex. 2 at 11-12; AEP-Ohio Ex. 33 at Ex. WAA-R3; Tr. Vol. VII at 1653-54.

¹⁸⁶ Tr. Vol. VII at 1652-53.

¹⁸⁷ IEU-Ohio Ex. 2 at 11.

¹⁸⁸ IEU-Ohio Ex. 2 at 13. One additional check on whether the POR program represents good policy is to examine how AEP addresses internally the purchase of receivables. AEP Credit purchases the receivables of the AEP operating companies and resells those accounts to third parties such as banks. When AEP Credit purchases receivables, it purchases them without recourse but at a discount. Tr. Vol. IV at 1195-97.

D. If the Commission approves a POR program for AEP-Ohio, it should refuse to authorize the BDR and direct that AEP-Ohio purchase accounts receivable at a discount

AEP-Ohio has failed to demonstrate that the Commission should authorize the POR program and BDR as proposed. The Commission, however, has indicated its interest in having the EDUs present proposals for POR programs.¹⁸⁹ If the Commission decides that AEP-Ohio should provide a POR program, the Commission should modify AEP-Ohio's proposal. As Mr. Bowser and Staff concluded, the POR program should be approved only if the Commission refuses to authorize the BDR and directs AEP-Ohio to purchase the receivables from CRES providers at a discount.¹⁹⁰ With these modifications, the CRES providers would be responsible for the market risk associated with bad debt of their own customers, removing the moral hazard inherent in AEP-Ohio's proposal.

V. THE PROPOSED ESP IS NOT MORE FAVORABLE IN THE AGGREGATE THAN AN MRO

Under R.C. 4928.143(C)(1), the Commission may approve or modify and approve an ESP only if it finds "that the electric security plan so approved, including its pricing and all other terms and conditions, including any deferrals and any future recovery of deferrals, is more favorable in the aggregate as compared to the expected results that would otherwise apply under section 4928.142 of the Revised Code."¹⁹¹

¹⁸⁹ *In the Matter of the Commission's Investigation of Ohio's Retail Electric Service Market*, Case No. 12-3151-EL-UNC, Finding and Order at 21 (Mar. 26, 2014).

¹⁹⁰ IEU-Ohio Ex. 2 at 13-14; Staff Ex. 14 *passim*. Retail Energy Supply Association ("RESA") agrees that a POR program that required purchase of accounts receivable at a discount is acceptable. Tr. Vol. XI at 2673-74.

¹⁹¹ R.C. 4928.143(C).

The proposed ESP fails this test. As a result, the Commission must modify the proposed ESP before it can be approved.

AEP-Ohio's testimony indicates that the proposed ESP would be quantitatively more favorable than an MRO by \$44.1 million over the three-year term of the ESP.¹⁹² (Only two years of the ESP term may be implemented if the Commission authorizes AEP-Ohio to have the option to terminate the ESP after two years as AEP-Ohio requests.¹⁹³) According to AEP-Ohio, there is no comparative benefit resulting from the CBP since all SSO load would be secured through auctions under either an MRO or the proposed ESP.¹⁹⁴ The \$44.1 million quantitative benefit would result from the extension of the Residential Distribution Credit Rider, a credit to residential base distribution charges that would terminate on May 31, 2015 if not extended as a provision of the proposed ESP.¹⁹⁵ AEP-Ohio also notes that it would avoid the cost of a distribution rate case if its Distribution Investment Rider ("DIR") proposal is authorized,¹⁹⁶ but the testimony does not assign any quantitative value to that avoided cost.¹⁹⁷ According to AEP-Ohio, there are no other quantifiable costs or benefits of the proposed ESP.¹⁹⁸ Thus, the total quantitative benefit of the ESP identified by AEP-Ohio is \$44.1 million.

¹⁹² AEP-Ohio Ex. 7 at 4.

¹⁹³ AEP-Ohio Ex. 1 at 15.

¹⁹⁴ AEP-Ohio Ex. 7 at 4.

¹⁹⁵ *Id.*

¹⁹⁶ *Id.*

¹⁹⁷ Nor should any benefit to the DIR be included in the ESP v. MRO Test, based on prior Commission precedent. IEU-Ohio Ex. 1B at 22, citing *In the Matter of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Authority to Provide for a Standard Service Offer Pursuant to Section 4928.143, Revised Code, in the Form of an Electric Security Plan*, Case No. 12-1230-EL-SSO, Opinion and Order at 10 (July 18, 2012) ("*FirstEnergy ESP III*") (the quantitative costs associated with recovery of incremental distribution investment through either a rider or a base rate case should be considered a wash).

¹⁹⁸ IEU-Ohio Ex. 1B at 20, citing response to OCC Interrogatory 3-025.

AEP-Ohio also points to non-quantifiable benefits to support approval of the proposed ESP. According to AEP-Ohio, the proposed ESP provides a faster move to a market-based SSO than would otherwise be available, provides through the PPAR a hedge for customers that will stabilize their prices, and provides benefits through the POR program.¹⁹⁹

AEP-Ohio's Application and testimony misapply the ESP v. MRO Test in two respects. First, AEP-Ohio fails to quantify the effect of the PPAR on the ESP side of the ESP v. MRO Test. The failure to assign a cost to the PPAR is not consistent with prior Commission decisions, and a proper accounting of the rider demonstrates that the ESP is quantitatively worse than an MRO. Second, the non-quantifiable benefits on which AEP-Ohio relies to support approval of the proposed ESP are neither a lawful basis for such approval nor supported by the evidence. Therefore, the proposed ESP fails the ESP v. MRO Test.²⁰⁰

A. The known costs of the PPAR must be accounted for in the ESP v. MRO Test

In prior cases in which EDUs have sought approval of an ESP, the Commission has stated that the known costs of riders that could be approved in an ESP but not an MRO must be accounted for on the ESP side of the ESP v. MRO Test. In AEP-Ohio's last ESP case, for example, AEP-Ohio sought and received authorization to include a Generation Resource Rider with a known cost of \$8 million over the term of the ESP.

¹⁹⁹ AEP-Ohio Ex. 7 at 4-5.

²⁰⁰ Staff also relies on non-quantifiable benefits to support its finding that the ESP, as modified by Staff's removal of various riders including the PPAR, satisfies the ESP v. MRO Test. On a quantified basis, Staff's proposed ESP was \$44.1 million more favorable in the aggregate than an MRO. Staff Ex. 15 at 5. As discussed below, the Commission may not rely on the non-quantifiable benefits identified by either AEP-Ohio or the Staff to support a finding that the proposed ESP is more favorable in the aggregate than an MRO.

Additionally, the Commission modified the ESP so that it included a Retail Stability Rider that cost approximately \$388 million over the term of the ESP. The Commission apparently concluded that it could not lawfully approve either rider as a term of an MRO. Offsetting the known costs of the riders by the \$9.8 million benefit that the Commission estimated resulted from the blending of the base generation, fuel, and auction prices the Commission approved, the Commission concluded that the ESP was \$386 million worse than an MRO.²⁰¹

As noted above, AEP-Ohio concedes in its direct testimony that the PPAR is not a provision available in an MRO.²⁰² Thus, the Commission must account for the known costs of the PPAR on the ESP side of the ESP v. MRO Test.

B. The known cost of the PPAR is \$82 million to \$116 million over the term of the proposed ESP; as a result, the proposed ESP is \$38 million to \$72 million worse than an MRO

AEP-Ohio provided three estimates of the cost of the PPAR to customers. Its initial estimate of the cost of the PPAR is \$52 million.²⁰³ This estimate includes an assumption that OVEC can realize substantial annual cost savings during the term of the ESP. Those cost savings, however, are speculative because OVEC has not made any commitment to realize them and AEP-Ohio has not committed to flow the anticipated cost reductions to customers if OVEC does not deliver them.²⁰⁴ If the

²⁰¹ *ESP II*, Opinion and Order at 75. As noted in IEU-Ohio's appeal, the Commission's calculation of the costs of the ESP II substantially understates its costs. *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 Section 4928.143, Revised Code, in the Form of an Electric Security Plan*, Sup. Ct. Case No. 2013-0521, First Merit Brief of Appellant Industrial Energy Users-Ohio at 11-23 (Aug. 12, 2013).

²⁰² AEP-Ohio Ex. 7 at 5.

²⁰³ IEU-Ohio Ex. 1B at KMM-5.

²⁰⁴ Tr. Vol. II at 552.

speculative cost savings are removed, a conservative estimate of the cost of the PPAR is \$82 million during the term of the ESP.²⁰⁵

An estimate updated for future energy prices and expected generation output suggests an even higher cost is likely. OCC provided estimates of both the energy price corrected for the proper delivery point and generation output based on the recent history of the OVEC plants.²⁰⁶ Based on these adjustments and the removal of the speculative cost reductions previously noted, the cost to customers jumps to \$116 million over the term of the ESP.²⁰⁷

As discussed above, AEP-Ohio initially concluded that the PPAR could be either a charge or credit and provided no estimate of its cost in the Application. Once hearings began, it then claimed that the PPAR would produce an \$8 million benefit. These claims are inconsistent with all the other evidence in the record that demonstrates that the PPAR, directionally, will be a cost to consumers over the term of the ESP. It is also inconsistent with Mr. Allen's pre-Application conclusion that the PPAR could be either a charge or credit and therefore should be left out of the billing comparisons. Thus, the claim that the PPAR will produce a customer benefit is unsupported and not credible.

The only other party suggesting the PPAR might benefit customers in any financial sense is Ohio Energy Group ("OEG"). OEG provides an estimate based on the same information as that used by AEP-Ohio to support its 7¢ solution. As OEG's witness pointed out, however, he based his recommendation for a PPAR with a term of

²⁰⁵ IEU-Ohio Ex. 1B at 21.

²⁰⁶ *Id.* at 10-28.

²⁰⁷ *Id.* at 7.

9.5 years on the assumption that the PPAR would provide value to customers only if the PPAR remained in effect for a sufficient amount of time for electric prices to reach sufficient levels to offset the costs of OVEC's operation.²⁰⁸ In the shorter term covered by the proposed ESP, the rider will result in a charge to customers.²⁰⁹

The credible evidence of the cost of the PPAR, therefore, is that it is likely to result in an \$82 million charge to customers. The amount it adversely affects customers may range from \$82 million to \$116 million.²¹⁰ When the cost of the PPAR is included on the ESP side of the ESP v. MRO Test, it offsets the \$44.1 million benefit of the extension of the distribution credit, and the proposed ESP is quantitatively \$38 million to \$72 million worse than an MRO.

C. The Commission may not lawfully weigh the non-quantifiable benefits against the quantifiable costs of the proposed ESP

Although AEP-Ohio claimed that the proposed ESP was quantitatively more favorable than an MRO by \$44.1 million, it also claimed that the proposed ESP would provide non-quantifiable benefits. On the record in this case, the Commission cannot lawfully or reasonably approve the proposed ESP based on that claim.

In analyzing whether the proposed ESP satisfies the ESP v. MRO Test, the Commission must engage in reasoned decision making. In a contested case, R.C. 4903.09 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 Ohio Supreme Court ("Court") has stated, the Commission in assessing

²⁰⁸ OEG Ex. 3 at 15-16.

²⁰⁹ *Id.* at 14.

²¹⁰ IEU-Ohio Ex. 1B at 21; OCC Ex. 15 at 26.

the record must explain its rationale, respond to contrary positions, and support its decision with appropriate evidence.²¹¹ “The commission cannot decide cases on subjective belief, wishful thinking, or folk wisdom.”²¹² Thus, R.C. 4903.09 imposes on the Commission a requirement to apply an objective standard to the ESP v. MRO Test.

Although the Commission has “weighed” non-quantifiable benefits against the quantifiable costs of an ESP,²¹³ there must be some reasonable metric or other basis on which this weighing is done. AEP-Ohio does not provide the Commission any basis on which it can “weigh” the non-quantifiable benefits against the costs that the proposed ESP will impose on both shopping and nonshopping customers. Reliance on these non-quantifiable benefits, therefore, would require the Commission to base its decision on subjective and unsupported beliefs and guesses provided by AEP-Ohio. R.C. 4903.09 requires more than AEP-Ohio’s “trust me” approach.

D. If the Commission may consider the non-quantifiable benefits, AEP-Ohio has failed to demonstrate that the proposed ESP provides any non-quantifiable benefits to customers that “outweigh” its substantial costs

As noted above, AEP-Ohio claims that the non-quantifiable benefits of the proposed ESP consist of a faster transition to a market-based SSO than would be available under an MRO, increased price stability if the PPAR is authorized, and customer benefits resulting from the POR. Statutory requirements including the state energy policy, prior Commission orders, and the record in this case, however, require the Commission to find that proposed ESP does not have non-quantifiable benefits and

²¹¹ *In re Application of Columbus Southern Power Co.*, 128 Ohio St.3d 512, 519 (2011).

²¹² *Consumers' Counsel v. Pub. Util. Comm'n of Ohio*, 61 Ohio St.3d 396, 406 (1991) (quoting *Columbus v. Pub. Util. Comm'n of Ohio*, 58 Ohio St.2d 103, 104 (1979) (Brown, J., dissenting)).

²¹³ *ESP II*, Opinion and Order at 77.

whatever benefits may exist do not “outweigh” the substantial costs of the proposed ESP to customers.

1. The Commission cannot lawfully and reasonably assign a benefit to the ESP because AEP-Ohio agrees to implement a CBP to fulfill its obligation to provide a default service offer

AEP-Ohio’s claim that the Commission should assign a benefit to a faster move to a CBP to set the default generation supply price is based on a fundamental misconception about the statutory outcomes required by Chapter 4928. The General Assembly has declared retail generation service to be a competitive service.²¹⁴ The General Assembly’s expressed goal is to encourage customer choice through actions by individual customers having comparable and non-discriminatory access to a diverse group of CRES providers.²¹⁵ The goal includes a statutory scheme that specifically limits the role of the EDU to that of a default supplier of competitive services and prohibits an EDU from being directly engaged in the business of providing competitive services.²¹⁶ 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.²¹⁷ Under the applicable requirements of an ESP or MRO, the SSO must be either market-tested (ESP) or market-based (MRO). The Commission cannot elevate the outcome already required by Ohio law, a market-based SSO, to avoid a finding that the proposed ESP, which burdens customers with unlawful charges, is more favorable in the aggregate than an MRO.

²¹⁴ R.C. 4928.03.

²¹⁵ R.C. 4928.02(A).

²¹⁶ R.C. 4928.17.

²¹⁷ R.C. 4928.14.

By assigning some subjective, but apparently substantial, benefit to the “quicker” move to a competitively bid SSO, AEP-Ohio again seeks to unreasonably and unlawfully reverse the priorities clearly expressed in Ohio law. There is not any benefit to the proposed ESP because AEP-Ohio agrees to implement a CBP to fulfill its obligation to provide a default service offer that must already meet a market-based test.

2. AEP-Ohio seeks to double-count the benefits of a faster move to a market-based SSO

As AEP-Ohio’s testimony indicates, the Commission previously recognized the transition to an ESP based on a CBP as a non-quantifiable benefit of the ESP approved in AEP-Ohio’s last SSO case.²¹⁸ Based on the Commission’s prior holding that an EDU may not count as a benefit of the proposed ESP a benefit previously recognized in the approval of a prior ESP, the Commission cannot lawfully and reasonably “double count” the so-called faster move to market-based rates in this case.

Rejecting the double count is required by the Commission’s order in FirstEnergy’s last ESP case. In that case, FirstEnergy argued that its decision to forgo regional transmission expansion plan (“RTEP”) costs should be considered a quantifiable benefit of the proposed ESP. Staff testified that forgoing recovery of the RTEP costs should not be treated as a quantifiable benefit because FirstEnergy had agreed to forgo recovery of the RTEP costs in a prior ESP proceeding. The Commission agreed, stating “that the benefit of this credit was a result of the Commission’s decision in the ESP 2 Case and cannot be considered a benefit of the ESP 3 to be reflected in the ESP v. MRO analysis.”²¹⁹

²¹⁸ AEP Ohio Ex. 7 at 5.

²¹⁹ *FirstEnergy ESP III*, Opinion and Order at 55 (July 18, 2012).

In AEP-Ohio's ESP II case, the Commission recognized a non-quantifiable benefit of the ESP arising from a faster move to a market-based ESP than would occur under an MRO.²²⁰ Because the Commission previously credited AEP-Ohio with a non-quantifiable benefit of this "faster move," it would be unlawful and unreasonable to count it again as a benefit of the proposed ESP.

3. The PPAR will harm customers and competition without providing price stability

AEP-Ohio further claims that the PPAR is a non-quantifiable benefit of the proposed ESP because "it provides increased rate stability for customers."²²¹ The PPAR, however, will impose a significant new cost on customers through a nonbypassable rider and inject additional price volatility.

As discussed above, the PPAR likely will result in an additional charge on all customers during the term of the proposed ESP of \$82 to \$116 million. Further, as discussed previously, the design of the PPAR (which includes an over/under adjustment provision) and the structure of the other riders making up the rates of shopping and nonshopping customers (which include annual or more frequent adjustments) make it unlikely that the "hedge" will be of any benefit to customers. Based on the record in this case demonstrating that the PPAR likely will increase customer rates or at best do nothing to hedge customer bills, the Commission cannot reasonably conclude that the rider provides a non-quantifiable benefit to customers.

More practically, however, the PPAR would likely inject additional volatility into prices for both shopping and nonshopping customers. Shopping customers, including

²²⁰ *ESP II*, Opinion and Order at 76 (Aug. 8, 2012).

²²¹ AEP-Ohio Ex. 7 at 5.

residential customers, can secure long-term contracts of up to three years at a fixed rate.²²² Nonshopping customers would benefit from the stability provided by the laddering and staggering of the CBP.²²³ Authorization of the PPAR, however, would increase price risk for both shopping and nonshopping customers.²²⁴ As Mr. Murray explained:

The only stability provided by the PPA Rider is the stability provided AEP-Ohio (as an equity owner of OVEC) through a guaranteed return of and on its generation investments funded by captive retail distribution customers through the PPA Rider. As proposed by AEP-Ohio, the PPA Rider provides no stability to any SSO or non-SSO customer at all because it is an unknown cost or credit that will vary in amount over the term of the proposed ESP III and the variation will be reflected in the charge that is periodically adjusted and reconciled as the PPA Rider is implemented along with the several other riders and adjustment mechanisms. The only guarantee for shopping and non-shopping retail customers provided by the PPA Rider is that their rates will remain unpredictable for the entire term of the ESP III. Indeed, for shopping customers who have selected fixed price offers from CRES providers, the proposed PPA Rider would add uncertainty and instability to their delivered price of electricity.²²⁵

It would be far easier to provide ESP customers with a stable generation price by directing AEP-Ohio to conduct a single, descending clock auction for all SSO generation supply necessary for the entire ESP term or longer prior to the start of the proposed ESP.²²⁶ Moreover, a single auction for generation service for SSO customers (and those wishing to return to the SSO), as opposed to the imposition of a nonbypassable generation-related charge that is not authorized by a provision of R.C. 4928.143, would

²²² AEP-Ohio Ex. 33 at Ex. WAA-R3; Tr. Vol. XIII at 3284-85.

²²³ Staff Ex. 16 *passim*; Tr. Vol. XIII at 3279-80.

²²⁴ Tr. Vol. XIII at 3141. As one witness supporting a modified PPAR pointed out, none of the factors driving the PPAR rate is known. Tr. Vol. XI at 2594.

²²⁵ IEU-Ohio Ex. 1B at 25-26.

²²⁶ *Id.* at 26.

have the added advantage over the PPAR of being legally authorized as a term of the proposed ESP.

As discussed previously, the PPAR also harms customers because it would frustrate the energy policy of the State to ensure customer choice.²²⁷ In opposition to that policy, the PPAR would impose a charge on customers, allegedly to secure price stability, when they can already manage price volatility through their choice of many options available in the retail electricity market.

Further, as discussed above, the PPAR will have no effect on reliability of service; that role is a function of PJM, and it is already addressing concerns about reliability and price volatility raised by the January 2014 weather events.

Also as noted above, the PPAR is anticompetitive. If the PPAR is approved, AEP-Ohio faces no market price risk for its OVEC Entitlement, and AEP-Ohio would look to only its affiliated unregulated generation company as a source for any additional PPAs if it sought to expand the “hedge.”²²⁸ In contrast, competitors that face price risk hourly do not have a regulatory backstop such as the PPAR. Contrary to AEP-Ohio’s repeated assertions,²²⁹ the PPAR would place unregulated generation providers at a competitive disadvantage.

The PPAR thus fails to provide a non-quantifiable benefit in several ways. It would likely increase the customer’s bill while frustrating competition, violating state policy supporting customer choice, and increasing price risk for those customers that

²²⁷ R.C. 4928.02(A) & (B).

²²⁸ Tr. Vol. I at 110-11.

²²⁹ See, e.g., Tr. Vol. II at 566; AEP-Ohio Ex. 7 at 10.

are seeking to reduce volatility through either CRES contracts or the SSO. Rather than providing a non-quantifiable benefit, the PPAR would be harmful to customers.

4. The POR program will not provide a non-quantifiable benefit to customers

AEP-Ohio and Staff also state that the POR program would provide non-quantifiable benefits to customers.²³⁰ (The POR program recommended by Staff would substantially modify AEP-Ohio's proposal. The effect of those modifications would not result in the POR program providing any unique benefit to customers; however, Staff's proposal would remove the negative effects of the BDR.) If the POR program is authorized, Staff claims that it is likely to increase the number of registered CRES providers, provide additional payment options for customers, and provide CRES providers with more predictable payment.²³¹ According to AEP-Ohio, these benefits would not be available under an MRO.²³² The alleged benefits of the POR, however, did not withstand the rigors of a hearing: as previously discussed, AEP-Ohio failed to demonstrate that customers will benefit from its POR program or that the benefits could not be realized through the market.

The POR program also improperly shifts the risk of bad debt expense of CRES providers to all customers. Under the proposed POR program, CRES providers will be relieved of the market discipline associated with bad debt by operation of the purchase of receivables without recourse and the BDR.²³³ The shift of this risk is not a benefit to customers.

²³⁰ AEP-Ohio Ex. 7 at 5; Staff Ex. 15 at 4-5.

²³¹ AEP-Ohio Ex. 7 at 5; AEP-Ohio Ex. 11 at 4-6; Staff Ex. 15 at 4-5.

²³² AEP-Ohio Ex. 7 at 5.

²³³ AEP-Ohio Ex. 2 at 13.

5. The distribution riders will not provide a non-quantifiable benefit because the same benefits can be realized under an MRO; further, AEP-Ohio failed to provide evidence showing that distribution investment will improve customer satisfaction or service quality

Staff offers that a non-quantifiable benefit of the proposed ESP results from some of the distribution riders AEP-Ohio is seeking to continue and expand.²³⁴ The benefits of the distribution riders, however, can be realized through a base distribution case and thus are equally available under an MRO.²³⁵ As the Commission has previously determined, “these costs should be considered substantially equal and removed from the ESP v. MRO analysis.”²³⁶

Furthermore, AEP-Ohio failed to demonstrate that the distribution riders would provide the benefits it claimed. According to Mr. Dias, AEP-Ohio’s witness addressing the merits of the distribution riders, his claim that the distribution riders would provide increased customer satisfaction through increased investment in distribution infrastructure was based on a *Public Utilities Fortnightly* article appended to his testimony.²³⁷ He “used this information to help [him] understand and validate [his] entire comprehensive plan.”²³⁸

AEP-Ohio’s reliance on the article, however, was misplaced. AEP-Ohio could not provide the data on which the article was based, the study was not performed by

²³⁴ Staff Ex. 15 at 3-4. Staff’s support of the distribution riders proposed by AEP-Ohio is limited in several ways. First, Mr. Baker noted that Staff believed that existing distribution system was aligned with customer reliability expectations, but did not support the expansion of one rider as requested by AEP-Ohio. Staff Ex. 10 *passim*. Mr. Liphtratt recommended significant modification of the Storm Damage Cost Recovery Rider. Staff Ex. 12. Mr. Willis recommended that the Commission refuse to authorize the Sustained and Skilled Workforce Rider. Staff Ex. 8.

²³⁵ AEP-Ohio Ex. 7 at 4.

²³⁶ *FirstEnergy ESP III*, Opinion and Order at 56 (July 18, 2012).

²³⁷ AEP-Ohio Ex. 4 at Ex. SJD-2.

²³⁸ Tr. Vol. II at 361.

AEP-Ohio, the witness was not aware if AEP-Ohio had participated in the study, the witness was not aware of any independent review of the results of the study, and the authors of the study did not testify in support of it.²³⁹

In addition to the evidentiary and methodological issues the study presented, the study did not provide statistically significant support for its claim that additional investment will positively affect customer satisfaction. The study consisted of a regression analysis of several factors and survey results of customer satisfaction. As the article itself concluded, net distribution investment was not statistically significant as an independent variable correlated with customer satisfaction at the 1%, 5% or 10% levels of confidence.²⁴⁰ Statistically, net investment in distribution was irrelevant.

AEP-Ohio also has not demonstrated that additional distribution investment will improve distribution reliability. Mr. Dias stated that it is impossible to know if distribution service will improve if AEP-Ohio increases its spending on distribution facilities.²⁴¹

In summary, the record does not demonstrate that the distribution riders provide a qualitative benefit that supports approval of the proposed ESP. Even if the Commission approves the whittled list of distribution riders recommended by the Staff, the Commission has already determined that benefits of distribution investment should be treated as a wash in the ESP v. MRO Test. Further, AEP-Ohio failed to demonstrate that the evidence on which it relied to support its claim that its proposed distribution program would improve customer satisfaction was methodologically sound. Even if the study was sound, the results indicate that any effect of net distribution investment on

²³⁹ Tr. Vol. II at 360-68

²⁴⁰ AEP-Ohio Ex. 4 at Ex. SJD-2 at 6 (Fig. 6).

²⁴¹ Tr. Vol. II at 368-69.

customer satisfaction was statistically meaningless. Finally, AEP-Ohio concedes that the increased distribution investment funding it is seeking will not guarantee improved distribution reliability. Accordingly, there is no support for the Staff's claim that the distribution riders are a benefit to customers of the proposed ESP.

E. Before approving the proposed ESP, the Commission must modify it to remove the unlawful and unreasonable riders and POR program

The Commission cannot approve the proposed ESP because it is less favorable in the aggregate than an MRO. It is quantitatively less favorable than an MRO by tens of millions of dollars. The non-quantifiable benefits cannot be “weighed” against the costs of the proposed ESP because AEP-Ohio did not provide any objective evidence to support that “weighing.” Moreover, the provisions of the proposed ESP that AEP-Ohio (and Staff) alleged would produce non-quantifiable benefits either would not produce the claimed results, produce results that were negligible, or would more likely be harmful to customers and customer choice.

Under R.C. 4928.143(C)(1), the Commission may modify and approve the proposed ESP. To produce an ESP that would pass the ESP v. MRO Test, the Commission should remove the unlawful and unreasonable provisions. The unlawful and unreasonable provisions include the PPAR, the POR program and BDR as proposed, and the BTCR.

If the Commission removes the unlawful and unreasonable provisions, the proposed ESP as modified would satisfy an objective application of the ESP v. MRO Test. By removing the PPAR, the proposed ESP would be quantitatively more

favorable in the aggregate than an MRO by \$44.1 million.²⁴² Removing the PPAR and BDR also would eliminate the anticompetitive and anti-consumer harms these riders would cause. Rejection of the BTCR would maintain the appropriate market signals available to customers through customer choice and remove the risk of double-billing. Accordingly, the Commission should modify the proposed ESP to remove the unlawful and unreasonable provisions and thereby bring the proposed ESP into compliance with the ESP v. MRO Test.

VI. CONCLUSION

Based on policy outcomes the Commission is to ensure, the law the Commission is to apply, and the record in this case, the Commission should not authorize the PPAR, the BTCR, and the POR program because they are illegal, unreasonable, or both. If the Commission nonetheless authorizes a POR program, the POR program should be modified to remove the BDR and provide that AEP-Ohio will purchase accounts receivable at a discount. If the Commission approves a nonbypassable BTCR, it also should provide a mechanism so that current shopping customers are not charged twice for transmission-related services. Additionally, the proposed BTCR should be modified to provide the correct price signals to customers.

Additionally, the Commission should not approve the proposed ESP without modifications because it fails an objective, cost-based application of the ESP v. MRO Test. If the Commission removes the objectionable riders (particularly the PPAR),

²⁴² This claimed result is the same that occurs under the Staff's position. Staff's recommendation to approve the ESP is based on the removal of all provisions the Staff does not support. Staff Ex. 15 at 5; Tr. Vol. IX at 2206.

however, the proposed ESP would satisfy the statutory test that the ESP be more favorable in the aggregate than an MRO.

Respectfully submitted,

/s/ Frank P. Darr

Frank P. Darr (Counsel of Record)

Matthew Pritchard

MCNEES WALLACE & NURICK LLC

Fifth Third Center

21 East State Street, 17th Floor

Columbus, OH 43215-4228

Telephone: (614) 469-8000

Telecopier: (614) 469-4653

fdarr@mwncmh.com

Attorney for Industrial Energy Users-Ohio

CERTIFICATE OF SERVICE

In Accordance with Rule 4901-1-05, Ohio Administrative Code, the PUCO's e-filing system will electronically serve notice of the filing of this document upon the following parties. In addition, I hereby certify that a service copy of the foregoing *Initial Brief of Industrial Energy Users-Ohio* was sent by, or on behalf of, the undersigned counsel for IEU-Ohio to the following parties of record this 23rd day of July 2014, via electronic transmission.

/s/ Frank P. Darr _____

Frank P. Darr

Steven T. Nourse (0046705)
Matthew J. Satterwhite (0071972)
AMERICAN ELECTRIC POWER
CORPORATION
1 Riverside Plaza, 29th Floor
Columbus, Ohio 43215-2373
stnourse@aep.com
mjsatterwhite@aep.com

Daniel R. Conway (0023058)
PORTER WRIGHT MORRIS & ARTHUR
Huntington Center
41 South High Street
Columbus, Ohio 43215
dconway@porterwright.com

ON BEHALF OF OHIO POWER COMPANY

David F. Boehm (0021881)
Michael L. Kurtz (0033350)
Jody Kyler Cohn (0085402)
BOEHM, KURTZ & LOWRY
36 East Seventh Street, Suite 1510
Cincinnati, Ohio 45202
dboehm@BKLawfirm.com
mkurtz@BKLawfirm.com
jkylercohn@BKLawfirm.com

ON BEHALF OF THE OHIO ENERGY GROUP

William L. Wright (0018010)
Werner Margard (0024858)
Devin Parram (0082507)
Katherine Johnson (0091064)
Assistant Attorneys' General
180 E. Broad Street, 6th Floor
Columbus, Ohio 43215-3793
William.wright@puc.state.oh.us
werner.margard@puc.state.oh.us
Devin.Parram@puc.state.oh.us
katherine.johnson@puc.state.oh.us

**ON BEHALF OF THE STAFF OF THE PUBLIC
UTILITIES COMMISSION OF OHIO**

Maureen R. Grady (0020847)
Assistant Consumers' Counsel
OFFICE OF THE OHIO CONSUMERS'
COUNSEL
10 West Broad Street, Suite 1800
Columbus, Ohio 43215-3485
grady@occ.state.oh.us

**ON BEHALF OF THE OFFICE OF THE OHIO
CONSUMERS' COUNSEL**

Rocco D'Ascenzo (0077651)
DUKE ENERGY OHIO, INC.
139 East Fourth Street
Cincinnati, Ohio 45202
Rocco.D'Ascenzo@duke-energy.com

Elizabeth H. Watts
Assistant General Counsel
DUKE ENERGY OHIO
155 East Broad Street, 21st Floor
Columbus, Ohio 43215
Elizabeth.Watts@duke-energy.com

ON BEHALF OF DUKE ENERGY OHIO, INC.

Barth E. Royer (0016999)
BELL & ROYER CO., LPA
33 South Grant Avenue
Columbus, Ohio 43215-3927
BarthRoyer@aol.com

Gary A. Jeffries (0071742)
DOMINION RESOURCES SERVICES, INC.
501 Martindale Street, Suite 400
Pittsburg, PA 15212-5817
Gary.A.Jeffries@dom.com

**ON BEHALF OF DOMINION RETAIL, INC.
D/B/A DOMINION ENERGY SOLUTIONS**

Richard L. Sites (0019887)
OHIO HOSPITAL ASSOCIATION
155 East Broad Street, 15th Floor
Columbus, Ohio 43215-3620
ricks@ohanet.org

Thomas J. O'Brien (0066249)
Dylan F. Borchers (0090690)
BRICKER & ECKLER LLP
100 South Third Street
Columbus, Ohio 43215-4291
tobrien@bricker.com
dborchers@bricker.com

**ON BEHALF OF THE OHIO HOSPITAL
ASSOCIATION**

Phillip B. Sineneng (0083406)
THOMPSON HINE LLP
41 South High Street, Suite 1700
Columbus, Ohio 43215
PhilipSineneng@ThompsonHine.com

**ON BEHALF OF DUKE ENERGY RETAIL
SALES, LLC AND DUKE ENERGY
COMMERCIAL ASSET MANAGEMENT, INC.**

Mark A. Whitt (0067996)
Andrew J. Campbell (0081485)
Gregory L. Williams (0088758)
WHITT STURTEVANT LLP
The KeyBank Building, Suite 1590
88 East Broad Street
Columbus, Ohio 43215
whit@whitt-sturtevant.com
campbell@whitt-sturtevant.com
williams@whitt-sturtevant.com

Vincent Parisi (0073283)
Lawrence Friedeman (0018902)
INTERSTATE GAS SUPPLY, INC.
6100 Emerald Parkway
Dublin, Ohio 43016
vparisi@igsenergy.com
lfriedeman@igsenergy.com

**ON BEHALF OF INTERSTATE GAS SUPPLY,
INC.**

Kimberly W. Bojko (0069402)
Mallory M. Mohler (0089508)
CARPENTER LIPPS & LELAND LLP
280 Plaza, Suite 1300
280 North High Street
Columbus, Ohio 43215
Bojko@carpenterlipps.com
Mohler@carpenterlipps.com

ON BEHALF OF OMA ENERGY GROUP

Mark A. Hayden (0081077)
Jacob A. McDermott (0087187)
Scott J. Casto (0085756)
FIRSTENERGY SERVICE COMPANY
76 South Main Street
Akron, Ohio 44308
haydenm@firstenergycorp.com
jmcdermott@firstenergycorp.com
scasto@firstenergycorp.com

**ON BEHALF OF FIRSTENERGY SOLUTIONS
CORP.**

Colleen L. Mooney (0015668)
Cathryn N. Loucas (0073533)
OHIO PARTNERS FOR AFFORDABLE
ENERGY
231 West Lima Street
Findlay, Ohio 45839-1793
cmooney@ohiopartners.org
cloucas@ohiopartners.org

**ON BEHALF OF OHIO PARTNERS FOR
AFFORDABLE ENERGY**

Mark S. Yurick (0039176)
Zachary D. Kravitz (0084238)
TAFT, STETTINIUS & HOLLISTER LLP
65 East State Street, Suite 1000
Columbus, Ohio 43215
myurick@taftlaw.com
zkravitz@taftlaw.com

ON BEHALF OF THE KROGER Co.

Judi L. Sobecki (0067186)
THE DAYTON POWER AND LIGHT COMPANY
1065 Woodman Drive
Dayton, Ohio 45432
judi.sobecki@aes.com

**ON BEHALF OF THE DAYTON POWER AND
LIGHT COMPANY**

Joseph M. Clark (0080711)
DIRECT ENERGY
21 East State Street, 19th Floor
Columbus, Ohio 43215
joseph.clark@directenergy.com

**ON BEHALF OF DIRECT ENERGY
SERVICES, LLC AND DIRECT ENERGY
BUSINESS, LLC**

Trent Dougherty (0079817)
OHIO ENVIRONMENTAL COUNCIL
1207 Grandview Avenue, Suite 201
Columbus, Ohio 43212-3449
tdougherty@theOEC.org

John Finnigan (0018689)
Senior Regulatory Attorney
ENVIRONMENTAL DEFENSE FUND
128 Winding Brook Lane
Terrace Park, Ohio 45174
jfinnigan@edf.org

**ON BEHALF OF THE OHIO ENVIRONMENTAL
COUNCIL AND ENVIRONMENTAL DEFENSE
FUND**

Michael R. Smalz (0041897)
OHIO POVERTY LAW CENTER
555 Buttles Avenue
Columbus, Ohio 43215-1137
msmalz@ohiopoverlylaw.com

Peggy P. Lee (0067912)
SOUTHEASTERN OHIO LEGAL SERVICES
964 E. State Street
Athens, Ohio 45701
plee@oslsa.org

**ON BEHALF OF THE APPALACHIAN PEACE
AND JUSTICE NETWORK**

M. Howard Petricoff (0008287)
Gretchen L. Petrucci (0046608)
VORYS, SATER, SEYMOUR AND PEASE LLP
52 East Gay Street
P.O. Box 1008
Columbus, Ohio 43216-1008
mhpetricoff@vorys.com
glpetrucci@vorys.com

David I Fein
Vice President, State Government
Affairs-East
EXELON CORPORATION
10 South Dearborn Street, 47th Floor
Chicago, IL 60603
david.fein@exeloncorp.com

Cynthia Fonner Brady
Assistant General Counsel
EXELON BUSINESS SERVICES COMPANY
4300 Winfield Road
Warrenville, IL 60555
cynthia.brady@constellation.com

Lael Campbell
EXELON
101 Constitution Avenue, NW
Washington, DC 20001
Lael.Campbell@constellation.com

**ON BEHALF OF CONSTELLATION
NEWENERGY, INC. AND EXELON
GENERATION COMPANY, LLC**

M. Howard Petricoff
Gretchen L. Petrucci
VORYS, SATER, SEYMOUR AND PEASE LLP
52 East Gay Street
P.O. Box 1008
Columbus, Ohio 43216-1008
mhpetricoff@vorys.com
glpetrucci@vorys.com

**ON BEHALF OF THE RETAIL ENERGY
SUPPLY ASSOCIATION**

Nicholas McDaniel (0089817)
ENVIRONMENTAL LAW & POLICY CENTER
1207 Grandview Avenue, Suite 201
Columbus, Ohio 43212
NMcDaniel@elpc.org

**ON BEHALF OF THE ENVIRONMENTAL LAW
AND POLICY CENTER**

Lisa M. Hawrot
SPILMAN THOMAS & BATTLE, PLLC
Century Centre Building
1233 Main Street, Suite 4000
P.O. Box 831
Wheeling, WV 26003-8731
lhawrot@spilmanlaw.com

Derrick Price Williamson
SPILMAN THOMAS & BATTLE, PLLC
1100 Bent Creek Blvd., Suite 101
Mechanicsburg, PA 17050
dwilliamson@spilmanlaw.com

Steve W. Chriss
Senior Manager, Energy Regulatory
Analysis
WAL-MART STORES, INC.
2001 SE 10th Street
Bentonville, AR 72716-0550
Stephen.Chriss@walmart.com

Tai C. Shadrick
SPILMAN THOMAS & BATTLE, PLLC
300 Kanawha Blvd. East
Charleston, WV 25301
tshadrick@spilmanlaw.com

**ON BEHALF OF WAL-MART STORES EAST,
LP AND SAM'S EAST, INC.**

Samantha Williams
NATURAL RESOURCES DEFENSE COUNCIL
20 N. Wacker Drive, Suite 1600
Chicago, IL 60606
swilliams@nrdc.org

**ON BEHALF OF THE NATURAL RESOURCES
DEFENSE COUNCIL**

Kevin R. Schmidt (0086722)
ENERGY PROFESSIONALS OF OHIO
88 East Broad Street, Suite 1770
Columbus, Ohio 43215
Schmidt@sppgrp.com

**ON BEHALF OF THE ENERGY
PROFESSIONALS OF OHIO**

Stephanie M. Chmiel (0087555)
THOMPSON HINE LLP
41 S. High Street, Suite 1700
Columbus, Ohio 43215
Stephanie.Chmiel@ThompsonHine.com

**ON BEHALF OF BORDER ENERGY
ELECTRIC SERVICES, INC.**

Gregory J. Poulos (0070532)
ENERNOC, INC.
471 E. Broad Street, Suite 1520
Columbus, Ohio 43215
gpoulos@enernoc.com

ON BEHALF OF ENERNOC, INC.

J. Thomas Siwo (0088069)
BRICKER & ECKLER LLP
100 South Third Street
Columbus, Ohio 43215-4291
tsiwo@bricker.com

**ON BEHALF OF PAULDING WIND FARM II
LLC**

Sarah Parrot (0082197)
Greta See
Attorney Examiners
PUBLIC UTILITIES COMMISSION OF OHIO
180 East Broad Street, 12th Floor
Columbus, OH 43215
sarah.parrot@puc.state.oh.us
Greta.See@puc.state.oh.us

ATTORNEY EXAMINER

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