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 Pursuant to § 4928.143, Revised Code, in the Form of an Electric Security Plan.	:	Case No. 13-2385-EL-SSO
In the Matter of the Application of Ohio Power Company for Approval of Certain Accounting Authority.	:	Case No. 13-2386-EL-AAM

POST-HEARING BRIEF

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

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INTRODUCTION

This initial post-hearing brief represents Staff of the Public Utilities Commission of Ohio's ("Staff") position regarding Ohio Power Company's ("AEP-Ohio" or the "Company") latest standard service offer application. AEP-Ohio proposes new riders in its application, and also proposes modifications to some existing riders. Staff will first address some of these new riders, then discuss some proposed changes to existing riders. Lastly, Staff discusses its recommendations regarding other aspects of AEP-Ohio's application. Staff believes that, with Staff's proposed modifications, the Commission should approve AEP-Ohio's application.

DISCUSSION

A. Staff's Position Regarding New Riders Proposed by AEP-Ohio

1. The Purchase Power Agreement Rider ("PPA Rider")

a. The PPA rider conflicts with the Commission's policy goal of transitioning to a fully competitive market.

i. The PPA rider contradicts the primary goal of AEP-Ohio's last ESP case, which was to transition AEP-Ohio to a fully competitive market.

Staff opposes AEP-Ohio's PPA rider for many reasons. Staff's primary concern, however, is that the PPA rider conflicts with the Commission's goal of moving to a fully competitive market. The Commission has been moving towards full market competition for over a decade.[1] In AEP-Ohio's last ESP case, the Commission discussed this transition to full competition, and the role AEP-Ohio's ESP II played in this transition:

> Thirteen years ago our general assembly approved legislation to begin paving the way for electric utilities to transition towards market-based pricing, and provide consumers with the ability to choose their electric generation supplier. While the process has not been easy, we are confident that this plan

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[1] *In the Matter of the Application of Ohio Power Company for Authority to Establish a Standard Service Offer Pursuant to § 4928.143, Revised Code, in the Form of an Electric Security Plan*, Case Nos. 13-2385-EL-SSO, *et al.* ("*Ohio Power ESP*") (Staff Ex. 18 (Prefiled Direct Testimony of Dr. Hisham M. Choueiki) at 7) (May 20, 2014) ("Choueki Direct").

> will result in the outcome the general assembly intended
> under both Senate Bill 3 and Senate Bill 221.[2]

The Commission's goal in the *ESP II Case* was clear. The objective was to expeditiously transition AEP-Ohio's generation assets to a fully competitive market. The Commission stated that this transition was one of the "most significant of the non-quantifiable benefits" of the *ESP II Case*. [3] The Commission found that an important justification for the Rate Stabilization Rider ("RSR") - arguably the most contentious aspect of the ESP II case- was that the RSR would ensure that AEP-Ohio would meet the "finish line of a fully-established competitive electric market."[4] Once AEP-Ohio reaches this "finish line", corporate business decisions and market forces will dictate the success or failure of AEP-Ohio's former[5] generation assets, *not* the Commission. Regulated cost-of service recovery for AEP-Ohio's generation assets will cease to exist when this goal is reached.

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2 *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Authority to Establish a Standard Service Offer Pursuant to 4928.143, Ohio Rev. Code, in the Form of an Electric Security Plan*, Case Nos. 11-346-EL-SSO, *et al*. (hereafter "*ESP II Case*") (Opinion and Order at 76) (Aug. 8, 2012).

3 *Id*. at 76.

4 *Id*. at 36. The Commission stated that "but for the RSR it would be impossible for AEP-Ohio to completely participate in full energy and capacity based auctions beginning in June 1, 2015." *Id*. at 76.

5 All of AEP-Ohio's former generation assets, except OVEC, have been transferred to AEP Genco.

AEP-Ohio is near the "finish line" of full competition, and will soon become a "wires only" company that no longer sells electricity to Ohio ratepayers.[6] However, before it even reaches the "finish line", AEP-Ohio asks to the Commission to reverse course and begin "reregulating"[7] some of AEP-Ohio's generation assets. The PPA rider will move AEP-Ohio in the exact opposite direction of market-based competition. It would provide AEP-Ohio a guaranteed revenue stream for its generation assets, irrespective of market forces.[8] This includes a return on equity for AEP-Ohio and the other OVEC Sponsoring Companies. [9] Further, AEP-Ohio would receive this nonmarket-based cost recovery despite the fact it will no longer sell electricity to Ohio ratepayers.

Staff is concerned that going down the PPA rider path may ultimately be a mistake. Not only would it defeat the whole point of AEP-Ohio's *ESP II Case,* it will also invite all Ohio EDU's to seek guaranteed cost recovery for generation assets that are *not* committed to Ohio ratepayers and are *not* regulated by the Commission.

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6 Choueki Direct at 9.

7 Staff uses the term "reregulation" lightly because the regulatory role the Ohio Commission would play in AEP-Ohio's PPA proposal would be much more limited than the Commission's traditional role. The Ohio Commission's jurisdiction (or lack thereof) over potential PPA's is discussed more fully below.

8 Tr. I at 29-30 (AEP-Ohio witness Vegas admits that AEP-Ohio recovers any cost through the PPA rider to the extent the cost are not recovered in the market).

9 Tr. XIII at 3217; Tr. II at 556 (AEP-Ohio witness Allen admitting the OVEC Sponsoring Companies receive a return on equity as part of the OVEC costs).

ii. The PPA rider is unwarranted because there are more appropriate methods of stabilizing customer prices that are currently being used by the Commission and shopping customers.

Instead of focusing on the guaranteed cost recovery aspect of the PPA rider, AEP-Ohio promotes the PPA rider as a "cost stabilization mechanism." Staff addresses AEP-Ohio's failure to prove the existence of this cost-stabilizing effect later in this brief; what should be noted here is that there are currently more effective methods of mitigating market volatility than the PPA rider.[10] Staff witness Choueiki testified that the Commission's practice of staggering and laddering SSO auction products has successfully addressed market volatility.[11] AEP-Ohio witness Allen acknowledged that the laddering and staggering of auction products "smooth out the impact of price changes for SSO customers"[12] and have "the effect of mitigating short-term changes in market prices for SSO customers."[13] AEP-Ohio witness McDermott admits that SSO customers pay a blended auction price, and are not exposed to real-time energy market volatility.[14]

While the SSO auction structure mitigates market volatility for SSO customers, shopping customers have market-based options that alleviate market volatility. Most

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10 Choueiki Direct at 10.

11 *Id*. at 10-11; Tr. XII at 2934.

12 *Ohio Power ESP* (Company Ex. 32 (Rebuttal Testimony of William A. Allen) at 2) (Jun. 20, 2014) ("Allen Rebuttal").

13 Allen Rebuttal at 3.

14 Tr. XIII at 3141.

commercial and residential customers that are shopping purchase electricity on a fixed-price basis.[15] AEP-Ohio witness McDermott admitted that only a very few number of customers – primarily large customers – buy on an index that is tied to PJM's hourly or day-ahead market.[16] He also admitted that these few, large customers are sophisticated enough to buy hedges or call options, which mitigate market volatility.[17] The record shows that there are already a number of fixed-price offers available in AEP-Ohio's territory. Currently, 51 residential CRES offers for fixed-price contracts in AEP-Ohio's territory.[18] 31% of these offers are for terms of more than a year.[19]

Although the current market contains these various hedging options for customers, AEP-Ohio wants to force a nonmarket-based, nonbypassable hedge on all of its customers. This proposal is unwarranted. The current market, where customers can shop and voluntarily choose fixed-price arrangements or other hedging options, should be allowed to run its course. Allowing the market to continue developing is consistent with the Commission's policy goals. The PPA rider is not.

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[15] Tr. XIII at 3084.

[16] *Id*.

[17] *Id*.

[18] Allen Rebuttal, Ex. WAA-R3, at 1.

[19] *Id*.

iii. If the PPA rider is granted, the Commission would have no authority to disallow PPA rider costs, and would have almost no power to challenge PPA rider costs.

Another problem with the PPA rider is that the Commission's role in regulating the prudency of AEP-Ohio's generation-related costs will be very limited or, even worse, nonexistent. The PPAs will be subject to the Federal Energy Regulatory Commission's ("FERC") jurisdiction, not the Commission's.[20] PPA rider costs will not be subject to prudency review by the Commission, and the Commission will not have the ability to independently disallow any costs AEP-Ohio assess its retail customers. Rather, if the Commission disagreed with certain PPA costs, the Commission would have to file a complaint at FERC and the Commission would have the burden of proving that these costs were unreasonable.[21]

And, to make matters worse, a heightened burden of proof would be applied because the Commission would be challenging a rate established by a FERC-approved contract. The U.S. Supreme Court has held that, under the *Mobile Sierra* doctrine, FERC must presume that a rate set by a wholesale-energy contract is just and reasonable.[22] The only way to overcome this presumption is to show that the contract "seriously harms

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[20] Tr. I at 31-33.

[21] *Id*. at 34.

[22] *NRG Power Mktg., LLC v. Maine Pub. Utilities Comm'n*, 558 U.S. 165, 130 S. Ct. 693 (syllabus) (2010).

the public interest." The U.S. Supreme Court stated that this requires a finding of "unequivocal public necessity" or "extraordinary circumstances", which goes well beyond the "just and reasonable" standard.[23]

This would be a complete departure from how OVEC's costs are treated today. The Commission currently reviews the prudency of OVEC costs in Fuel Adjustment Clause ("FAC") cases because the costs relate to AEP-Ohio's actual supply of electricity to SSO customers.[24] AEP-Ohio has the burden of proof in FAC cases. These FAC cases will end on June 1, 2015 when AEP-Ohio moves to 100% market-based auctions. At that time, Staff believes market forces should determine whether AEP-Ohio can recover its OVEC costs. This would be better than the PPA rider, which would burden all of AEP-Ohio's distribution customers with generation-related costs that the Commission no longer regulates.

iv. There are more appropriate and effective ways to address concerns about the PJM wholesale markets than the PPA rider.

Like many of the parties, Staff has concerns about market volatility and the continuing development of the wholesale markets. The PPA rider, however, is not a proper solution to issues in the wholesale markets. The Commission determined in the *ESP II Case* that AEP-Ohio's generation service should be market based. This determination is

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23 *Morgan Stanley Capital Grp. Inc. v. Pub. Util. Dist. No. 1 of Snohomish Cnty., Wash.*, 554 U.S. 527, 528, 128 S. Ct. 2733, 2735, 171 L. Ed. 2d 607 (2008).

24 R.C. 4928.143(B)(2)(a).

consistent with SB 3 and SB 221. To the extent AEP-Ohio has concerns about the wholesale market, the competitive wholesale market is under FERC's jurisdiction,[25] and that is the proper forum to address those concerns. Staff witness Choueiki testified regarding the continuing development of PJM's wholesale markets. He testified that the PJM energy market is already a competitive market.[26] To the extent the PJM capacity market is not fully competitive, Dr. Choueiki explained that Staff's "focus is on improving the capacity market in PJM because that benefits Ohio."[27] Both Dr. Choueiki and OCC witness Wilson discussed steps that are being taken at PJM to avoid market volatility and ensure adequate capacity prices. [28]

Although AEP-Ohio may claim the PPA rider will help address reliability concerns, AEP-Ohio witness Vegas admits that *reliability concerns are not the reason for the*

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25 Tr. XII at 2830.

26 *Id*. at 2999.

27 *Id*.

28 *Id*. at 2958; 2976, 2979 (Staff witness Choueiki discussing how some concerns about compensation for demand response that participates in the PJM auction have already been addressed; discussing PJM potentially auditing generators that receive capacity payments; discussing how PJM addressed concerns regarding increased reliance on capacity imports across RTO seems); Tr. X at 2496-2498, 2503-2505 (OCC witness Wilson discussing potential changes in rules due to the polar vortex; discussing the fact that PJM has a large amount of capacity that should be able to respond to another crisis if performance incentives are in place, discussing recent improvements in demand response).

OVEC PPA rider.[29] In addition, reliability of generation resources is under FERC's jurisdiction,[30] and the most recent Base Residual Auction ("BRA") shows that there are sufficient resources available for the next three years, which would cover the ESP term proposed by AEP-Ohio.[31] Staff witness Choueiki testified that the Commission has tools to address potential reliability needs in the future.[32] For example, the Commission could approve a nonbypassable rider to fund the construction of a new generating facility if the Commission determines that there is a need for the facility.[33] This process would be far superior to the PPA rider because it would require proof that a capacity need exists, the construction of the facility would involve a competitive bidding process, and the facility would actually supply power to AEP-Ohio's customers.[34]

In short, there are a number of systems in place to address price volatility and reliability concerns. Staff intends to continue working within these systems, and encourages AEP-Ohio to do the same. But, the PPA rider is not a proper or effective remedy to concerns with the PJM markets.

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29 Tr. I at 28.

30 Tr. XII at 2853.

31 Tr. XII at 2830, 3004.

32 *Id*. at 2853.

33 R.C. 4928.143(B)(2)(b).

34 *Id*.

b. The PPA rider should be denied because it would violate both Ohio and federal law.

The fact the PPA rider is contrary to the Commission's policy goals is clear. What is less clear is whether the PPA rider, if granted, would be lawful. Even if the Commission favors the general concept of the PPA rider, both Ohio and federal law preclude the rider as currently proposed by AEP-Ohio.

i. The PPA rider is not permitted under Ohio law.

a. OVEC costs are generation-related cost that AEP-Ohio cannot recover in an ESP once AEP-Ohio moves to 100% market-based pricing.

No provision in R.C. 4928.143 justifies the PPA rider. It is undisputed that AEP-Ohio would recover generation-related costs through the PPA rider.[35] The general rule is that generation service is not regulated by the Commission, and EDU's are only allowed to recover generation-related costs if these costs are permitted under R.C. 4928.141 to 4928.144.[36] AEP-Ohio recovers OVEC costs through the FAC, which is a bypassable charge permitted under R.C. 4928.143(B)(2)(a). These costs are only recoverable in an ESP today because R.C. 4928.143(B)(2)(a) allows EDU's to recover "the cost of fuel

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35 AEP-Ohio witness Spitznogle admitted that OVEC cost are "generation related." Tr. I at 265.

36 R.C. 4928.05(A)(1) ("On and after the starting date of competitive retail electric service, a competitive retail electric service supplied by an electric utility or electric services company shall not be subject to supervision and regulation … by the public utilities …. Nothing in this division shall be construed to limit the commission's authority under sections 4928.141 to 4928.144 of the Revised Code.")

used to generate the electricity supplied under the offer" and "the cost of purchased power supplied under the offer."

Once AEP-Ohio moves to 100% auction, AEP-Ohio will stop supplying Ohio customers with electricity from OVEC and AEP-Ohio will be a "wires only" company. At that point, Ohio law does not allow AEP-Ohio to continue recovering OVEC's generation-related cost through an ESP. How does AEP-Ohio address this legal issue? It tries to transform OVEC's generation-related, FAC cost into a "financial hedge." But the ending of the FAC mechanism is just one legal hurdle: AEP-Ohio also attempts to force shopping customers to pay for these generation-related costs even though shopping customers pay no cost related to OVEC today. If the Commission grants AEP-Ohio's request, the OVEC costs will become a new, nonbypassable burden for shopping customers.

b. Forcing all of AEP-Ohio's distribution customers to subsidize AEP-Ohio's generation-related assets would violate R.C. 4928.02(H).

The PPA rider would also violate R.C. 4928.02(H), which states that the Commission should:

> 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 to a product or service other than retail electric service, and vice versa, including by prohibiting the recovery of any generation-related costs through distribution or transmission rates.

The PPA rider would force all of AEP-Ohio's distribution customers, including shopping customers, to subsidize AEP-Ohio's generation assets. The Supreme Court of Ohio has criticized similar anti-competitive subsidies for EDU's in the past. In *Indus. Energy Users-Ohio v. Pub. Util. Comm*., 2008-Ohio-990, 117 Ohio St. 3d 486, 487-88, 885 N.E.2d 195, 198, the Court reversed a Commission decision that allowed AEP-Ohio to charge all of its distribution customers for costs related to the potential construction of a generation facility. The Court held that it was unlawful for the Commission to allow AEP-Ohio to use "revenues from noncompetitive distribution service to subsidize the cost of providing a competitive generation-service component."[37]

The Commission has previously addressed why it is important to comply with R.C. 4928.02(H).[38] In the *Sporn Case*, the Commission rejected AEP-Ohio's request to establish a non-bypassable charge that would recover plant closure costs for from all distribution customers, and discussed why such a charge would violate R.C. 4928.02(H):

> Additionally, the Commission notes that [AEP-Ohio's] recovery of the closure costs would be contrary to the state policy found in Section 4928.02(H), Revised Code. That policy requires the Commission to avoid subsidies flowing from a

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37 *Indus. Energy Users-Ohio* at ¶ 37. See also, *Elyria Foundry Co. v. Pub. Util. Comm*., 2007-Ohio-4164, 114 Ohio St. 3d 305, 315, 871 N.E.2d 1176, 1188. In *Elyria*, the Court reversed a Commission decision that allowed FirstEnergy to defer and recover fuel costs from all of FirstEnergy's distribution customers. The Court stated that the Commission violated R.C. 4928.02(G) - which subsequently became R.C. 4928.02(H) - "by allowing that generation-cost component to be deferred and subsequently recovered in a distribution rate case, or alternatively allowing FirstEnergy to apply generation revenues to reduce distribution expenses." *Elyria Foundry* at ¶ 47.

38 *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 ("*Sporn Case*").

> noncompetitive retail electric service to a competitive retail electric service. [AEP-Ohio] seeks to establish a nonbypass-able charge that would be collected from all distribution cus-tomers by way of the PCCRR. Approval of such a charge would effectively allow the Company to recover competitive, generation-related costs through its noncompetitive, distribu-tion rates, in contravention of the statute. Accordingly, we find that [AEP-Ohio's] request for cost recovery should be denied.[39]

The *Sporn Case* is very instructive. In the *Sporn Case*, the Commission not only explained that AEP-Ohio's request for a nonbypassable charge would result in an anti-competitive subsidy, but also explained that recovery would be unlawful because there was no statutory justification for recovery of plant closure costs under R.C. 4928.143.[40] The PPA rider request suffers from the same flaws as AEP-Ohio's request in the *Sporn Case*. Both requests seek recovery of generation-related costs, but neither is allowed under any provision of the ESP statute.

Just like it did in the *Sporn Case*, the Commission should reject AEP-Ohio's cur-rent attempt to "recover competitive, generation-related costs through its noncompetitive, distribution rates, in contravention of the statute."[41]

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[39] *Sporn Case* (Finding and Order at 19) (Jan. 11, 2012).

[40] *Id*.

[41] *Id*.

ii. The PPA rider would be preempted by the Federal Power Act.

The PPA rider runs afoul of federal law, as well. The United States Court of Appeals, Fourth Circuit, recently held in *PPL EnergyPlus, LLC v. Nazarian* that Maryland's scheme to subsidize generators participating in the PJM markets was preempted under the Federal Power Act.[42] At issue in *Nazarian* was an order issued by the Maryland Public Service Commission that required electric utilities to enter into long-term purchase power agreements with generators.[43] In these long-term contracts ("contracts for differences" or "CfDs"), the generators were required to sell energy and capacity in the PJM market. The CfDs provided a guaranteed revenue stream to the generators, so long as the energy and capacity cleared the PJM markets. The CfDs did not require the generator to actually sell any energy or capacity to the electric utilities. In addition, the electric utilities would pass the differences between the PJM market revenues and the "contract price" on to ratepayers as charges or credits.[44]

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42 *PPL EnergyPlus, LLC v. Nazarian*, 4th Cir. No. 13-2419, 2014 WL 2445800 (Jun. 2, 2014). See also *PPL EnergyPlus, LLC v. Hanna*, 977 F. Supp. 2d 372, 406 (D.N.J. 2013) (the U.S. District Court of New Jersey held that similar New Jersey program that required utilities to enter into CfDs with generators was preempted by the Federal Power Act).

43 *Nazarian*, at *2-3.

44 *Id*. at *2-3.

The Court held that Maryland's order was unlawful because "it functionally sets the rate that [the generator] receives for sales into the PJM market."[45] The Court indicated that Maryland's "system of rebates and subsidies" supplanted the prices offered in the PJM capacity and energy market, which ultimately "compromise[d] the integrity of the federal scheme and intrude[d] on FERC's jurisdiction." The Court explained how Maryland's scheme had the "potential to seriously distort the PJM auction's price signals, thus "interfer[ing] with the method by which the federal statute was designed to reach its goals."[46] Because Maryland ratepayers would be providing a generator (a bidder in the PJM auction) with a guaranteed revenue stream, the generator would be indifferent about the price it bid into PJM auctions and potentially drive down the auction prices. This would not only send inaccurate price signals regarding the need for new generation, but it would also disadvantage other bidders that do not receive guaranteed cost recovery.

The similarities between AEP-Ohio's PPA rider and Maryland's CfDs are aplenty. The PPA rider, like the CfDs, establishes a "cost plus" recovery mechanism that provides guaranteed recovery for the generator, regardless of the revenues actually received from the PJM markets. Like the Maryland CfDs, the PPA rider is characterized as a "hedge"

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45 *Nazarian* at *5.

46 *Id*. at *8.

or "financial arrangement," and not a contract for the sale of energy or capacity.[47] And, most importantly, the PPA rider would result in AEP-Ohio being compensated for its participation in the wholesale market in a manner that conflicts with the federally administered the PJM auction, just like Maryland's CfDs. This is the crux of the preemption problem. The PPA rider would remove any incentive for AEP-Ohio to bid a price into the PJM auction that is based on marginal costs, and would be inherently anti-competitive to other wholesale generators bidders.

AEP-Ohio asks the Commission to stir up a legal hornets' nest with its PPA rider request. But, there is an easy way for the Commission to avoid this dilemma: deny the PPA rider.

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[47] The unsuccessful defendants in New Jersey and Maryland tried to characterize the CfDs as "hedges" or "financial arrangements." *PPL Energyplus, LLC v. Nazarian*, 974 F. Supp. 2d 790, 835 (D. Md. 2013)) (The U.S. District Court, Maryland, "agree[d] … that the CfD is critically distinguishable from a swap or similar agreement and *cannot be categorized as a 'purely financial arrangement'*…")(emphasis added); and *Hanna*, 977 F. Supp. 2d at 406 ("In the defendants' view, the [CfDs] are purely financial contracts that do not involve physical sales of electricity….The Court finds that the [CfDs] occupy the same field of regulation as the [FERC] and *intrude upon the [FERC's] authority to set wholesale energy prices* through its preferred RPM Auction process.") (emphasis added).

c. AEP-Ohio failed to prove that the PPA rider will actually stabilize customer rates.

AEP-Ohio's rationale for proposing the PPA rider is to "stabilize customer rates."[48] AEP-Ohio has the burden of proving that this stabilizing effect exists.[49] AEP-Ohio failed to meet this burden. A number of intervenors will, presumably, discuss in their post-hearing briefs how AEP-Ohio failed prove that the PPA rider will stabilize customer rates. Staff, however, would point out some of the most alarming evidentiary flaws in AEP-Ohio's PPA rider case.

i. AEP-Ohio's own cost-estimate shows that the OVEC PPA rider will cost customers at least $52 million during the ESP Period.

A substantial amount of evidence shows that the PPA rider will impose significant costs on customers during the term of ESP III. AEP-Ohio's own estimate indicates that the PPA rider will cost customers $52 million during the term of ESP III.[50] AEP-Ohio witness Vegas stands behind this $52 million cost-estimate, and believes it is reasonable.[51] There is also evidence that the PPA rider may cost customers substantially more

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48 *Ohio Power ESP* (Company Ex. 1 (Application) at 14) (Dec. 20, 2013) ("Application"); Company Ex. 2 (Direct Testimony of Pablo A. Vegas at 13) (Dec. 20, 2013) ("Vegas Direct"); Company Ex. 7 (Direct Testimony of William A. Allen at 8) (Dec. 20, 2013) ("Allen Direct").

49 R.C. 4928.143(C)(1).

50 *Ohio Power ESP* (IEU Ex. 1B (Direct Testimony of Kevin M. Murray at 9-10) (May 6, 2014) ("Murray Direct") (public version).

51 Tr. I at 110.

than $52 million. Both IEU-Ohio witness Murray and OCC witness Wilson testified that the PPA rider cost could rise to $82 million during the term of the ESP if certain "lean improvement" cost reductions fail to materialize.[52] It is quite possible these cost-reductions will never materialize because AEP-Ohio witness Allen admitted that neither OVEC nor AEP-Ohio has committed to these cost-reductions.[53] Based on this evidence alone, it appears that the PPA rider could be extremely costly for customers during the ESP III term.

ii. At best, the record is unclear whether the PPA Rider will stabilize customer rates because AEP-Ohio presented inconsistent evidence regarding the potential costs or benefits of the PPA rider.

Even if the Commission does not agree with the cost-estimates of IEU-Ohio or OCC, the record still does not support adoption of the PPA rider. This is because AEP-Ohio presented various, conflicting estimates regarding the potential costs of the PPA rider. AEP-Ohio's own estimates, which have changed throughout the hearing, range from a $52 million cost to an $8.4 million benefit during the term of ESP III.

AEP-Ohio initially provided the parties with "three different scenarios" of the potential costs or benefits of the PPA rider. AEP-Ohio witness Vegas acknowledged that these three scenarios were inconsistent, stating that some scenarios showed "costs", while

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[52] Murray Direct at 10-11; OCC Ex. 15A (Direct Testimony of James F. Wilson at 13) (May 6, 2014) ("Wilson Direct").

[53] Tr. II at 552.

others showed a "benefit."[54] AEP-Ohio witness Allen also acknowledged the inconsistency in these three "scenarios" prepared by AEP-Ohio.[55] Although one scenario indicated that the PPA rider would cost customers $52 million during the ESP III term, Mr. Allen initially testified that the cost of the PPA rider was "neutral," and he chose not to incorporate any quantifiable cost or benefit regarding the PPA rider in his ESP v. MRO analysis.[56]

The confusion regarding the true cost of the PPA rider does not end there. AEP-Ohio witness Allen developed a fourth scenario during the hearing,[57] which was unveiled for the parties for the first time during his cross-examination. AEP-Ohio witness Allen's latest scenario indicates that the PPA rider will lead to an $8.4 million credit during the ESP. The latest scenario, however, is inconsistent with AEP-Ohio's original estimate of a $52 million cost for the PPA rider during the ESP Period.[58] And this latest scenario is inconsistent with Mr. Allen's testimony indicating that the PPA rider will be cost-neutral

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54 Tr. I at 149.

55 Tr. II at 635.

56 *Id*. at 507.

57 *Id*. at 484-485 (AEP-Ohio witness Allen admitted that he developed the latest scenario the day before he took the stand, which was after the hearing had began.)

58 *Id*. at 508. ("Question: Could you tell me… what the cost over the ESP period on Attachment 1 is? Answer: What Attachment 1 would indicate would be that the PP rider would have a cost of $52 million.)

during the ESP Period.[59] It is also inconsistent with Mr. Allen's ESP v. MRO test, where he did not assign any quantifiable benefit to the PPA rider.[60]

AEP-Ohio may believe that any and all of these many scenarios are reasonable. The question, however, is which one should the Commission rely on to determine the PPA rider will "stabilize rates for customers"? There is an approximately $62.4 million swing between AEP-Ohio's best and worst case cost-scenarios.[61] There are simply too many discrepancies in AEP-Ohio's fluctuating cost-estimates for AEP-Ohio to claim that the PPA rider will stabilize rates for customers.

iii. There are various unknown factors that make it virtually impossible to determine whether the PPA rider will actually stabilize rates for customers.

Putting aside the dueling scenarios, there are other unknowns regarding the PPA rider that hurt AEP-Ohio's "price stability" claim. The evidence shows that potential fluctuations in OVEC's costs and changes in market prices may erase any potential stability that the PPA rider can purportedly provide. AEP-Ohio witness Vegas admits that AEP-Ohio is not guaranteeing a certain level of credits or a benefit to customers from the

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59 Tr. II at 507, 605.

60 *Id*. at 602. ("I did not analyze [the PPA rider] as a quantifiable benefit.")

61 The difference between $52 million costs and $8.4 million credit is $62.4 million.

PPA rider.[62] Rather, AEP-Ohio is "just offering a hedge" and the results of this hedge will "depend on future market prices."[63]

Another unknown factor regarding the PPA rider is potential changes in OVEC's costs. The success or failure of the PPA rider depends on the stability of OVEC's costs. Although AEP-Ohio touts the relative stability of OVEC costs, there are a number of factors that could greatly increase the costs of operating the OVEC units over the next few years. Some of these factors include additional capital expenditures, increases in coal prices, and future environmental regulations.[64] Whether or not customers will benefit financially from the PPA rider also depends largely on the market, which cannot be predicted by AEP-Ohio. AEP-Ohio witness Allen admits that the PPA rider will be a net charge to customers during the ESP Period if market prices remain low.[65]

Because the PPA rider is inherently tied to the PJM day-ahead market, the PPA rider will reflect the potentially volatile PJM market fluctuations.[66] Contrast this with SSO prices. SSO prices are established by 12-month through 41-month full requirements contracts resulting from competitive auctions.[67] These prices are fairly stable over

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62 Tr. I at 149.

63 *Id*.

64 *Id*. at 152-153.

65 Allen Direct at 11.

66 Wilson Direct at 30.

67 *Id*. at 29; Tr. XII at 2809.

time. AEP-Ohio witness McDermott admits that the SSO auction is an "effective method of mitigating price volatility"[68] and admits the SSO auction mitigates price fluctuations.[69] The PPA rider will simply upset the price stability that the SSO auction already provides.[70] AEP-Ohio witness McDermott also admitted that the PPA rider introduces an additional element of market risk for CRES customers that have fixed price contracts. [71]

Even if the PPA rider results in a credit for customers during the ESP Period, the proposed PPA rider is such a "small hedge"[72] that the credit will have little, if any, stabilizing effect on customers' rates. AEP-Ohio's portion of OVEC generation represents only 5 to 6 percent of the total connected load of AEP-Ohio,[73] which means any impact of the OVEC PPA rider on a particular customer's bill will be *de minimis* from the customer's perspective. In addition, generation supply is only about half of the customer's

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68 *Ohio Power ESP* (Company Ex. 32 (Rebuttal Testimony of Karl A. McDermott) at 11) (Jun. 23, 2014) ("McDermott Rebuttal").

69 *Id*.

70 Tr. VIII at 3141-3142 (AEP-Ohio witness McDermott admits that the PPA rider introduces an additional element of risk for SSO customers).

71 *Id*.

72 Tr. II at 571.

73 *Id*. at 480.

bill.[74] This means the relatively small “hedging” impact of the PPA rider may be easily erased by other factors, such as potential increases in AEP-Ohio’s other riders.[75]

iv. The PPA rider will destabilize prices for customers currently in fixed-price arrangements and force these customers to pay twice for nonexistent price stability.

The market already provides a method for hedging against market volatility- fixed price contracts. The PPA rider will effectively eliminate the value of these fixed price contracts by introducing an unwanted element of variability and market risk. And that’s just part of the problem: shopping customers on fixed-price contracts would be forced to pay twice for nonexistent price stabilization. They would pay once (voluntarily) through contract premiums for the fixed-price arrangement and again (involuntarily) through the nonbypassable PPA rider. Such a result would be unjust and certainly would not constitute “price stability.”

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[74] Wilson Direct at 31.

[75] *Ohio Power ESP* (Company Ex. 13 (Prefiled Direct Testimony of Andrea E. Moore) Ex. AEM-1 at 1) (Dec. 20, 2013) (“Moore Direct”).

d. If the Commission adopts the PPA rider, it should place the conditions on the rider recommended by Staff.

If the Commission approves the PPA rider, Staff recommends that the Commission place some conditions on the rider. Staff witness Choueiki made a number of recommendations regarding conditions that should be placed on the PPA Rider. The following are Staff's recommended conditions:

i. <u>There should be no "expanded PPA rider"</u>. The PPA rider should be limited to the OVEC assets only.[76]

ii. <u>The Commission should require AEP-Ohio to include in the terms of the PPA that the expenses are subject to a prudency review of the Commission</u>.[77] Including such a provision in the PPA would, hopefully, avoid some of the issues discussed above regarding the applicability of the *Mobile Sierra* doctrine at FERC.

iii. <u>The Company should allow Staff to evaluate the bidding strategies used for the OVEC, and compare those with the bidding strategies used by AEP Genco</u>.[78] Staff is concerned that the AEP-Ohio regulated business unit that bids the OVEC may use different bidding strategies than those used by its unregulated affiliate, AEP Genco.

These conditions may minimize some of Staff's concerns. But, they assuredly will *not* cure all the ills discussed above. The only surefire way for the Commission to do so is deny the PPA rider.

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76 Choueiki Direct at 11-12.

77 *Id*. at 12-13.

78 *Id*. at 13.

2. Sustained and Skilled Workforce Rider ("SSWR")

The Company proposes to implement a new program designed to ensure the availability of a sustained and skilled workforce.[79] The Sustained and Skilled Workforce Rider ("SSWR") would recover incremental operations and maintenance ("O&M") labor costs.[80] These costs would be incurred to hire, train, and deploy 150 field construction and construction support employees. Capital costs associated with these employees would be recovered through the existing DIR mechanism.[81] The putative purpose of this proposal is to support a "comprehensive strategy for long-term improved reliability."[82]

Company witness Dias describes the Company's reliability strategic plan in his direct testimony.[83] Staff applauds the development and implementation of a reliability strategic plan. Staff agrees that the plan proposed by the Company, as otherwise discussed herein, is generally aligned with programs supported by prior Commission authorized riders and customer expectations. Such a plan will also clearly benefit AEP-Ohio customers. Staff respectfully submits, however, that not all components of that plan, including the SSWR, warrant approval in this proceeding.

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79 Application at 9.

80 *Id*. at 11.

81 *Ohio Power ESP* (Company Ex. 4 (Pre-filed Direct Testimony of Selwyn J. Dias at 26-27) (Dec. 20, 2013) ("Dias Direct").

82 Application at 11.

83 Dias Direct at 3.

The Company's SSWR proposal is predicated on a projection that additional employees will "be required to execute the infrastructure investment plan."[84] This is in large part due to increasing reliance on contractor resources of variable availability in what witness Dias described as a "constrained labor market."[85]

Staff generally does not dispute the Company's underlying predicates – that additional workers will be needed, or that increasing reliance on contact workers has created uncertainty and cost. But Staff disagrees that recovery in the form of the proposed SSWR should be approved in the context of an Electric Security Plan. As Staff witness Willis testified:

> [t]he proper recovery mechanism is through a distribution rate case. If the Applicant believes it has insufficient internal resources to implement its existing "suite of riders and mechanism" in the future, then the Company could hire and begin training the labor forces it believes are necessary to implement its distribution reliability plan the Commission has previously approved.[86]

To this extent, Staff agrees with the observations made by OCC witness Effron. Mr. Effron noted, for example, that the retirement of employees elsewhere in the company may well offset costs incurred by the addition of these new employees, and may

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84 Dias Direct at 23.

85 *Id*. at 25.

86 *Ohio Power ESP* (Staff Ex. 8 (Pre-filed Direct Testimony of Wm. Ross Willis) at 4) (May 20, 2014) ("Willis Direct").

well not increase either the total employee complement or actual labor expense.[87] Favorably noting the Staff Report in the 2007 Vectren rate case[88], Mr. Effron succinctly summarized the position consistently taken by Staff that the costs of hiring new employees to address an aging workforce should be subject to normal regulation practices for test year expenses, and not recovered through a rider.[89]

The Company's proposal is little more than an effort to accelerate cost recovery while avoiding a base rate case and the scrutiny that such cases entail. In essence, the Company posits that any cost that "supports" its comprehensive reliability strategy could be recovered through a rider approved in an ESP proceeding. But while Company witness Dias acknowledged that "the cost to achieve continuous and increasing reliability improvements will increase exponentially" as the Company improves reliability,[90] it seeks to avoid both regulatory lag and scrutiny by substituting single issue *post hoc* prudence reviews.

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[87] *Ohio Power ESP* (OCC Ex. 18 (Pre-filed Direct Testimony of David J. Effron) at 22) (May 6, 2014) ("Effron Direct").

[88] *In the Matter of Vectren Energy Delivery of Ohio, Inc.*, Case Nos. 07-1080-GA-AIR and 07-1080-GA-ALT (Staff Report of Investigation at 10) (Jun. 16, 2008).

[89] Effron Direct at 21-22.

[90] Dias Direct at 6.

3. NERC Compliance and Cybersecurity Rider ("NCCR")

The NCCR would be a placeholder rider established from the date of the ESP III order through June 2018.[91] Through this rider, AEP-Ohio could track and defer compliance costs of new NERC requirements or new interpretations of existing NERC requirements and request recovery for these costs during the ESP III term.[92] Staff opposes the NCCR at this time because of the vast uncertainty associated with the rider. AEP-Ohio is asking for authority to establish a rider to recover an indeterminate amount of costs that will be incurred at an unknown time for undefined investments to follow NERC standards that do not currently exist and will not apply to AEP-Ohio as a distribution company. It is virtually impossible to know less about what might be contained in this rider than we do currently.

Staff has no reason to believe that AEP-Ohio, as a distribution company, will incur costs for compliance with NERC standards because NERC does not have the authority to establish NERC standards for distribution companies. The Federal Power Act gives NERC the authority "to establish and enforce reliability standards for the bulk-power system."[93] The term "bulk-power system" includes transmission and generation facilities, but "does not include facilities used in the local distribution of electric energy."[94] In

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91 Vegas Direct at 16.

92 *Id*.

93 16 U.S.C. § 824o(a)(2).

94 16 U.S.C. § 824o(a)(1).

other words, NERC does not have the authority to establish NERC standards for AEP-Ohio as a distribution company. To the extent AEP-Ohio has to comply with NERC requirements for its transmission functions, a mechanism is already in place (the Transmission Cost Recovery Rider (TCRR)) to enable AEP-Ohio to recover those costs.[95]

Beyond the issue of whether AEP-Ohio, as a distribution company, is subject to NERC standards, Staff has no understanding of the types of investments AEP-Ohio would seek recovery for in the NCCR, the magnitude of those investments' costs, or how those costs would be appropriately allocated among AEP-Ohio's corporate functions.[96] Consequently, neither the Staff nor the Commission has a sense of the potential magnitude of the costs AEP-Ohio would seek recovery for in the NCCR. The Company could seek to recover a thousand dollars, a million dollars, or a billion dollars. There is no way of knowing.

Until the Company is able to identify and quantify its cybersecurity and reliability related expenditures, Staff is unable to assess the appropriateness and adequacy of those expenditures. Staff is also unable to determine whether the Company has properly allocated its NERC compliance costs to its generation and transmission functions so that it does not improperly pass those costs onto AEP-Ohio's distribution customers.

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95 This recovery would occur, if at all, through a rate determined by the FERC.

96 *See Ohio Power ESP* (Staff Ex. 5 (PUCO-Staff Pearce Company Data Request at 43).

Staff recognizes that the Commission has approved placeholder riders in the past.[97] Staff has even supported some of these riders.[98] But, Staff believes that it is premature to give the Company a means to recover its NERC compliance costs when the Company has not demonstrated that it would be subject to NERC standards as a distribution entity[99], not identified its potential investments for cybersecurity and reliability standards, not quantified the costs of those investments, and not explained how those costs would be properly allocated to its generation, transmission, and distribution functions. Simply put, the NCCR involves too much uncertainty for Staff to support the rider at this time.

4. Auction Cost Recovery Rider ("ACRR")

The Company is proposing to collect all costs associated with the competitive bid process through the Auction Cost Recovery Rider ("ACRR"). Recovery of this rider is

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97 *ESP II Case*; *In the Matter of the Application of Duke Energy Ohio, Inc., for Approval of an Electric Security Plan*, Case No. 08-920-EL-SSO (Opinion and Order at 17) (Dec. 17, 2008); *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company and The Toledo Edison Company for Authority to Establish a Standard Service Offer Pursuant to R.C. 4928.143 in the Form of an Electric Security Plan*, Case No. 08-935-EL-SSO, *et al*. (Opinion and Order at 12, 15) (Mar. 25, 2009).

98 *ESP I Case*; *ESP II Case*.

99 Staff believes that the Company cannot show this.

on a per kWh basis and will be updated quarterly.[100] This rider replaces the Auction Phase-in Rider ("APIR").

Staff generally agrees with the Company's proposal. However, the Company should be allowed to collect only the prudently incurred costs associated with the competitive bid process. Furthermore, Staff is amenable to quarterly updates to the ACRR rider, but Staff recommends that rider ACRR be subjected to an audit on an annual basis. Staff recommends that the Commission direct the Company to work with Staff regarding details of the audit process, if the Commission believes such an audit process is warranted.

In addition, Staff recommends that the Commission ensure that there is no overlap of costs between the ACRR and the APIR.[101] Staff is concerned that there is the potential for an overlap in costs because the ACRR is replacing the APIR.[102] The Commission can easily address this concern by stating in its order in this case that Staff should ensure that there is no overlap during future audits of the ACRR rider.[103] This way, any future Staff member that may be auditing the ACRR rider will be made aware that this potential for overlap of costs exists and will watch for this potential issue.[104]

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[100] *Ohio Power ESP* (Staff Ex. 7 (Prefiled Direct Testimony of Matthew D. Snider) at 7) (May 20, 2014) ("Snider Direct"); Moore Direct at Ex. AEM-4.

[101] Snider Direct at 3.

[102] *Id*.

[103] *Id*.

[104] *Id*.

5. Purchase of Receivables and Bad Debt Rider

Staff supports the concept of AEP-Ohio implementing a purchase of receivable ("POR") program.[105] Staff, however, has a number of recommendations regarding the structure of AEP-Ohio's proposed POR program.

a. The Commission should adopt Staff's proposed CRES specific discount rate calculation.

i. AEP-Ohio should implement a discount rate as opposed to a bad debt rider because this will allow the Commission and AEP-Ohio to measure the potential impact of CRES uncollectible expenses.

Although Staff supports a POR program, Staff believes that AEP-Ohio should implement a discount rate instead of a bad debt rider. Implementing a discount rate before a bad debt rider would be consistent with Commission precedent, and allow AEP-Ohio to gain experience regarding the potential cost impact of CRES uncollectible charges.[106] The Commission and Staff have well over a decade of experience with POR programs, discount rates, and bad debt riders from Ohio's large gas utilities. The four large gas utilities[107] that currently have POR programs previously purchased competitive supplier

105 *Ohio Power ESP* (Staff Ex. 14 (Prefiled Direct Testimony of Patrick Donlon) at 4) (May 20, 2014) ("Donlon Direct").

106 *Ohio Power ESP* (Staff Ex. 13 (Prefiled Direct Testimony of Barbara Bossart) at 6) (May 20, 2014) ("Bossart Direct").

107 The East Ohio Gas Company *d.b.a* Dominion East Ohio, Vectren, Duke Energy Ohio, Inc., and Columbia Gas of Ohio.

receivables at a discount rate.[108] These gas utilities purchased receivables at a discount rate for years until 2003, when the uncollectable expense rider was established for these utilities.[109]

Staff witness Bossart testified that starting a POR program with a discount rate allows utilities to gain experience regarding the impact of the uncollectible charges attributable to suppliers.[110] This experience is important because suppliers are subject to the market, not Commission oversight.[111] This makes it difficult for the Commission or Staff to evaluate the potential impact the suppliers' uncollectable charges will have on customers if a bad debt rider is granted.[112] Requiring AEP-Ohio to implement a discount rate before a bad debt rider is a reasonable first step in AEP-Ohio's POR program, and consistent with the Commission' experience with other utility POR programs.

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108 Donlon Direct at 6.

109 *In the Matter of the Joint Application of the East Ohio Gas Company d.b.a. Dominion East Ohio, et al. for Approval of an Adjustment Mechanism to Recover Uncollectable Expenses*, Case No. 03-1127-GA-UNC (Finding and Order) (Dec. 17, 2003).

110 Bossart Direct at 6.

111 *Id*.

112 *Id*.

ii. Staff's proposed discount rate would properly balance CRES suppliers' and AEP-Ohio's interest by properly allocating risk.

Staff recommends that AEP-Ohio implement a discount rate calculation method that calculates separate discount rates for each CRES provider.[113] Staff witness Donlon explained in detail the mechanics of calculating this discount rate in his testimony.[114] What is important to note here is that Staff's CRES specific discount rate achieves three goals: (1) it ensures that each specific CRES provider pays only their incremental share of expenses[115]; (2) it properly accounts for the amount of uncollectible revenue that AEP-Ohio will experience from purchasing the receivables from each specific CRES provider[116]; and (3) it ensures that AEP-Ohio recovers the incremental cost of collection specific to each CRES provider.[117]

Staff also recommends that AEP-Ohio implement a POR discount cap of 5%.[118] The POR discount cap is the maximum that AEP-Ohio can discount the purchase of

113 Donlon Direct at 7.

114 *Id*.

115 *Id* at 8.

116 *Id*. at 9.

117 *Id*. at 10.

118 *Id*. at 11.

receivables of any one CRES provider. [119] The POR discount incentivizes AEP-Ohio to minimize its collection costs and diligently enforce its collection practices.[120]

In addition, Staff recommends that AEP-Ohio implement a partial payment tracking methodology in conjunction with the discount rate.[121] This internal tracking mechanism would allocate a customer's partial payment that does not completely pay the amount owed in the customer's bill.[122] Staff proposes that partial payments be allocated, after taxes, to the three services on the bill (generation, transmission, and distribution) based on the percentage each service represents on the particular bill.[123] This partial payment tracking mechanism is simply an internal allocation process that ensures the discount rate calculation is accurate.[124] It is not intended to change the Commission's partial payment priority rules.[125]

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119 Donlon Direct at 11.

120 *Id*.

121 *Id*. at 12.

122 *Id*.

123 Staff witness Donlon provided an example of how this would work. Take a customer that has a $105 bill. The bill consists of $5 of taxes and government fees, $25 for transmission charges, and $25 distribution charges, and the remaining $50 is for generation. Assume the customer pays only $25 dollars of their bill. First, $5 will allocated to pay taxes and government fees. Then, from the remaining $20, each service would receive a proportional share: $5 for distribution, $5 for transmission, and $10 for generation. Donlon Direct at 13.

124 *Id*.

125 *Id*.; Ohio Adm. Code 4901:1-10-22(G).

iii. Cost of Implementing the POR Program

AEP-Ohio estimates that it will cost approximately $1.5 million to implement a fully automated POR program. In addition to this $1.5 million, the Company forecasted $207,600 in incremental, annual O&M support cost. The Company proposes to collect those cost through a fee charged to the participating CRES providers.

If the Commission adopts Staff's proposed discount rate, Staff believes that recovery of the $207,600 through a fee to CRES providers is unnecessary because the estimated incremental O&M support costs will be assigned through the credit and collection adder. Staff, however, agrees with AEP-Ohio's proposal to assess CRES providers a yearly per-consolidated bill fee for the estimated $1.5 million cost of implementing a fully automated POR program.[126] Staff believes that the yearly per-consolidated bill fee should be adjusted annually.[127] When AEP-Ohio performs its annual calculation of the discount rate, it should also true-up the yearly per-consolidated bill fee. This true-up should compare actual cost of implementation with the cost estimates, and also include an adjustment for the most recent consolidating billing customer numbers.

Staff does not believe a hard cap on the cost to implement the POR program is necessary.[128] However, Staff recommends that AEP-Ohio track the cost of implementing the POR program. If the AEP-Ohio believes that implementation costs will exceed 10%

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126 Donlon Direct at 13-14.

127 *Id*.

128 *Id*. at 14.

of its $1.5 million estimate (or $150,000), it should notify the participating CRES providers and Staff. CRES providers should then be allowed to request that the Commission audit AEP-Ohio's implementation cost. If such a request is made by a CRES provider, the Commission should determine if an audit of the POR project implementation costs should be performed.[129]

b. If the Commission does not adopt Staff's recommended discount rate, another option is for AEP-Ohio to implement a bad debt rider, with a discount rate, that focuses on generation only.

If the Commission does not agree with Staff's discount rate proposal, there is another option available for the Commission that Staff believes is reasonable. Staff would also support an uncollectable expense mechanism that focuses on generation only. In addition, the bad debt rider still should include some form of discount rate. Staff witness Donlon testified that one of his primary concerns was making sure the discount rate or bad debt rider – whichever route the Commission chooses - is related to generation only.[130] Staff witness Donlon testified that he is concerned that AEP-Ohio's bad debt rider proposal uses an approximately $12 million uncollectable expense baseline established in AEP-Ohio's last distribution rate case. AEP-Ohio proposes to adjust the bad debt rider based upon the amount of uncollectable expense incurred above or below this baseline. This would allow AEP-Ohio to, in essence, adjust its uncollectable expense

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[129] Donlon Direct at 14.

[130] Tr. IX at 2171.

baseline, which relates to transmission and distribution. Staff is uncomfortable with this methodology, especially since AEP-Ohio recently had uncollectable expenses that exceeded this $12 million baseline. AEP-Ohio witness Moore testified that AEP-Ohio's uncollectable expense for 2013 was approximately $22.5 million.[131] $7.2 million of this amount was due to Ormet, which Staff understands was an unusual circumstance.[132] However, even after removing Ormet's uncollectable expense, AEP-Ohio still had approximately $15 million of uncollectable expenses for 2013, which would exceed the $12 million baseline proposed by AEP-Ohio.

Staff witness Donlon testified that it would be more appropriate for AEP-Ohio to adjust its uncollectable expenses for distribution and transmission in a distribution rate case.[133] Staff believes an uncollectable expense mechanism that focuses on generation only would be a more reasonable option than AEP-Ohio's current proposal.[134] This would make the $12 million baseline in base distribution rates irrelevant, and simply focus the bad debt rider on CRES receivables and generation-related uncollectable costs.[135]

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131 Tr. IV at 1108.

132 *Id*.

133 Donlon Direct at 6.

134 Tr. IX at 214.

135 *Id*. at 2172.

c. Only residential and GS-1 customers should be included in the POR program.

If the Commission adopts a bad debt rider, Staff recommends that the POR program apply to all residential and GS-1 customers that participate in consolidated billing. Staff witness Donlon testified that customers larger than GS-1 should be excluded from the POR program, even if they participate in consolidated billing.[136] Staff makes this recommendation because it is concerned about the potential impact of large commercial and industrial uncollectible debt on customers.[137] Recent events legitimize Staff's concerns. AEP-Ohio's 2013 bad debt expense reached $22.5 million, which included a $7.2 million charge-off associated with Ormet.[138] This shows that including large customers in the POR program could have a severe impact on residential customers' rates.

d. If the Commission approves a bad debt rider, the Commission should ensure that AEP-Ohio has strong collection practices in place.

If the Commission grants AEP-Ohio's request for a bad debt rider, Staff requests that the Commission order AEP-Ohio to work with Staff to ensure AEP-Ohio has strong collection practices in place. Because the bad debt rider will collect both CRES and AEP-Ohio uncollectable expenses from customers, it important to determine if AEP-Ohio

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136 Donlon Direct at 4.

137 Bossart Direct at 7.

138 *Id*.

has collection practices and procedures in place that will sufficiently control bad debt expenses.[139]

Staff asked AEP-Ohio for a variety of information regarding its collection practices.[140] Although AEP-Ohio provided Staff with many reports, it did not provide Staff with any criteria or benchmarks that it uses to evaluate its collection performance.[141] For example, Staff witness Bossart testified that AEP-Ohio provided reports regarding the collection practices of its outside collection agencies. This information showed that the outside collection agencies' percent of outstanding debt collected was 10.2% and 11.8% in years 2012 and 2013, respectively.[142] However, AEP-Ohio did not provide information indicating whether AEP-Ohio's considers these percentages good, bad, or simply average. As Staff witness Bossart explained, Staff was unable to determine what criteria AEP-Ohio uses to evaluate the various percentages and the information contained in the collection reports.[143] In addition, AEP-Ohio witness Moore was not aware if AEP-Ohio uses any particular criteria to evaluate the effectiveness of its collection activities.[144] Ms.

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139 Bossart Direct at 4.

140 *Id*.

141 *Id*.

142 *Id*.

143 *Id*.

144 Tr. IV at 1117.

Moore also indicated that AEP-Ohio does not have any particular benchmarks that it uses to determine if it should terminate its relationship with an outside collection agency.[145]

The issue of developing strong collection practices is not new to the Commission. In the Commission's review of the large gas companies' credit and collection practices, the Commission's auditor stated that it is a preferred practice for utilities to oversee their outside collection agencies' performance, and also perform routine audits to ensure compliance with utility standards. The auditor indicated that this process is necessary to ensure the effectiveness of collection activities.[146] Staff witness Bossart testified that AEP-Ohio needs to have specific evaluation criteria in place to properly evaluate outside and internal collection practices.[147]

Staff is not singling out AEP-Ohio. Staff witness Bossart testified that Duke currently has certain collection criteria that it uses to monitor and evaluate its collection practices.[148] AEP-Ohio may claim it has similar benchmarks. If this is true, great. But Staff was not provided such information during this case.[149] Staff would simply like AEP-Ohio to share this information with the Staff. This is a reasonable request. Staff

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145 Tr. IV at 1119.

146 Bossart Direct at 4-5.

147 *Id*.

148 Tr. VIII at 1905.

149 *Id*. at 1911.

asks that the Commission order AEP-Ohio to share this information with Staff before any bad debt rider is implemented.

B. Modifications to Existing Riders

1. Distribution Investment Rider ("DIR")

In general, Staff supports continuation of the Distribution Investment Rider ("DIR") as approved in the Company's prior SSO case.[150] Staff believes, however, that a number of changes should be made to the rider as proposed by AEP-Ohio.

a. General Plant accounts should not be included in the DIR.

Staff opposes the inclusion of General Plant in the DIR. The request to include the recovery of General Plant in a rider is another example of the Company's unfettered effort to avoid distribution rate cases. Staff submits that such recovery is neither consistent with the intent of the ESP statute, nor the Commission's directives with respect to the DIR.

In the Company's last SSO case, AEP-Ohio stated that the purpose of the DIR was to "ensure continued investment in the distribution system without the risk of regulatory

[150] *Ohio Power ESP* (Staff Ex. 17 (Pre-filed Direct Testimony of Doris McCarter) at 2) (May 20, 2014) ("McCarter Direct").

lag."[151] The intent was to streamline "recovery of costs associated with distribution investments which will encourage investment that can improve reliability."[152]

The Commission approved the Company's DIR, finding that "adoption of the DIR and the improved service that will come with the replacement of aging infrastructure will facilitate improved service reliability and better align the Company's and its customers' expectations."[153] In addition, the Commission found that:

> granting the DIR mechanism requires Commission oversight. We believe that it is detrimental to the state's economy to require the utility to be reactionary or allow the performance standards to take a negative turn before we encourage the electric utility to proactively and efficiently replace and modernize infrastructure and, therefore find it reasonable to permit the recovery of prudently incurred distribution infrastructure investment costs. AEP-Ohio is correct to aspire to move from a reactive to a more proactive replacement maintenance program. The Company is directed to work with Staff to develop a plan to emphasize proactive distribution maintenance that focuses spending on where it will have the greatest impact on maintaining and improving reliability for customers.[154]

The Commission has repeatedly emphasized the importance of Commission oversight, and the need for the Company to quantify the actual reliability improvements achieved as a result of implementation of its DIR plans. In fact, the Commission was

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151 *ESP II Case* (AEP-Ohio Post-Hearing Brief at 87) (Jun. 29, 2012).

152 *Id*. at 89.

153 *ESP II Case* (Opinion and Order at 46) (Aug. 8, 2012).

154 *Id*. at 47.

critical of the Company's 2013 DIR because it did "not quantify, for many of the components, the reliability improvements that are expected to occur through the DIR investments, nor does it address the issue of double recovery or demonstrate that DIR spending levels will exceed AEP Ohio's capital spending levels in recent years."[155]

Staff respectfully requests that the Commission reaffirm its directive that "AEP Ohio's DIR spending should be focused on those components that will *best* improve or maintain reliability."[156] Quite simply, General Plant does not satisfy that criteria.

As Staff witness McCarter testified, the overall nature of the assets recorded in the General Plant accounts are more appropriately considered for recovery in a distribution rate case. Expenses to be recovered in the DIR should be directly related to maintaining reliability of distribution service.[157]

But the type of General Plant expenses that the Company is requesting to include in the DIR do not, in fact, directly relate to the reliability of distribution service. At best, the expenses proposed to be included would be incurred for plant that would *support* maintaining reliability, but not directly relate to it. One example is the radio system that the company proposed to upgrade. As Staff witness McCarter testified on cross-examination, the radio system is a general communications system that is used for a multitude

155 *In the Matter of the Commission's review of Ohio Power Company's Distribution Investment Rider Plan*, Case No. 12-3129-EL-UNC (Finding and Order at 10) (May 29, 2013) ("2013 DIR Plan Case").

156 *Id*. at 12.

157 McCarter Direct at 3.

of purposes, including use by maintenance crews.[158] Likewise, the service centers, while also used for storing equipment, among other functions, do not directly impact reliability.

It is, as Staff witness McCarter testified, a matter of degree.[159] Virtually *everything* the Company does could be an improvement or support an improvement or maintenance of reliability. General Plant is very far removed from the "the replacement of aging infrastructure" that the Commission has relied on for approving the Company's DIR Plans.[160]

Staff's concern is highlighted by the Company's testimony that virtually all expenses "supporting" distribution could conceivably be recovered through the DIR:

> Q: Can you think of any capital account supporting the distribution system that the company would consider inappropriate for inclusion in the DIR?
>
> * * *
>
> A (Company Witness Dias). Not that come to mind right now.
>
> Q. And that would be consistent with the basic premise that you've been explaining today of accelerating recovery through a rider mechanism until such time as we reset the game, as it were, in a distribution case; is that correct?
>
> A. That is correct.[161]

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158 Tr. IX at 2290.

159 *Id*. at 2292.

160 *2013 DIR Plan Case* (Finding and Order at 10) (May 29, 2013).

161 Tr. II at 437-438.

The DIR was never intended to recover the costs of all capital expenditures. It was not intended to be a substitute for distribution rate cases. Rather, it was intended to "encourage the electric utility to proactively and efficiently replace and modernize infra-structure."[162] General Plant does not satisfy this objective, and the costs of investing in merely "supportive" facilities should be excluded from the DIR.

b. Gross-Up Factor

The Company has proposed to include a Gross-Up Factor in its carrying charge calculation for the riders included in the proposed ESP. The proposed Gross-Up Factor would recover AEP-Ohio's obligation to fund a portion of the PUCO and OCC budgets. The Company posits that inclusion of a Gross-Up Factor in the riders is appropriate because AEP-Ohio will, mathematically, need to pay more to the PUCO and OCC as the its revenues grow. The Company's concern is short-sighted, overstated, and misplaced.

The Gross-Up Factor percentage is derived from a set dollar amount the Company is obligated to pay to fund the PUCO and OCC. If there is an over-collection in any given year it is credited against the dollar amount the Company owes the following year. There are only two scenarios where AEP-Ohio may actually owe a larger dollar amount in a subsequent year: (1) if its revenues increased disproportionately to the revenues of all of the other regulated public utilities operating in Ohio, and (2) an increase in the PUCO and/or OCC budgets. The latter scenario has not occurred in recent years, and is not

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162 *ESP II Case* (Opinion and Order at 47) (Aug. 8, 2012).

expected to occur in the foreseeable future. While AEP-Ohio's revenues may increase if its Application is approved, the Company has failed to demonstrate that revenues would increase so disproportionately as to justify this change in the Gross-Up factor. Permitting the Company to include PUCO and OCC budget assessments in the Gross-Up Factor increasing rider revenues is inappropriate.

c. Adjustments should be made to the property tax rate and the net plant to which it is applied.

Staff supports the testimony of OCC witness Dave Effron with respect to adjusting the carrying cost rate. As OCC witness Effron testified, the Company's proposal to calculate the carrying cost rate using a property tax rate based on the ratio of property taxes to net plant, rather than on the ratio of property taxes to gross plant, is inappropriate.[163] Rather, the depreciation reserve should be adjusted to eliminate the cumulative amortization of the excess depreciation reserve since December 31, 2011 to more accurately reflect the change in the base on which property taxes are calculated.[164] Staff supports this adjustment.[165]

Staff acknowledges that other adjustments may also be appropriate. Specifically, Ms. McCarter testified that changes in property tax rates could also be accounted for, and

[163] *Ohio Power ESP* (OCC Ex. 18 (Pre-filed Direct Testimony of David J. Effron) at 9) (May 6, 2014) ("Effron Direct").

[164] *Id*. at 10.

[165] McCarter Direct at 4.

probably should be if the carrying charge is to be accurately assessed.[166] The record, however, is devoid of any such evidence, nor was any such adjustment proposed by the Company either in its Application or in rebuttal. Consequently, OCC witness Effron's adjustment is the only record-supported adjustment that should be made to the property tax rate.

d. Revenue Requirement Charge calculation

Staff concurs with the specific annual (January 1 to December 31) revenue caps proposed by AEP.[167] These caps were revised during the hearing by Company witness Moore.[168] Staff witness McCarter also agreed with Ms. Moore's revision.[169]

But Staff was concerned about AEP's DIR customer charge calculation for 2015, 2016 and 2017. It appeared to Staff witness McCarter that the Company, in translating the revenue caps to the estimated percentage of bill charge, used a calculation basing the percentage on an average using five months of the current year cap with seven months of the succeeding year's cap. Staff would oppose such a method since it would effectively allows the increase in the succeeding year's cap to raise the percentage charged on current customer bills.[170]

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166 Tr. IX at 2305.

167 McCarter Direct at 5.

168 Tr. IV at 1003.

169 Tr. IX at 2307.

170 McCarter Direct at 5.

It appears, however, that that is not the Company's intent. When asked about that calculation, Company witness Moore testified:

> Q. So Ms. McCarter's testimony states that AEP uses a calculation that bases the percentage of bill charge on an average using five months of the current year cap but then seven months of the succeeding year's cap. Is that an accurate description of the company's methodology?
>
> A (Company witness Moore). I think that for -- what I would like to clarify is that the rider calculation itself would continue as it does today and that would be on an annual basis. I think there might have been confusion on AEM Exhibit 2 where we have a column where we're showing the June through May weighted rate, which is looking at five months and seven months. And that was for the purpose of looking at the rider rate in a PJM year. But the rate itself that the company -- if I'm understanding her testimony, and we can get clarity from her, *but the rate itself that we're actually asking for approval of, it would be handled the exact same way as it is today. We would do it on an annual basis.*
>
> Q. On a calendar basis.
>
> A. Correct.[171]

Staff accepts this clarification, and respectfully requests that the Commission direct that the rider calculation continue unchanged.

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171 Tr. IV at 1106-1007 (emphasis added).

e. The Company should provide the information requested by Staff, and in the form requested.

Staff witness McCarter made a number of recommendations about information that the Company should include in subsequent DIR filings. Specifically, Ms. McCarter recommended that the Company should:

- Indicate what plant in service is being recorded and recovered in the Enhanced Vegetation Rider, the gridSMART Phase II Rider and the Solar Rider (and any other rider which is recovering Distribution plant in service), and provide this information by Plant Account and Subaccount for each rider.

- Use the jurisdictional allocations and accrual rates for each account and subaccount that were approved in the Company's last distribution rate case[172].

- Include a full reconciliation between the functional ledger and FERC form filings as well as detailed workpapers showing the jurisdictional allocation, accrual rates and reserve balances for each account and subaccount for any rider being used to collect costs recorded in the Distribution Plant Accounts, both by rider and as a grand total.

- Detail the DIR revenue collected by month and to date in its filings to demonstrate compliance with authorized annual revenue caps.

- Highlight and quantify any further changes proposed to be made to its capitalization policy in the DIR filing preceding the implementation of the change.

- File a fully updated depreciation study by November 2016 with a study plant date of December 31, 2015.[173]

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172 *ESP II Case*.

173 McCarter Direct at 5-7.

Company witness Dias acknowledged that it would be his responsibility to have an opinion on these recommendations.[174] He was, however, unfamiliar with those recommendations at the time of his cross-examination.[175] Nonetheless, he indicated that it is the Company's goal to make information available if feasible. As the Company offered no contrary view on rebuttal, Staff presumes that the Company found all of Ms. McCarter's recommendations to be feasible, and requests that the Commission direct the Company to comply with those recommendations.

2. Enhanced System Reliability Rider ("ESRR")

Staff opposes the Company's proposed ESRR increase. The ESRR program was approved in the ESP I to facilitate the transition to a cycle-based vegetation management program.[176] The program includes tree trimming, the widening of rights-of-way, and the removal of trees, which reduces the risk of trees contacting lines.[177] In the *ESP II Case*, the Commission approved (a) $16 million for 2014 for the transition to a cycle-based vegetation management program and (b) $18 million of O&M for 2015 and each year after for maintenance of the program.[178] The transition tree-trimming program was needed because many of AEP-Ohio's circuits had not been trimmed end to end in many

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174 Tr. II at 441.

175 *Id*.

176 Dias Direct at 10.

177 *Id*. at 14.

178 *Id*. at 10.

years.[179] Catching up on these circuits involved more trimming and higher costs than the more routine trimming required to maintain a four-year trim cycle.[180] The Company expects to have fully transitioned to the four-year maintenance cycle in 2014.[181]

In its Application, the Company has stated that, beginning in 2015, it needs $25 million of O&M to fund the cycle-based maintenance program instead of the $18 million that the Commission approved in the ESP II.[182] Staff opposes the proposed ESRR increase from $18 million to $25 million.

In formulating $18 million estimate, the Company's experienced foresters weighed and assessed identifiable factors to estimate the cost of ESRR maintenance activities.[183] These factors included AEP's system-wide historical trim costs, inflation of material and labor, the volume of forestry work, the type of vegetation scheduled for clearing, the amount of "hotspotting" required, and the growth rates that impact vegetation during any given year.[184] In contrast, the Company's proposed ESRR increase is based on AEP-Ohio's average cost per mile (during the years 2009 through 2012) of the

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179 *Ohio Power ESP* (Staff Ex. 10 (Prefiled Direct Testimony of Peter K. Baker) at 9) (May 20, 2014) ("Baker Direct").

180 *Id*.

181 Tr. II at 445.

182 Dias Direct at 10.

183 Baker Direct at 8.

184 *Id*.

Company's catch-up program.[185] AEP-Ohio reduces that average by 30 percent to compute its $25 million estimate.[186] The Company based the 30% reduction on the experience of its sister Company, the Public Service Company of Oklahoma, when that company switched from its transition program to maintenance program.[187]

The Company's earlier estimate better represents the costs associated with a cycle-based vegetation maintenance program.[188] AEP-Ohio's earlier, $18 million estimate, is based on AEP's nationwide routine vegetation management costs instead of the costs of a special, more-expensive, catch-up project.[189] Also, AEP-Ohio anticipates that it will complete its catch-up program this year, which indicates that there has been a substantial improvement in tree clearance that will only need routine maintenance going forward.[190] Furthermore, Staff disagrees with the 30 percent cost reduction that the Company applied based on its Oklahoma sister company's experiences. The Company has not presented any evidence that Oklahoma's tree-trimming activities are comparable to Ohio's. It is very possible that the Oklahoma Company had less trees to trim in its catch-up program and therefore the difference (30 percent) between the cost of its catch-up program and

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185 Baker Direct at 8.

186 *Id*.

187 Tr. II at 446.

188 Baker Direct at 10.

189 *Id*.

190 *Id*.

maintenance program would be less than it would be in Ohio. In the *ESP II Case*, the Company used a comprehensive methodology to determine that its O&M costs for the tree-trimming program would be $18 million. The Company's Application in this case fails to demonstrate that its former methodology was flawed or that its methodology in this Application is accurate or an improvement upon that earlier methodology.

Additionally, more effective mechanisms exist to ensure the Company recovers the appropriate amount if the Company's expenditures exceed $18 million. Once the Company has begun its maintenance program, and the actual costs of the program are known, those actual costs could be used in AEP-Ohio's annual ESRR true-up filing to improve the accuracy of AEP-Ohio's cost projection for the following year. Also, if the Company experienced ESRR O&M expenses that exceeded its earlier $18 million estimate, the Company would have an opportunity to present those expenditures to Staff. Staff would then assess those expenditures and could recommend the Commission allow recovery for those expenditures. Consequently, Staff recommends that the Commission reject the Company's proposed ESRR increase from $18 million to $25 million and instead utilize the mechanisms already in place to ensure AEP-Ohio recovers the appropriate amount for its ESRR activities.

3. Storm Damage Recovery Rider ("SDRR")

The Company first requested a SDRR in its last distribution rate case. That case was stipulated by a "black box" settlement, which was approved by the Commission, although neither the stipulation nor the Opinion and Order so much as mentioned the SDRR.

The Company further sought to have the Commission approve the SDRR in its companion *ESP II Case*. In that case, Company witness Kirkpatrick stated that the purpose of the rider was "to recover only the incremental expenses incurred as a result of major storm events."[191] The Commission approved establishment of the SSDRR as part of the *ESP II Case*.[192] The Commission, however, modified the Company's proposed SDRR:

> In establishing its storm damage recovery mechanism, AEP-Ohio failed to specify how recovery of the deferred asset would actually work or would occur. As proposed, it is unknown when AEP-Ohio would seek recovery, or whether anything over or under $5 million would become a deferred asset or liability. As it currently stands, the storm damage recovery mechanism is open-ended and should be modified.
>
> Therefore, we find that AEP-Ohio may begin deferral of any incremental distribution expenses above or below $5 million, per year, subject to the following modifications. Further, throughout the term of the modified ESP, AEP-Ohio shall maintain a detailed accounting of all storm expenses within its storm deferral account, including detailed records of all incidental costs and capital costs. AEP-Ohio shall provide this information annually for Staff to audit to determine if additional proceedings are necessary to establish recovery levels or refunds as necessary.
>
> In the event AEP-Ohio incurs costs due to one or more unexpected, large scale storms, AEP-Ohio shall open a new docket and file a separate application by December 31 each year

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191 *ESP II Case*, (AEP-Ohio Ex. 110 (Direct Testimony of Thomas L. Kirkpatrick) at 20) (March 30, 2012) ("Kirkpatrick Direct").

192 *ESP II Case* (Opinion and Order at 68-69) (Aug. 8, 2012).

> throughout the term of the modified ESP, if necessary. In the event an application for additional storm damage recovery is filed, AEP-Ohio shall bear the burden of proof of demonstrating all the costs were prudently incurred and reasonable.[193]

The Company seeks to continue the SDRR in this case. In general, Staff supports both the continuation of the rider and the modifications proposed by the Company.[194] Staff does, however, take issue with several of the proposed modifications.

a. Carrying Charges

The Company proposed to establish a carrying charge based on its Weighted Average Cost of Capital ("WACC"). While Staff agrees that a carrying charge is appropriate, it respectfully submits that a carrying charge based on the latest approved cost of long-term debt should be applied to any difference between the total major storm cost and the $5 million baseline at the end of the previous calendar year. Staff witness Lipthratt testified that it is more appropriate to use the cost of long-term debt than the WACC given the type of expenses that would flow through the rider. Specifically, he testified that it would be inappropriate to use WACC since there would be no capital costs included in the rider.[195]

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193 *ESP II Case* (Opinion and Order at 68-69) (Aug. 8, 2012).

194 *Ohio Power ESP* (Staff Ex. 12 (Pre-filed Direct Testimony of David Lipthratt) at 3) (May 20, 2014) ("Lipthratt Direct").

195 Tr. VII at 1690.

b. Types of Recoverable Charges and Incremental Labor

As noted above, the Commission approved the SDRR for recovery of incremental distribution expenses above an established threshold. Staff witness Lipthratt testified about which expenses are incremental in nature, and are therefore appropriate for recovery. Specifically, he testified that:

- The first 40 straight-time labor hours that an employee works in a week is considered to be in base rates and should not be included in the SDRR.
- Overtime performed by union employees would be considered incremental labor and should be included in the SDRR.
- Management overtime should not be considered as incremental since these employees are usually salaried and any such expense would be strictly discretionary.[196]

c. Mutual Assistance Revenues

Mutual assistance refers to voluntary agreements that allow for one utility to provide another utility resources, labor (both utility employees and contractors), and equipment in order to perform restoration services.[197] The Commission has recognized the importance of mutual assistance arrangements, and has approved the recovery of incremental costs associated with supporting external responders.[198] The cost responsibility

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196 Lipthratt Direct at 3.

197 *Id*. at 6.

198 *In the Matter of the Application of Ohio Power Company to establish Initial Storm Damage Recovery Rider Rates*, Case No. 12-3255-EL-RDR (Opinion and Order at 22) (Apr. 2, 2014) (hereafter "*Storm Damage Case*").

for providing employees and equipment to another utility are and should be borne by the receiving utility, and should not be recovered in the SDRR.

There is, however, an issue that this Commission has yet to address in a storm damage recovery case. The Commission has yet to consider whether revenues received by a company for mutual assistance work performed by its employees should be treated as an offset to the expenses sought to be recovered.

At the outset, Staff wishes to clarify its position. First and foremost, Staff agrees that the Company should be entitled to recover all of its prudently incurred incremental storm damage recovery costs.[199] But it should not necessarily be entitled to retain all of revenues received from other utilities for mutual assistance rendered. Staff witness Lipthratt, in his pre-filed direct testimony, stated that "Staff believes the entire amount reimbursed to Ohio Power Company for mutual assistance should be applied as a reduction to the SDRR revenue requirement."[200] Staff clarifies that it does not intend to suggest that *all* reimbursements should *necessarily* be applied as an offset, but that revenues should be reviewed to determine if they *should* be applied as an offset.

The analysis is the same as for the types of recoverable charges and incremental labor described above. Staff reasonably believes that the first 40 straight-time hours that

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199 The principal issue here is labor. As Staff witness Lipthratt testified, incidental expenses such as meals and lodging for employees providing mutual assistance in another jurisdiction would be incremental if not considered in establishing base rates. Tr. VII at 1708.

200 Lipthratt Direct at 7.

an employee works in a week has already been charged to and recovered from ratepayers through base rates. The Company's argument that "the expenses and revenues associated with providing mutual assistance to peer utilities in emergencies are not included in base rates"[201] is without merit. The Company argues "mutual assistance expenses and revenues are included in Account 186."[202] Staff believes that regardless of how mutual assistance revenues and expenses are reported for financial reporting reasons, the employee count and regular hours of these employee assigned to mutual assistance were used to develop current base rates for rate making purposes. The first 40 hours of straight-time labor for Company employees who work on storm repair for another utility (mutual assistance) has already been included in base rates, even though subsequently reported for financial reporting purposes within Account 186. Consequently, revenues received from the host utility for these hours may constitute a double recovery and, if so, should be offset against the SDRR. Overtime hours for mutual assistance provided, on the other hand, would not have been contemplated in setting base rates, and it would be inappropriate to offset revenues for that work against the SDRR.[203]

Staff is not seeking any change to the mutual assistance revenues in this case. The record in this case is inadequate to determine whether any such expenses incurred are

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201 Allen Rebuttal at 10.

202 *Id*. at lines 21-22.

203 Tr. VII at 1697.

currently being recovered in base rates. Rather, Staff requests that the Commission reaffirm and expand it previous authorization of this rider. The Company should continue to bear the burden of proof of demonstrating all of its incremental storm damage costs were prudently incurred and reasonable. But Staff submits that the Company should also bear the burden of proof of demonstrating that the revenues received were incremental – that is, not already recovered through base rates.

The Commission previously ordered the Company to maintain a detailed accounting of all storm expenses, including detailed records of all incidental costs and capital costs, and provide this information annually for Staff to audit. Because offsets may be appropriate, Staff respectfully requests that the Commission further order that the Company maintain a detailed accounting of all expenses incurred and revenues received for providing mutual assistance to other utilities and provide this information to the Staff annually, as well. Such revenues should not automatically be applied as an offset to SDRR expenses, but the Commission should determine, in each storm damage recovery case, whether any offset should be made.

Staff's intent is to not discourage the use of mutual assistance.[204] Rather, Staff wishes to ensure that the Company is not double recovering revenues, once from ratepayers and secondly from host utilities, especially when the service provided does not directly benefit them. Consequently, Staff is willing to work cooperatively with the

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[204] Tr. VII at 1715.

Company, outside of a storm damage recovery proceeding, to ensure that no double recoveries occur.

d. Rate Design

Finally, Staff witness Lipthratt testified that customers should continue to be billed as they have been as a result of the Storm Damage Case. In that case the parties agreed that customers should be assessed a fixed charge. Staff believes that a fixed charge for the SDRR is appropriate, and that the Company's request that recovery be based on a percentage of distribution revenue should be rejected. The Company should separate the total allowed recovery amount between residential and non-residential customers based on the percentage of distribution revenue (from the prior full calendar year) and then divide the amount in each category by the number of customers in their respective categories.[205]

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[205] Lipthratt Direct at 7-8.

C. Additional Issues Regarding AEP-Ohio's Application

1. AEP-Ohio's proposed auction structure and competitive bidding process should be modified to reduce customers' exposure to potential rate volatility.

a. AEP-Ohio's proposed auction structure should be modified to reduce customers' exposure to potential rate volatility.

Staff recommends that the Commission modify AEP-Ohio's proposed SSO auction structure. Staff witness Strom expressed concerns about AEP-Ohio's plan to restrict its initial auctions to products that terminate at or before May 31, 2017.[206] Staff witness Strom testified that the primary reason AEP-Ohio proposes the May 31, 2017 product termination date is to provide AEP-Ohio the unilateral right to terminate the ESP early.[207] AEP-Ohio's initial auctions would then be followed with procurements of one year products with delivery ending May 31, 2018.[208] AEP-Ohio's proposed mix of auction products will subject SSO customers to uncertainty and potential rate volatility in both 2017 and 2018.[209] Staff witness Strom testified that AEP-Ohio's proposed SSO structure has an inadequate amount of product blending, which will expose customers to potential rate

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206 *Ohio Power ESP* (Staff Ex. 16 (Prefiled Direct Testimony of Raymond W. Strom) at 2-4) (May 20, 2014) ("Strom Direct").

207 *Id*. at 2-3.

208 *Id*.

209 Strom Direct at 2-3.

volatility.[210] OCC witness Kahal agrees.[211] OCC witness Kahal testified that AEP-Ohio's "portfolio structure runs the risk of introducing more rate volatility than necessary."[212]

Staff witness Strom proposed three options that will provide more price stability for SSO customers. First, the Commission should reject AEP-Ohio's early termination proposal.[213] This would eliminate AEP-Ohio's purported justification for the May 31, 2017 termination of all auction products. Second, the Commission should adopt Staff witness Strom's alternative product mix, which would eliminate the 100% termination at June 1, 2017 and increase auction blending.[214] This additional auction blending will reduce customers' exposure to potential price spikes.[215] Third, the Commission should adopt a five year ESP, which would further reduce uncertainty and the frequency of potential rate volatility occurrences over the long term.[216]

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210 Tr. IX at 2246

211 *Ohio Power ESP* (OCC Ex. 13 (Direct Testimony of Matthew I. Kahal) at 51) (May 6, 2014) ("Kahal Direct").

212 *Id*.

213 Strom Direct at 4; Staff provides additional reasons for rejecting the early termination provision later in this brief.

214 Strom Direct at 3, Ex. RWS-1.

215 Tr. IX at 2248-2250.

216 Strom Direct at 3.

Staff witness Strom also recommends that the Commission require AEP-Ohio to propose its next SSO well in advance of the termination of ESP III.[217] This would allow AEP-Ohio to blend its last procurements of ESP III with the initial procurements of next SSO. Preventing a 100% termination of auction products at the end of ESP III is yet another way the Commission can reduce uncertainty and potential rate volatility occurrences. This recommendation could be applied to either a three or five year ESP.

In sum, Staff's primary goal is eliminating or mitigating potential price spikes by increasing product blending and reducing 100% termination of auction products. The Commission has a number of reasonable tools that can help achieve this goal, and Staff recommends that the Commission use these tools to modify AEP-Ohio's proposed auction schedule.

b. Staff recommends modifications to AEP-Ohio's proposed Competitive Bidding Process.

Staff also has recommendations regarding AEP-Ohio's proposed competitive bidding process ("CBP"). AEP-Ohio witness LaCasse testified that the Commission has the right to reject the CBP auction results only if one or more of the following occurs: (1) the auction was not oversubscribed on the basis of the indicative offers; (2) there were not four or more bidders; or (3) a bidder won more than 80% of the tranches available at the

[217] Strom Direct at 4.

start of the auction.[218] Staff witness Strom testified that the Commission's ability to reject the CBP auction results should not be limited to these three issues. [219] The Commission will be provided information regarding the auction that addresses significant issues that go beyond these three criteria. The Commission will receive information from Staff about how each auction progresses, reports on the auctions from the auction manager, and information from the Commission's consultant.[220] If the Commission is limited to considering three specific criteria, all this additional information provided to the Commission will be essentially meaningless.[221]

Further, pursuant to the bidding rules, all three of the listed criteria will essentially be known prior to the commencement of each auction.[222] So, if any of these three criteria are not met, the auction probably should not even take place.[223] Staff recommends that the Commission clarify that it will ultimately determine what criteria will be used to determine if the auction results should be rejected.

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218 *Ohio Power ESP* (Company Ex. 15 (Direct Testimony of Chantale LaCasse) (Dec. 20, 2013) at 29) ("LaCasse Direct").

219 Strom Direct at 4-5.

220 *Id*.

221 *Id*.

222 *Id*.

223 *Id*.

Staff also recommends that the Commission clarify that it retains the right to modify and alter the load cap or any other feature of the CBP process for future auctions. The Commission recently made this clear in DP&L's SSO case:

> Finally, the Commission notes that we reserve the right to modify and alter the load cap or any other feature of the CBP process for future auctions as the Commission deems necessary based upon our continuing review of the CBP process, including the reports on the auction provided to the Commission by the independent auction manager, the Commission's consultant, DP&L, and Staff.[224]

Staff believes the same reservation of rights should be applied to the CBP in this case.[225]

2. The Commission should reject AEP-Ohio's proposed early termination provision.

Staff witness Strom provided sufficient reasons for rejecting AEP-Ohio's proposed early termination provisions. There are, however, even more reasons AEP-Ohio's proposal should be denied. If AEP-Ohio's request is granted, it will have the ability to unilaterally terminate its ESP for virtually any reason.[226] AEP-Ohio witness Vegas testified that the "decision to terminate would be made solely by the company based on a change in rule or law."[227] AEP-Ohio will unilaterally define what is a "change in rule or

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224 *In the Matter of the Application of The Dayton Power and Light for Approval of its Electric Security Plan*, Case No. 12-426-EL-SSO (Opinion and Order at 16-17). (Sep. 4, 2013).

225 Strom Direct at 6.

226 Tr. I at 68- 69.

227 *Id*.

law." This means that the potential triggers for this termination provision could be limitless.[228] AEP-Ohio claims it will notify the Commission after it terminates its ESP, but the Commission will play no role in deciding whether termination is warranted. In addition, the Commission will not have the ability refuse termination, regardless of the rationale used by the Company to justify the termination.

AEP-Ohio's request for an early termination provision is unwarranted. If AEP-Ohio has concerns about changes in rules or laws that affect its ability to operate as an EDU, it can always raise those concerns with the Commission. But giving AEP-Ohio the power to unilaterally terminate its ESP would create insecurity for all parties involved, except AEP-Ohio. AEP-Ohio's proposal should be denied outright.

3. Stand-by Service

Stand-by Service provides generation-related backup and planned maintenance services for partial-service customers who generate some of their own electricity on-site. Currently, the Company has different tariffs for generation that apply to partial service customers versus SSO customers.

Staff initially interpreted the Company's Application to mean that the Company wanted to eliminate stand-by service for partial-service customers.[229] After filing its

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228 Tr. I at 137 ("I think a very broad range of issues could be considered when considering whether or not it makes sense and it's necessary to change the last year of this ESP.")

229 *See* Moore Direct at 9-10.

Application, the Company clarified its position and confirmed that it would continue to provide generation-related backup and planned maintenance through applicable SSO rates.[230] But, the Company would not have different tariffs that would apply to partial service customers versus SSO customers. Instead, generation-related charges for backup power and planned maintenance services would be billed under the SSO riders for energy (GENE), capacity (GENC), and auction costs (ACCR) based on the actual energy (kWh) used for those services during a billing period. Partial service customers would reference the SSO tariff to obtain details on their service and rates instead of referencing a stand-by service tariff.

Staff agrees that it is appropriate for the Company to provide stand-by service to partial-service customers at least as long as the SSO is in place. However, given the potential confusion for partial-service customers, Staff believes that the stand-by service tariff should be maintained, and instead, reference the applicable riders for generation-related services (GENE, GENC, ACCR), along with the appropriate tariffs for distribution service. This will make it easier for customers to understand how backup and planned maintenance charges will be calculated and ensure that customers are aware that the services are provided through the SSO. Staff believes that these changes will further the energy policy of the State of Ohio, as outlined in R.C. 4928.02(K), which encourages the "implementation of distributed generation across customer classes through regular

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[230] *Ohio Power ESP* (Staff Ex. 1 (PUCO-Staff Schaefer Company Data Request) at 88) (Exhibit filing Jun. 17, 2014).

review and updating of administrative rules governing critical issues such as… standby charges."[231]

4. AEP-Ohio Load Zone

Staff recommends the Commission order the Company to petition PJM to create an AEP-Ohio load zone for the competitive bid process as soon as is practicable and to work with Staff to overcome potential obstacles in this process. As proposed, AEP-Ohio's proposed procurement auctions will require winning bidders to deliver electricity to the AEP Load Zone. The Company, in its Application, recognizes that "at a time in the future it may be appropriate to request that PJM establish an AEP Ohio Aggregate pricing point that would be used to settle AEP Ohio load."[232] Staff believes the creation of a new pricing point that better reflects the auction product and would be an improvement to the auction procurement process.[233]

Currently, the AEP Load Zone is an aggregation of load buses that are located across all of AEP's east operating companies including, but not limited to, AEP-Ohio. Therefore, even though the objective of the competitive bidding process is to procure energy for the State of Ohio, suppliers bid a product into the auction that covers several

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231 *Ohio Power ESP* (Staff Ex. 6 (Prefiled Direct testimony of Krystina M. Schaefer) at 3-4) (May 20, 2014) ("Schaefer Direct").

232 Application at 7.

233 *Ohio Power ESP* (Staff Ex. 9 (Prefiled Testimony of Timothy W. Benedict) at 2) (May 20, 2014) ("Benedict Direct").

states. This obvious mismatch can be resolved through the creation of an AEP Ohio Load Zone. Additionally, Staff hypothesized and confirmed through modeling that it would be less expensive to deliver energy to an AEP Ohio zonal price point as compared to the AEP Load Zone.[234]

To create an AEP-Ohio Load Zone, AEP would have to petition PJM to define the new pricing point, and would then amend the Company's Master Supply Agreement to reflect the change. The Master Supply Agreement would notify potential suppliers that they would deliver energy to the AEP-Ohio Load Zone as opposed to the AEP Load Zone.

The creation of an AEP-Ohio Load Zone would improve the competitive bidding process and lead to lower prices for customers. Therefore, the Staff recommends that the Commission order AEP-Ohio to petition PJM to create an AEP-Ohio Load Zone as soon as practicable and to work with Staff to overcome any potential obstacles that may arise.

5. AEP-Ohio Reliability Expectations

R.C. 4928.143(B)(2)(h) requires the Commission to examine the reliability of a utility's distribution system to ensure the customers' and utility's reliability expectations are aligned before it approves an electric utility's distribution infrastructure or modernization incentive as part of its ESP. Under O.A.C. 4901:1-10-10(B)(2), each electric utility must file an application with the Commission and work with Staff and other parties to

[234] Benedict Direct at 3.

establish minimum reliability performance standards. Once reliability standards are set, the utility's performance is monitored against its reliability standards to ensure the standards are met. If the standards are met then Staff considers the utility's reliability expectations to be in alignment with those of its customers.

In 2011 and 2012, AEP-Ohio had separate reliability standards for its two operating companies, Ohio Power Company (OPC) and Columbus Southern Power Company (CSP). For those years, OPC met its system average interruption frequency index (SAIFI) and customer average interruption duration index (CAIDI) standards, but CSP missed its CAIDI standard. The Commission addressed CSP's 2011 CAIDI performance in the ESP II proceeding and found that the Company's reliability expectations were consistent with those of its customers.

The Commission has not yet considered CSP's 2012 CAIDI miss. Staff has investigated that miss and Staff's analysis indicated that it was caused by a substantial reduction in the number of short-duration customer interruptions.[235] That reduction resulted from the Company's programs to reduce customer outages.[236] That same year, CSP achieved its best SAIFI performance on record. Staff concluded that the CAIDI miss was not a reliability issue but rather a mathematical side-effect of the Company's efforts

235 Baker Direct at 4-5.

236 *Id.*

to reduce customer service interruptions.[237] AEP-Ohio met its SAIFI and CAIDI standards in 2013.[238] Also, AEP-Ohio's reliability survey results indicate that its customers were generally satisfied with the Company's ability to provide service without interruption and that satisfaction levels were higher than those supporting the Company's prior reliability standards. Therefore, Staff recommends the Commission find that AEP-Ohio's reliability expectations aligned with those of its customers.[239]

6. Retail Energy Supply Associations' Market Energy Plan Proposal

Staff is not opposed to the Retail Energy Supply Association's ("RESA") Market Energy Plan ("MEP") proposal. Staff believes, however, that the Commission should place some conditions on the program if it approves of the MEP program. First, the Commission should state in its order that Staff has final authority regarding how the MEP program is going to be implemented. RESA witness Pickett testified that RESA is not opposed to Staff having final authority regarding how the MEP program is implemented. [240] In addition, the Commission should clarify that all the customer enrollment processing and notification rules in O.A.C. 4901:1-10 and 4901:1-21 apply to the MEP program.

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[237] Baker Direct at 4-5.

[238] *Id*. at 5.

[239] *Id*. at 6.

[240] Tr. Vol. VIII at 2027.

Further, the Commission should order AEP-Ohio to track the following information, and report this information to Staff upon request:

- The number of customers enrolled in the MEP.

- The number of customers who, at the end of the initial 6 month program, return to SSO, choose a different supplier, or remain with the initial supplier.

Staff believes these conditions will help ensure that MEP program is aligned with the Staff's and Commission's expectations, and will help Staff monitor the success of the MEP program.

CONCLUSION

Staff recommends that the Commission approve AEP-Ohio's application, with the above modifications. Staff believes these modifications will result in an ESP that will benefit all parties involved.

Respectfully submitted,

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PROOF OF SERVICE

I hereby certify that a true copy of the foregoing **Post-Hearing Brief** submitted on behalf of the Staff of the Public Utilities Commission of Ohio, was served by regular U.S. mail, postage prepaid, or hand-delivered, upon the following Parties of Record, this 23rd day of July, 2014.

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