

**BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO**

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

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

INITIAL BRIEF OF ENVIRONMENTAL LAW AND POLICY CENTER

Respectfully submitted,
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July 23, 2014

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I. INTRODUCTION

The Public Utilities Commission of Ohio (“PUCO” or the “Commission”) has before it the Application of the Ohio Power Company (“AEP” or “Company”) for approval of an Electric Security Plan.¹ AEP has proposed in its Application to remove the residential time-differentiated generation rates. ELPC opposes the elimination of these tariffs because doing so would be inconsistent with Commission orders and detrimental to both consumers and the environment. The Company’s Application also includes the introduction of a new rider. The Power Purchase Agreement (“PPA”) Rider is described by the Company as a “hedge against market volatility,”² but in reality this rider allows AEP to recover costs from consumers that constitute a bailout of its coal plants that would require AEP customers to pay for additional costs – including future environmental compliance – associated with these and other obsolete generation resources of AEP’s choosing. Such a mechanism violates Ohio law, which first requires a

¹ Pursuant to R.C. 4928.141 (A), 4928.143, and Ohio Adm. Code 4901:1-35

² Application at 8.

finding of need and a competitive bid process for the inclusion of such a mechanism in an ESP.

The PPA scheme undermines the past fifteen years of the Commission's work deregulating the electric generation market in Ohio and creating a competitive wholesale market with a diversity of supplies and suppliers. For the reasons presented in this brief, the Environmental Law and Policy Center urges this Commission to reject AEP's coal plant bailout PPA Rider.

II. LAW

Ohio policy strongly favors market-based competition in the provision of electric service:

It is the policy of this state to do the following throughout this state: [...] (H) 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;³

The PUCO maintains the authority to further this policy provision in order to create a level playing field for competitive retail electric service providers ("CRES"). In addition, the Commission is also charged with forwarding the policy of creating a "diversity of supplies and suppliers"⁴ through a competitive market for Ohio electric utility customers.

Power Purchase Agreements may be permitted in Ohio, but only through a specific, statutory path presented in R.C. 4928.143(B)(2)(c). The law requires that any

³ R.C. 4928.02(H).

⁴ R.C. 4928.02(C).

generation resource included in an Electric Security Plan (“ESP”) have a pre-determination of need by the Commission and that the resource be competitively bid:

The plan may provide for or include, without limitation, any of the following [...] The establishment of a nonbypassable surcharge for the life of an electric generating facility that is owned or operated by the electric distribution utility, **was sourced through a competitive bid process** [...] However, **no surcharge shall be authorized unless the commission first determines in the proceeding that there is need for the facility based on resource planning projections** submitted by the electric distribution utility.

R.C. 4928.143(B)(2)(c) (Emphasis Added).

In addition the law requires that each facility considered under this portion of the law be “newly used and useful on or after January 1, 2009.”⁵ This means that a PPA mechanism under an ESP cannot be used in conjunction with an asset constructed and operational after January 1st, 2009. Thus, only generation resources that meet these specific requirements are available to be included in an ESP. As presented below, the Ohio Valley Electric Corporation (“OVEC”) Resources do not meet these requirements, nor has AEP executed or completed the statutory process.

Finally, Ohio law for corporate separation provides for the separation of noncompetitive and competitive retail electric service:

Except as otherwise provided in sections 4928.142 or 4928.143 or 4928.31 to 4928.40 of the Revised Code and beginning on the starting date of competitive retail electric service, no electric utility shall engage in this state, either directly or through an affiliate, in the businesses of supplying a noncompetitive retail electric service and supplying a competitive retail electric service, or in the businesses of supplying a noncompetitive retail electric service and supplying a product or service other than retail electric service, unless the utility implements and operates under a corporate separation plan that is approved by the public utilities commission under this section...⁶

⁵ R.C. 4928.143(B)(2)(c).

⁶ R.C. 4928.17 (A).

The prohibition on the provision of noncompetitive service extends to a “product or service other than retail electric service...” Corporate separation plans that seek to evade these requirements must face high hurdles to demonstrate that competition is not diminished or threatened in Ohio.⁷

III. ARGUMENT

A. The Commission should require Ohio Power to continue offering its time-of-use tariffs.

Time-of-use (“TOU”) tariffs or rates are optional time-differentiated rates for customers that charge a different price for energy depending on the time of day. During peak times, the price the customer pays for energy is higher, while the price is cheaper during off-peak hours. The TOU rates send customers an important price signal and discourage energy use at peak time. Under its current ESP, AEP offers time of use rates, and AEP now wants to change its policy.

AEP has proposed in its Application “to remove the residential time-differentiated generation rates,”⁸ claiming that “standard TOU tariffs are legacy rates from a cost of service model for a vertically integrated utility that is no longer applicable under the current market construct and can be more appropriately obtained in the market from CRES providers.”⁹ ELPC opposes the elimination of these tariffs because doing so would be inconsistent with Commission orders and detrimental to both consumers and the environment.

The Commission has supported TOU rates as consistent with the policy of the state of Ohio to “[e]ncourage innovation and market access for cost-effective supply- and

⁷ R.C. 4928.17 (B) and (C).

⁸ Direct Testimony of AEP Witness Moore at 10.

⁹ Direct Testimony of AEP Witness Spitznogle at 12.

demand-side retail electric service including, but not limited to, demand-side management, *time-differentiated pricing*, waste energy recovery systems, smart grid programs, and implementation of advanced metering infrastructure.”¹⁰ In evaluating FirstEnergy’s standard service offer in 2008, the Commission stated that it “believes that . . . time-differentiated pricing ha[s] the potential to promote an open, fair, and transparent competitive solicitation by giving customers the information needed to control their electricity bills and make appropriate decisions regarding the purchase of power, and by providing a potential check on the abuse of market power.”¹¹ In March of this year, after AEP filed its Application, the Commission made its support of TOU rates even more explicit:

The Commission believes that the EDUs’ time-differentiated rate pilot programs should be made available to SSO customers until the market sufficiently develops for CRES providers to begin offering this service. The Commission believes that time-differentiated rates are a generation service that should be offered by generation service providers, which in this instance is the SSO provider.¹²

The Commission should reject AEP’s argument that CRES providers are better situated to provide TOU rates. AEP Witness Vegas testified during cross-examination that he was unaware of *any* CRES providers that currently offer TOU rates or intend to offer them in the near future.¹³ Moreover, as the Commission explained, when AEP customers are non-shopping and receiving service under the SSO, AEP is a generation service provider and should offer time-differentiated rates. According to AEP Witness

¹⁰ R.C. § 4928.02(D) (emphasis added).

¹¹ See *In the Matter of the Application of Ohio Edison Co., The Cleveland Electric Illuminating Co., and The Toledo Edison Co. for Approval of a Market Rate Offer to Conduct a Competitive Bidding Process for Stand. Serv. Offer Electric Generation Supply, Acctg. Modifications Associated with Reconciliation Mechanism, and Tariffs for Generation Serv.*, Case No. 08-936-EL-SSO, Nov. 25, 2008 Opinion and Order at 15.

¹² *In the Matter of the Commission’s Investigation of Ohio’s Retail Electric Service Market*, Case No. 12-3151, March 26, 2014 Finding and Order at 38.

¹³ Transcript at 79.

Allen, only around 28.4% of AEP's residential customers are shopping customers who receive their service from a CRES provider.¹⁴ Given that AEP cannot point to a single CRES provider offering TOU rates and that the vast majority of AEP's residential customers receive service under the SSO, the Commission should reject AEP's argument that its customers will be adequately served by competitive suppliers.

In addition to being inconsistent with Ohio policy and the PUCO's recent orders, eliminating TOU rates would be bad for consumers and the environment. TOU rates help customers use energy more efficiently by incentivizing lower use during peak hours. This efficiency saves customers money on their electric bills and in turn provides the environmental benefits of lower peak usage. The benefits of TOU rates are even more attainable now that AEP has completed Phase 1 of its gridSMART program and has submitted its application to increase its rollout of smart meters in Phase 2.¹⁵ These smart meters will provide both AEP and its customers with even greater usage information, which makes offering dynamic and time-differentiated pricing even easier.

With no CRES providers currently offering TOU rates to customers, now is clearly not the time to eliminate AEP's TOU offerings. The Commission should reject this piece of AEP's application and require them to offer uncapped TOU rates to residential customers.

B. The Commission Should not Approve the Power Purchase Agreement Rider because the Proposal Violates Ohio Law.

The proposed PPA rider violates Ohio law in two ways. First, the statute requires a showing of need and that competitive bidding procedures have been followed before a

¹⁴ Transcript at 694-95.

¹⁵ See *In the Matter of the Application of Ohio Power Company to Initiate Phase 2 of its gridSMART Project and to Establish the gridSMART Phase 2 Rider*, Case No. 13-1939-EL-RDR.

rider mechanism such as this may be approved, and AEP has not made the required showing. Second, the proposed rider runs counter to the deregulation of the Ohio electric market and violates the corporate separation rules.

AEP describes the PPA rider in the testimony of witnesses Vegas and Allen. The OVEC facilities are the only generation facilities owned in part by Ohio Power. AEP has been granted a temporary waiver of its corporate separation plan, because AEP alleges other part owners of the OVEC asset have prevented AEP from divesting its ownership share. To this point, the Commission has simply allowed AEP to sell the output of the OVEC facility into the PJM marketplace. In this case, AEP requests a significant alternation to the waiver that is inconsistent with Ohio's ESP law and its competitive electricity marketplace and places undue risk on customers.

Witness Vegas describes the PPA rider as a mechanism that would allow AEP to continue to sell its allocation of OVEC into the PJM market. As outlined by Vegas, the innovation in this application would be a new rider applicable for all customers lasting for the three years of the term of the ESP and extendable into the future by the Company.¹⁶ Ostensibly offered to reduce "future market volatility," in its function the rider would make AEP whole for any operational losses for OVEC during the term of the ESP. Hence, if OVEC assets sold power into PJM at a loss, or if these assets became uneconomic, the rider would require customers for the term of the ESP to pay AEP for any operational losses faced by the company. Thus, the rider would essentially eliminate operational risk at the facility and effectively act as a quasi-regulation of it.

As proposed, AEP's PPA rider is nonbypassable, meaning that all customers would have to pay it or be subject to it regardless of whether or not they want it or

¹⁶ Direct Testimony of Pablo Vegas at page 13 and AEP Application at 7-8.

whether or not they have managed any volatility concerns they have through CRES offers or another hedging mechanism.¹⁷ This aspect of the PPA proposal violates Ohio law.

Staff Witness Choueiki explained the proper way to incorporate a nonbypassable PPA into an ESP under Ohio law:

Not as simple as that. I mean, there would have to be an assessment of need and there will need to be a competitive bid, you're missing necessary conditions before you get to yeah, I want to build a power plant.¹⁸

He further states:

My understanding is that [a PPA rider] would also have to be competitive. It can't be just a purchased power agreement carte blanche cost-based agreement without us having the authority to challenge anything in that PPA. So that the spirit of the law, the way I understand it, is the Commission in Ohio has authority over the PPA.¹⁹

Accordingly then Ohio's law regulating the competitive market allows PPAs only through an entirely different process than proposed by AEP. AEP requests all applicable and necessary waivers to the Ohio Administrative Code through its application.²⁰ The burden of proof in this proceeding is on AEP.²¹

As discussed above, the plain language of R.C. 4928.143(B)(2)(c) requires the establishment of a need for a particular resource, and requires a competitive process for its acquisition.²² AEP has not undertaken either of these essential steps. There has been no Commission proceeding to establish a need for a volatility management PPA, and the PPA is by AEP's own admission a non-competitive product.

Prior to Commission approval of this mechanism, AEP must demonstrate that

¹⁷ Transcript at page 540.

¹⁸ Transcript at page 2818 lines 6 to 10.

¹⁹ Transcript at page 2819 lines 5 to 11.

²⁰ AEP Application at 16.

²¹ R.C. 4928.143(C)(1).

²² R.C. 4928.143(B)(2)(c).

volatility in Ohio is such a problem for customers that the AEP does not have options in the competitive marketplace for customers. AEP has failed to meet this burden.

In its application and through the testimony of witnesses Allen and Vegas, AEP asserts that the rider is proposed to “capture the benefit” of the OVEC contract, and that AEP’s asset is stable when compared to the market.²³ In no portion of its testimony or application has AEP definitively established that volatility poses a problem. As discussed in detail below, parties present evidence that volatility is not an issue in Ohio; that the SSO adequately protects against volatility, and that pending greenhouse gas rules make OVEC an inherently more volatile asset than the market. Most importantly, the fact that consumers don’t want this rider is strong evidence that it is not needed. For example, Industrial Energy Users of Ohio (“IEU”) witness Murray indicates that volatility is not a problem for customers, and has not been for members of IEU.²⁴

Additionally, even assuming that volatility is a serious problem, AEP has failed to demonstrate that it does not have other volatility management options that would obviate the need to enter into an anti-competitive agreement with its affiliate. AEP attempts to argue that fixed-price contracts are an inferior hedging tool for customers, because such contracts have end dates. However, AEP’s proposed solution suffers the same defect. First, AEP’s proposal lasts for only three years, after which it could be terminated by the Commission or AEP. More importantly, AEP states that it retains the right to withdraw the ESP, and the PPA rider with it, *at any time*.²⁵ This makes the PPA rider a considerably weaker hedge than a fixed-price contract because under a fixed-price contract a provider cannot unilaterally withdraw that fixed price at any time. AEP’s

²³ Direct Testimony of Pablo Vegas at page 13.

²⁴ Transcript at page 1543.

²⁵ Transcript at page 3243.

proposed solution could be revoked by the company at a moment's notice. Hence, it provides no security to customers.

In addition to the aforementioned, ELPC also notes that the Commission has already definitively ruled on this issue, and rejected AEP's approach in a previous AEP PPA proposal in 2013.²⁶ AEP had proposed to comply in part with Ohio's renewable energy laws by adopting a nonbypassable PPA with a large Ohio solar facility, arguing that it would reduce customer costs in the purchase of renewable energy credits. In that case, AEP was required by law to procure solar energy credits, and attempted to justify the PPA on these grounds. In the ruling the Commission determined AEP had not met its burden of proof after parties to the proceeding had put before the Commission considerable evidence about the need for a long-term solar renewable energy credit ("REC") procurement strategy. The Commission found that solar projects already in the marketplace could supply necessary RECs for AEP for the foreseeable future.²⁷ As a result the Commission did not find that AEP demonstrated need for the PPA. AEP has failed to reach a point in this case where the Commission is even capable of reviewing need, as it has not filed in a separate docket a request to establish the necessity for a nonbypassable volatility hedge.

The PPA rider also violates Ohio law by allowing AEP to continue the provision of non-competitively bid electric services. The strength and integrity of competitive electricity markets is a critical state goal and objective. AEP has not met the high burden for demonstrating that such anti-competitive provision of service is needed. Corporate separation plans may allow such provision of service, but only after considerable hurdles

²⁶ *In the Matter of the Long-Term Forecast Report of Ohio Power Company and Related Matters*, Case No. 10-501-EL-FOR, January 9 2013 Opinion and Order, Finding 9 at 30.

²⁷ Case No. 10-501-EL-FOR, January 9 2013 Opinion and Order, at 26.

designed to protect the competitive marketplace are met. Need must be established by AEP, and a competitive process instigated by AEP and the Commission. Neither event has occurred in this case. AEP has not met these hurdles, and its efforts to avoid the statutory requirements of ORC 4918.17 should be denied.

C. The Commission Should not Approve the Power Purchase Agreement Rider because OVEC Resources Are Inherently Volatile in Light of proposed Environmental Regulations, Especially Carbon Rules.

Even assuming that there is a need for a hedge against volatility, the OVEC plants are particularly poorly suited to that purpose. Greenhouse gas (“GHG”) rules and other federal environmental regulations directed at coal plants create significant potential impact on the future of OVEC operations and render the OVEC PPA rider a significant gamble for customers. The GHG, coal ash, effluent limitation guidelines, and other rules undermine any ability for the aging OVEC coal plants to serve as a stable volatility hedge in the manner proposed by AEP. In fact, these aging plants face more upward pressure on costs than other generation, as evidenced by widespread coal-plant retirements around the country, and are therefore less suited to AEP’s purported hedging purpose than other generation options. Accordingly, the uncertainty associated with these rules makes the OVEC generation facilities dangerous and risky for customers, and the record demonstrates that OVEC generation is likely to be inherently more volatile than market generation.

AEP admits that the impacts to the facility of these rules will not be fully understood anytime soon, and that the results could be dramatic.²⁸ The record also demonstrates that the rules will push coal generation prices up, and that they will have a

²⁸ Transcript at page 528.

direct impact on OVEC's cost structure. OEG Witness Taylor testified:

Q. Okay. Would you agree with me that those rules could affect OVEC's costs?

A. They would have the impact on both OVEC's costs as well as have a positive impact on market prices, raising market prices, when those rules go into effect.²⁹

AEP appears to believe that GHG rules will cause a general rise in electric prices and that this rise will somehow benefit the coal plants that remain in operation. Essentially, AEP wants to put customers in a situation where market prices may very well go up, and they are left paying to support higher priced power that would benefit the company.

Even AEP witness Vegas volunteered that new carbon rules could be one of the reasons AEP might pull and revoke its ESP. Specifically, in answer to a question on under what circumstances AEP might abandon its ESP, Vegas states:

Well, the issues are broad, as you've described, and we've seen just in this year alone, we have seen substantive rule change recommendations made to PJM, we have seen federal court challenges to the outcomes of PJM auctions resulting from court decisions related to the demand response component of the PJM market operation, we've seen new guidelines published around greenhouse gas regulation, and sometime during the term of the ESP the states are going to be expected to come up with their response which could certainly affect the supply provisions for residents in the state of Ohio.³⁰

This admission demonstrates again the considerable risk AEP proposes placing on customers through the PPA rider mechanism and the expanded PPA option. Even OEG, which supports the rider, admits that coal generation faces considerable cost exposure. Under cross examination OEG witness Taylor discussed the potential impact of GHG rules on coal, admitting that coal resources would face more cost exposure than

²⁹ Transcript at page 528 line 6 to 11.

³⁰ Transcript at page 67 lines 6-17.

alternatives like nuclear or gas.³¹

As a result the PPA rider is likely to create more, not less volatility for customers. Because the OVEC coal plants face considerable risks from pending GHG rules they are by their very nature “volatile” assets. AEP admits that the uncertainty, and by extension the volatility is considerable. Witness Vegas states of these rules: “I don’t think any of the utilities at this point understand the specific unit implications....”³² When asked what those implications might mean for the operations or environmental compliance spending at the OVEC facilities, Vegas responded: “So at this point we don’t know.”³³ This is particularly troubling, considering that AEP continually asserts in this proceeding that it knows and understands the operational cost structure of the OVEC plants. It would make far more sense to hedge with generation that faced little or no greenhouse gas rule exposure and competitively bid that generation.

If the Commission were to approve the PPA rider, Ohio may be forced to upgrade efficiency at the OVEC coal plants to comply with GHG regulations. In its June 2014 proposed rule, EPA based its emission reductions targets on four general building blocks that states could use: 1) increased efficiency of existing generation, 2) increased dispatching of existing lower-carbon generation, 3) increased reliance on renewable energy, and 4) demand-side energy efficiency.³⁴ EPA has estimated that the costs of efficiency upgrades to existing coal plants will be \$100 per kW.³⁵ If the OVEC PPA is approved these costs are could be added to ratepayers’ bills.

Also troubling is the fact that approval of this PPA will have profound

³¹ Transcript at 2586.

³² Transcript at page 177 lines 19 and 20.

³³ Transcript at page 177 line 3.

³⁴ 79 Fed. Reg. 34,830 (June 18, 2014).

³⁵ 79 Fed. Reg. 34,830, 34,861 (June 18, 2014).

implications for Ohio's potential cost effective compliance with EPA GHG rules, while also reducing Ohio's compliance options. In a telling exchange under cross examination from OEG, AEP witness Vegas made clear that the company plans to repeat its uncompetitive process for OVEC with future energy efficiency and renewable energy acquisitions. Specifically, AEP offers that if the state of Ohio were to propose efficiency, renewables, and gas conversion to implement a GHG rule it should do so through a PPA model instead of through competitive supply, so customers could capture the benefit.³⁶ AEP also suggests that by approving a coal PPA, the PUCO leaves options open for future greenhouse gas rule compliance options via other PPAs.³⁷ AEP's anti-competitive suggestions notwithstanding, such a proposal would do the opposite of allowing customers to capture the benefit of increased efficiencies resulting from a GHG rule. Customers would be best served by competitive procurement of the sufficient renewable energy and energy efficiency necessary to allow Ohio to cost-effectively manage GHG rule compliance.

There is no doubt that older polluting coal facilities are losing out in the marketplace to cleaner, newer facilities. AEP recognizes that many of its unregulated coal facilities are being retired, and replaced in PJM with cleaner and more efficient facilities. The following exchange occurred between AEP witness Vegas and a representative of the Ohio Energy Group ("OEG"):

A. Approximately, a little over 2,000 megawatts that will be retired. Q. Have those units, are those units projected to be retired because you've done an analysis that they're not economic in a competitive market? A. Given the requirements, the environmental control requirements for those plants, the economic analysis showed that it wouldn't be prudent to keep

³⁶ Transcript at page 126.

³⁷ Transcript at page 127.

those plants running.³⁸

In other words, these facilities could not clean up their emissions, and still stay competitive. Accordingly, they will be shut down to make way for new generation in PJM. The same fate could easily befall OVEC's 1950s-built coal plants, but under the current rider proposal, AEP could keep an uneconomic OVEC plants running indefinitely, with customers footing the bills for power that costs more than other resources on the market.

The proposed rider exposes customers to tremendous uncertainty and risk associated with GHG rules. Such risk will be compounded if AEP is allowed to expand the PPA option, and add other legacy coal generation to the rider. OVEC and the coal assets AEP may roll into future riders are inherently volatile and therefore fail as effective hedges for customers.

D. The PUCO Should not Approve the Power Purchase Agreement Rider as a part of the ESP because the Proposed Rider Creates Potential Corporate Separation Issues that Violate Ohio Law.

The PPA proposal violates Ohio law and Ohio Administrative Rules that govern corporate separation.³⁹ The Ohio Revised Code states:

Except as otherwise provided in sections 4928.142 or 4928.143 or 4928.31 to 4928.40 of the Revised Code and beginning on the starting date of competitive retail electric service, no electric utility shall engage in this state, either directly or through an affiliate, in the businesses of supplying a noncompetitive retail electric service and supplying a competitive retail electric service, or in the businesses of supplying a noncompetitive retail electric service and supplying a product or service other than retail electric service, unless the utility implements and operates under a corporate separation plan that is approved by the public utilities commission under this section...⁴⁰

³⁸ Transcript at page 122 lines 6-15.

³⁹ Ohio Revised Code 4928.17 (A) states that "Except as otherwise provided in sections 4928.142 or

⁴⁰ R.C. 4928.17 (A).

The prohibition on the provision of noncompetitive service extends to a “product or service other than retail electric service...”⁴¹ AEP is clearly attempting to supply a noncompetitive product or service associated with generation in a manner that disadvantages other suppliers and harms the competitive marketplace.

The proposed PPA rider allows the Company to petition and potentially pass through to customers additional purchase agreement costs of AEP’s choosing:

...The Company will have the ability to petition the Commission to allow the inclusion of additional PPAs (or similar products subsequently approved by the Commission) in the PPA rider throughout the ESP term.⁴²

This broad provision potentially allows AEP to prop up several more aging, obsolete coal plants through a bilateral contract that all customers will pay for. The Commission should reject this proposal as overly broad and in violation of Ohio corporate separation law. This proposal erodes the benefits associated with a competitive marketplace and unwinds fifteen years of Commission efforts to build a functioning competitive marketplace in Ohio.

Under cross examination, AEP witness Pablo Vegas demonstrated AEP’s desire to turn a single PPA mechanism for the OVEC facilities into a vehicle for the support of many affiliated, unregulated generation assets. Counsel for OCC asked AEP Witness Vegas about the prospect of future bailout rider requests. Vegas explained that AEP would like, as part of this proceeding, the right to come back to the Commission and ask for future bailout rider support. He further stated that the facilities contemplated by AEP to be part of such expansion would only be those previously owned by AEP’s regulated

⁴¹ R.C. 4928.17 (A).

⁴² AEP Application at 8.

arm and now owned by AEP's unregulated affiliates.⁴³ This violates Ohio Revised Code 4928.17 by allowing AEP to prop up assets owned by its corporately separated affiliate.

Ohio law requires a competitive auction or process for the procurement of energy supply and services in order to use competition to secure the best possible prices for services for customers. Despite this, AEP has stated its intention to further rely on an anti-competitive path. There is no customer benefit justification for such a limited and uncompetitive process. AEP understands that there are competitive and legal ways to develop a hedge that benefits customers and avoids corporate separation challenges. Witness Vegas acknowledged this when he was asked during cross-examination about a competitive auction alternative and in response suggested that the PPA proposal in the application would have the same effect.⁴⁴

There is strong evidence in this case that AEP's intentions have nothing to do with customer benefit. While AEP's witnesses attempt to justify the PPA rider on the dubious grounds that despite its cost it might at some point in the future provide a weak volatility hedge for customers, the story AEP is telling investors and the press is very different. AEP witness Vegas discussed the broad corporate effort of AEP to quasi-regulate newly deregulated facilities in order to create shareholder value.⁴⁵

Furthermore, AEP's PPA rider request is a major deviation from the competitive marketplace that could be emulated by other utilities if approved. The record demonstrates that FirstEnergy is considering proposing its own sets of PPA riders.⁴⁶ Accordingly, it is clear that a decision in this case approving such a mechanism could

⁴³ Transcript at page 26, and page 180 line 21 "It is the company's intention to only look at the generating assets that AEP Ohio formally owned...".

⁴⁴ Transcript Vol 1 page 180

⁴⁵ Transcript at page 182.

⁴⁶ Transcript at page 1415.

usher in a wholesale re-regulation of Ohio's electricity marketplace. This is a step that should not, and cannot occur in a series of PUCO cases, as re-regulation is an exclusively legislative step.

It is obvious that this proposal would undermine competition and consumer choice in Ohio if adopted. The PPA rider will result in several plants having their operational cost risks eliminated, while all others participating in the competitive market are not. Those facilities therefore would operate at a huge advantage and this distorts the market. There are many struggling generation facilities in Ohio that would benefit greatly from the elimination of operational risk. No other CRES owned facility would have the opportunity to have its operations subsidized by such a PPA.⁴⁷

Staff witness Choueiki recognizes that customer choice is also threatened by the proposal. In cross-examination he stated:

What I'm worried about is the end-user. You're recommending that we authorize you to sell insurance to an end-user that may not want it. They may have a four-year contract already. Some of our CRES providers were offering four-year contracts and seven-year contracts.⁴⁸

Consumers should have the right to balance their interests in low prices, with exposure to volatility. AEP's proposal would deny them that right.

Finally, in a recent Order the Commission stated that it would conduct audits of Ohio electric distribution utilities to ensure that each was corporately separated from its non-regulated affiliates.⁴⁹ By allowing AEP to potentially intertwine the interests of its EDU with the interests of its unregulated affiliate, the Commission would be taking a step backwards before the first corporate separation audit is performed. The PPA

⁴⁷ Transcript at pages 2598 to 2599.

⁴⁸ Transcript at page 2914 lines 18 to 23.

⁴⁹ *In the Matter of the Commission's Investigation of Ohio's Retail Electric Service Market*, Case No. 12-3151-EL-COIeed cite or two from Order in 12-3151, Finding and Order, Finding 16 at page 17.

proposal by AEP represents an attempt to institutionalize non-competitive generation support, and the development of this proposal should be added to the list of subjects the Commission reviews through its corporate separation audit of AEP. The Commission should not approve even the potential for AEP to prop up a fleet of aging coal plants soon to be owned by its non-regulated affiliate. The proposed rider should be rejected.

E. AEP Presented no Evidence Demonstrating that the Proposed Power Purchase Agreement Rider Improves Reliability for Customers.

The complete record of the hearing, testimony, and the application itself show that fuel diversity and electric system reliability will not in any way be addressed or impacted by the OVEC PPA rider. AEP has insisted throughout this proceeding that approval of this mechanism, or disapproval, will have no impact on how the plants are operated. Therefore, denying the PPA will have no impact on the operation of the OVEC facility and by extension the reliable provision of electricity in Ohio.⁵⁰

AEP witness Vegas plainly stated through testimony that the PPA rider was proposed solely to reduce “price volatility” risks for customers. AEP has not put forth reliability concerns as a justification for the PPA rider.⁵¹

This has not stopped AEP from attempting to argue that reliability is somehow at issue in this proceeding. To the extent they have been properly raised, AEP’s reliability arguments are misplaced. In fact, there is strong evidence in the record that PJM’s reliability record is stellar. OCC witness Wilson explains in cross-examination the significant market resilience of PJM and the extensive preparations PJM has made in

⁵⁰ Transcript at page 28.

⁵¹ Transcript at page 27.

response to the polar vortex event.⁵²

AEP attempts to portray that polar vortex event as justification for the development of the PPA mechanism, as a sign of high volatility and reliability challenges in Ohio. The record does not support this conclusion. Staff witness Choueki explained that large central generation facilities like the OVEC facilities were the cause of the polar vortex problem: “That’s correct. Although during the polar vortex the issue wasn’t demand response. Demand response actually worked. What didn’t work was generation performance.”⁵³ AEP also attempts to make the argument that natural gas increases volatility, but again staff witness Choueki counters this with the facts, noting that 20,000 megawatts of coal were out of service during the vortex event and that this was the real challenge during the crisis.⁵⁴ Accordingly, there is strong evidence that during events like the polar vortex, *coal facilities like OVEC actually increased volatility and were a major cause of reliability issues.*

Further undermining AEP’s misplaced reliability claims are the many examples of the addition of new generation to the PJM footprint and to Ohio in particular. For instance, under cross examination AEP witness Vegas acknowledges the addition of 184 megawatts of new renewable resources being added to the generation mix in Ohio, and that this will both improve fuel diversity and reliability in Ohio.⁵⁵

No AEP witness, or witness of any party, has provided any evidence that approval of the PPA rider for OVEC will in any way positively affect reliability for customers in the state of Ohio. AEP witness Vegas stated in cross-examination that future PPA riders

⁵² Transcript at pages 2496 and 2497.

⁵³ Transcript at page 2977 lines 21 to 24.

⁵⁴ Transcript at page 2990.

⁵⁵ Transcript at page 64.

could be justified by “reliability concerns and the ongoing operation of power plants that are serving customers in Ohio.”⁵⁶ Accordingly, the place for discussion of any reliability issues belongs in a proceeding initiated by AEP or the Commission considering the need, in the legal definition, for action to preserve or enhance reliability for customers in Ohio. To date, no such properly developed proceeding is on the docket. Until such a proceeding, any AEP effort to justify the proposed PPA rider on reliability concerns must be rejected.

F. The Commission Should not Approve the Power Purchase Agreement Rider because there is Ample Evidence on the Record that it will Fail.

The proposed rider will not work for customers and is not needed. Evidence from both supporting and opposing witnesses makes this clear. AEP has not sufficiently justified this proposal to the Commission, and because there is strong evidence on the record indicating it will not work, it should be rejected.

First, the proposed hedge lacks all the hallmarks of an effective, traditional backstop against volatility. Witness Campbell for RESA states that the PPA bailout proposal provides no benefits to customers.⁵⁷ Throughout this proceeding, the hedge has often been compared to an insurance policy. But the analogy fails. AEP argues that this hedge has no costs,⁵⁸ but an effective “insurance policy” for customers should have a cost. AEP’s view makes little economic sense; a hedge or insurance policy has costs associated with it because another party is taking on risk. For the PPA rider the situation is reversed: consumers will insulate the owners of the OVEC facility from operational risk, and consumers will have no guarantee that they will see any economic benefit from

⁵⁶ Transcript at pages 27-28 lines 25-1.

⁵⁷ Transcript at page 1603.

⁵⁸ Transcript at page 1606.

the hedge.

Unlike most fixed-price contracts, which are guaranteed hedges—meaning that the contracting party promises a fixed price under most circumstances—the OVEC hedge includes no such guarantee for customers. Even the proposal’s one supporter, OEG, admits that there is no guarantee that the OVEC rider will reduce volatility.⁵⁹

Furthermore, there is strong evidence in the record that volatility is already effectively managed through other means. Staff witness Choueiki established that consumers in Ohio are sufficiently protected from volatility risks by the SSO auction process. Choueiki disputes the very idea that there is a volatility problem, explaining that the Commission’s SSO auction process allows for sufficient reduction of volatility; stating that “the way we have it currently is the way to hedge.”⁶⁰

The proposal also lacks merit because— as even its proponents recognize— OVEC is an expensive asset, relative to market. Through cross-examination OEG’s witness, testifying in favor of the PPA rider, admitted that the facility provides power at a price more expensive than the market price.⁶¹

The process to develop the OVEC rider was not open and competitive. As a result, other potentially more beneficial and less costly hedging options were not examined. Neither AEP nor the Commission have examined other generation that may prove more stable and effective at providing a financial hedge for customers. For instance, there is evidence in this case that during volatility events, demand response performed considerably better than fixed coal generation assets like OVEC.⁶² As

⁵⁹ Transcript at page 2563.

⁶⁰ Transcript at page 2815.

⁶¹ Transcript at page 2548.

⁶² Transcript at page 2977.

discussed above, much has been made in this case of the considerable risks posed to the OVEC facilities by pending greenhouse gas rules. Other assets like gas, wind, and hydro face considerably less risk from those rules, and may actually benefit in price performance from them.

Accordingly, it would only be logical to review those assets, as well as other strategies, before placing a huge bet on OVEC coal plants on behalf of customers. AEP has failed to review these other options, and as a result customers will be forced to face massive uncertainty if the PPA rider proposal is accepted by this Commission.

The viability of the OVEC proposal rests heavily on massive market and policy questions outside of the control of AEP. The company attempts to make much of the possibility of changes to PJM's reliance and use of demand response. AEP speculates that a recent court decision that could potentially impact the PJM marketplace will be upheld, and then will result in demand response being dramatically reduced as a force for lowering prices.⁶³ AEP's proposal is therefore based on another speculative bet beyond its rosy expectations for GHG rules. If in contrast to AEP's expectation demand response remains a major part of the PJM system, and prices remain low as a result, OVEC will not be an effective financial hedge at all.

It is abundantly clear then that AEP has designed this PPA rider in a manner that is not effectively coupled with its stated aims of reducing volatility for customers. Instead it looks much more like a direct benefit to the Company, with little or no consumer benefit justification. Accordingly, it should be rejected by the Commission.

⁶³ Transcript at page 1617.

G. The Commission Should not Approve the Power Purchase Agreement Rider because Nearly All Customers Oppose the Rider.

Almost universally, customers and their representatives in this proceeding do not want this rider. The residential, commercial, and industrial customers that oppose the rider do so because it is not needed and it will harm customers.

There is one group that has expressed support, but in a curious way that actually undermines the case for the rider. OEG supports the rider, but wants its members only to be allowed to avoid its charges. In testimony and on the stand, OEG's witness asserts that OEG members—large customers purchasing large amounts of energy—should be exempt from the PPA rider charges.⁶⁴

Contrary to the desires of the customer groups opposed to the proposal, AEP would like to rush the PPA rider forward and lock it into place as soon as possible, arguing that this is a one-time opportunity for customers that must be taken advantage of. Specifically, in cross-examination by AEP of OEG witness Taylor, the Company attempts to establish that “benefit would be lost” if the PPA rider were denied in its entirety.⁶⁵ In fact, customers are likely to save money if the Commission delays a decision on the PPA rider. All parties except AEP estimate substantial costs to customers from the PPA rider through the term of the ESP, with estimates ranging from \$21 million to over \$100 million.⁶⁶ AEP's estimate, which has been challenged aggressively by customer representatives in this case, projects a meager \$8 million in benefits for customers in the 3-year ESP period. Therefore, it is more likely than not that significant costs would be avoided if a decision on this PPA mechanism were delayed.

⁶⁴ Transcript at page 2552 and OEG Witness Taylor Direct Testimony page 7 line 19.

⁶⁵ Transcript at pages 2633 and 2634.

⁶⁶ Transcript at page 2541.

IV. CONCLUSION AND PPA RECOMMENDATIONS

The Commission should reject AEP's PPA rider and AEP's proposed elimination of time of use tariffs because these proposals are inconsistent with Commission orders and law. Approving the PPA rider would allow AEP to circumvent the competitive process required by law and place an unfair burden on customers. It should be rejected in its entirety. Alternatively, if the Commission believes the PPA rider issue requires further review, it could open another docket to actually examine issues of price volatility, reliability, corporate separation, and customer attitudes toward potential solutions.

For the reasons stated above, the Environmental Law and Policy Center requests the Commission to reject the portion of the Ohio Power Company's Electric Security Plan proposing a Power Purchase Agreement Rider and the elimination of the TOU tariffs.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing *Initial Brief of the Environmental Law and Policy Center* has been served electronically upon those persons listed below this 23rd day of July, 2014.

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This foregoing document was electronically filed with the Public Utilities

Commission of Ohio Docketing Information System on

7/23/2014 5:18:26 PM

in

Case No(s). 13-2385-EL-SSO, 13-2386-EL-AAM

Summary: Brief Initial Brief of Environmental Law and Policy Center electronically filed by Mr. Robert Kelter on behalf of Environmental Law & Policy Center