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

REPLY BRIEF BY THE OFFICE OF THE OHIO CONSUMERS' COUNSEL

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I. INTRODUCTION

The Ohio Power Company ("AEP Ohio" or "Utility") seeks the approval of the Public Utilities Commission of Ohio ("PUCO" or "Commission") for its third Electric Security Plan ("ESP" or "Plan"). AEP Ohio is already charging consumers the highest electric rates in the state.

No issue in this case takes more precedence than the Power Purchase Agreement ("PPA") Rider.[1] Here, AEP Ohio is asking the government (through the PUCO) to require customers to guarantee profits on uneconomic generating units that are supposed to be deregulated. PUCO Staff Witness Choueiki testified that AEP Ohio's proposal should be rejected because it's a move in the opposite direction from Ohio's turn to markets for the pricing of electric service.[2]

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[1] OCC Ex. 16 (Wilson).

[2] Staff Ex. 18 at 9 (Choueiki).

AEP Ohio should be "on its own," as required in R.C. 4928.38, with respect to the risks and rewards of all of its generating units. But instead, AEP Ohio wants customers to act as involuntary investors or guarantors in AEP Ohio's venture with the Ohio Valley Electric power plants. AEP Ohio wants its customers to protect it from any losses it might incur in the competitive marketplace related to OVEC. At the same time AEP Ohio wants to be guaranteed a profit on its OVEC investment. This is a bad deal for customers. And it is the tip of a large iceberg. AEP Ohio wants the PUCO to approve the PPA Rider so that it can seek approval of future PPAs with other uneconomic generation facilities. These future PPAs could cost customers billions of dollars more over the long term. Moreover, the Utility is using this ESP case to insulate itself from the rigors of the market and to protect its own financial security. It is unfortunate for customers that the electric utilities are even allowed such a thing as an "electric security plan" now that their generation service is supposed to be deregulated.[3]

The PPA Rider should be rejected. The Office of the Ohio Consumers' Counsel ("OCC") explained on Initial Brief why the PPA is unreasonable, unjust, and unlawful.[4]

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[3] See *In re: Retail Market Investigation*, Case No. 12-3151-EL-UNC, Concurring Opinion of Chairman Snitchler at 2-3. OCC cites this Concurring Opinion for the single purpose of affirming the Chairman's conclusion that there should be no more ESPs once an EDU is procuring 100% of its SSO load through a competitive bid process.

[4] OCC Brief at 37-80.

II. ARGUMENT

A. The PUCO Should Reject AEP Ohio's Proposed Power Purchase Agreement ("PPA") Rider, Which Is Intended To Make Customers Of Regulated Electric Service Pay AEP Ohio For A Generation Service That Is Deregulated Under The 2008 And 1999 Laws.

In its Brief, the PUCO Staff states that AEP Ohio's proposed PPA Rider "conflicts with the Commission's goal of moving to a fully competitive market," the path paved by the General Assembly's approval of Senate Bill 3 in 1999 and Senate Bill 221 in 2008.[5] OCC agrees. OCC also agrees with the PUCO Staff that adoption of a PPA Rider would be a reversal of course, moving "AEP-Ohio in the exact opposite direction of market-based competition" and would "defeat the whole point of AEP-Ohio's *ESP II Case*."[6] And AEP Ohio's proposal has already invited other Ohio EDUs "to seek guaranteed cost recovery for generation assets that are not committed to Ohio ratepayers and are *not* regulated by the Commission."[7] Because it would constitute a dramatic and inadvisable policy change, and for all of the reasons discussed below, AEP Ohio's PPA Rider proposal would undermine the General Assembly's objectives and harm customers. It should not be adopted.

1. The PPA Rider would not be a reliable tool to promote rate stability for customers during the term of the ESP. Even if it promoted rate stability, its effect on rate stability would be small.

It is telling that the electric utility with the highest rates in the state would be asking the regulator to approve plans premised on "stability" instead of what Ohioans most need now – lower electricity prices. AEP Ohio claims the PPA is a tool that will

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[5] PUCO Staff Brief at 2.

[6] PUCO Staff Brief at 4.

[7] PUCO Staff Brief at 4.

promote rate stability for customers when energy market prices may be volatile. Rate stability may be of some value to some customers. But even AEP Ohio's own hypothetical calculation, with a $5.00/MWh change in energy market prices in a single year and no change in OVEC costs for the same period, indicates only a $0.35/MWh impact on customers' rates.[8] Even if AEP Ohio's hypothetical tracked with reality (which, as OCC explained in its brief is unlikely[9]), the annual "benefit" of this market hedge to a typical residential retail customer using 1 MWh per month would be only $2.29.[10] And this market hedge could be an additional cost to customers instead of a savings.[11]

The more fundamental consideration, however, is ensuring that consumers in Ohio are provided "reasonably priced retail electric service."[12] That should mean lower, more affordable electric bills. AEP Ohio's PPA Rider will not further this policy of the State. Indeed, as OCC witness Wilson testified, customers of AEP Ohio are likely to pay dearly for the promise of rate stability.[13] Ohioans do not need rate stability at a price of $116 million.

Customers of AEP Ohio have already paid hundreds of millions of dollars to AEP Ohio in the name of rate stability. Charges for rate stability started as early as 2006, following the end of the market development period for electric utilities. In 2006, AEP Ohio customers began paying rates designed to provide rate certainty to customers and

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[8] AEP Ohio Ex. 33, Ex. WAA-R2 (Allen).

[9] OCC Brief at 50-52.

[10] AEP Ohio Ex. 33, Ex. WAA-R2 (Allen).

[11] Tr. XIII at 3213, 3225 (Allen).

[12] R.C. 4929.02(A).

[13] OCC Ex. 15A at 7, 25 and Ex. 17A (Wilson).

financial stability for AEP Ohio.[14] Under the rate stabilization plan approach, customers collectively paid $527 million to AEP Ohio for non-cost based generation rate increases over a three-year period.[15]

Then in 2009, with AEP Ohio's first electric security plan, customers again were charged $368 million (plus carrying costs) of non-cost based rates[16] to provide certainty (stability) for both the utility and its customers.[17] The stability to the Utility came in the form of provider of last resort charges. In 2012, in AEP Ohio's second ESP, customers were required to pay another $508 million[18] through a Retail Stability Rider to AEP Ohio to maintain its financial integrity.[19] This Retail Stability Rider was approved by the PUCO as a way to "promote stable retail electric service prices and ensure customer certainty."[20] And in a separate (but related) case, AEP Ohio's Capacity Case,[21]

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

[15] Id. at 15.

[16] The POLR rates were determined by the Supreme Court of Ohio to be without evidentiary support and the Court reversed the PUCO and remanded the case. *In re: Columbus S. Power,* 128 Ohio St.3d 512, 2011-Ohio-1788, ¶ 29. The PUCO, on remand, agreed, finding that the POLR was not cost based and was not supported by the record. *In the Matter of the Application of Columbus Southern Power Company for Approval of its Electric Security Plan; an Amendment to its Corporate Separation Plan; and the Sale or Transfer of Certain Generating Assets*, Case No. 08-917–EL-SSO, Remand Order at 33. (Oct. 3, 2011).

[17] *In the Matter of the Application of Columbus Southern Power company for Approval of its Electric Security Plan; an Amendment to its Corporate Separation Plan; and the Sale or Transfer of Certain Generating Assets*, Case No. 08-917–EL-SSO, Remand Order at 18 (Oct. 3, 2011).

[18] *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Authority to Establish a Standard Service Offer Pursuant to Section 4928.143, Revised Code, in the Form of an Electric Security Plan,* Case No. 11-346-EL-SSO Opinion and Order at 35 (Aug. 8, 2012).

[19] *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Authority to Establish a Standard Service Offer Pursuant to Section 4928.143, Revised Code, in the Form of an Electric Security Plan,* Case No. 11-346-EL-SSO Opinion and Order at 35 (Aug. 8, 2012).

[20] Id.

[21] *In the Matter of the Commission Review of the Capacity Charges of Ohio Power Company and Columbus Southern Power Company,* Case No. 10-2929-EL-UNC, Opinion and Order (July 2, 2012).

customers were ordered to pay AEP Ohio an additional $463 million[22] (plus carrying charges) to stabilize or provide certainty for retail electric service.[23]

With all of these hundreds of millions of dollars in rate stability payments from customers to the Utility, one would expect AEP Ohio customers to have benefitted by receiving stable generation rates. But, instead AEP Ohio customers have stabilized AEP Ohio's profits. And residential customers are paying, on average, the highest utility rates in the state.[24] During this same time frame, customers were kept from enjoying the historically low market generation rates because AEP Ohio had not fully transitioned to 100% market-based rates. And in 2009 and 2010, as a result of the ESP and the financial stability payments customers made, Columbus Southern Power Company was found to have significantly excessive earnings.[25]

The PPA Rider is not about stability for customers. It is about adding to AEP Ohio's profits. AEP Ohio asks the government (PUCO) to require customers to guarantee (via a subsidy) AEP Ohio's profit on its OVEC investment. And customers would bear the risk of increased charges if the market value of the OVEC power sold into

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[22] See AEP Ohio Ex. 7 at 12 (Allen testified that the deferred capacity charge regulatory asset balance is $463 million as of May 31, 2015.

[23] *In the Matter of the Application of Columbus Southern Power company and Ohio Power Company for Authority to Establish a Standard Service Offer Pursuant to Section 4928.143, Revised Code in the Form of an Electric Security Plan*, Case No. 11-346-EL-SO, Entry on Rehearing at ¶18(where the PUCO described the capacity deferrals as fitting within R.C. 4928.143(B)(2)(d) because they have the effect of providing certainty for retail electric service by allowing CRES suppliers to purchase capacity at market prices while allowing AEP Ohio to continue to offer reasonably priced electric service to customers who chose not to shop). (Jan. 30, 2013).

[24] See OCC Ex. 11 at 13.

[25] See *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Administration of the Significantly Excessive Earnings Test under Section 4928.1433(F), Revised Code, and Rule 4901:1-35-10, Ohio Administrative Code*, Case No. 10-1261-EL-UNC, Opinion and Order (Jan. 11, 2011); *In the Matter of the Application of Columbus Southern Power Company for Administration of the Significantly Excessive Earnings Test under Section 4928.143(F), Revised Code, and Rule 4901:1-35-10, Ohio Administrative Code, et al.*, Case No. 11-4571-EL-UNC, Opinion and Order (Oct. 23, 2013).

the market is less than AEP Ohio's share of OVEC costs. OCC Witness Wilson estimated that the increased charges could reach $116 million over three years. The PPA Rider is AEP Ohio's proposal for the government (PUCO) to make customers bail-out generating plants that cannot compete on their own in the market that Ohio deregulated. But the government should not permit AEP Ohio – no matter how adept the Utility may be at using regulation for a source of funds – to transform customers into involuntary investors. AEP Ohio should bear the burden of its OVEC investment. The PUCO should reject the PPA Rider.

Moreover, there is little basis for AEP Ohio's claims that the PPA Rider will benefit customers by providing rate stability. AEP Ohio argues that PJM market rates are volatile and that "it cannot be disputed that the PPA Rider will promote rate stability, especially over the long term."[26] AEP Ohio attributes stability to the PPA Rider over the "long-term," a speculative time frame that is not at issue here, where a three-year term ESP is proposed.

AEP Ohio's claims of rate stability are exaggerated and without a sound basis. First, AEP Ohio claims that the PPA Rider provides "a financial hedge that would move in the opposite direction of market prices."[27] AEP Ohio emphasizes its projections that OVEC's costs will remain stable over the ESP period and that market prices may be volatile and will fluctuate because of extreme weather. But the market prices AEP Ohio is talking about here are hourly market prices and day-ahead market prices. Those prices have little effect on SSO customer generation rates or the rates of customers who have selected their own generation suppliers and have chosen a fixed price contract. The

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[26] AEP Ohio Brief at 43-52.

[27] AEP Ohio Brief at 45, *citing* Tr. I at 28 (Vegas).

generation rates for customers who have selected these options will not be affected by changes in hourly and day-ahead market prices because their rates are based upon long-term wholesale contracts with terms of one, two, or three years.[28]

In fact, since the PPA Rider's net cost charged to customers is calculated as the difference between OVEC's costs and volatile PJM hourly and day-ahead market prices, the volatility of those market prices will actually be reflected in the PPA Rider.[29] Moreover, as OCC witness Wilson testified, "OVEC's coal generation provides only a partial hedge of market electric energy costs" because of inter-fuel competition.[30] And, as Mr. Allen admitted, and as a number of parties emphasized in their briefs, coal costs may be substantially impacted in the future by EPA's new proposed regulations to limit carbon emissions.[31]

In seeking approval of its proposed PPA, AEP Ohio makes untrue claims about the basis for customer opposition to its plan. AEP Ohio contends that various parties' criticisms of AEP Ohio's claim that "the PPA Rider would move in the opposite direction of market prices" are "non-substantive and based on a potential lag issue relating to the rider's true-up mechanics."[32] AEP Ohio also claims that intervenors "do not challenge the premise" that the PPA Rider would mitigate the effects of volatile market prices.[33] As support for its position, AEP Ohio points to OCC witness Wilson's testimony that the

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[28] OCC Brief at 49; OCC Ex. 15A at 29-30 (Wilson).

[29] *Id.*

[30] OCC Brief at 50-51, *quoting* OCC Ex. 15A at 32 (Wilson).

[31] Tr. II at 528; Constellation/Exelon Brief at 12; ELPC Brief at 11-15; OEC/EDF Brief at 17-18; OPAE/APJN Brief at 40-41.

[32] AEP Ohio Brief at 46.

[33] AEP Ohio Brief at 46.

PPA Rider "may be about as likely to move in the same direction as the opposite direction."[34]

AEP Ohio claims that OCC and other intervenors do not challenge whether the PPA Rider "would mitigate the effects of volatile market prices." That claim is simply untrue. Indeed, the referenced statement from Mr. Wilson directly challenges AEP Ohio's claims of mitigation.

And, for the first time in its brief, AEP Ohio admits what OCC Witness Wilson concluded when it states "the Company acknowledges the effect that reconciliation component of the rider (operating on a one-year lag) could create."[35] In contrast, during the evidentiary hearing AEP Ohio's witnesses would not concede this point because it undermines AEP Ohio's claim that the PPA Rider would mitigate volatility.[36]

AEP Ohio claims there is a theoretical benefit that may appear over time, but not necessarily during the ESP term. It states that "the PPA Rider will produce a credit when OVEC's . . . costs (at the time the costs are incurred) are below market prices. . . . Conversely, if OVEC costs are above market prices, the PPA Rider will produce a charge."[37] That is "what the Company meant in saying the PPA Rider moves in the opposite direction as market prices."[38]

But OVEC's facilities are not unique in this regard. The same could be said of natural gas combined cycle generation facilities or renewable fuel facilities. There is no evidence in this record that the costs of operating any generation facilities are any more

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[34] AEP Ohio Brief at 46.

[35] AEP Ohio Brief at 46.

[36] Tr. I at 50 (Vegas); Tr. II at 517 (Allen).

[37] AEP Ohio Brief at 46.

[38] AEP Ohio Brief at 46-47.

or less stable than OVEC's coal fired combustion turbines. Consequently, this AEP Ohio argument for the PPA Rider lacks a basis.

AEP Ohio also relies on its witness' testimony that the "PPA Rider will be a credit more often than a charge and so the PPA Rider overall would operate to mitigate higher market prices."[39] This claim, however, does not address whether the PPA Rider will be price-stabilizing *during the ESP term*. As discussed in OCC's Brief and below, the PPA Rider will cost customers money over the term of the ESP. Moreover, as a result of the PPA Rider's undermining of incentives to control operational costs for facilities participating in the PPA hand-out, it is more probable that customers will see no or little benefit. This situation is further exacerbated by the fact that this subsidized generation could be operated (or not operated) to the benefit of the Utility's unregulated merchant generation not participating in the PPA subsidy program.[40]

AEP Ohio's next argument – that market prices are more volatile on the high side than on the low side – is equally unavailing.[41] AEP Ohio spends a significant amount of time discussing this proposition and how it might affect the outcome of the PPA Rider. But it then admits what has been evident throughout this proceeding – that it has not made the analysis to show the benefit to customers from its claims.[42] AEP Ohio recognizes that a "probabilistic model . . . could be used to do a more sophisticated

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[39] AEP Ohio Brief at 47.

[40] The Fourth Circuit Court of Appeals expressed similar concerns regarding the ability of a Maryland utility to manipulate the market where new generating capacity was subsidized. *PPL Energy Plus, LLC v. Hanna,* No. 13-2419, 2014 WL 2445800, 2014 U.S. App. LEXIS 10155 (June 2, 2014).

[41] AEP Ohio Brief at 47-50.

[42] AEP Ohio Brief at 49.

simulation that would reflect the added value of the PPA Rider using the probability of extreme weather during the ESP term."[43] "But AEP Ohio did not perform the analysis."[44]

AEP Ohio thus did not carry its burden of proof to show this effect, even though it claims an "exponential financial benefit" on the very next page.[45] While AEP Ohio points out that none of the other parties did such an analysis either, no other party bears the burden of proof for which AEP Ohio is responsible. Moreover, AEP Ohio's claims regarding this effect were first presented during Mr. Allen's cross-examination and then in his Rebuttal Testimony, leaving little opportunity for response.[46]

In addition to AEP Ohio's failure to produce actual evidence of its claimed weather-related benefits of the PPA Rider, AEP Ohio ignores again how rates are set for most customers – SSO customers and those purchased fixed price options from marketers. Those rates are not set based upon volatile hourly and day-ahead market prices but on long-term contracts that do not subject customers to that volatility. AEP Ohio's claims that customers will benefit from the PPA Rider because their rates will be less subject to volatility in the hourly and day-ahead energy markets caused by weather simply do not make sense in this context.

AEP Ohio also emphasizes as its "*raison d'etre*" "long-term rate stability." AEP Ohio points to the Ohio Energy Group's proposal for a 9 ½ year rate plan,[47] and then points to "the potential of an expanded PPA." But as discussed in OCC's Brief, the OEG proposal is inconsistent with the term of AEP Ohio's proposed ESP, contrary to the clear

[43] AEP Ohio Brief at 49.

[44] AEP Ohio Brief at 49.

[45] AEP Ohio Brief at 50.

[46] Tr. II at 512, 518-519 (Allen).

[47] AEP Ohio Brief at 51-52.

intent of the law and it would exacerbate the PPA Rider's harm to customers.[48] And AEP Ohio's proposal for an "expanded PPA" would effectively re-regulate (but without a prudence review) a utility-selected fleet of generation assets without appropriate cost controls. This would undermine the state's goal of bringing competition to generation markets and significantly harm customers.[49] The OEG proposal lacks any merit, is not appropriately the subject of this proceeding, and should be rejected.

2. As emphasized in the PUCO Staff Brief, AEP Ohio's proposed Power Purchase Agreement Rider would abruptly reverse Ohio's move to a fully competitive market for generation. That course is intended to ensure that all customers are provided reasonably priced retail electric service through competitively supplied generation.

On Brief, the PUCO Staff reiterates the well-founded testimony of its witness, Dr. Choueiki.[50] Dr. Choueiki testified that the PUCO has been moving towards full market competition for over a decade. And he testified that approval of AEP Ohio's proposed PPA Rider would be reversing Ohio's course before the "finish line" has even been reached. Granting a PPA Rider is a move in the opposite direction, Dr. Choueiki declared. [51] Approval of the PPA Rider would "provide a guaranteed revenue stream for [AEP Ohio's] generation assets, irrespective of market forces" and include "a return on equity for AEP-Ohio and the other OVEC Sponsoring Companies."[52] The PUCO Staff notes that this government-guaranteed, cost-based revenue recovery would occur even

[48] OCC Brief at 77-80.

[49] OCC Brief at 79-80.

[50] PUCO Staff Brief at 2-4; PUCO Staff Ex. 18 at 9.

[51] PUCO Staff Ex. 18 at 9; PUCO Staff Brief at 2-4.

[52] PUCO Staff Brief at 4.

though AEP Ohio "will no longer sell electricity to Ohio ratepayers."[53] Well said. OCC agrees.

The PUCO should not entertain AEP Ohio's re-regulation proposal. The PUCO should not undo the General Assembly's process that was initiated in 1999. That process was to replace cost-based regulation with competitive market pricing in the Ohio electric generation market. It is this process that the General Assembly envisioned as a tool to ensure reasonably priced retail electric service for customers in the State of Ohio. The PUCO should carry-out the General Assembly's directives.

3. The PPA Rider is not permitted under Ohio law and would cause customers to bear costs that are not related to providing retail electric service under the Standard Service Offer.

a. No provision of Senate Bill 3 or Senate Bill 221 justifies the PPA Rider.

The PUCO Staff declares that "[n]o provision in R.C. 4928.143 justifies the PPA Rider."[54] OCC agrees.[55] The PUCO Staff then points out that, currently, AEP Ohio recovers OVEC costs through its Fuel Adjustment Clause ("FAC"). As the PUCO Staff notes, the fuel adjustment clause is a "bypassable charge permitted under R.C. 4928.143(B)(2)(a)."[56] That subsection allows EDUs to collect the "cost of fuel used to generate the electricity under the offer" and the "cost of purchased power supplied under the offer."[57] But when AEP Ohio moves to 100% auction – and is not actually generating electricity or using purchased power supplied "under the offer," there is no longer a basis

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[53] PUCO Staff Brief at 4.

[54] PUCO Staff Brief at 11.

[55] OCC Brief at 46-47.

[56] PUCO Staff Brief at 11.

[57] PUCO Staff Brief at 12.

to charge customers for these costs.[58] And that state of affairs will commence on June 1, 2015.

The PUCO Staff is correct that after June 1, 2015, there will be no basis to charge an SSO customer for any generation costs or fuel costs other than those incurred associated with the PUCO-administered auctions.[59] As the PUCO Staff also correctly emphasizes, the PPA Rider is proposed as a non-bypassable rider and would thus also place OVEC costs on shopping customers who are not paying for such costs today.[60] But no customer (shopping or non-shopping) should have to pay these costs.

Moreover, it is clear that R.C. 4928.143(B)(2)(a) pertains to costs that are incurred to generate the electricity supplied under the SSO. Here, though, the PPA Rider attempts to collect costs that are unrelated to supplying power to SSO customers. The OVEC transaction is not related to power purchase costs that are used to supply SSO service. Because OVEC power is required to be sold into the market under the terms of the PUCO's order in Case No. 12-1126-EL-UNC, the PPA Rider would not constitute the cost of power purchased to supply customers under R.C. 4928.143(B)(2)(a). Instead, the OVEC transaction is a financial hedge that is unrelated to the physical procurement of power that R.C. 4928.143(B)(2)(a) addresses. It is unreasonable to expect captive monopoly Utility customers to guarantee the profits of any generation in Ohio, especially if that generation service is not provided directly to those same customers for their benefit.

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[58] PUCO Staff Brief at 12.

[59] OCC Brief at 46-47.

[60] PUCO Staff Brief at 12.

b. AEP Ohio's position is mistaken that it can charge customers a PPA Rider because it is a term, condition or charge relating to "default service," "bypassability" and "limitations on customer shopping."

To ensure reasonably priced retail electric service is made available to consumers in the State of Ohio, the General Assembly imposed limits on the charges that an electric distribution utility could collect under an ESP. Those limits are contained, inter alia, in R.C. 4928.143(B)(2). The Ohio Supreme Court has confirmed that R.C. 4928.143(B)(2) limits what a utility may seek under an ESP.[61] The Court ruled that if a provision does not fit within one of the categories listed following subsection (B)(2), it is not authorized by statute.

As discussed in Brief, AEP Ohio never specified on the record how the PPA Rider qualified as a charge under R.C. 4928.143(B)(2). And OCC argued that the PPA Rider does not fit into any of the categories authorized by the law.[62]

In its Brief, AEP Ohio claims that the charge relates to "default service and addresses (non) bypassability" and that it "could also be considered a limitation on customer shopping to the extent it is viewed as selling a generation hedging service to shopping customers even though they are purchasing generation service from a CRES provider."[63]

AEP Ohio's proposed PPA Rider does not relate to the provision of default service. As well established on the record in this proceeding, the proposed charge would

[61] *In re: Columbus S. Power Co.*, 128 Ohio St.3d 512, 520, 2011-Ohio-1788.

[62] OCC Brief at 47-48.

[63] AEP Ohio Brief at 27-28.

be a financial hedge.[64] It would not specifically relate to the provision of default service because the PUCO has required that AEP Ohio's entitlement be sold into PJM's Reliability Pricing Model ("RPM") auctions. And the suggestion that any proposed charge qualifies as a charge related to bypassability because the charge is either bypassable or non-bypassable (because all charges are either one or the other) makes little sense. All charges are either bypassable or non-bypassable and the General Assembly certainly did not intend for R.C. 4928.143(B)(2)(d) to be so broadly construed as to be meaningless.

Under Ohio rules of statutory construction, each subsection of the law is intended to have meaning.[65] A reasonable interpretation of this language would be that the charge should be related to conditions that affect customer shopping. Construing this section in pari materia with R.C. 4928.02, the charges must also meet the objectives of the law. One of those objectives is to "[e]nsure the availability of unbundled and comparable retail electric service that provides consumers with the supplier, price, terms, conditions, and quality options they elect to meet their respective needs."[66]

But the PPA Rider does not pertain to the provision of unbundled services that facilitate customer shopping. Customer shopping involves the actual procurement of power from market participants. The PPA Rider is not related to the procurement of power. Power from OVEC is sold into the PJM market. The OVEC transaction is a financial hedge that has nothing to do with the unbundling of services and the structuring of services to facilitate shopping. Nor is the charge related to bypassability since there is

[64] Tr. III at 747 (Allen).

[65] R.C. 1.47 presumes that the "entire statute is intended to be effective."

[66] R.C. 4928.02(B).

no provision of utility services that is bypassed. The proposed PPA Rider is, therefore, inconsistent with R.C. 4928.143(B)(2)(d).

c. R.C. 4928.02(H) makes it unlawful to for AEP Ohio to collect revenues from distribution service customers to subsidize competitive generation service based on market prices, as acknowledged by the PUCO Staff, IEU-Ohio, and OCC.

Both the PUCO Staff and IEU-Ohio explain that the PPA Rider would violate R.C. 4928.02(H). That law prohibits anticompetitive subsidies running from an electric utility's noncompetitive distribution service to its competitive generation services.[67] OCC agrees.[68] OCC also agrees that the Supreme Court of Ohio cases of *Indus. Energy Users-Ohio v. Pub. Util. Comm.*,[69] and *Elyria Foundry Co. v. Pub. Util. Comm.*[70] support the principle articulated in R.C. 4928.02(H).

While those cases predated other changes made in Senate Bill 221, R.C. 4928.02(H) was not changed. The holdings of those cases are thus, intact. In *Indus. Energy Users-Ohio*, the Supreme Court of Ohio reversed a PUCO finding authorizing the use of distribution revenues to subsidize the cost of a generation facility.[71] And in *Elyria Foundry*, fuel costs in a standard service offer were not permitted to be deferred for later recovery through a non-bypassable distribution charge, i.e. a charge applicable to all customers.[72]

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[67] PUCO Staff Brief at 12-14; IEU-Ohio Brief at 13-15.

[68] *See* OCC Brief at 53.

[69] 2008-Ohio-990, 117 Ohio St. 3d 486, 487-88, 885 N.E. 2d 195, 198. The Supreme Court's references in the case to R.C. 4928.02(G) are to the same language now in R.C. 4928.02(H) due to the 2008 addition, in Senate Bill 221, of R.C. 4928.02(F).

[70] 2007-Ohio-4164, 114 Ohio St. 3d 305, 315, 871 N.E. 2d 1176, 1188.

[71] 2008-Ohio-990, 117 Ohio St. 3d 486, 487-88, 885 N.E. 2d 195, 198.

[72] 2007-Ohio-4164, 114 Ohio St. 3d 305, 315, 871 N.E. 2d 1176, 1188.

Similarly, in the instant case, the costs of OVEC (or the credit), which varies from market prices, are proposed to be flowed back to all customers through the PPA Rider. But such a charge to customers would subsidize the utility's generation costs. The PPA Rider would be a subsidy of the cost of the OVEC generation facilities by all captive monopoly distribution service customers. Indeed, both SSO and shopping customers would be subjected to the charge although ***neither*** is receiving the generation output from OVEC through AEP Ohio.

OCC also agrees with the PUCO Staff and IEU-Ohio that the PUCO's decision in the *Sporn Case*[73] supports the parties' position that the PPA Rider is not authorized by the law. In that case the PUCO found "no statutory basis within Section 4928.143, Revised Code, or anywhere else in the Revised Code" for the recovery of plant closure costs. The PUCO's *Sporn* decision also found that collecting a generation-related cost such as a "plant closure cost" from all customers would violate R.C. 4928.02(H). This rationale applies to the hedging costs that the PPA Rider seeks to collect. Those OVEC hedging costs result from generation sold to PJM, but funded by all of AEP Ohio's captive distribution customers. The PUCO should find that AEP Ohio's PPA Rider would be an unauthorized charge to customers violating R.C. 4928.143 and R.C. 4928.02(H).

4. The PPA Rider is preempted by federal law under which the rates charged to customers for OVEC's wholesale service are set.

OCC also agrees with the PUCO Staff and IEU-Ohio that the PPA Rider is preempted by the Federal Power Act, consistent with the recent Fourth Circuit Court of

[73] *In the Matter of the Application of Ohio Power Company for Approval of the Shutdown of Unit 5 of the Philip Sporn Generating Station and to Establish a Plant Shutdown Rider*, Case No. 10-1454-EL-RDR, Finding and Order at 19 (January 11, 2012).

Appeals decision in *PPL Energy Plus, LLC v. Nazarian.*[74] There, the Fourth Circuit upheld a District Court decision finding that Maryland's authorization for a new generator to recover the difference between PJM's RPM clearing price and the generator's revenue requirements was preempted under the Federal Power Act.[75] The Fourth Circuit upheld the District Court's ruling that the Contract for Differences (CfD) "payments had the effect of setting the ultimate price that CPV [Commercial Power Ventures Maryland, LLC] receives for its sales in the PJM auction, thus intruding on the Federal Energy Regulatory Commission's ("FERC") exclusive authority to set interstate wholesale rates."[76]

There is little difference between AEP Ohio's PPA Rider request and Maryland's contract for differences payments to an electricity generator. The PPA Rider would recover the difference between AEP Ohio's share of OVEC costs and the sale of its share of OVEC into the PJM market. By doing this, the PPA Rider would be a "contract price guaranteed" by the PUCO which "supersedes the PJM rates" that AEP Ohio would otherwise recover for its OVEC interest – "rates established through a FERC-approved market mechanism."[77] As a result, it has the "potential to seriously distort the PJM auction's price signals."[78] The PPA Rider would set the price received by AEP Ohio at a

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[74] PUCO Staff Brief at 15-17; IEU-Ohio Brief at 21-22, *citing PPL Energy Plus, LLC v. Nazarian,* 753 F.3d 467, 2014 U.S. App. LEXIS 10155 (4th Cir. June 2, 2014).

[75] *PPL Energy Plus, LLC v. Nazarian,* 753 F.3d 467, 2014 U.S. App. LEXIS 10155.

[76] *PPL Energy Plus, LLC v. Nazarian,* 753 F.3d 467, 474, 2014 U.S. App. LEXIS 10155 at *13.

[77] *PPL Energy Plus, LLC v. Nazarian,* 753 F.3d 467, 477, 2014 U.S. App. LEXIS 10155 at *21.

[78] *PPL Energy Plus, LLC v. Nazarian,* 753 F.3d 467, 478, 2014 U.S. App. LEXIS 10155 at *26.

wholesale market and would violate the Supremacy Clause of the U.S. Constitution,[79] upon which FERC's preemptive authority is based.

In its Brief, AEP Ohio argues that "the proposed PPA Rider would not affect retail or wholesale competition in Ohio" because "AEP Ohio would bid each of these generation related items – capacity, energy, and ancillaries etc. – into the PJM market."[80] AEP Ohio states that all of the revenues would be used to offset costs billed to AEP Ohio by OVEC and that "[n]one of the energy or capacity associated with the Company's OVEC entitlement would be bid into the auction or used to offset any of the SSO load included in the auction."[81] AEP Ohio argues that, along with the non-bypassable nature of PPA Rider, the sale of AEP Ohio's energy and capacity into the PJM market will ensure that the PPA Rider "will have no adverse impact on the SSO auction or the ability of CRES providers to compete for customers on a level playing field."[82]

But, as the Fourth Circuit's decision makes clear, where a generator's costs are subsidized by a charge such as the Maryland contract, the generator will naturally have incentives to withhold energy or capacity from the market.[83] That will adversely affect the operation of the market.

The proposed PPA Rider rate violates federal, as well as Ohio, law and should be rejected.

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[79] U.S. Const. Art. VI provides "This Constitution, and the laws of the United States which shall be made in pursuance thereof; and all treaties made, or which shall be made, under the authority of the United States, shall be the supreme law of the land; and the judges in every state shall be bound thereby, anything in the Constitution or laws of any State to the contrary notwithstanding."

[80] AEP Ohio Brief at 25-26.

[81] AEP Ohio Brief at 26.

[82] AEP Ohio Brief at 26.

[83] *PPL Energy Plus, LLC v. Nazarian*, 753 F.3d 467, 478, 2014 U.S. App. LEXIS 10155 at *26.

5. AEP Ohio's proposed PPA Rider would leave customers without the protection of a prudence review and without incentives for protecting customers from unreasonable charges associated with inefficient operations.

As the PUCO Staff and other parties recognized, AEP Ohio's claim that its PPA Rider will somehow "stabilize customer rates" is inconsistent with the facts and its own witnesses' testimony.[84] The PUCO Staff appropriately points to AEP Ohio's "various, conflicting estimates regarding the potential costs of the PPA Rider."[85] These estimates range from "a $52 million cost to an $8.4 million benefit during the term of ESP III" and Mr. Allen's decision "not to incorporate any quantifiable cost or benefit regarding the PPA Rider in his ESP v. MRO analysis."[86]

The PUCO Staff also points out inconsistencies between the testimony of AEP Ohio's President's and that of Mr. Allen.[87] And the PUCO Staff points out, as OCC did, how Mr. Allen developed a fourth scenario – his most optimistic scenario, which he "unveiled for the parties for the first time during his cross-examination."[88] The PUCO Staff appropriately asks which of these scenarios is reasonable and which one "should the Commission rely on to determine [if?] the PPA will 'stabilize rates for customers'?"

The answer, of course, is that the net cost that the PPA Rider will impose on customers is affected by many factors and, in evaluating net cost, the PUCO must judge which assumptions are most reasonable. The factors, as the PUCO Staff points out,

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[84] PUCO Staff Brief at 18-25.

[85] PUCO Staff Brief at 19.

[86] PUCO Staff Brief at 19-20.

[87] PUCO Staff Brief at 18-21.

[88] PUCO Staff Brief at 20.

include primarily future market prices and potential changes in OVEC costs.[89] And on the cost side, as the PUCO Staff argues, "there are a number of factors that could greatly increase the costs of operating the OVEC units over the next few years," including "additional capital expenditures, increases in coal prices, and future environmental regulations."[90]

The factors contributing to different estimates of the net cost of the PPA Rider are discussed in numerous parties' briefs. As IEU-Ohio concludes, "[t]he credible evidence of the cost of the PPA, therefore, is that it is likely to result in an $82 million charge to customers. The amount it adversely affects customers may range from $82 million to $116 million."[91] And the PUCO Staff concludes, looking at the estimates of OCC witness Wilson and IEU-Ohio witness Murray, that "the PPA Rider could be extremely costly for customers during the ESP III term."[92]

6. AEP Ohio's estimate of an $8.4 million benefit to customers over the ESP term should not be relied upon. OCC witness Wilson's estimate of a cost to customers of $116 million provides a reliable estimate of the outcome of the PPA Rider over the ESP term.

a. AEP Ohio's forecast of OVEC (AEP Ohio Ex. 8) understates the cost to consumers as it relies on outdated market prices and incorporates substantial cost reductions that will likely never be realized.

OCC witness Wilson demonstrated that the cost of the PPA Rider to customers was likely to be approximately $116 million over the term of the ESP.[93] He developed

[89] PUCO Staff Brief at 21-22.

[90] PUCO Staff Brief at 22.

[91] IEU-Ohio Brief at 56.

[92] PUCO Staff Brief at 19.

[93] OCC Brief at 56-69.

this estimate by making appropriate adjustments to the only model AEP Ohio produced in discovery which showed the net cost to customers of the PPA Rider.[94] Mr. Wilson's adjustments are described in OCC's briefs. These adjustments eliminate Mr. Allen's projected reductions in OVEC costs due to its LEAN improvements, use updated (May 2014) market prices, and adjust the generation output to be more consistent with recent historic levels of generation.

Although AEP Ohio initially set the PPA Rider rate to zero,[95] it apparently realized the weakness of its claim at the time of the hearing. At the hearing, when Mr. Allen was cross-examined on his direct testimony, he asserted for the first time that there was an $8.4 million benefit to customers over the ESP term.[96] Mr. Allen constructed a new net cost to customers based upon OMA Ex. 3, Attachment 2. AEP Ohio later presented Mr. Allen's calculation through rebuttal testimony as AEP Ohio Ex. 8A (CONFIDENTIAL). Mr. Allen described his calculation on cross-examination for the first time as follows:

> A. So what one would do is take the energy revenues from, say, Attachment 2 for 2015 and in that case a seven-twelfths estimate would be reasonable, as well as a seven-twelfths estimate for the energy expenses. On the capacity revenues it wouldn't be appropriate to just take a seven-twelfths value from that exhibit because it reflects two different capacity periods within the PJM planning years. And so you would have to isolate based on the RPM price for the '15-'16 planning year what that value is for the first year.
>
> On the demand expense side it would be appropriate to do a calculation assuming seven-twelfths because the demand

[94] OCC Brief at 58-69.

[95] AEP Ex. 12, Ex. DMR-1 (Roush); Tr. I at 47 (Vegas); Tr. III at 917-19, 923, 930 (Roush).

[96] Obviously, no party had an opportunity to review these numbers or test the reasonableness of Mr. Allen's assumptions regarding this exhibit before presenting their own prepared direct testimony in this proceeding.

> charge is relatively constant across the year on a dollar per month basis.
>
> And so when you do that calculation, what you show is in year 1 the PPA -- and, sorry, there's another adjustment that would be appropriate to make on the demand charge is that you would want to look at the more recent OVEC data on the budget for OVEC for the demand charges that was presented in OEG Set 2, Interrogatory 2-004, you would use that to come up with the demand charge.
>
> Putting those together what you see is that in year 1 the PPA charge would be $6.2 million to customers, in year 2 the PPA rider would produce a credit to customers of $2.8 million, and in year 3 the PPA rider would produce a benefit to customers of $11.8 million.[97]

AEP Ohio's last minute efforts to manufacture numbers to make the PPA Rider seem like a benefit to customers is nothing short of pulling a rabbit out of a hat. It relies on Mr. Allen's claims that it is appropriate to take 7/12 of energy revenues, energy expenses, and demand charges from 2015 (June through December) to calculate his new number. It also relies on a 5/12 assumption for energy revenues, energy expenses' and demand charges for 2018. Mr. Allen's concept that you can use annual calendar data (from two different years) to estimate effects during an ESP period that runs three years (from June 2015 through June 2018) is unreasonable. With electric prices being highly seasonal, any annual estimate created to cover a three year period (with partial years of 2015 and 2018) is problematic, and will likely produce an unreliable estimate.

Moreover, although Mr. Allen and AEP Ohio have claimed that Mr. Allen's analysis in AEP Ex. 8/8A is the most updated analysis in this proceeding, that analysis utilized the September 2013 market prices and generation forecast from OMA Ex. 3. The only update from September 2013 is, according to Mr. Allen, OVEC's updated budget of

[97] Tr. II at 485-86 (Allen).

O&M costs and demand charges.[98] He did not update any other aspect of the forecast from Attachment 2. Instead he continues to rely on outdated market prices and generation output, and denies that August/September 2013 forward market prices are outdated in today's market.[99]

But the PUCO should not rely on AEP Ohio Ex. 8/8A because it is based on outdated market prices. Additionally, the OVEC budget estimates for LEAN improvements are simply not credible as discussed in OCC's brief.[100] AEP Ohio's claim that AEP Ohio Ex. 8 is "based on the most updated and accurate information"[101] is simply nonsense. Other than the OVEC budget for O&M and demand charges, it uses the data from September 2013. In comparison, OCC witness Wilson uses much more current data --May 2014 forward market prices.

AEP Ohio also claims that AEP Ohio Ex. 8/8A provides a "reliable long-term evaluation of the PPA Rider well beyond the ESP term."[102] But this claim, in addition to being untested, is also irrelevant to this proceeding. This case concerns the proposed ESP term June 2015 through May 2018. Although AEP Ohio points to OEG witness Taylor's proposal for a 9 ½ year term, it violates the law, is highly speculative, and would be harmful to customers as discussed at length in OCC's Brief.[103] There is no reasonable basis for AEP Ohio's suggestion for the PUCO to "evaluate the long-term benefits of the PPA Rider when considering whether to adopt the proposal." Doing so is inconsistent

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[98] Tr. II at 493, 504-05 (Allen).

[99] Tr. II. at 495-496 (Allen).

[100] OCC Brief at 58-62.

[101] AEP Ohio Brief at 52, n.39 and at 53.

[102] AEP Ohio Brief at 54.

[103] OCC Brief at 77-80.

with the three-year ESP term that AEP Ohio has proposed[104] and with the two-year term that could result if the Utility is granted its proposed unilateral right to terminate its plan. The PUCO should disregard any suggestion of a longer-term PPA Rider and should not give any credence to AEP Ohio's or Mr. Taylor's longer-term projections given the 3-year term of the ESP.

b. OCC Witness Wilson's calculation of $116 million in net costs to customers should be relied upon by the PUCO in rejecting AEP Ohio's proposed PPA.

Determining the cost to customers of the PPA Rider requires preparing an estimate based upon the best information available. OCC witness Wilson prepared just such an estimate using May 2014 forward market prices. AEP Ohio did not. It failed to re-run its August 2013 run of its dispatch model to reflect updated forward market prices despite ready availability of this information. Mr. Allen could simply have asked the two analysts who perform such modeling for AEP Service Corporation[105] to update the earlier analyses. But he didn't. This is very telling. AEP Ohio only wants to reflect those changes that would reduce the net cost of OVEC to consumers. This way it is an easier sell to the PUCO. AEP Ohio doesn't want to reflect changes it knows will have the effect of increasing the net cost of OVEC to customers. AEP Ohio's analysis is outdated and cannot be relied upon.

Yet AEP Ohio criticizes OCC Witness Wilson because he had to make rough adjustments to AEP Ohio's model to reflect the expected net cost to customers based on

[104] Notably, AEP Ohio has even suggested that the PPA Rider could be in place for period of time that is shorter (not longer) than its three-year term. Under AEP Ohio's alleged unilateral right to terminate, the ESP and the PPA Rider could be ended in two years.

[105] Tr. II at 491 (Allen).

current forward market prices and more recent historic OVEC generation.[106] AEP Ohio's criticism is not well founded.

Mr. Wilson made reasonable adjustments to AEP Ohio's analysis for good reasons. While AEP Ohio is correct that those adjustments will not reflect the actual dispatch for every hour under the model (because Mr. Wilson did not have the model at his disposal), they reflect reasonable estimates of the overall impact of those adjustments. OCC Witness Wilson explained the purpose of making such an adjustment to AEP Ohio's counsel:

> Q. Okay. Now, do you agree if inputs of a model change significantly, then you have to rerun the model to get a valid result?
>
> A. I agree that if the inputs have changed significantly, that to have a result that's entirely consistent with all the inputs you would have to rerun the model, but sometimes you can instead make an estimate based on a much simpler approach.
>
> * * *
>
> A. . . . I would say that to have dispatch model results that are fully consistent with the dispatch model's inputs, if you change the inputs, you would then rerun the dispatch model. But to have results that are based on something a dispatch model did and then some of those inputs changed, there can be more simpler and straightforward approaches to adjusting those results that are still valid. They're not an exact reflection of what the dispatch model would have said had you rerun it, but they may be very close and they may be sufficiently valid depending on the application of the analysis.[107]

Mr. Wilson acknowledged that he did not rerun the model and that his adjustments are not going to dispatch appropriately in every hour. Mr. Wilson's

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[106] AEP Ohio Brief at 54-57.

[107] Tr. X at 2451-2452 (Wilson).

adjustments to AEP Ohio's outdated analysis are reasonable. In contrast, AEP Ohio has chosen to approach this issue like an ostrich with its head in the sand. When strong support and analysis are available but not furnished, one can only suppose that the production of strong evidence is counter to that party's objectives. Thus, AEP Ohio has limited the information that the PUCO has to determine what the expected net cost to customers is under the PPA Rider. Mr. Wilson (and IEU witness Murray) pointed out the effect of removing $30 million in LEAN improvements from AEP Ohio's model and the balance ($116 million - $82 million = $34 million) for Mr. Wilson's other adjustments.

In addition, as OCC pointed out in its Initial Brief, Mr. Allen knows very little about OVEC budgeting. And he made no comparisons or analysis of OVEC's success in meeting its budget projections, let alone budget reductions of the magnitude that he included as OVEC's most recent projections in IEU Ex. 8.[108] While AEP Ohio's Mr. Allen claimed that the LEAN and other OVEC cost savings are "sufficiently certain to be used in the rider estimate,"[109] no demonstration was presented to this effect by him. While Mr. Allen is "confident" of the reasonableness of the LEAN savings, he testified that he has "never reviewed the accuracy of the five-year operating budgets or the current operating budget" for OVEC.[110] Further, his testimony on this subject about what others at the company may have said to him regarding the accuracy of OVEC budgets

[108] OCC Brief at 60-61.

[109] AEP Ohio Brief at 59.

[110] Tr. II at 512 (Allen).

historically is unreliable hearsay.[111] His testimony should not be relied upon.

7. AEP Ohio's argument that the PUCO should require customers to protect it through reregulating part of its generation is unreasonable.

OCC, the PUCO Staff, and other parties have all advocated that, with the implementation of full market-based SSO rates, the transition to a competitive market for generation in Ohio should be at an end. Except, all of a sudden, AEP Ohio wants to pull back so that it is protected from the market and guaranteed a return on its investment. It wants to re-regulate the price customers pay for OVEC. And it makes a lengthy pitch to do so by reviewing the history of implementing Senate Bill 3 and Senate Bill 221. It argues, in large part, that the slow pace of transition has been necessary to protect customers from high market prices.[112] AEP Ohio further argues that Senate Bill 221 established a new and extended transition period to "very gradually subject customers to market rates over a period of six to 10 years."[113] AEP Ohio also points to a "cooperative partnership between the Commission and AEP Ohio" over this period, including after Senate Bill 221 to "pull back from the market-based rates cliff."[114]

None of these AEP Ohio claims are based on any record evidence in this proceeding. The simple fact is that customers have long been deprived of the benefits of competitive market prices that are below AEP Ohio's legacy generation rates. Had the

[111] Tr. II at 510 (Allen). Although the PUCO has admitted hearsay into evidence in previous cases, it has done so noting the appropriate weight to be given such evidence is within its expertise. *See, for example, In the Matter of the Application of Ohio Power Company and Columbus Southern Power Company for Authority to Merge and Related Approvals, et al.,* Case No. 10-2376-EL-UNC, et al., 2011 Ohio PUC LEXIS 1325, * 29, Opinion and Order (December 14, 2011). Mr. Allen's lack of personal knowledge regarding the OVEC budgeting process from which he could critically assess fellow workers' statements regarding the subject weighs against giving Mr. Allen's testimony any weight.

[112] AEP Ohio Brief at 33-37.

[113] AEP Ohio Brief at 38.

[114] AEP Ohio Brief at 38-39.

historical differential between wholesale market prices and AEP Ohio's base generation rates been at issue in this proceeding, OCC and other parties would have demonstrated the hundreds of millions of dollars of savings lost to customers by having to pay above-market rates for generation – in addition to the hundreds of millions paid to AEP Ohio to encourage it to transition to competition. The slow pace of transitioning to market based rates has benefited AEP Ohio. The Utility has the highest residential rates in the state, on average. But that is not the issue in this proceeding.

The PUCO determined in Case No. 11-346-EL-SSO that AEP Ohio's generation rates would be determined by market prices effective June 1, 2015. It is AEP Ohio's inability to accept that decision – and to accept the risk associated with its generation assets -- that has it revisiting the historic regulatory well. Rather than honoring the General Assembly's directive for a competitive marketplace, AEP Ohio seeks authority to further defer the transition to competition. AEP Ohio's pitch to the PUCO is to leave in place a system of compensation for generation investment based on a cost-plus model. That should not be entertained.

8. The PUCO Staff is correct that the auction design alone is adequate to mitigate volatility for SSO customers, without AEP Ohio's proposal.

The PUCO Staff, as well as OCC and IEU-Ohio, argued that the PPA Rider would not reduce rate volatility.[115] And the Staff recommended adopting other approaches, such as staggered and laddered auction products, to produce an appropriate level of price stability for SSO customers. But AEP Ohio claimed otherwise, arguing that Dr. Choueiki is mistaken that the use of staggered auction procurement and laddering of

[115] PUCO Staff Brief at 18-24; OCC Brief at 48-52; IEU-Ohio Brief at 24-28.

multiple products is a more effective approach to mitigate rate volatility than the PPA Rider.[116]

Dr. Choueiki is right. AEP Ohio is wrong. AEP Ohio's claim that the PPA Rider will somehow operate counter to the market rather than following the market was shown by OCC witness Wilson to be unsound. And by AEP's own admission, the effect of the PPA Rider on volatility is de minimus. Mr. Allen's rebuttal exhibit WAA-R2 shows that the stability effect of OVEC, even based on Mr. Allen's highly speculative assumptions, would be just $.35/MWh.

AEP Ohio argues that laddering/staggering "only partially mitigates rate volatility and does not mitigate fundamental changes in market rates."[117] Certainly, no approach – hedging or otherwise -- will "completely" mitigate price changes for an indefinite period of time. The question is not whether any volatility mitigation tool is "partial" but whether it makes sense and can be obtained at a reasonable cost and under reasonable terms. The PPA Rider does not achieve those objectives. Staggering and laddering of competitive SSO auctions are far better tools for these purposes. SSO auctions reflect the fuel diversity upon which the SSO supplier's offer is based and they reflect the multi-year products required by the auctions. And the SSO suppliers bear the risk of delivering the required supplies to customers at the auction price while remaining profitable. AEP Ohio isn't willing to shoulder that risk.

AEP Ohio also argues that staggering/laddering doesn't help shopping customers or those participating in governmental aggregation programs.[118] But it is not meant to.

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[116] AEP Ohio Brief at 60-63.

[117] AEP Ohio Brief at 60-61.

[118] AEP Ohio Brief at 60-61.

Customers select competitive suppliers because of the different options that they offer. A non-bypassable PPA Rider would force customers who are shopping to continue to rely on AEP Ohio's selection of generating resources to set the overall price they are paying. Customers who are shopping are participating in the market because they want a different choice – they don't want what the electric utility has to offer and they certainly don't want to be forced to take what the electric utility has to offer.

AEP Ohio is right about one thing though – prices vary. And the decisions that customers make – whether to take SSO service or shop and, if shopping, the rate, terms and length of their contract, will determine the price they pay. Choice is not intended to eliminate the potential for risks and rewards – it is intended to give customers the ability to determine what risks and rewards they want to assume. AEP Ohio's PPA Rider would effectively take that choice away from customers by establishing a non-bypassable subsidy for generation service that they themselves did not choose. AEP Ohio's proposal is counter to the entire concept of competitive markets, would be counterproductive to choice, and should be rejected.

AEP Ohio also argues that, in contrast to the risk premium included in marketers' fixed price offers, "the PPA Rider involves a differential between cost and market without an additional premium."[119] This is an inane statement – the difference between market price and cost **is** the risk premium and captive customers are responsible for that risk premium. In contrast, customers purchasing a fixed price offer from a marketer do not bear the risk that the market will produce a different price than they agreed to pay. The marketer bears that risk.

[119] AEP Ohio Brief at 62.

AEP Ohio claims that customers looking for stability will not find it in the market. AEP Ohio points to the fact that most (72.4%) offers in AEP Ohio's service territory are for 12 months or less and the longest offers are for 36 months.[120] This point however is overstated. AEP Ohio has proposed a PPA Rider price to change annually (every 12 months). Thus, most offers are equal in length to the PPA Rider price and many are longer. And customers can choose the longer-term, 36-month contracts if they so desire. These contracts are as long as the entire ESP period. Customers cannot choose a PPA Rider price that will not change for more than 12 months; they are stuck with a 12-month PPA Rider and with the under- or over- collection that will inevitably occur.

Moreover, the fact that there can be volatility in supplier and governmental aggregation prices is reflective of the market. Customers who choose not to have a longer-term fixed price do subject themselves to the risk that their price will rise during their shorter-term contract renewals, but they are making a choice of such shorter-term contracts. While customer education is needed to ensure that customers are aware of the risks they are taking and their options, competitive markets for all products are prone to changes/volatility in rates.

Forcing the PPA Rider on captive monopoly customers would undermine the operation of the competitive market. And it would undermine the objective of allowing customers to bear the risk with which they are comfortable. The PUCO should reject the PPA Rider.

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[120] AEP Ohio Brief at 62.

9. Although the PJM market for capacity and energy continues to be imperfect, it is a substantially better construct for customers than cost-based payments for OVEC under the PPA Rider.

As OCC and other parties have argued, the discipline of the market provides better value to customers than the historic cost-based regulatory regime that AEP Ohio would seek to perpetuate with its PPA Rider.[121] But AEP Ohio argues that the PJM capacity and energy markets are "far from fully functioning, transparent and effective."[122] AEP Ohio points to regulatory reforms that it claims "will cause the market prices to increase over time, as compared to the largely fixed and stable OVEC costs being included in the PPA Rider proposal."[123] AEP Ohio also argues that the "cost of maintaining reliability under the PJM construct (usually transmission fixes) is also significant and should be considered."[124]

The PJM market is certainly not perfect. It continues to undergo changes, as discussed by OCC witness Wilson, and it operates according to established rules based on an ongoing review process involving numerous stakeholders. AEP Ohio discusses many of those rules. And it suggests that the operation of the market in accordance with these administratively-determined rules and ongoing stakeholder process means that reliance on "market forces is a misnomer and a red herring."[125] AEP Ohio further points out that there is an ongoing process of reform at PJM, contending that "[a]ll of these reforms will

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[121] OCC Brief at 71-72.

[122] AEP Ohio Brief at 64.

[123] AEP Ohio Brief at 64.

[124] AEP Ohio Brief at 64.

[125] AEP Ohio Brief at 65.

likely take a significant amount of time and either come with a price tag or increase PJM market prices if successful."[126]

But AEP Ohio provided no evidence that the PJM-administered energy markets and pending market reforms will dramatically affect prices, especially during the ESP term. These markets have been in place for some period of time, and the ongoing stakeholder review process will stabilize rates in the PJM market over time rather than result in exacerbation of prices as AEP Ohio suggests.

AEP Ohio criticizes both OCC witness Wilson and PUCO Staff witness Choueiki for having confidence in PJM's ability to address problems in the operation of the PJM market through the ongoing stakeholder process.[127] But, as AEP Ohio acknowledges, it is a participant in these reform efforts.[128] More importantly for purposes of this proceeding is that any issues in the PJM capacity or energy markets are unlikely to have any significant impact on market prices paid by AEP Ohio's customers during the ESP III period. As AEP Ohio witness Vegas testified, because PJM capacity prices have been determined through the end of the ESP period (2017 – 2018), any rules issues are unlikely to have a substantial effect on capacity prices during the ESP term.[129] And with respect to energy prices, "the SSO suppliers, in bidding a specific price for a specific period of time, bear the risk of variations in price in the day-ahead and monthly energy markets to meet their share of . . . customer energy requirements."

[126] AEP Ohio Brief at 65-66.

[127] AEP Ohio Brief at 66-67.

[128] AEP Ohio Brief at 67.

[129] Tr. I at 62-63 (Vegas).

Thus, AEP Ohio's emphasis on PJM rules changes is of little significance. The rules changes will have a limited effect on SSO prices during the term of the ESP. While these issues might be worthy of debate for periods beyond the 2017/2018 RPM BRA auction period, they will have limited effect in this proceeding.

10. To the extent that any PPA Rider is approved (which it should not be), the PUCO should make clear that it is limited to OVEC and should end customers' payments for OVEC upon sale or transfer of AEP Ohio's OVEC interest.

If the PUCO were to approve a PPA Rider in any form despite the numerous legal problems and absence of demonstrated benefit, it should protect customers from additional harm by making clear that the PPA Rider is limited to AEP Ohio's interest in OVEC. The PUCO should also make clear that the PPA Rider can only continue until AEP Ohio can sell or transfer its interest in OVEC and that AEP Ohio must continue to make good faith efforts to do so under the terms of the ICPA. Likewise, the PPA should be limited to the term of the ESP.

AEP Ohio clearly sees approval of the PPA Rider for OVEC as a foot in the door to re-regulate and subsidize a substantial portion of its "Ohio legacy plants."[130] Pointing to the testimony of its witness Dr. McDermott, AEP Ohio argues that the PUCO should hold the PPA Rider open for expansion to other plants in the future.[131] At the same time, AEP Ohio's proposed early termination provision would enable AEP Ohio to take advantage of an upswing in market prices (or favorable coal prices) by abandoning the PPA Rider after two years.

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[130] AEP Ohio Brief at 67-69.

[131] AEP Ohio Brief at 68, *citing* AEP Ohio Ex. 32 at 10 (McDermott).

Even if AEP Ohio could somehow get the illegal and harmful PPA Rider approved for OVEC, the PUCO should stop right there. AEP Ohio cites to the testimony of Dr. Choueiki acknowledging that "the OVEC contractual entitlement was unique and could be approved as a legacy contract."[132] But AEP Ohio misrepresents Dr. Choueiki's testimony. Dr. Choueiki only testified that the PUCO's allowance of AEP Ohio to temporarily retain its OVEC interest is unique.[133] He did not testify that the OVEC generating asset is, in any way, unique. And he clearly stated that he has the same objections to both the proposed OVEC PPA and any expanded PPA.[134]

And even if there is a basis for saying that the OVEC generating asset is unique, that suggests that other generating assets are not unique and the allowance of an expanded PPA with respect to them would not be justified. AEP Ohio's argument is inconsistent.

It should be emphasized that AEP Ohio has not proposed a PPA to address any generation asset other than OVEC. AEP Ohio suggests that the mere approval of a PPA Rider provides a vehicle to consider the re-regulation and subsidization of other legacy assets. And AEP Ohio wants the PUCO to apply a different, lighter standard to such review. But any proposal AEP Ohio submits should stand on its own and must meet all of the legal and regulatory standards and requirements against which the OVEC PPA is being evaluated in this case. If anything, the PUCO should ensure that any other generation asset that AEP Ohio seeks to re-regulate is subjected to the same scrutiny applied to the OVEC assets. Finally, if the PUCO moves forward to approve the OVEC

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[132] AEP Ohio Brief at 68, *citing* Tr. XII at 3037 (Choueiki).

[133] Tr. XII at 3037, 3039-3040 (Choueiki).

[134] Tr. XII at 3040 (Choueiki).

PPA, it must ensure that the charges to customers are on a nonbypassable, nondiscriminatory basis.[135] Moreover, to ensure the efficient operations of the facility, the Utility should share on a 50/50 percent basis all monetary risks (and alleged benefits) associated with the facility's operational costs and revenues.[136]

B. Under The Terms Of The PUCO's Order In Case No. 12-1126-EL-UNC, AEP Ohio Has A Continuing Duty To Seek To Transfer OVEC Assets. The PUCO Should Not Entertain AEP Ohio's Request For A PPA Rider Without Examining Whether AEP Ohio Has In Good Faith Sought To Transfer The Assets. This Is Necessary To Prevent Harm To Customers That Follows From AEP Ohio Retaining Its Interest In OVEC And Requesting Customers To Guarantee AEP Ohio Profits On Its OVEC Interest.

OCC emphasized that AEP Ohio has a continuing duty to make good faith efforts to transfer its OVEC interest, thus preventing any need to consider AEP Ohio's proposed PPA Rider and the harm it would cause customers.[137] But AEP Ohio has not made such continuing efforts.

AEP Ohio claims that "there is no reason to try to transfer the OVEC contractual entitlement again because the same conditions that led the OVEC owners to withhold their consent for transferring AEP Ohio's share – AEP Genco's credit rating being lower than AEP Ohio's – continue to exist."[138] AEP Ohio claims that these same reasons apply, circumstances have not changed, and "there is no reason for AEP Ohio to try again."[139]

But as discussed in OCC's and IEU-Ohio's Briefs, there are numerous ways under the terms of the Amended and Restated Inter-Company Power Agreement

[135] OCC Brief at 75-76.

[136] OCC Brief at 74-75.

[137] OCC Brief at 37-42.

[138] AEP Ohio Brief at 25.

[139] AEP Ohio Brief at 25.

("ICPA") to approach this issue.[140] As OCC and IEU-Ohio have emphasized, Section 9.182 of the ICPA allows for a transfer to a Permitted Assignee, i.e. an affiliate with an investment grade credit rating. And Section 9.183 permits AEP Ohio to assign its interest to a third party, so long as it first provides a Right of First Refusal to the other parties to the OVEC agreement.

AEP Ohio does not explain in its brief why either of these are not pursuable options. For instance, while AEP Genco may not have an investment grade credit rating, other operating companies of AEP Ohio might have had such required credit ratings.[141] Thus, AEP Ohio's interest could be assigned to another AEP operating company or an unrelated third party. But AEP Ohio did not pursue these options.

Instead, AEP Ohio attempts to skirt these issues. It suggests that it can do nothing else to transfer its interest since it tried once, but could not obtain consent of the other Sponsoring Companies. AEP Ohio's disregard for the varied options to transfer its OVEC interest under the terms of the ICPA is telling. By not engaging in good faith efforts to transfer its OVEC interest, it has disregarded the directive of the PUCO, as conveyed in its Opinion and Order at Case No. 12-1126-EL-UNC.[142] Because AEP Ohio has failed to demonstrate its efforts to transfer its OVEC interest, contrary to its duty to do so, the PUCO should not entertain AEP Ohio's proposed PPA Rider.[143]

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[140] OCC Brief at 41-42; IEU-Ohio Brief at 34-36.

[141] IEU-Ohio Brief at 35; Tr. II at 580-82.

[142] OCC Brief at 37-42.

[143] OCC Brief at 37-42.

C. AEP Ohio Does Not Have The Unilateral Right To Terminate Its ESP One Year Early.

In its ESP Application, AEP Ohio "reserves the right" to terminate its ESP one year early.[144] AEP's unprecedented reservation would give it the unilateral power to terminate its ESP for a number of purposes (none of which are necessarily fair for customers). AEP Ohio can terminate if there are: (1) "substantive changes in Ohio Law (including rules or orders of the Commission) affecting standard service offer (SSO) obligations and/or SSO rate plan options under Chapter 4928 of the Revised Code" or (2) "a substantive change in federal law (including FERC rules or order) or PJM tariffs or rules with respect to capacity, energy or transmission regulation or pricing that has an impact on SSO obligations and/or rate plan options."[145]

In its Brief OCC argued that there was no support for AEP Ohio's proposition.[146] No statutory authority. No case law. Other intervenors, including Constellation, Ohio Manufacturers' Association, and RESA recognized this as well[147] and similarly urged the PUCO to reject this provision of the ESP. Yet, in its initial brief, AEP Ohio failed to provide any support for its unilateral right to terminate. AEP has no authority to unilaterally terminate an ESP. AEP cannot rewrite the law. And as a creature of statute, the PUCO cannot either.[148]

[144] Application at 15 (Dec. 20, 2013).

[145] Id.

[146] OCC Brief at 154-157.

[147] See Constellation Brief at 25-26; OMA Brief at 3-6; RESA Brief at 34-36.

[148] *Cleveland Electric Illuminating Co. v. Pub. Util. Comm.* (1975), 42 Ohio St.2d 403, 330 N.E.2d 1, 1975 Ohio LEXIS 510, 71 Ohio Op.2d 33; *Dayton Communications Corp. v. Pub. Util. Comm.* (1980), 65 Ohio St.2d 302, 307 [18 O.O.3d 478]; *Consumers' Counsel v. Pub. Util. Comm.* (1981), 67 Ohio St.2d 153, 166 [O.O.3d 96]. *Montgomery County Bd. of Comm'rs v. Pub. Util. Comm.* (1986), 28 Ohio St.3d 171; 503 N.E.2d 167; 1986 Ohio LEXIS 818. See also, *Pike Natural Gas Co. v. Pub. Util. Comm.* (1981), 68 Ohio St.2d 181, 22 O.O.3d 410, 429 N.E.2d 444; *Werlin Corp. v. Pub. Util. Comm.* (1978), 53 Ohio St.2d 76, 7

AEP Ohio insists that it needs flexibility to adapt to a litany of changes in rules or laws that affect the PJM Market and/or in the state of Ohio.[149] AEP Ohio also claims that the right to terminate the ESP early and reopen it in the event of significant changes is "reasonable, prudent, and necessary to protect the customers and the Company's interest."[150]

Assuming arguendo that the PUCO has the authority to allow AEP Ohio the unilateral right to terminate the ESP, the PUCO should not be persuaded by such rhetoric. As noted by OMA, the flexibility that AEP Ohio seeks would deprive consumers of the predictability and security associated with a three year set term for the ESP.[151] And the flexibility AEP Ohio seeks may cause uncertainty in the market, adding risks and costs[152] which would likely be passed onto customers. But there are more reasons why AEP Ohio's unilateral right to terminate should be rejected.

The PUCO Staff noted that, under the Utility's proposal, the PUCO would not play a role is determining whether termination is warranted. And the PUCO would not have the ability to refuse termination.[153] The PUCO Staff instead offered that if AEP Ohio has concerns, it should bring those concerns to the PUCO's attention. This appears to be a reasonable approach that is consistent with what the PUCO has recognized as its

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O.O.3d 152, 372 N.E.2d 592; *Ohio Pub. Interest Action Group, Inc. v. Pub. Util. Comm*. (1975), 43 Ohio St.2d 175, 72 O.O.2d 98, 331 N.E.2d 730.

[149] AEP Ohio Brief at138.

[150] Id. at 139.

[151] OMA Brief at 3-6.

[152] See Constellation Brief at 25-26; Direct Energy Brief at 12; RESA Brief at 34-36.

[153] PUCO Brief at 68-69 (citing PUCO Staff Witness Strom).

continuing jurisdiction over a Utility's ESP.[154] And under such an approach other parties could participate in the process. Such an approach is vastly different from the heavy-handed unilateral termination right AEP Ohio insists it has.

Finally, the PUCO should be mindful of the slippery slope upon which it is standing atop. As pointed out by OMA, if the PUCO were to allow AEP Ohio this early termination right, it would set dangerous precedent for the other EDUs.[155] Indeed, at least one other EDU, Duke Energy Ohio, has already copied AEP Ohio's approach and incorporated a unilateral termination provision in its proposed ESP.[156]

The PUCO should find that AEP Ohio's early termination provision is unlawful and unreasonable. It should be rejected.

D. AEP Ohio's Proposed Electric Security Plan Is Less Favorable In The Aggregate For Customers Than A Market Rate Offer, And Thus The PUCO Should Modify And Approve The Plan.

AEP Ohio concluded that its ESP passes the more favorable in the aggregate test that is set forth under R.C. 4928.143(C).[157] AEP Ohio stands alone in this respect. AEP Ohio points to the PUCO Staff as supporting its conclusion that its ESP passes the more favorable in the aggregate test. But the Staff's analysis does not support AEP Ohio's conclusion. When the PUCO Staff undertook its own analysis, it evaluated the ESP as

[154] See, e.g., *In the Matter of the Application of Columbus Southern Power Company for Approval of a Mechanism to Receive Deferred Fuel Costs Ordered Under Section 4928.144, Ohio Revised et al.*, Case No. 11-4920-EL-RDR. Finding and Order at ¶35 (finding that "AEP Ohio's ESP, including its phase in plan…is subject to the ongoing supervision and jurisdiction of the Commission"), (Aug. 1, 2012).

[155] OMA Brief at 3-6.

[156] See *In the Matter of the Application of Duke Energy Ohio for Authority to Establish a Standard Service Offer Pursuant to Section 49218.143, Revised Code, in the Form of an Electric Security Plan, Accounting Modifications and Tariffs for Generation Service*, Case No. 14-481-EL-SSO et al., Application at 16-17 (May 29, 204).

[157] AEP Ohio Ex. 7 at 3 (Allen Direct).

modified by it.[158] While the PUCO Staff concluded that the Staff modified ESP passed the MRO v. ESP test, its modifications are not consistent with AEP Ohio's proposed ESP. Thus, to argue that the PUCO Staff agrees with AEP Ohio on this point is misleading and compares apples to oranges.

OCC Witness Kahal testified[159] that the ESP produces results that are less favorable in the aggregate than the expected MRO results.[160] IEU Ohio Witness Murray came to the same conclusion.[161] AEP Ohio's ESP does not pass the statutory test. The test is designed to protect customers from results under government regulation (the ESP) that are less favorable for customers than competitive market results (the MRO). On this basis, the PUCO cannot approve the ESP because the Utility failed to prove that the ESP complies with R.C. 4928.143(C)(1).

While much has already been said in OCC's initial brief to counter the arguments presented by AEP Ohio in its initial brief,[162] there are a few issues left to address. AEP Ohio addresses a few qualitative benefits of the ESP and OCC's $240 million calculated price for the ESP. These arguments will be addressed seriatim.

[158] Tr. IX at 2202 (Turkenton).

[159] OCC Ex. 13 at 24-26 (Kahal).

[160] Id. at 13.

[161] See IEU Ex. 1B at 27 (Murray).

[162] See OCC Brief at 6-26.

1. The qualitative benefits to customers should not be considered as part of the ESP v. MRO analysis. But if qualitative benefits are considered, the PUCO should conclude that the qualitative benefits to customers are either non-existent or outweighed by the significant costs imposed upon customers.

AEP Ohio presents a new-found argument that the ESP provides a qualitative benefit over an MRO by being a "more holistic approach to address many components of electric service" as compared to the MRO, which is "primarily a plan for power procurement."[163] AEP Ohio also claims that the "reliability benefits" that the DIR provides to customers are likely to be delivered sooner under an ESP rider than if a traditional rate base distribution case were used to recover the same investments.[164]

Before addressing the merits of the so-called qualitative benefits of the ESP to customers, it should be noted that using qualitative factors to reduce or cancel out more objective quantitative analysis is unreasonable, as noted by OCC Witness Kahal.[165] And it may be determined to be unlawful as well, as the Ohio Supreme Court will be addressing this very issue in the NOPEC appeal of the FirstEnergy ESP.[166]

AEP Ohio counts as a qualitative benefit to customers the fact that it can seek to collect money from customers that address many different components of electric service, including distribution related investments. But while this may be a benefit to the utility, it cannot be counted as a benefit to customers. In fact, from a customer's perspective this "holistic" approach is detrimental to ensuring that customers have reasonably priced retail electric service, a policy of the State under R.C. 4928.02.

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[163] AEP Ohio Brief at 140.

[164] Id. at 141.

[165] OCC Ex. 13 at 10 (Kahal).

[166] S.Ct. 13-513.

Under the "holistic approach" the electric service elements of an ESP are only those that the utility chooses to include, or selects. This "selective" approach of the EDU actually precludes a more "holistic" review by the PUCO of the utility's distribution rates. A "holistic" review of distribution rates occurs when a distribution rate case is filed (i.e. a complete review of distribution revenue and expenses). Another example of the selective (not holistic) approach taken in this ESP is the Utility's PPA proposal. Assuming that the PPA is needed and is a hedge (contrary to OCC's position) – AEP Ohio unilaterally chooses what "hedge" (power plant) they include in the plan. This precludes review by the PUCO of whether the Utility-offered PPA is the best and most cost-effective way to hedge for consumers.

Additionally, the "holistic" approach is problematic when it allows the utility to collect significant distribution investment through a rider mechanism, as opposed to a base distribution rate case. OCC Witness Effron testified that collecting costs through a rider in an ESP is contrary to sound ratemaking practice.[167] This is because it is single-issue ratemaking reduces or eliminates the incentive for a utility to control costs. And even worse, a rider can potentially incent a utility to make uneconomic choices, according to OCC Witness Effron.[168]

Another matter to consider in weighing the so-called holistic approach under the ESP is the fact that it proliferates the use of rider mechanisms. As noted by Walmart, with no less than 23 riders in AEP Ohio's tariffs, it makes it untenable for customers to evaluate their rates.[169] Walmart suggests (and OCC concurs) that the PUCO should

[167] OCC Ex. 18 at 4 (Effron).

[168] Id.

[169] Walmart Brief at 2.

evaluate ways to simplify rates, which may include requiring the utility to file a base distribution rate case.

AEP Ohio also discusses the qualitative reliability benefits that the Distribution Investment Rider provides. The utility alleges that the reliability benefits would likely be delivered sooner than would be the case if a traditional rate base distribution case was used to collect the investments.[170] But, the fact remains that two years into the DIR program, AEP Ohio has not yet provided evidence that the existing unexpanded (and considerably less expensive) DIR has in fact improved service reliability.

The qualitative benefits that AEP Ohio alleges do not tip the scale toward adopting an ESP instead of an MRO. These benefits are illusory at best or outweighed by the quantitative and significant costs. The PUCO should decline to use qualitative factors to reduce or cancel out more objective quantitative analysis. Doing so is unreasonable and may be unlawful as well.

2. The cost to customers of the ESP is $240 million, which does not even include the additional $116 million cost of the PPA Rider.

AEP Ohio argues that OCC Witness Kahal's $240 million cost to customers is overstated because Witness Kahal included as a cost the net change ($1.83/MWh) for the distribution investment rider. The Utility claims that for purposes of the MRO test, the revenue requirements associated with incremental distribution investments are considered to be the same whether they are collected through an ESP or through a distribution rate case conducted with an MRO.[171] AEP Ohio cites to the PUCO's decision in

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[170] AEP Ohio Brief at 141.

[171] Id. at 144-145.

FirstEnergy's ESP case, Case No. 12-1230-EL-SSO.[172] But AEP Ohio's arguments that rely solely on the PUCO's decision in *FirstEnergy* are misplaced.

In *FirstEnergy,* the PUCO sided with its Staff in concluding that that the distribution rider and a distribution rate case would achieve the same result. This conclusion was based in part on testimony by Company Witness Ridmann, who presented an analysis showing that it would recover a like amount of distribution-related investments through a traditional rate case.[173] The PUCO called it a "wash," which came directly from Staff Witness Fortney's description of his analysis of the ESP v. MRO test. But, when Mr. Fortney's testimony is examined it is clear that he explicitly considered his conclusion based on a "long run" analysis,[174] which is inconsistent with the statutory mandate under R.C. 4928.143(C). Under R.C. 4928.143(C), the analysis is focused on the term of the ESP,[175] not some infinite long term period, during which the utility may seek a distribution rate case. Thus, the underlying basis of the PUCO's decision in *FirstEnergy* was unlawful, and should not be followed here.

Additionally, to believe that a wash will in fact occur because the utility can seek to collect the distribution investment through a base rate proceeding is purely speculative and unrealistic. A distribution rate case would afford all parties and the PUCO an opportunity to extensively review any rate increase request, including inquiries in discovery, the consideration of expert testimony, and the presentation of argument by all affected persons to ensure that the resulting distribution rates approved by the PUCO are

[172] *FirstEnergy*, Case No. 12-1230-EL-SSO, Opinion and Order at 55 (July 18, 2012).

[173] AEP Ohio has not come forward with such information in this case, which distinguishes it from the *FirstEnergy* case.

[174] See *In re: FirstEnergy*, Case No. 12-1230-EL-SSO, Opinion and Order at 55 (July 18, 2012).

[175] Deferrals however, approved under an ESP must be considered, if approved as part of the ESP. See R.C. 4928.143(C).

just and reasonable. In the past, such a deliberative process has most often led to an eventual reduction of a Utility's original rate increase request with the decision being rendered nine to twelve months after the application is filed.

For example, this deliberative process in the last AEP Ohio distribution rate case considered an application filed in January of 2011 and resulted in a PUCO order in December 2011. In AEP Ohio's distribution rate case (the first in two decades) it requested $96.3 million in total (Ohio Power, Columbus Southern Power) annual rate increases. [176] The PUCO issued an order, based on the settlement, in which it approved *a zero base distribution rate increase.*[177] This vividly illustrates the fact that although rate requests may be filed, the outcome is not guaranteed.

While Ohio Power could certainly request a $240 million distribution rate increase, there is no evidence or guarantee that the PUCO would award such an increase request. Even if the PUCO were to approve an increase in the Utility's distribution rates at that time, there is no indication that the PUCO would award an increase of $240 million over three years. Consequently, including a prediction of the amount, if any, of a distribution rate increase that Ohio Power would obtain in a potential future PUCO proceeding is speculative at best, and should be removed from the ESP/MRO analysis.

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[176] See *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company, Individually and, if Their Proposed Merger is Approved, as a Merged Company (collectively, AEP Ohio) for an Increase in Electric Distribution Rates,* Case No. 11-351-EL-AIR, Application, Schedule A-1 (Feb. 28, 2011).

[177] Id., Opinion and Order (Dec. 14, 2011).

3. The Utility's Proposed Residential Distribution Credit Is Not a Quantifiable Benefit to Customers. Additionally, the extended DIR proposed could allow the Utility to double-recover distribution costs from customers.

The only quantifiable benefit that AEP Ohio Witness Allen could identify for the ESP is AEP Ohio's Proposed Continuation of the Residential Distribution Credit Rider ("DCR" or "Credit").[178] Witness Allen testified that as part of the ESP III, AEP Ohio is voluntarily extending the Credit through May 31, 2018.[179] Otherwise the Credit is currently scheduled to expire May 31, 2015.[180] This rate Credit will reduce residential customer bills by $14.688 million per year.[181] Thus, according to Mr. Allen, the benefit of the Credit will amount to $44 million over the ESP term or $29 million if AEP Ohio exercises its unilateral right to terminate the ESP after two years.[182]

OCC Witness Kahal concluded that the DCR is not a new benefit of the ESP III.[183] Mr. Kahal came to this conclusion after reviewing the origin of the Residential DCR and analyzing its purpose. OCC Witness Kahal testified that the Credit was established to fully offset the $46.7 million rate increase authorized in AEP Ohio's last distribution rate case.[184] The DCR rate credit protected customers from the potential that AEP Ohio would over-collect its distribution investments through distribution rates and

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[178] See OCC Ex. 13 at 20, citing to AEP Ohio Response to OCC Interrogatory No. 3-25 (Kahal).

[179] AEP Ohio Ex. 7 at 4 (Allen Direct).

[180] OCC Ex. 13 at 19 (Kahal).

[181] Id. (Kahal).

[182] Id. at 19-20 (Kahal).

[183] Id. at 28 (Kahal).

[184] OCC Ex. 13 at 27 (Kahal); *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company, Individually and if Their Proposed Merger is Approved, as a Merged Company (collectively, AEP Ohio) for an Increase in Electric Distribution Rates*, Case No. 11-351-EL-AIR, Opinion and Order (Dec. 14, 2011) (adopting Stipulation with DIR revenue credit); Stipulation and Recommendation at 6-7 (Nov. 23, 2011).

the distribution investment rider.[185] The potential for AEP Ohio to over-collect from customers existed due to the combination of charges from the distribution rate case and the DIR mechanism from the ESP at that time.[186] That potential exists now to a greater extent because AEP Ohio has proposed an expanded DIR that is nearly double the size of the prior DIR.

In its initial brief AEP Ohio summarily dismisses Mr. Kahal's concern that there will be excess revenue collections under the DIR during the ESP III.[187] But the fact remains that a static credit for the ESP term ($14 million per year) will be applied to a offset a much larger DIR investment—one that is expanded to nearly double the magnitude of the prior DIR program. And without a base rate proceeding to sort out what distribution investment is being collected through existing base rates vs. what is being collected through the expanded DIR, there is a real potential that the Utility is double-recovering. Indeed, if the expanded DIR is approved, a distribution rate case would be essential to ensure against double recovery.

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[185] See, e.g., *In the Matter of the Application of the Columbus Southern Power Company and Ohio Power Company, Individually and, if Their Proposed Merger is Approved, as a Merged Company (collectively, AEP Ohio for an Increase in Electric Distribution Rates*, Case No. 11-351-EL-AIR, Opinion and Order at 10 (Dec. 14, 2011) (acknowledging that the credit eliminates any potential for double recovery).

[186] OCC Ex. 13 at 27 (Kahal).

[187] AEP Ohio Brief at 144.

E. Distribution-Related Issues

1. The Utility has not demonstrated that customers will benefit from its proposal to continue and expand the Distribution Infrastructure Rider. The PUCO should reject the proposal, or in the alternative, not increase the DIR or expand it to include general plant.

OCC opposed continuing and almost doubling the DIR from $365.7 million[188] to $660.1 million.[189] OCC also opposed the expanding the DIR by $32.1 million[190] to cover general plant.[191] OCC argued that even if the PUCO were to continue any aspect of the DIR, then it should modify the property tax calculation.[192]

OCC's position was based on the testimony of OCC Witnesses Effron and Williams. OCC argued that the DIR would increase rates to customers, which would be especially hard on low-income customers.[193] The OCC also argued that AEP Ohio has failed to quantify the service reliability improvement that customers would experience attributable to the DIR since its inception, thus violating one of the PUCO's requirements for the DIR program.[194] OCC pointed out that the record in this case lacks an indication of how service reliability will be improved by the DIR program. Indeed, AEP Ohio has not demonstrated that the existing DIR program has accomplished its goals of providing reliability benefits for customers. There is no record that supports doubling the DIR spending. Customers should not be expected to pay these charges.

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[188] OCC Ex. 11 at 29 (Williams).

[189] AEP Ohio Ex.4 at 16, Table 1 (Dias) [$241.9 + $214.8 + $235.5 = $692.2 less general plant of $32.1 = $660.1].

[190] AEP Ohio Ex. 4 at 16, Table 1 (Dias).

[191] OCC Brief at 85. No party supported AEP Ohio proposal to expand the DIR to include general plant.

[192] OCC Brief at 90.

[193] OCC Brief at 36.

[194] OCC Brief at 81, See also Case No. 11-346-EL-SSO, Opinion and Order at 46.

Other than the PUCO Staff, all parties that addressed the DIR opposed it.[195] OMAEG, OPAE, APJN, and Kroger all argued that the Utility should not be allowed to use single-issue ratemaking to fund its infrastructure needs. These parties pointed out that using a distribution rate case process more fairly balances the needs of customers with those of the Utility.[196] All of those parties also echoed OCC's concern with the doubling of DIR spending in only three years.[197]

The PUCO itself had raised a similar concern with the DIR in AEP Ohio's first ESP case in Case No. 08-917-El-SSO. In that case, the PUCO rejected the DIR proposal noting that, "while SB 221 may have allowed companies to include such provisions in its ESP, the intent could not have been to provide a blank check to the utilities."[198] By permitting the DIR to almost double in size after only three years, without the required service reliability improvement quantifications, the PUCO would be essentially providing AEP Ohio with a "blank" check of over a half a billion dollars.

In its Brief, AEP Ohio argued that the DIR needs to continue, double in size, and expand as part of its long-term strategy with multiple activities on multiple fronts.[199] AEP Ohio argued that the DIR was reasonable and permissible under the statute.[200] Finally, AEP Ohio alleged that the expansion of the DIR to include general plant is needed.[201]

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[195] OMAEG Brief at 6-10, OPAE and APJN Brief at 31-38, Kroger Brief at 4-6.

[196] OMAEG Brief at 7-8, OPAE and APJN Brief at 31, Kroger Brief at 4-5.

[197] OMAEG Brief at 8, OPAE and APJN Brief at 33, Kroger Brief at 4-5.

[198] *In re AEP-Ohio*, Case No. 08-917-EL-SSO, Opinion and Order at 32 (March 18, 2009).

[199] AEP Ohio Brief at 73.

[200] AEP Ohio Brief at 73-77.

[201] AEP Ohio Brief at 7-78.

a. Continuation and doubling of the DIR program will impose significant costs on customers and is not reasonable.

AEP Ohio takes the approach in this case that the Utility cannot be proactive in replacing aging infrastructure without the DIR program.[202] The Utility cites the PUCO Order in the 11-346 ESP case for this same argument.[203] However, this claim distorts what the PUCO said about the DIR when it approved the program. The PUCO stated that

> it is detrimental to the state's economy to require the utility to 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 costs.[204]

Although the PUCO did encourage proactive and efficient replacement of aging infrastructure, the PUCO did not say that distribution infrastructure investment should and could only occur as part of an ESP case. Nor did it rule that distribution infrastructure investment could not be addressed in a distribution rate case.

AEP Ohio's argument misinterprets the PUCO Order to support the claim that without the DIR program the Utility is somehow unable to proactively address the issue of aging infrastructure. That claim is wrong. There is nothing in the distribution rate case process that precludes any utility from addressing the issue of aging infrastructure. The only difference is that using the DIR Rider instead of a distribution rate case accelerates the Utility's ability to charge customers. In addition, the DIR program isolates DIR investment from all of the Utility's other expenses and revenues. This prevents a complete evaluation of all of the Utility's finances.

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[202] AEP Ohio Brief at 75.

[203] AEP Ohio Brief at 75.

[204] Case No. 11-346-EL-SSO, Opinion and Order at 47.

The Utility argued that if it had to charge customers for infrastructure costs through a distribution rate case instead of the DIR Rider, service reliability would decrease.[205] However, in making this allegation, the Utility offered no supporting documentation or analysis, and more importantly was not able to offer a timeline over which any such alleged deterioration would occur.[206] Moreover, in response to OCC INT No. 13-310, AEP Ohio did not indicate that service reliability would decline if the DIR is not continued.[207] This claim was only made during cross-examination of AEP Ohio Witness Dias.[208]

The Utility, however, needs to do more than broadly claim that it cannot provide reliable service if it does not get the DIR approved. The Utility has to prove its claim, and to that end the Utility has the burden of supporting its claims with data and documentation. The Ohio Supreme Court addressed this matter recently clarifying the utility burden of proof in a case involving an electric utility Rider, by concluding that the utility in that case (Duke Energy Ohio) had the burden of demonstrating that the costs were prudently incurred and reasonable:

> so **Duke had to prove a positive point**: that its expenses had been prudently incurred. The commission did not have to find the negative: that the expenses were imprudent. Accordingly, if the evidence was inconclusive or questionable, the commission could justifiably reduce or disallow cost recovery.[209]

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[205] Tr. II at 319 (Dias).

[206] Tr. II at 320 (Dias).

[207] OCC Ex. 11 at JDW-14 (Williams).

[208] Tr. II at 319 (Dias).

[209] *In re Duke Energy Ohio, Inc., to Establish and Adjust the Initial Level of its Distribution Reliability Rider*, 131 Ohio St.3d 487,488, 2012-Ohio-1509, 967 N.E.2d 201, 2012 Ohio Lexis 849 (2012). (Emphasis added).

The Court has further clarified the type of evidence necessary to meet its burden of proof in a PUCO railroad case where the Court held that:

> We are also of the opinion that mere expressions of judgment by witnesses, testifying as experts, that freight rates are reasonable, do not have such probative value as to outweigh established, concrete facts inconsistent with such expressions of judgment.[210]

In this case, there is no documentation in the form of any analysis to support the claim that service reliability would deteriorate without the DIR.[211] Even that claim is suspect because the witness was not able to identify over what period of time any such alleged service reliability deterioration might occur.[212] In addition, there is no analysis or documentation in the record to support claims that prior to the implementation of the DIR, the Utility's was in need of additional monies beyond what was obtainable through distribution base rate cases to improve and maintain service reliability.[213] The PUCO approved the DIR program in order to achieve improvements in service reliability.[214] Despite this objective, there is no documentation in the record -- the Utility did not quantify the service reliability improvements -- that AEP Ohio achieved the promised service reliability improvements.

AEP Ohio also seems to be making the argument that OCC and other parties argued that the Utility cannot address the aging infrastructure issue unless and until performance standards decline.[215] Again this position mischaracterizes the arguments

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[210] *Hocking Valley R. Co. v. Public Utilities Comm*., 117 Ohio St. 304, 309, 158 N.E. 648, 1927 Ohio lexis 237, 5 Ohio L. Abs. 700 (1927).

[211] Tr. II at 319 (Dias).

[212] Tr. II at 320 (Dias).

[213] Tr. II at 320 (Dias).

[214] Case No. 11-346-EL-SSO, Opinion and Order at 46.

[215] AEP Ohio Brief at 73-75.

made by the parties in the case that oppose the DIR program. OCC did not take the position that infrastructure should not be replaced until performance standards decline. Rather, OCC and other parties took the position that infrastructure issues that are tied to service reliability could be addressed through distribution rate cases. In addition, Kroger noted that the Utility DIR proposal included continuous increases and expansion of the DIR and the use of more new riders.[216] Kroger recognized that utilities need to be able to properly maintain the distribution system, and to properly staff its workforce. However, Kroger noted that the use of the DIR and other Rider is not the best way to collect these charges form customers.[217] Instead the more balanced approach of charging customers the costs of distribution infrastructure is in a distribution rate case, where all revenue and cost issues are examined.

OMAEG noted that the Utility did not support its claims of service reliability deterioration with any analysis and thus that any additional DIR investment without sufficient documentation supporting alleged benefits was not a prudent investment.[218] OCC agrees.

The Utility's DIR proposal in this case would increase the cost of the program from $365.7 million during the last ESP period to $660.1 million in this time period.[219] This estimate does not include projections of an additional $215.3 million for 2018. [220] These dollar amounts far and away eclipse the magnitude of the original DIR program and should give the PUCO cause to re-evaluate the programs.

[216] Kroger Brief at 5-6.

[217] Kroger Brief at 6.

[218] OMAEG Brief at 10.

[219] OCC Brief at 80.

[220] OCC Brief at 80.

In this proceeding, AEP Ohio did not quantify the service reliability improvements from the prior level of DIR spending. In addition, the Utility provided no documentation or analysis demonstrating that the almost doubling the magnitude of the DIR program spending would provide customers with a similar significant increase in service reliability. In fact, AEP Ohio concedes that there is no assurance of any service reliability improvements from the DIR when it states, "The DIR provides a streamlined approach to recovery of costs associated with distribution investments, which will encourage **investments that can improve reliability**."[221] It is noteworthy that the Utility did not say that the DIR investment would improve reliability and again there was no quantification offered for this hoped for improvement.

Even if the PUCO were to conclude that the original DIR program should continue, the increase in the magnitude of the program over the prior amount is also unsupported. AEP Ohio relies on its customer surveys to argue that the Utility and customers interests are aligned, as the statute (R.C. 4918.143(B)(2)(d)) requires.[222] However, there is nothing in the customers' surveys that suggests customers want (or are willing) to pay double for an unquantified level of improvement for reliability. While customers would obviously prefer to reduce power outages, this should not be construed as some widespread endorsement that customers support giving more of their hard earned money to AEP Ohio. There must be some balance between the cost of electric service and the reliability of that service.

[221] AEP Ohio Brief at 78. (Emphasis added).

[222] AEP Ohio Brief at 78-79.

The Utility's argument fails to address any of the serious affordability issues that were raised in the Testimony of OCC witness Williams.[223] Under the current rates, AEP Ohio charges its customer electric bills that are already 19.5 percent higher than the statewide average electric bill.[224] In addition, 21.8 percent of AEP Ohio customers are at-risk[225] of losing service. Under these circumstances customers can ill afford the gargantuan DIR program spending increases proposed in this proceeding.

Finally, AEP Ohio argues that the proposed DIR program is supported by the statute and thus should be approved.[226] Again, in making this argument, AEP Ohio overstates the statutory support for its position. Although RC 4928.143(B)(2)(h) does allow a DIR program, the statute does NOT make such a program mandatory. Rather as AEP Ohio states, "the Commission **may** include in an ESP" provisions "regarding distribution infrastructure and modernization incentives" [227] In addition to being discretionary, the statute (R.C. 4928.143(B)(2)(d)) requires the PUCO to determine that the customers' and the utility's expectations are aligned regarding service reliability. Only after determining that those expectations are aligned should the PUCO allow distribution charges in the ESP.

AEP Ohio argues that it met the requirements of the statute because its survey results show that customers' and the Utility's interests are aligned. However, as noted above, AEP Ohio's reliance on the customer survey to show that its interests and those of customers are not aligned regarding the costs associated with service reliability because

[223] OCC Ex. 11 at 10-19 (Williams).

[224] OCC Ex. 11 at 14 (Williams).

[225] OCC Ex. 11 at 19 (Williams).

[226] AEP Ohio Brief at 76.

[227] AEP Ohio Brief at 76 (Emphasis added).

of the bias in its customer survey. The Utility is relying on customer surveys that were not designed to elicit a customer response or reaction to the impact that the price of that alleged service reliability on customer's views and interests. Asking a customer their views on service reliability while ignoring a price component is almost guaranteed to produce the type of results that the Utility achieved -- where the majority of customers expect service reliability to remain about the same.[228] Those results do not support continuation of the DIR, let alone doubling its size.

b. The PUCO should not expand the DIR to include general plant and increase charges to customers.

In addition to almost doubling the size of the DIR, AEP Ohio also proposed that the DIR be expanded by another $32 million[229] to include general plant. All of the intervenor parties to the case, including the PUCO Staff, unanimously opposed this expansion. Whereas, the statute does permit a Rider mechanism to address "distribution infrastructure and modernization incentives," the statue does not speak to general plant additions.[230] The Utility's own action confirms this inasmuch as AEP Ohio cites to the statute in support of the general DIR program, but does not mention the statute in discussing general plant inclusion.[231] That is because R.C. 4928.143(B)(2) does not include general plant investment as a provision that is permitted under an ESP.

OCC's Witness argued that the general plant proposed to be included in the DIR expansion was not appropriate for inclusion because it was by definition not

[228] AEP Ohio Ex.4 at 5, Exhibit SJD-1(Dias).

[229] AEP Ohio Ex. 4 at 16, Table 1 (Dias).

[230] R.C. 4928.143(B)(2)(h).

[231] AEP Ohio Brief at 75-76.

infrastructure.[232] PUCO Staff recommended that the PUCO should reaffirm that "DIR spending should be focused on those components that will best improve or maintain reliability."[233] The PUCO Staff concluded that general plant expenses support maintaining reliability but does not directly relate to it.[234] The PUCO Staff Witness emphasized that the radio system (which is the largest component of the general plant) would be used for a multitude of purposes, many of which are not directly related to reliability.[235] Moreover, PUCO Staff noted that the AEP Ohio witness agreed that under the Utility's interpretation virtually all expenses that support distribution functions could be recovered through the DIR.[236] This view contradicts the intent of the statute, which limits distribution provisions in an ESP to infrastructure and modernization incentives.

AEP Ohio argued that general plant should be included in the DIR because the Staff might have supported inclusion of certain investments categorized as general plant (the radio system) in the DIR if they had been fully reviewed by the PUCO Staff.[237] Essentially the Utility argument is based on what might have happened under different circumstances. That argument ignores the fact that in the circumstances present in this case, the PUCO Staff recommended that general plant (including the radio system) should not be included in the DIR.[238] Regardless of what the PUCO Staff may have recommended at a another time under different circumstances, the fact is that under the

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[232] OCC Ex. 18 at 14 (Effron).

[233] PUCO Staff Brief at 45.

[234] PUCO Staff Brief at 45.

[235] Staff Brief at 45-46.

[236] Staff Brief at 46 citing Tr. II at 437-438 (Dias).

[237] AEP Ohio Brief at 82, citing Tr. IX at 2295.

[238] Tr. IX at 2292 (McCarter).

circumstances presented in this case, the PUCO Staff concluded that it was inappropriate to expand the DIR to include general plant.

AEP Ohio pledged in Brief that it would continue to work with Staff and any outside auditor to ensure that any necessary data is provided to ensure a transparent understanding of the DIR spending.[239] This pledge is nothing more than an acknowledgement that the Utility will do what it is has been required to do in the past. The more serious issue is that the pledge does not address is how the Utility will show a quantifiable benefit to customers by improved service reliability.

c. If the PUCO approves the DIR program, the property tax calculation should be modified to protect customers.

OCC Witness Effron proposed a property tax modification to the DIR if the PUCO determines that the DIR program should continue.[240] Mr. Effron noted that a modification of the depreciation reserve used to calculate property taxes was necessary to eliminate the cumulative amortization if the excess depreciation reserve and the net plant to which the property tax is applied.[241] The PUCO Staff agreed with the OCC-proposed modification.[242]

AEP Ohio argued on Brief that neither the OCC nor Staff witness determined if the property tax rate had increased since 2011.[243] Although AEP Ohio raised this concern, the Utility offered no proof -- either in cross-examination of OCC Witness

[239] AEP Ohio Brief at 82.

[240] OCC Ex. 18 at 11(Effron).

[241] OCC Ex. 18 at 11 (Effron).

[242] PUCO Staff Ex. 18 at 4-5 (McCarter).

[243] AEP Brief at 83.

Effron or PUCO Staff Witness McCarter, or in any rebuttal presentation -- that the property tax rate had in fact increased since 2011.

In addition, although the Utility is implying that Mr. Effron did not look back into the existing tax rates to make his determination about AEP Ohio's plant and changes in policies when the Utility cross-examined the OCC Witness, the cross-examination was asking about the effect of changes in capitalization policy and not the property tax modification.[244] Thus the question and answer was regarding a separate and completely unrelated issue.

Moreover, AEP Ohio's argument against the Staff position suggests that the DIR should cover changes in the property tax rate, as well as the effect of plant additions. When making this suggestion, AEP Ohio offered no justification for this position. In addition, there is no basis for including tax changes as part of infrastructure facilities that are the subject of R.C. 4928.143(B)(2)(d).

If the PUCO approves the DIR then it should modify the tax rate as recommended by OCC and the PUCO Staff.

2. AEP Ohio did not demonstrate a need to charge customers for the unlawful Sustained and Skilled Workforce Rider. The PUCO should protect customers from the negative impacts of this unsupported Rider by rejecting the Sustained and Skilled Workforce Rider.

OCC argued that the PUCO should reject the $14.2 million[245] SSWR because AEP Ohio did not demonstrate the need to charge customers for it. Also, the proposed SSWR is not a proper charge under R.C. 4928.143(B)(2).[246] The PUCO Staff also

[244] Tr. XII at 2747 (Effron).

[245] AEP Ohio Ex.4 at 27 at Table 5 (Dias).

[246] OCC Brief at 101-102.

opposed the inclusion of the SSWR in an ESP proceeding.[247] Instead, Staff recommended that the issue be addressed in a distribution rate case.[248] The Staff also agreed with OCC Witness Effron[249] that the retirement of employees could offset the costs of new employees. That means the result could be no actual increase in the total number of employees or actual labor expense.[250] And that means customers should not be paying AEP Ohio more money for, in essence, nothing.

OPAE and the APJN also opposed the SSWR, noting that the SSWR does not meet the criteria for costs that should be charged to customers through a rider,[251] and that the costs are more appropriately reviewed as part of a distribution rate case.[252] In addition, OMAEG also opposed the SSWR because AEP Ohio has the alternative of using a distribution rate case to charge customers for these costs. Using a distribution rate case to charge these costs to customers is a luxury that other businesses -- like the members of OMAEG -- do not have.[253]

Although AEP Ohio agreed that any SSWR-related costs and customer charges could be recovered in a distribution rate case, the Utility argued that the SSWR was needed as a part of an overall long-term service reliability plan.[254] AEP Ohio also argues that the Legislature allowed recovery of SSWR-related costs in an ESP proceeding.

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[247] Staff Brief at 27.

[248] Staff Brief at 27, see also Staff Ex. 8 at 4 (Willis).

[249] OCC Ex. 18 at 22 (Effron).

[250] Staff Brief at 27-28.

[251] OPAE and APJN Brief at 37.

[252] OPAE and APJN Brief at 37.

[253] OMA Brief at 19.

[254] AEP Ohio Brief at 99.

But, the Utility identified no specific section of the law that would allow such a charge. Instead, a review of the statute indicates that it protects customers from such payments as SSWR charges. For example, SSWR charges are not costs related to fuel used to generate electricity, not the cost of purchased power, and not the costs associated with emission allowances or federally mandated carbon or energy taxes.[255] In addition, SSWR are not construction work in progress costs involved with   construction of a generation facility.[256] They are not costs associated with the establishment of a non-bypassable surcharge for the life of an electric generating facility that is owned or operated by the electric distribution utility,[257] or charges relating to limitations on customer shopping for retail electric generation service, bypassability, standby, back-up, or supplemental power service.[258]

Moreover, these costs are not related to automatic increases or decreases in any component of the SSO price,[259] or associated with carrying costs of the utility's cost of securitization.[260] SSWR costs are not related to transmission, ancillary, congestion, or any related service required for the standard service offer,[261] or provisions regarding the Utility's distribution service.[262] Finally, the costs have nothing to do with economic development.[263]

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[255] R.C. 4928.143(B)(2)(a).

[256] R.C. 4928.143(B)(2)(b).

[257] R.C. 4928.143(B)(2)(c).

[258] R.C. 4928.143(B)(2)(d).

[259] R.C. 4928.143(B)(2)(e).

[260] R.C. 4928.143(B)(2)(f).

[261] R.C. 4928.143(B)(2)(g).

[262] R.C. 4928.143(B)(2)(h).

[263] R.C. 4928.143(B)(2)(i).

The Ohio Supreme Court has previously ruled that costs not listed under R.C. 4928.143 are not appropriate for charging to customers in an ESP case:

> In its sixth proposition of law, OCC argues that R.C. 4928.143(B)(2) does not permit AEP to recover certain carrying costs associated with environmental investments. That section states, "the [electric security] plan may provide for or include, without limitations, any of the following," and then lists nine categories of cost recovery. OCC argues that this section permits plans to only include *only listed* items; the commission and AEP argue that B(2) permits unlisted items. We agree with OCC. [264]

AEP Ohio argues that the SSWR is needed as a part of an overall long-term service reliability plan.[265] In addition to the lack of statutory support in R.C. 4928.143, there is no precedent for such a rider in Ohio. The only other utility to even propose such a rider was Vectren Energy of Ohio ("Vectren").[266] In the Vectren case, the PUCO Staff took the position that the costs associated with the hiring of new employees to address the issue of an aging workforce "should be subject to normal regulation practices for test year expenses."[267] In other words any increase in expenses associated with the hiring or training of additional employees would be offset against other increases or decreases in other expenses or revenues. The case was settled without including the rider.[268] AEP Ohio did not demonstrate that a distribution rate case using normal regulation and the test year standard could not address any need for new or replacement employees.

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[264] *In Re Application of Columbus Southern Power Company et al.*, 128 Ohio St.3d 512,519, 520 (2011).

[265] AEP Ohio Brief at 99.

[266] *In the Matter of Vectren Energy of Ohio Inc.*, Case No. 07-1080-GA-AIR.

[267] *In the Matter of Vectren Energy of Ohio Inc.*, Case No. 07-1080-GA-AIR, Staff Report at 10 (June 6, 2008).

[268] *In the Matter of Vectren Energy of Ohio Inc.*, Case No. 07-1080-GA-AIR, Opinion and Order at 3-5 (January 7, 2009).

SSWR costs are not authorized by the law. And a distribution rate case is available for the Utility to propose such charges to customers. The PUCO should reject the SSWR proposal in this case.

3. AEP Ohio did not demonstrate a need for the rider to charge customers for NERC and Cybersecurity costs that the Utility might not ever incur. The PUCO should protect customers from the unsupported and completely speculative NERC and Cybersecurity cost rider by rejecting the rider.

OCC argued that the North American Electric Reliability Corporation ("NERC") and Cybersecurity Rider was not a proper charge under the law. This is because NERC and Cybersecurity costs are not one of the items listed for recovery under R.C. 4928.143(B)(2), and the Ohio Supreme Court has ruled that utility's ESP is limited to provisions explicitly set forth under RC. 4928.143(B)(2). [269] The PUCO Staff agreed that the NERC and Cybersecurity Rider was not an appropriate charge for this case, but for other reasons.

The PUCO Staff opposed the riders because of the magnitude of the uncertainty associated with those charges.[270] PUCO Staff argued that AEP Ohio did not demonstrate that it would incur NERC and Cybersecurity compliance charges because the NERC did not have the authority to establish standards for distribution companies, like AEP Ohio.[271] The PUCO Staff also argued that there was too much uncertainty associated with any

[269] OCC Brief at 104.

[270] Staff Brief at 29.

[271] Staff Brief at 29.

future NERC and Cybersecurity costs to approve a rider in this proceeding.[272] OPAE and APJN also argued that the NERC and Cybersecurity Rider is premature at this time.[273]

In addition, OMAEG noted that AEP Ohio admitted that the NERC and Cybersecurity costs are anticipatory in nature, and should not be approved for recovery unless or until the alleged "significant future increases" in costs that the Utility predicted actually come to fruition.[274] OMAEG noted that by waiting to approve a charge until there are actual NERC and Cybersecurity charges, the PUCO can ensure that customers will not pay for any costs that might not need to be incurred by the Utility.[275] AEP Ohio argued that the NERC and Cybersecurity Rider was a necessary placeholder to enable the Utility to charge customers for NERC and Cybersecurity costs in the future.[276]

On one hand AEP Ohio argued that NERC and Cybersecurity costs could not be absorbed within existing budgets.[277] Yet at the same time, AEP Ohio did not provide any quantification or estimation of the type and magnitude of the potential charges.[278] Thus AEP Ohio is arguing that costs that are unknown cannot be absorbed into existing budgets. Because the costs are unknown, it is impossible to say that they cannot be absorbed into existing budgets. This is especially true in light of the fact that it is not clear that AEP Ohio as a distribution utility will have to even comply with the NERC

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[272] Staff Brief at 29.

[273] OPAE and APJN Brief at 38.

[274] OMAEG Brief at 20.

[275] OMAEG Brief at 20-21.

[276] AEP Ohio Brief at 102.

[277] AEP Ex. 2 at 17-18 (Vegas).

[278] Tr. VI at 1423 (Pearce).

standards.[279] As a result, the Staff rejected the Utility proposal.[280] AEP Ohio argued that the PUCO should approve the NERC and Cybersecurity Rider because the PUCO Staff Witness noted that the Staff would not oppose NERC compliance charges.[281]

But AEP Ohio's claim of PUCO Staff support is overstated. The PUCO Staff Witness stated that the Staff did not "desire AEP or any company to be in a position of noncompliance with regards to NERC, especially NERC SIP."[282] This is not the ringing endorsement that the Utility is alleging. Rather it indicates that Staff did not want the Utility to be noncompliant.[283] But because the NERC requirements have not yet been established, the concern over noncompliance is overstated and premature.

AEP Ohio also argued that because the PUCO has approved other Riders at an initial level of $0.00, there is precedent for the approval of the NERC and Cybersecurity Rider at $0.00.[284] AEP Ohio pointed to the Generation Resource Rider ("GRR") as an example of such precedent.[285] However, that example is easily distinguished because of the level of uncertainty surrounding the NERC and Cybersecurity Rider components. As the PUCO Staff witness noted not only was there no cost estimate in the record, but there was no firm standard in place that AEP Ohio had to comply.[286] Thus, with the NERC and Cybersecurity Rider, AEP Ohio is asking for a Rider to collect unknown costs from customers associated with an unknown standard that may or may not be applicable to the

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[279] Staff Brief at 29.

[280] Staff Ex. 11 at 4-5.

[281] AEP Ohio Brief at 103; Tr. VI at 1424 (Pearce).

[282] Tr. VI at 1424 (Pearce).

[283] Tr. VI at 1423, 1425 (Pearce).

[284] AEP Ohio Brief at 103.

[285] AEP Ohio Brief at 103.

[286] Tr. VI at 1432 (Pearce).

Utility at some unknown time in the future. In contrast the GRR Rider costs, although not incurred at the time when the GRR Rider was approved, were at least known as far as to the type of costs that would be included and when they might be incurred.[287]

AEP Ohio is best positioned to estimate the NERC and Cybersecurity costs that would be charged to customers in the Rider. Yet despite bearing the burden of proof in this case, the Utility provided no cost quantification or estimate. As a result of AEP Ohio's unwillingness or inability to quantify or even estimate the NERC and Cybersecurity costs, the PUCO should reject the Rider. Failing to quantify or estimate any costs associated with the NERC and Cybersecurity costs enables the Utility to "game the system" by setting up future charges for customers while at the same time precluding all of the parties and the PUCO from fully evaluating all aspects of the proposed Rider before it is approved.

Moreover, as a matter of policy, the PUCO should be concerned with creating even more Riders, especially in light of the significant number of riders that already burden customers.[288] Creating more Riders with associated higher costs would further exacerbate the unaffordability of electric rates that are the highest in the State.[289] This would impede the PUCO from carrying out the policy of R.C. 4928.02(A) -- ensuring that reasonably priced electric service is made available to customers in Ohio.

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[287] Case No. 11-346-EL-SSO, Opinion and Order at 20, where the PUCO noted that the GRR would be used to recover costs associated with the Turing Point facility. The PUCO also noted that AEP Ohio provided an estimate for the revenue requirement for the facility. Such an estimate is missing with regards to NERC and Cybersecurity costs.

[288] Kroger brief at 6, Walmart and Sam Club Brief at 2.

[289] OCC Ex. 11 at 4-7 (Williams).

Although the PUCO has noted that it is not unprecedented for it to adopt a mechanism, with a rate of zero as part of an ESP,[290] those instances can be distinguished from this case. The Duke[291] and FirstEnergy[292] cases cited were both stipulated cases,[293] whereas this case has been litigated. Because those cases were stipulated, they cannot serve as precedent for this case because of language in the Stipulations that expressly prohibits using the Stipulation provisions as precedent in other cases.[294]

Because of the uncertainty regarding the NERC and Cybersecurity costs, and the availability of a distribution rate case when, and if, those costs are actually incurred, the PUCO should reject AEP Ohio's proposal for a NERC and Cybersecurity Rider.

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[290] Case No. 11-346 Opinion and Order at 24-25.

[291] *In re Duke Energy-Ohio*, Case No. 08-921-EL-SSO, Opinion and Order (December 17, 2008).

[292] *In re FirstEnergy*, Case No. 08-935-El-SSO, Opinion and Order (March 25, 2009).

[293] *In re Duke Energy-Ohio*, Case No. 08-902-EL-SSO, Stipulation (October 27, 2008), Stipulation Addendum (October 27, 208), Letter Supporting Stipulation (November 10, 2008), Letter Supporting Stipulation (November 19, 2008); *In re FirstEnergy*, Case No. 08-935-EL-SSO, Stipulation (February 19, 2009).

[294] *In the Matter of the Commission's Investigation Into the Modification of Intrastate Access Charges; In the Matter of the Application of United Telephone Company of Ohio d/b/a Sprint for Authority to File and Make Effective Revised Tariff Sheets to its General Exchange Service Tariff, P.U.C.O. No. 5, to Establish a Late Payment Charge*, Case No. 00-127-TP-COI, Opinion and Order at 27 ("Moreover, a stipulation from one case cannot serve as precedent and is not binding on the Commission in a separate contested case.")(June 28, 2001); *In the Matter of the Application of Columbus Southern Power Company for Authority to Amend its Filed Tariffs to Increase the Rates and Charges for Electric Service*, Case No. 91-418-EL-AIR at 12 ("Clearly, a stipulation in a proceeding is never considered as precedent for other cases. The parties to the Dayton Power & Light stipulation specifically provided that the stipulation is not binding in any other proceeding, nor is it to be offered or relied upon in any other proceeding.") (July 2, 1992); *In the Matter of the Inclusion of Take-or-Pay Costs in the Gas Cost Recovery Clause of the Waterville Gas & Oil Company and Related Matters; In the Matter of the Inclusion of Take-or-Pay Costs in the Gas Cost Recovery Clause of The Waterville Gas Company and Related Matters*, Case No. 88-1308-GA-UNC, Opinion at 8 (June 6, 1989).

4. Under the PUCO's criteria the AEP Ohio retail market is competitive. AEP Ohio did not demonstrate a need for, or the benefits of a Purchase of Receivables (POR) Program with a Bad Debt Rider that would force customers to pay higher rates. The PUCO should protect customers by rejecting the Purchase of Receivables Program and the Bad Debt Rider that are an anticompetitive subsidy.

OCC opposed the POR and Bad Debt Rider proposed by AEP Ohio because the program does not provide customers with any quantifiable benefits, but it would cause them to bear increased costs.[295] In addition, the POR and accompanying Bad Debt Rider would require the captive customers of a regulated utility to guarantee the uncollectible costs that marketers would otherwise incur as a normal cost of doing business in an unregulated competitive marketplace.[296] That is not consistent with Ohio law that precludes subsidies.[297] Requiring all customers to pay the bad debt costs of marketers who compete in an unregulated market would be a subsidy from the regulated business to an unregulated one.

IEU-Ohio also opposed the POR and Bad Debt Rider because AEP Ohio did not demonstrate the need for, or the benefits of, either.[298] IEU-Ohio also noted that the AEP Ohio proposal violated the terms of the Duke ESP Stipulation in Case No. 11-349-EL-SSO, because the Utility was using the Duke Stipulation as precedent to support its proposal, even though such use was specifically prohibited in the Duke Stipulation.[299]

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[295] OCC Brief at 90-96.

[296] OCC Brief at 100.

[297] R.C. 4928.02(H).

[298] IEU-Ohio Brief at 45.

[299] IEU-Ohio Brief at 45, 49-50. See *also In the Matter of the Application of Duke Energy Ohio for Authority to Establish a Standard Service Offer Pursuant to Section 4928.143, Revised Code in the Form of An Electric Security Plan, Accounting Modifications and Tariffs for Generation Service*, Case No. 11-349-EL-SSO et al., Stipulation and Recommendation at 2 (October 24, 2011). See also OCC footnote 261.

a. The AEP Ohio retail electric market is competitive. Thus there is no need for the Purchase of Receivables program and a Bad Debt Rider.

In their Briefs, the marketers argued that the lack of a POR is a barrier to entry.[300] In other words, marketers argued that the AEP Ohio retail electric market was not competitive because the lack of a POR limited the number of marketers participating.[301] Despite these claims, the fact remains that the lack of a POR was not a barrier to entry for IGS, Direct Energy, and Constellation (who participate in the AEP Ohio retail market and have intervened in this case) and the other numerous marketers that currently participate in the AEP Ohio retail electric market. The record demonstrates that 69 marketers are certified, 46 marketers have more than one customer and 29 are listed on the PUCO's apples-to-apples chart.[302] Thus for all of these marketers the lack of a POR was NOT a barrier to entry. It does not even make sense that the non-availability of a customer-paid subsidy in the form of a POR is a barrier to entry in a competitive market.

Some of the marketers argued that the AEP Ohio retail electric market was not competitive because of the lack of a POR.[303] However, in making the argument, the marketers and AEP Ohio disregard the prevailing definition of effective competition, recently adopted by the PUCO in its retail market investigation. The PUCO defined effective competition as measured by certain characteristics recommended by the PUCO Staff:

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[300] RESA Brief at 5, Constellation and Exelon Brief at 20.

[301] Tr. XI at 2675 (Bennett).

[302] Tr. III at 869 (Gabbard).

[303] Tr. XI at 2682-2683 (Bennett).

1. Participation in the market by **multiple sellers** so that an individual seller is not able to influence significantly the market price of the commodity;
2. Participation in the market by **informed buyers**;
3. Lack of **substantial barriers** to supplier entry into the market;
4. Lack of substantial barriers that may discourage customers participation in the market; and
5. Sellers offering buyers a variety of CRES products.[304]

According to PUCO standards for judging effective competition, all of the characteristics needed for effective competition exist in the AEP Ohio retail electric market today, without a POR and a Bad Debt Rider. First, as noted earlier, there are multiple CRES providers participating in the market. The fact that 69 marketers have been certified to participate in the AEP Ohio retail market without the existence of a POR is proof that the lack of POR is not a barrier to entry. Also, there is no indication that any one marketer acting alone has the market power to significantly influence the commodity price of electricity. Second, there has been no claim in the record that the customers in AEP Ohio's electric retail market are not informed buyers.

Third, there has been no demonstration that there are any "substantial" barriers to entry for marketers. Marketers argued that the lack of POR is a barrier to entry, but in making this claim, it is noteworthy that no marketer filed testimony on that matter. Indeed, Witness Bennett acknowledged that there was no evidence presented in this case that differed from evidence presented in the FirstEnergy ESP case. In that case, the PUCO concluded that the lack of a POR was not a barrier to entry.[305] Without any new

[304] *In the Matter of the Commission's Investigation of Ohio's Retail Electric Service*, Case No. 12-3151-EL-COI, Finding and Order at 6, 9. ("RMI Case") (Emphasis added).

[305] *In the Matter of Ohio Edison Company, The Cleveland Electric Illuminating Company, and Toledo Edison Company for Authority to Provide for a Standard Service Offer Pursuant to Section 4928.143, Revised Code, in the Form of an Electric Security Plan*, Case No. 12-1230-EL-SSO, Opinion and Order at 40 (July 18, 2012). ("FirstEnergy ESP Case") (Emphasis added).

or different evidence presented in this case, there are no grounds for the PUCO to reach a different decision. Moreover, even assuming arguendo that the lack of POR is a factor in preventing some marketers from participating in the AEP Ohio retail market, there has been no demonstration that it is a "substantial barrier" to entry, which is part of the PUCO's criterion for determining effective competition.

b. The PUCO Staff proposed an alternative that would cost customers less while still addressing the marketer concerns.

The PUCO also noted in its Retail Market Investigation Order that no individual metric is determinative and that the collective results are merely intended to help monitor the evolution of the market.[306] When taken in their entirety, it is clear that based on the PUCO's own standards, the AEP Ohio retail electric market is competitive, and the lack of a POR is not a barrier to entry. Thus, such arguments cannot justify imposing a POR through which customers of AEP Ohio would have to underwrite marketers bad debts via a non-bypassable surcharge to captive monopoly customers.

As part of the RMI Case Staff Report, the PUCO Staff proposed that electric utilities provide marketers with the total customer payment amount, amount billed by the supplier, amount of payment allocated to the supplier, date applied, and a payment plan flag.[307] This alternative would cost customers less than a POR, and would help marketers obtain more payment information in order to deal with their bad debt issues. The PUCO adopted the Staff's proposal and ordered the electric utilities to provide this information to marketers by September 26, 2014.[308]

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[306] *RMI Case*, Finding and Order at 10.

[307] *RMI Case*, Finding and Order at 20.

[308] *RMI Case*, Finding and Order at 21-22.

Adopting the AEP Ohio proposed POR is not in the public interest especially when a solution that would cost customers less has already been adopted by the PUCO. In addition to costing customers less, this alternative better preserves the separation between unregulated prices of the market and a regulated POR solution involving charges to monopoly customers intended to subsidize service competitive entry. It is antithetical to the concept of free markets to require captive monopoly customers to subsidize such markets.

c. A Purchase of Receivables Program would benefit the marketers' bottom line at customers' expense. A POR is not needed by marketers to compete in the AEP Ohio retail electric market. Customers should not have to underwrite the Marketers' bad debts.

A review of the record shows that a POR is not a need for marketers. The PUCO recognized this in the last FirstEnergy ESP case when it concluded that,

> the marketers have demonstrated that the purchase of receivables by the utility **is their preferred business model**, **there is no record in these proceedings demonstrating that the absence of the purchase of receivables has inhibited competition.**[309]

This is evident from the fact that most of the benefits for marketers from a POR with a Bad Debt Rider are real, substantial, and a can have a significant and quantifiable impact on the marketers' bottom line. For example, if a marketer today has a 5% bad debt rate that requires the bad debt to eventually be written off, then for every $10,000,000 in billings, the marketer would have to write off $500,000.[310]

Under the AEP Ohio POR proposal the marketer would not need to pursue through collections its bad debt expense because the Utility could collect these charges

[309] *FirstEnergy ESP Case*, Opinion and Order at 40 (July 18, 2012). (Emphasis added).

[310] Tr. XI at 2688 (Bennett).

for the marketer from all of its captive customers. Such a savings for the marketer is significant, especially when the savings would go directly to the marketer's bottom line.[311] Moreover, these guaranteed payments to marketers for Bad Debt would promote inefficient operations because the service provided would be incented not to go through the expense of pursuing collections because they are guaranteed paid by the Utility's captive distribution customers. This inefficient program can only result in higher non-payment and uncollectables. Moreover, this highlights the difference between the POR being a want (to improve the bottom line) and not a need (because the lack of a POR is a barrier to entry).

In addition, under the AEP Ohio proposal, the marketers would no longer have the ordinary business risk associated with bad debt.[312] Instead, marketers would be uniquely positioned in the business world by having regulatory certainty in a market where there is no regulatory pricing control. The marketers own witness could not point to any other non-commodity utility business that has such regulatory protection.[313] Such protection is simply a subsidy from all of AEP Ohio's customers -- shopping and SSO customers -- to the marketers. This is unlawful and contrary to R.C. 4928.02(H) which prohibits anticompetitive subsidies flowing from a noncompetitive retail electric service (distribution customers) to a competitive retail electric service (generation).

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[311] Tr. XI at 2688 (Bennett).

[312] Tr. XI at 2691-2692 (Bennett).

[313] Tr. XI at 2692 (Bennett).

d. Under AEP Ohio's Purchase of Receivables Program, customers could be disconnected for not paying bills from marketers. This proposal will likely cause more customers to be disconnected.

Also concerning is the AEP Ohio proposal to waive the PUCO rules to permit residential customers to be disconnected for non-payment of unregulated marketer charges.[314] Currently Rule 4901:1-10-19(A) prohibits a utility from disconnecting a customer due to nonpayment of a non-commodity related charge. The AEP Ohio proposal can only be expected to result in more disconnections for non-payment and additional charges for reconnection and other fees that make the AEP Ohio electric services even more unaffordable.[315]

Moreover, as noted by IEU-Ohio, the imposition of a POR with a Bad Debt Rider would eliminate the market discipline that comes with the business risk of not being able to collect the bad debt.[316] With no market risk, there is no incentive for marketers to follow sound business principles in marketing their services to customers because there is no down side risk once they get customers to buy, buy, buy. This end result might be beneficial for marketers but it is not for AEP Ohio's customers who would get stuck paying the bill for bad debt associated with transactions where sound business principles were set aside. Again, this would also have the impact of further negatively impacting the affordability of basic electric service for low income and at-risk customers.[317]

IEU-Ohio also noted that internally, AEP Ohio addresses purchase of receivables by having AEP Credit purchase the receivables of the various AEP operating companies

[314] OCC Ex. 11 at 22 (Williams).

[315] OCC Ex. 11 at 23 (Williams).

[316] IEU-Ohio Brief at 50.

[317] OCC Ex. 11 at 4-20 (Williams).

and then reselling them to banks or other third party institutions.[318] When AEP Credit purchases the receivables from AEP operating companies, it purchases them without recourse, but at a discount.[319] Thus through its own actions, AEP Ohio demonstrated that it is unwilling to pay the full cost of the third party's debt. But yet it would expect its customers to pay the full cost of marketers' bad debt under AEP Ohio's proposal.

Another aspect of the AEP Ohio POR proposal that causes customers' concerns is that it could result in some customers having to pay additional unlawful deposits.[320] AEP Ohio will impose additional deposits on shopping customers who have already paid a deposit to a marketer or is paying a rate that reflects their specific credit risk.[321] Such collections are not permitted under the law. Revised Code 4933.17 expressly prohibits the collection of a security deposit if the deposit is not requested within thirty days of the initiation of service.[322]

When the considerable marketer benefits from a POR are compared to the speculative and unquantifiable benefits for customers (i.e. more marketers might enter the already sufficiently competitive retail market, or marketers might offer more options) the balance tips far in favor of the marketers. Although marketers[323] and AEP Ohio[324] claim that some additional suppliers will participate in the AEP Ohio retail electric market for residential customers if a POR with a Bad Debt Rider is implemented -- no marketer testified that it would enter the market if a POR was put in place. No marketer

[318] IEU-Ohio Brief at 50.

[319] IEU-Ohio Brief at 50.

[320] OCC Ex. 11 at 24-25 (Williams).

[321] OCC Ex. 11 at 24-25 (Williams).

[322] R. C. 4933.17(B).

[323] RESA Ex. 3 at 7 (Bennett).

[324] AEP Ohio Ex.11 at 4 (Gabbard).

witness,[325] or AEP Ohio witness,[326] was able to provide any assurance that a single additional marketer would enter the market if a POR was implemented. Thus, the customer benefit of even a single additional marketer in the AEP Ohio retail market is pure speculation.

Moreover, even if additional marketers enter the market -- for whatever reason -- after a POR with a Bad Debt Rider is implemented, there is no way to measure the benefit, if any, that the additional market entrant would have on the price that customers pay. Thus, there is no way to compare the actual cost of a POR to any potential benefit. This is a bad deal for customers.

Another alleged benefit from a POR is that marketers would offer more services than they would without a POR.[327] Yet no marketer witness[328] or AEP Ohio[329] witness could identify any additional or different service offered in the Duke service territory – which has a POR and Bad Debt Rider -- than those offered in the AEP Ohio service territory -- without a POR and Bad Debt Rider. If in fact the existence of a POR would bring the benefit of more services -- then one would expect Duke's customers would have the option of more and different service choices. However, Duke's customers have no more or different options than AEP Ohio customers.[330]

The marketers' claim of the lack of a POR being a barrier to entry is also contradicted by the actions of PPL Energy Plus. Its witness supported the POR on behalf

[325] Tr. XI at 2683 (Bennett).

[326] Tr. III at 854-855 (Gabbard).

[327] RESA Ex. 3 at 7 (Bennett).

[328] Tr. XI at 2694 (Bennett).

[329] Tr. III at 830 (Gabbard)

[330] Tr. XI at 2694 (Bennett).

of RESA. The PPL Energy Plus employee was the only witness who testified on behalf of the POR for marketers in this case. The PPL Energy Plus employee claimed that his company was participating in the Ohio market[331] but not making offers to residential customers because of the lack of a POR.[332] However, he also acknowledged that PPL Energy Plus was not making offers to residential customers in the Duke service territory which has a POR.[333] If in fact the lack of a POR was the reason that PPL Energy Plus was not making offers to residential customers in the AEP Ohio service territory, then PPL Energy Plus should be making offers to residential customers in the Duke service territory which has a POR. Yet, PPL Energy Plus is not making offers in the Duke service territory. This is an example of PPL Energy Plus speaking louder through its actions, than through its words.

5. The IGS proposal to alter the Standard Service Offer is unlawful and unreasonable. The proposal would artificially raise the price of the Standard Service Offer that non-shopping customers pay. The PUCO should reject the IGS proposal.

In Brief, OCC argued that the PUCO should reject[334] the IGS proposal to fundamentally alter the SSO, which is an integral part of S.B. 221. The modifications proposed by IGS are not lawful and are contrary to R.C. 4928.141(A), which **requires** the Utility to provide customers with a standard service offer of all competitive retail electric services. Similarly, OPAE and APJN also opposed the IGS proposal noting that

[331] Tr. XI at 2689 (Bennett).

[332] Tr. XI at 2689-2690 (Bennett).

[333] Tr. XI at 2689-2690 (Bennett).

[334] OCC Brief at 123.

Marketers were seeking an unlawful end -- where customers would be forced into bilateral contracts with marketers.[335]

In addition, OPAE and APJN argued that the IGS proposal would artificially increase the SSO price, thus forcing customers to pay more for the default service that a significant number of residential customers rely upon.[336] This price increase in the form of a retail auction adder is intended to force customers out of the SSO and into contracts with marketers.[337] In addition to directly raising prices, this would also have the effect of forcing the elimination of the SSO. This could then indirectly increase prices further because it would reduce the number of options customers would otherwise have. OCC agrees with OPAE and APJN that IGS' proposal undermines the law (R.C. 4928.141), which requires the EDU's to offer an SSO.

The IGS proposal would exacerbate the current high rates that AEP Ohio customers pay,[338] by adding additional unwarranted charges to customers' bills. AEP Ohio also opposed the IGS proposal noting that the proposal was at the investigatory stage and would benefit from further discussion and development.[339] The PUCO should reject the IGS proposal.

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[335] OPAE and APJN Brief at 48.

[336] OPAE and APJN Brief at 49.

[337] OPAE and APJN Brief at 49.

[338] OCC Ex. 11 at 4-20 (Williams).

[339] AEP Ohio Brief at 148.

6. RESA's proposed Marketer Energy Plan is inadequate and exposes customers to potentially higher electric costs. The PUCO should reject the RESA proposal.

OCC opposed the RESA proposal for a marketer energy plan because it could confuse customers and lead to higher prices for customers.[340] RESA's proposal would require the Utility to market the MEP program to all customers who contact the Utility except for emergency or disconnections.[341] As contemplated by RESA, the MEP would represent a product that is an "approved product by the PUCO in order to give the customer the "theoretical level of security when they're engaging in the competitive market."[342] This approval by the PUCO could easily be taken for an endorsement of the product, where customers might only sign up for the MEP program because they thought that the regulator was encouraging them to do so. Such approval could be an issue if the customer then had a problem with the program and blamed the PUCO, because the PUCO approved the product. This could result in a blurring of the line between the regulator and a product that the regulator regulates.

In addition, the RESA proposal was overly general and lacked sufficient detail and customer benefits. Instead of a well though-out proposal that could provide real benefits to customers, RESA's proposal lacked information on key aspects such as terms and conditions[343] and the process for how a working group would fill in those blanks.[344]

[340] OCC Brief at 125.

[341] Tr. VIII at 1996-1997 (Pickett).

[342] Tr. VIII at 1958-1959 (Pickett).

[343] Tr. VIII at 1949 (Pickett).

[344] Tr. VIII at 1949, 1951 (Pickett).

Even the aspects of the RESA proposal that were presented as firm lacked any explanation or basis for why the proposal included those terms.[345] AEP Ohio opposed the RESA proposal noting that the proposal needed considerable further discussion and development.[346]

OPAE and APJN noted that a key problem with the proposal is how customers would be treated at the end of the initial six-month term.[347] OPAE and APJN opposed the proposal for its use of a teaser rate that could easily turn into higher rates at the end of the original six-month term[348] if customers were automatically renewed without affirmative action from the customer. Equally disturbing is the fact that the three percent teaser rate could be inferior to better offers that might be available in the market. And Marketers are relying on a PUCO endorsement of a marketer plan. [349] The marketers view this approval and sanctioning as being different than the offers that are listed on the PUCO Apples-to-Apples chart.[350] The PUCO should be wary of as endorsing such a product. Finally, pursuant to PUCO rules, new customers are not even informed about their rights and responsibilities to participate in choice until they receive the Customer Rights and Obligations Summary.[351]

OPAE and APJN also argued that RESA's proposal was unlawful because it violates R.C. 48928.02(H). That statute prohibits subsidies from flowing from regulated

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[345] Tr. VIII at 1943-1944 (Pickett).

[346] AEP Ohio Brief at 148.

[347] OPAE and APJN Brief at 50.

[348] OPAE and APJN Brief at 50.

[349] Tr. VIII at 1958 (Pickett).

[350] Tr. VIII at 1962-1963 (Pickett).

[351] Ohio Adm. Code 4901:1-10-12.

service to unregulated service.[352] The AEP Ohio call center, whose costs are currently charged to all customers as part of distribution rate base rates, would be used to market the marketer plan to non-shopping customers. Under the marketer plan the Utility call center would engage in action to directly benefit markers by encouraging and expediting customers to take service from marketers.[353] The law does not permit AEP Ohio to collect the costs associated with a third parties' marketing efforts from distribution customers.[354]

7. AEP Ohio's charges to customers for riders DIR, ESRR, SDRR and SSWR should be allocated fairly among customers according to cost-causation principles rather than over-allocating costs to residential consumers based on AEP Ohio's proposal.

To the extent the PUCO authorizes AEP Ohio to charge consumers for any of its proposed riders, OCC proposed that the PUCO allocate the riders among customer classes according to cost causation principles.[355] OCC's Brief describes OCC witness Jonathan Wallach's proposed allocation method for each rider.[356] AEP Ohio did not rebut Mr. Wallach's testimony or file a brief on Mr. Wallach's recommendation. The only party addressing OCC witness Wallach's proposal was the Ohio Energy Group ("OEG"). OEG argued that these costs should be allocated based on distribution revenues, as they are currently allocated, because they are "related to the provision of

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[352] OPAE and APJN Brief at 51.

[353] OPAE and APJNJ Brief at 51.

[354] OPAE and APJN Brief at 51.

[355] OCC Brief at 107-109.

[356] OCC Brief at 108.

distribution service" and the PUCO has previously approved this allocation methodology.[357]

As OCC witness Wallach testified, an allocation methodology, which is not based on cost-causation principles, should not be continued. He stated:

> A. Yes. It's fair to say that I'm shining a light on this issue and asking the Commission to consider an alternative cost allocation approach which I believe is more consistent with cost causation principles.[358]

OEG calls Mr. Wallach's allocation "a completely new formula that would require a fresh review of the cost of service and allocation methodology determined in AEP Ohio's last ESP case."[359] Not so. Mr. Wallach's recommendations are specific to the four riders – DIR, SSWR, SDRR, and ESSR -- that are being addressed in this proceeding. Allocation of costs within these riders does not affect the allocation of base distribution revenues. And Mr. Wallach's allocators make eminent sense rather than the current allocation based on distribution revenues, which is unrelated to the reasons for which these costs are incurred. As Mr. Wallach testified, DIR and the ESRR capital costs should be assigned in proportion to the allocation of net electric plant in service because they relate to capital spending on distribution. ESRR O&M costs should be allocated in proportion to the allocation of distribution O&M expenses because these costs relate to distribution O&M. This includes spending for distribution plant O&M, but excludes customer account expenses, customer services and sales expenses, and administrative and general expenses. SDRR expenses should be allocated in proportion to the allocation of distribution O&M expenses as well for the same reasons. And SSWR costs should be

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[357] OEG Brief at 27.

[358] Tr. X at 2407.

[359] OEG Brief at 27.

allocated in proportion to the allocation of distribution O&M labor expenses because they involve O&M labor costs.

Contrary to OEG's position, prescribing a different allocator for these costs would not constitute a *"mini rate case"*.[360] These riders pertain to discrete costs recovered apart from costs included in base distribution rates. An appropriate record has been established in this case based on Mr. Wallach's testimony. The PUCO should adopt Mr. Wallach's recommendations.

8. AEP Ohio's time-of-use rates, which provide savings to many customers, should not be eliminated.

AEP Ohio's time-of-use ("TOU") rates allow customers to benefit from using energy at times of the day when system usage and wholesale prices are typically lower. OCC supports the continuation of utility TOU rates, especially in the absence of marketer offers of a comparable time-of-use service.[361] AEP Ohio's proposal to eliminate these services is supported by several marketers.[362] AEP Ohio claims that "[f]ew customers take service" under the TOU tariffs and "those that do can more appropriately obtain comparable services in the market from CRES providers who are better positioned to offer them under the current market construct."[363]

But neither AEP Ohio nor any other party provided any evidence that marketers are offering TOU services or are prepared to do so in AEP Ohio's service territory. As discussed in OCC's Brief, OCC witness Williams testified there were no marketer TOU

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[360] OEG Brief at 27.

[361] OCC Brief at 109-112.

[362] AEP Ohio Brief at 70-71; IGS Brief at 21-22; Constellation/Exelon Brief at 23; RESA Brief at 32-33.

[363] AEP Ohio Brief at 70, *citing* AEP Ohio Ex. 3 at 12-13 (Spitznogle).

offers and AEP Ohio witness Vegas confirmed that this was the case.[364] Indeed, Mr. Vegas testified that he did not even know whether marketers had the Smart Meter data necessary to offer such services.[365] The Environmental Law & Policy Center ("ELPC") also pointed to the absence of TOU rate offers by marketers as indicating that customer demand to TOU offers will not be served in the current marketplace if these tariffs were to be eliminated.[366]

Currently, there are 915 customers on the standard TOU offering and there are 9,000 customers on AEP Ohio's experimental dynamic and time-differentiated pricing options offered through its gridSMART Phase 1 Initiative.[367] As emphasized by ELPC, Smart Meters may provide both AEP Ohio and its customers with greater usage information, making the offering of dynamic and time-differentiated pricing easier.[368] Neither service should be eliminated, especially when there are no alternatives. These rates provide clear savings to customers, and Smart Meters may enhance the information that can be gathered so that customers have opportunities to efficiently use electricity.

As was stated by OCC witness Williams, time-differentiated pricing by the utilities, with a level of PUCO oversight that accompanies a tariffed program, is appropriate as the market emerges for these complex rate programs.[369] In fact, the PUCO has encouraged EDUs with Advanced Metering Infrastructure/Smartgrid deployments to

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[364] OCC Brief at 110, *citing* Tr. I at 79 (Vegas); OCC Ex. 11 at 33, Ex. JDW-15 (Williams).

[365] Tr. I at 79 (Vegas).

[366] ELPC Brief at 5-6.

[367] OCC Ex. 11 at 33-34 (Williams).

[368] ELPC Brief at 6.

[369] OCC Ex. 11 at 34 (Williams).

implement pilot time-differentiated rate programs for this very reason.[370] AEP Ohio's proposal to eliminate programs that may help customers save money and to help further develop the market offerings of such programs is contrary to PUCO guidance. Moreover, continuing this time of use rate pilot program may assist to promote further customer understanding of these service offerings.

RESA argues that since the TOU rate would not be eliminated until June 2015, TOU offers from CRES suppliers may arise before then and, if not, the issue could be addressed then.[371] If a market develops by that time (which certainly is not guaranteed), RESA or another party could petition for the elimination of these rates as unnecessary. The record as it exists now does not support eliminating these tariffs.

9. AEP Ohio's proposal that it be allowed to charge customers for GridSmart Phase II costs through the Phase I pilot rider is premature, prior to the PUCO and parties reviewing the costs and benefits to customers of the GridSMART Phase I pilot.

AEP Ohio has proposed that its customers pay for gridSMART Phase II costs through continuation of the gridSMART Rider.[372] AEP Ohio also proposed that any remaining gridSMART Phase I costs be included in the Distribution Investment Rider for recovery.[373]

OCC recommended that it is premature for the PUCO to authorize a mechanism to charge customers for gridSMART Phase II costs. This is because the costs and benefits to customers of the gridSMART pilot program -- Phase I – and the authorization of Phase II is currently being reviewed by the PUCO in a different case, Case No. 13-1939-EL-RDR.[374] Notwithstanding that

[370] RMI Order at 37-38.

[371] RESA Brief at 33.

[372] AEP Ohio Brief at 87-88.

[373] AEP Ohio Brief at 87-88.

[374] OCC Brief at 112-113.

gridSMART Phase II has not yet been approved, AEP Ohio proposed that the existing gridSMART Rider be used to charge customers for the gridSMART Phase II costs.

The Ohio Environmental Counsel ("OEC") and Environmental Defense Fund ("EDF"), argued that certain issues "relating to whether those costs are prudent and all benefits accounted should be addressed" in this case.[375] Those issues include netting of operational cost savings of Phase II deployment against the costs of deployment and annual reporting of performance metrics to be developed through a collaborative stakeholder process.[376]

As discussed in OCC's brief, issues related to recovery of costs associated with gridSMART Phase I and Phase II should be considered in conjunction with the evaluation of the Phase I pilot and AEP Ohio's proposal for Phase II authorization. The PUCO should consider the comments filed in Case No. 13-1939-EL-RDR prior to ruling on any aspect of gridSMART Phase II. As discussed at that docket, AEP Ohio failed to provide an appropriate cost-benefit analysis or any real assurance that consumers will receive substantive benefits from deployment of gridSMART technologies for the considerable costs they would be asked to pay. This presents significant issues regarding continuing authorization, let alone expansion of gridSMART.[377] Until those issues are addressed, discussion of a Phase II rider is premature and should not be entertained in this proceeding. A cost recovery mechanism should be tailored to ensure that gridSMART is operated efficiently and effectively for the benefit of customers.

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[375] Joint OEC and EDF Brief at 6.

[376] Joint OEC and EDF Brief at 7-9.

[377] *In the Matter 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, Comments By The Office of the Ohio Consumers' Counsel (November 1, 2013).

10. AEP Ohio's proposal to extend the Pilot Throughput Balancing Adjustment Rider ("PTBAR") through the term of the ESP is contrary to the PUCO's requirement that it be evaluated before it is extended and could be harmful to customers.

AEP Ohio's Pilot Throughput Balancing Adjustment Rider ("PTBAR"), or "revenue decoupling mechanism," should not be continued through the term of the ESP as discussed in OCC's brief, without evaluating the costs and benefits of the rider to customers.[378] Because there has been no evaluation presented in this case, the PUCO should not extend the rider through May 2018.

The rider is experimental and was established on a pilot basis, through a Stipulation reached in AEP Ohio's last distribution rate case.[379] The PUCO specifically "established reporting requirements regarding how to measure the success of the pilot program" with a clear statement that it was not intended to be permanent and should only continue until a program evaluation is complete.[380]

AEP Ohio and NRDC argue for continuation of the rider through the ESP period. The ESP period runs through May 2018. That would mean that the PTBAR program would run for six years total. In arguing for the continuation of the rider through the ESP, AEP Ohio asserts that the PUCO "authorized the extension of the rider in Case Nos. 11-351-EL-AIR, *et al.* until otherwise ordered."

AEP Ohio misconstrues the PUCO's order in its last distribution rate case. The PUCO clarified in its Entry on Rehearing that "the opinion and order provides that the

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[378] OCC Brief at 113-114.

[379] OCC Ex. 11 at 37 (Williams).

[380] OCC Brief at 113-114, *citing In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company, individually and, if their proposed merger is approved, as a merged company (collectively AEP Ohio) for an increase in electric distribution rates*, 11-351-EL-AIR, Entry on Rehearing at 3 (Feb.14, 2012)

throughput balancing rider should be extended temporarily until such evaluation can be completed, *unless otherwise ordered by the Commission*."[381] Thus, the PUCO intended only an extension of the rider until the evaluation was completed, stating that the pilot was **not** intended to be permanent. With no evaluation of the rider in the context of this proceeding, there is no basis to continue the PTBAR for another four years.

Because the PTBAR was authorized for calendar years 2012, 2013, and 2014, the pilot evaluation should be completed and submitted by the time AEP Ohio submits its PTBAR true-up for 2014, the last year of the pilot. AEP Ohio has filed its PTBAR true-up at the beginning of March in each of the past two years and should submit its evaluation at the beginning of March 2015. If the continuation of the Rider is to be considered outside of a rate case, it should be evaluated either in conjunction with the PTBAR update or in EE/PDR proceedings during the same timeframe, as recommended by OCC witness Williams.

AEP Ohio witness Spitznogle acknowledged on cross-examination that the PTBAR was "designed to be assessed before it is implemented any further" and that no assessment was provided in AEP Ohio's application in this proceeding.[382] And, despite the requirement that the program be evaluated before continuing the pilot, Mr. Spitznogle testified that "until we hear otherwise" from the Commission, AEP Ohio has "no intention of changing this program."[383]

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[381] *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company, individually and, if their proposed merger is approved, as a merged company (collectively AEP Ohio) for an increase in electric distribution rates*, 11-351-EL-AIR, Entry on Rehearing at 3 (Feb.14, 2012)(emphasis added).

[382] Tr. I at 229 - 230.

[383] Tr. I at 231.

The PUCO was very clear that the rider was implemented on a pilot, not a long-term, basis. The entire purpose of a pilot is to test whether the program achieves the intended objectives for customers, for which it was designed. Indeed, in the PUCO's Opinion and Order at Case No. 11-351-EL-AIR, it raised concerns that the PTBAR "is not the unmitigated benefit to customers portrayed by the signatory parties."[384] The PUCO, directed "the signatory parties to prepare a detailed proposal regarding the type of data proposed to be obtained, how that data will be obtained, and metrics to evaluate the success of the pilot program." It directed the parties to file these metrics in Case No. 10-3126-EL-UNC "within six months of the issuance of this Opinion and Order."[385] And the signatory parties did just that, filing proposed metrics on June 14, 2012.[386]

The PUCO should follow the terms of the Stipulation and its order in the 2011 rate proceeding. In addition to evaluating the pilot program based on the metrics agreed to by the signatory parties, the PUCO should also implement the additional requirements it established in that proceeding. There, it stated that "it is necessary to take additional steps, beyond the Stipulation, to ensure that an adequate record is established to review

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[384] *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company, individually and, if their proposed merger is approved, as a merged company (collectively AEP Ohio) for an increase in electric distribution rates,* 11-351-EL-AIR, Opinion and Order, at 9 (Dec. 14, 2011).

[385] *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company, individually and, if their proposed merger is approved, as a merged company (collectively AEP Ohio) for an increase in electric distribution rates,* 11-351-EL-AIR, Opinion and Order at 10 (Dec. 14, 2011).

[386] *In Matter of Aligning Electric Distribution Utility Rate Structure with Ohio's Public Policies to Promote Competition, Energy Efficiency and Distributed Generation,* Case No. 10-3126-EL-UNC, Proposal Of Ohio Power Company And The Signatory Parties To The Public Utilities Commission Of Ohio's Opinion And Order In Case No. 11-351-EL-AIR, et al. dated December 14, 2011 (June 14, 2012). Although the PUCO acknowledged the signatory parties' proposal in its Finding and Order of August 21, 2013 at Case No. 10-3126-EL-UNC, the PUCO did not specifically adopt the metrics proposed by the signatory parties. Instead, the PUCO found that the problems with revenue decoupling were such that "if the Commission determines that a decoupling rate design should be implemented, such action should only be implemented during an electric utility's rate case." *In Matter of Aligning Electric Distribution Utility Rate Structure with Ohio's Public Policies to Promote Competition, Energy Efficiency and Distributed Generation,* Case No. 10-3126-EL-UNC, Finding and Order at 20 (Aug 21, 2013).

residential rate design at the conclusion of the three year pilot program." The PUCO specified:

> First, AEP-Ohio is directed to update its cost of service study, prior to the final year of the pilot program, and file the updated study in this proceeding. Interested parties will then be provided with an opportunity to comment upon the updated cost of service study. Second, unless otherwise ordered by the Commission, AEP-Ohio's residential distribution rates will be adjusted, on a revenue neutral basis, to rates which are consistent with the rate design recommended by Staff in the Staff Reports and which will produce the annual revenue requirement agreed to in the Stipulation.[387]

The PUCO was plainly concerned about whether the PTBAR would be harmful or helpful to customers, especially residential customers, and it wanted to ensure that the PTBAR could be fairly evaluated and rates set fairly for the future based upon an updated cost-of-service study. Thus, it not only directed the parties to develop metrics for evaluation of the PTBAR but imposed a requirement to revisit rates in setting any future charges. The PUCO should ensure that its directives are followed.

OCC notes that the metrics developed by the signatory parties (that included OCC and AEP Ohio) to the distribution rate case Stipulation are designed to address key issues with the PTBAR. These issues include (1) the magnitude of the rate adjustments; (2) whether rate adjustments result in credits, as well as, charges to customers; (3) whether the use of actual revenues, rather than weather-adjusted revenues, produced appropriate results; (4) whether the mechanism did in fact reduce AEP Ohio's disincentive to promote energy efficiency; (5) whether energy efficiency benefits, in terms of use per

[387] *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company, individually and, if their proposed merger is approved, as a merged company (collectively AEP Ohio) for an increase in electric distribution rates,* 11-351-EL-AIR, Opinion and Order at 10 (Dec. 14, 2011).

customer, were demonstrated; (6) comparison to the net lost revenue approach; and (7) operation of the 3% cap on increases to distribution revenues in each year.[388]

These metrics attest to the significant issues that should be addressed if any extension of the PTBAR is to be considered by the PUCO in conjunction with the pilot evaluation. In particular, OCC notes its concern with the use of actual revenues rather than weather-adjusted revenues to set the PTBAR. In addition, the PUCO's requirements that AEP Ohio produce an updated cost-of-service study and revisit residential distribution rates in particular speaks to the PUCO's concern with the appropriate cost allocation of PTBAR. OCC would emphasize in this regard its concern with the use of actual 2012 revenues to establish the baseline for the PTBAR when 2012 revenues may not be an appropriate baseline for any revenue decoupling mechanism.

In this light, if the PTBAR is to be extended, the PUCO should – as it clearly intended– revisit the details of the PTBAR. If the PUCO determines to extend the PTBAR, it should do so only with the aid of the metrics agreed to by the signatory parties (that included OCC and AEP Ohio). And it should adjust PTBAR annual revenues for normal weather, and compare those revenues to a weather-normalized baseline consistent with AEP Ohio's authorized distribution revenues from its last rate case, excluding any riders. The PUCO should also utilize the results of AEP Ohio's updated cost-of-service study – to be submitted before the end of 2014 – to implement a cost-based allocation of any throughput adjustment among customer classes. Interested parties should, of course,

[388] *In Matter of Aligning Electric Distribution Utility Rate Structure with Ohio's Public Policies to Promote Competition, Energy Efficiency and Distributed Generation,* Case No. 10-3126-EL-UNC, Proposal Of Ohio Power Company And The Signatory Parties To The Public Utilities Commission Of Ohio's Opinion And Order In Case No. 11-351-EL-AIR, et al. dated December 14, 2011 (June 14, 2012).

be given the opportunity to make a record on these issues before the PUCO determines to implement any extension of the PTBAR.

NRDC supports the extension of the PTBAR "as a tool to remove AEP's throughput incentive, which thereby frees the utility to help its customers save energy through energy efficiency and peak demand response ("EE/PDR") programs."[389] NRDC claims that the rider "is an important component of the ESP, as it addresses AEP's ongoing efforts to comply with the S.B. 221 energy efficiency requirements."[390] NRDC claims that the "[r]ider is working" based upon a statement to that effect in Comments filed by the PUCO Staff at Case No. 13-568-EL-RDR.[391]

But there is not testimony in this proceeding that the PTBAR is working for the benefit of customers. And NRDC's claims that AEP Ohio is exceeding its energy efficiency targets should be evaluated, as should the PTBAR, in AEP Ohio's energy efficiency proceedings, not in this proceeding, based upon a proper record. This was the purpose of the metrics agreed to by the signatory parties (including OCC and AEP Ohio) in the distribution rate case. We would look forward to working with AEP Ohio and NRDC and others in the proper process contemplated in the distribution case Order. The PUCO should not base its consideration of AEP Ohio's request on information that is not part of this record and has not been subjected to cross-examination or the opportunity for responsive testimony. The purpose of the metrics was to facilitate a review of the PTBAR based on evidence. The PUCO should only consider an extension of the PTBAR in conjunction with such evaluation.

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[389] NRDC Brief at 2-3.

[390] NRDC Brief at 3.

[391] NRDC Brief at 3.

11. This case began with AEP Ohio filing an application to, among other things, eliminate the interruptible credit that non-interruptible customers (including residential customers) subsidize. Now, one-half year later on brief, AEP Ohio changed its original position to state its non-objection to continuing its current credit for interruptible customers (meaning other customers would continue to pay AEP Ohio for the credit). Consistent with AEP's original application position and Ohio's movement to market pricing, the PUCO should seek ways to protect other customers that are paying for the credit.

After filing its application on December 20, 2013, AEP Ohio waited until its brief on July 23, 2014 to change its proposal on the credit for interruptible rate customers that all customers (including residential customers) pay for. In its Brief, AEP Ohio says that due to changed circumstances, including a D.C. Circuit decision, "the Company would not object to the Commission authorizing it to continue offering a modified version of schedule IRP-D."[392] AEP Ohio's late position supplement is unfair to the process of parties presenting evidence and recommendations to the PUCO on these issues, given that the utility's application is a focus of its ESP case. And it does not well serve the PUCO that depends upon the parties for providing informed recommendations for effective PUCO decision-making.

AEP Ohio provides a credit of $8.21/kW-day to customers under Rate Interruptible Power – Discretionary (Rate IRP-D). As of August 30, 2013, Mr. Spitznogle testified that there were only three customers receiving a credit under Rate IRP-D. Lost revenue from the IRP-D is currently recovered through AEP Ohio's Energy

[392] AEP Ohio Brief at 72-73.

Efficiency/Peak Demand Response Rider.[393] That means that all customers make the utility whole for the lost revenue from the interruptible rate credit.

AEP Ohio initially proposed, in its Application, to eliminate this tariff, stating that "the market can provide comparable offerings."[394] AEP Ohio witness Moore further explained:

> . . . the Company will be procuring the generation service needs of SSO customers through a full auction and AEP Ohio, as a wires company, may not be the entity best able to provide an interruptible service product (though there may be some limited opportunities to receive payment for load curtailment from the Company in connection with its peak demand reduction mandates).[395]

OEG objected to AEP eliminating Rate IRP-D, arguing that AEP Ohio is not a wires-only company as long as it maintains OVEC generation. OEG further noted that another EDU, FirstEnergy, has maintained its interruptible program even though it has been a wires-only company since the mid-2000s.[396] OEG also argued that the PUCO approved an interruptible credit for Duke's customers in its last ESP case even while ordering Duke to divest its generation.[397] OEG also pointed out that all of the PJM Base Residual Auctions for the period through the term of the ESP have already occurred and customers "cannot now bid their interruptible load into these PJM auctions."[398]

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[393] *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Authority to Establish a Standard Service Offer Pursuant to Section 4928.143, Revised Code, in the Form of an Electric Security Plan; In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of Certain Accounting Authority,* Case No. 11-346-EL-SSO, et al., Opinion and Order of August 8, 2012 at 26.

[394] AEP Ohio Ex. 3 at 12 (Spitznogle).

[395] AEP Ohio Ex. 13 at 9 (Moore).

[396] OEG Brief at 18.

[397] OEG Brief at 18-19.

[398] OEG Brief at 19.

AEP Ohio responded to OEG in discovery that customers could either seek to replace a Curtailment Service Provider that did not actually sign up its load or bid its interruptible load into an incremental auction.[399] However, OEG pointed to the unreasonableness of the first option and the low values for capacity achieved in previous incremental auctions as significantly impairing the value which could be realized.[400] OEG also pointed to the D.C. Circuit Court's decision in *Electric Power Supply Association v. Federal Energy Regulatory Commission,*[401] finding that states have exclusive jurisdiction to regulate retail demand response in the energy markets. OEG states that this calls into question whether demand response resources can be bid into PJM capacity auctions.[402]

In its Brief, AEP Ohio says that due to changed circumstances, including the above-referenced D.C. Circuit decision, "the Company would not object to the Commission authorizing it to continue offering a modified version of schedule IRP-D."[403]

Consistent with AEP's original application position and Ohio's movement to market pricing, the PUCO should seek ways to protect other customers (including residential customers) that are paying for this above-market credit. The current IRP-D rate of $8.21/kW-day (that other customers are subsidizing) is significantly higher than the current RPM rates for demand response. One approach for protecting other customers (who are paying the subsidized above-market prices) would be continuing the IRP-D for only as long as customers cannot bid their demand response into the PJM

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[399] OEG Brief at 19.

[400] OEG Brief at 19-20.

[401] 753 F.3d 216, 2014 U.S. App. LEXIS 9585 (D.C. Cir. May 23, 2014).

[402] OEG Brief at 20.

[403] AEP Ohio Brief at 72-73.

auction or cannot sign up their demand response with an existing Curtailment Service Provider.

F. Auction Issues

1. The PUCO should reject AEP Ohio's proposal to charge residential consumers a $30 million cost premium (or more) for capacity procured in the full requirements auction for SSO load.

AEP Ohio proposes adjustments to the blended costs used to derive the customer class SSO retail auction rates, including those for residential customers. The effect of the adjustment is to assign a substantial cost premium for capacity supplied to residential SSO customers as compared to other classes. This causes the implicit capacity component of the SSO prices for residential SSO customers to be different and more expensive than the capacity for non-residential SSO customers. Under AEP Ohio's approach this $30 million annual cost premium would apply to each all of the auctions over the three year ESP term. That means that over the term of the ESP the cost of the premium could be as high as $90 million for residential customers.

OCC Witness Kahal testified that such a premium is not justified because it is based on an incomplete consideration of the costs of serving the residential SSO load. [404] First, AEP Ohio's adjustment is administratively determined and is not derived from the market or wholesale bidder behavior.[405] As noted by Mr. Kahal, there is nothing in the behavior of bidders in the wholesale auction that demonstrates there must be such a price premium for residential customers. If wholesale suppliers do not require a premium price

[404] OCC Ex. 13 at 56-57 (Kahal).

[405] Id. at 56 (Kahal).

to serve residential customers under their full requirements contract, then there can be no justification for AEP Ohio's contrived residential cost penalty.

Second, the residential customer class has a large load -- accounting for about 62% of total SSO load.[406] As also confirmed by Dr. LaCasse, a large load attracts more bidders and therefore a more competitive bidding result.[407] Third, as compared to the highly market-sensitive nonresidential customers, residential customers have less of a tendency to shop, with less abrupt movement to the market.[408] This suggests that wholesale full requirements contract suppliers will perceive less migration risk (i.e., load uncertainty that cannot be effectively hedged) associated with residential load than non-residential load.

In AEP Ohio's Initial Brief it claims that OCC Witness Kahal's recommendations should not be accepted.[409] First, AEP Ohio notes that Witness Roush's adjustment is consistent with the methodology the PUCO has approved for other unnamed Ohio utilities.[410] Additionally, AEP Ohio characterizes Mr. Kahal's position as "overstated" and "selective."[411] According to AEP Ohio, Mr. Kahal fails to account for the heightened risk that the residential class presents as a result of abrupt migration of significant amounts of load to CRES through local government aggregation.[412] AEP Ohio also criticizes Mr. Kahal for not conducting any analysis to demonstrate his conclusion. AEP

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[406] OCC Ex. 13 at 57 (Kahal).

[407] AEP Ohio Witness LaCasse discusses the importance of the size of the SSO load in auctions. AEP Ohio Ex. 15 at 11.

[408] OCC Ex. 13 at 57 (Kahal).

[409] AEP Ohio Brief at 21.

[410] AEP Ex. 12 at 5 (Roush).

[411] AEP Ohio Brief at 21.

[412] Id.

Ohio also argues that Mr. Kahal fails to consider other risks associated with residential customers such as the weather-sensitive nature of residential usage. AEP Ohio argues that Mr. Kahal's alternative recommendation for a separate auction for residential SSO customers would introduce an undue and unnecessary complexity (and thus cost) into the competitive bid process.[413]

But AEP Ohio has not convincingly demonstrated the costs of providing capacity to residential SSO customers is greater than the costs of providing capacity to other SSO customers. It must do so in order to justify charging residential SSO customers more for capacity. This is because Ohio law prohibits discriminatory pricing of utility services. R.C. 4928.02(A) requires ensuring that consumers have "nondiscriminatory" retail electric service. R.C. 4905.33 prohibits a public utility from charging greater or lesser compensation for services rendered for "like and contemporaneous service under substantially the same circumstances and conditions." R.C. 4905.35 prohibits a utility from giving any "undue or unreasonable preference or advantage" to any person.

The capacity that is to be provided through wholesale suppliers to non-shopping residential customers is no different than the capacity wholesale suppliers provide to non-shopping commercial and industrial customers. A system where residential SSO (non-shopping) customers could pay $30 million more for capacity, per year for three years, contrasted with industrial and commercial SSO customers is discriminatory. It violates R.C. 4928.02(A), and R.C. 4905.33 and 4905.35. Moreover, this new unwarranted charge would have the overall effect of increasing merchant generator offerings because SSO auction rate prices are used as the benchmark for comparison to marketer offerings.

[413] AEP Ohio Brief at 22.

AEP Ohio tries to differentiate the capacity service supplied to residential customers from capacity service supplied to non-residential customers by pointing to risks that wholesale suppliers face from residential customer behavior. It alleges that residential customers cause greater risks because of aggregation and weather-sensitive usage.[414] But these alleged risks do not demonstrate that it costs AEP Ohio more to secure capacity through the competitive bid auction to residential customers than non-residential customers. AEP Ohio has not shown how these alleged risks equate to costs to provide capacity to residential SSO customers. Moreover, municipal aggregation has been available as an option for several years, and despite this market feature, residential SSO load has remained far more stable than non-residential load. It is implausible that wholesale full requirements contract suppliers would require a premium to supply the very large, stable, and relatively low risk residential load.

And even assuming arguendo that AEP Ohio could demonstrate that the risks from residential customers translate into costs to the wholesale suppliers (which it has not done in this proceeding), it fails to consider the countervailing risks that OCC Witness Kahal identified. Importantly, Mr. Kahal testified that that migration risk (away from SSO) is far greater on non-residential side than it is on the residential side, notwithstanding municipal aggregation.[415] And Mr. Kahal noted that the other half of the equation is that migration risk (back to the utility's SSO) presents a large risk, caused primarily by commercial and industrial customers, not residential customers. This is a consequence of the significant amount of switching by the industrial and commercial

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[414] AEP Ohio Brief at 21-22.

[415] Tr. IX at 2106 (Kahal).

customers as opposed to the much lower switching by residential customers.[416] And with aggregation customers, the migration risk back to the utility is, by statute[417] the market price of power incurred by the utility to serve the customer. Thus, aggregation customers do not pose any migration risk in coming back to the utility.

OCC witness Kahal offers an empirical alternative to eliminating this penalty: when conducting the auctions (as proposed by Dr. LaCasse) simply allows bidders to bid separately to serve residential and non-residential loads. Doing so is a market-based approach that creates no administrative or technical problems for the auctions. AEP Ohio attempts to portray this alternative as one which is unduly complex. This is not correct and reflects a misunderstanding of the auction process that AEP itself proposes.

It is true that Mr. Kahal's primary recommendation of simply eliminating the pricing penalty would be simpler. In fact, it is simpler than even AEP Ohio's proposal. But if the PUCO rules that a pricing penalty is reasonable, the alternative of a separate residential full requirements contract product is entirely feasible. It does not require a separate auction. It would require, however, AEP Ohio and the PUCO deciding whether to have multiple or single non-residential products in the auction. That is the only "complication." In fact, AEP Ohio in its brief reveals its true concern with OCC's proposal. That concern seems to be that non-residential loads may appear to be less attractive to suppliers due to their small size (compared to the very large and stable residential load).

The PUCO should decline to impose a cost premium for Ohio's residential electric customers. There is no cost basis to support this charge. Charging residential

[416] See, e.g., AEP Ohio Ex. 7 at 13 (Allen Direct).

[417] R.C. 4928.20(J).

SSO customers $30 million a year more for capacity than non-residential SSO customers is discriminatory. It violates 4928.02(A), and R.C. 4905.33 and 4905.35.

2. The auction procurement process for SSO supply should be modified to provide the opportunity for potentially lower prices for consumers through a mix of one-and two-year full requirements contracts throughout the six scheduled auctions.

Dr. LaCasse testified that there should be a mix of one-year and two-year full requirements contracts ("FRCs") for the first two scheduled auctions (September 2014 and March 2015).[418] However, Dr. LaCasse did not propose any two-year FRCs for the remaining four auctions. According to Dr. LaCasse, 100% of the procurement during those auctions will be through one-year FRCs.[419]

OCC Witness Kahal testified that Dr. LaCasse's proposal is unduly skewed toward one-year contracts. AEP Ohio's plan is overwhelmingly one year contracts, all expiring in May 2018. Because one year contracts are used, the auction may be limiting the opportunity potentially lower prices for consumers. This is because more suppliers are likely to participate if there are varied contract terms.[420]

Witness Kahal also explained that AEP Ohio's design of the auction provides the potential for greater rate volatility than is necessary. Mr. Kahal proposed that the PUCO could accomplish a 50/50 mix of one and two-year contracts by changing the procurement in the fifth and sixth auctions.[421] Instead of procuring via 100% one-year contracts in those two auctions, the solicited products could be a 50/50 mix of one-year and two-year contracts. This would allow the SSO load to be served by a reasonable mix

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[418] AEP Ohio Ex. 15 at 11-12 (LaCasse).

[419] Id. at CL-10 (LaCasse).

[420] OCC Ex. 13 at 50 (Kahal).

[421] Id. at 52 (Kahal).

of one and two-year contracts in all three years of ESP III. In addition, this would allow the contracts to overlap during the post May 31, 2018 time period.[422]

Staff Witness Strom similarly expressed concerns that the proposed restructuring of AEP Ohio's auctions would subject SSO customers to uncertainty and potential rate volatility for 2017 and 2018.[423] He offered a number of options to address this issue including rejecting the early termination provision, and extending the ESP for a five-year period, as opposed to a three-year period.[424]

In AEP Ohio's Brief, AEP Ohio claims that Kahal (and Strom's) criticisms are overstated. AEP Ohio argues that there is no evidence beyond the witness' conjecture that rate volatility will be increased materially under the Utility's laddering proposal.[425] AEP Ohio also links the structure of auctions to its early termination rights.[426] In other words, because AEP Ohio believes it has the right to unilaterally terminate its ESP; it cannot adopt the laddering approach recommended by OCC and the PUCO Staff.

But AEP Ohio ignores the fact that the PUCO (and other jurisdictions[427]) have recognized the importance of laddering products "to smooth generation rates and provide rate stability."[428] To characterize it as conjecture is simply wrong.

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[422] OCC Ex. 13 at 52 (Kahal).

[423] PUCO Staff Ex. 16 at 2-3 (Strom).

[424] Id. at 3-4.

[425] AEP Ohio Brief at 12.

[426] Id.

[427] OCC Witness Kahal testified that both Maryland and New Jersey use overlapping supply contracts to lessen potential rate volatility. OCC Ex. 13 at 51 (Kahal).

[428] *In the Matter of Ohio Edison Company, the Cleveland Electric Illuminating Company, and the Toledo Edison Company for Authority to Provide for a Standard Service Offer Pursuant to Section 4928.143, Revised Code, in the form of an Electric Security Plan*, Opinion and Order at 56 (July 18, 2012).

Moreover, it would appear that the biggest impediment to the laddering approach is AEP Ohio's belief that it has a unilateral right to terminate after a two-year period. But, as discussed supra, AEP has no authority to unilaterally terminate its ESP. If the PUCO correctly rules that AEP Ohio does not have the unilateral right to terminate, then there will be no reason that the auctions cannot be appropriately structured (with laddering) to address volatility in rates that might otherwise detrimentally affect customers.

After all, AEP Ohio acknowledges that generation pricing volatility is a problem.[429] That is the purported reason AEP Ohio proposes the PPA Rider. So if mitigation of rate volatility in the generation market is a vitally important policy objective for the PUCO, as AEP Ohio argues, then AEP Ohio should not advocate for a SSO contract portfolio that contributes to that volatility.

OCC has proposed a relatively simple and non-intrusive fix to AEP Ohio's portfolio. OCC proposes moving to a very reasonable 50/50 mix of one year and two year contracts in place of the mostly yearly contracts. This will significantly improve contract laddering, mitigate rate volatility for SSO customers, and reduce market-timing risk without in any way disrupting AEP Ohio's competitive bid process framework. The PUCO should adopt OCC's recommendation.

[429] See, e.g., AEP Ohio Ex. 2 at 13 (Vegas).

G. Financial Issues

1. AEP Ohio's proposed equity cost of 10.65% is unreasonable for charging to customers and should not be adopted. Instead, an equity cost of 9% should be used as recommended by OCC Witness Woolridge.

AEP Ohio requested authority to charge customers for profit at a rate of return based on a 10.65% equity cost rate.[430] The 10.65% return on equity was derived from a discounted cash flow ("DCF"), Empirical Capital Asset Pricing Model ("ECAPM"), and Utility Risk Premium ("URP") analyses conducted by Dr. Avera.[431]

OCC instead proposed a return on equity rate of 9% as recommended by OCC Witness Woolridge.[432] Dr. Woolridge's return on equity ("ROE") was developed under a discounted cash flow analysis and the traditional Capital Asset Pricing Model ("CAPM"). Accepting Dr. Woolridge's recommendation would mean adopting a weighted cost of capital (or rate of return) of 7.45% as opposed to the 8.24% proposed by Dr. Avera.

Dr. Woolridge testified that there are a number of reasons why a 9% ROE is appropriate and fair for AEP Ohio in this case. Most importantly, after the completion of corporate separation and transfer of its generation assets to an affiliate on December 31, 2013, AEP Ohio is now a distribution-only electric utility. As a wires-only entity, AEP has lower risk than it had as an integrated generation, transmission, and distribution owner.

In its Brief, OCC also presented legal arguments to support its filed recommended return on equity. These legal arguments included reference to the windfall to AEP Ohio, from the Ohio Supreme Court decision earlier this year.[433] That windfall permitted AEP

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[430] AEP Ohio Ex. 19 at 5 (Avera).

[431] AEP Ohio Ex. 19 (Avera).

[432] OCC Ex. 12A (Woolridge).

[433] *In re: Application of Columbus S. Power Co*., 2014-Ohio-462, ¶56.

Ohio to keep $368 million in Provider of Last Resort ("POLR') charges collected from its customers. OCC argued that the windfall to AEP Ohio, funded by customers, should be re recognized by the PUCO as a factor for reducing the profit that the PUCO sets for AEP Ohio to charge customers (and for maximizing the return to customers of any significantly excessive profits).[434]

In AEP Ohio's Brief, AEP Ohio claims that OCC's recommendations should be rejected.[435] AEP Ohio characterizes Dr. Woolridge's recommendation as producing an inordinately low ROE result, and concludes that the result stems from his taking a different approach from Dr. Avera on a number of issues.[436] And while AEP Ohio then goes on to explain Dr. Avera's approach, it does not say how Dr. Woolridge's approach is wrong.

AEP Ohio defends Dr. Avera's exclusion of 25% of the results under his discounted cash flow analysis. OCC Witness Woolridge described the approach as a "very significant error."[437] According to AEP Ohio Dr. Avera was just following the procedure that the FERC prescribes.[438] Additionally, AEP Ohio claims it would be illogical to include DCF results in the analysis that are at or below the long-term corporate bond rates.

Apart from the fact that FERC does not control how the PUCO should conduct its discounted cash flow analysis, AEP Ohio's representation is not correct. In FERC's discounted cash flow analysis FERC uses the <u>current</u> utility interest rate plus 100 basis

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[434] See, e.g., *In the Matter of the Application of The Cincinnati Gas & Electric Company for an Increase in Electric Rates in its Service Area,* Case No. 91-410-EL-AIR, Opinion & Order at 206 (May 12, 1992).

[435] AEP Ohio Brief at 11-112.

[436] Id.

[437] OCC Ex. 12 at 62 (Woolridge).

[438] AEP Ohio Brief at 112.

points to establish the low-end outlier test.[439] Dr. Avera, on the other hand uses projected utility interest rate plus 100 basis points to establish low-end outliers. Further it is not illogical to include in the DCF results that are at or below long term corporate bond rate. When a median is used, as Dr. Woolridge recommended, the impact of outliers is minimized.[440] With the use of a median, there is no asymmetry like that which occurs when Dr. Avera excludes the results of 25% of his DCF analysis.

AEP Ohio also defends the earnings per share ("EPS") growth rates that Dr. Avera used in his DCF analysis.[441] Dr. Avera used Wall Street analysts and Value Line estimates of earnings per share in his DCF analysis. AEP Ohio claims that analysts' and Value Lines' estimates of EPS growth rates proved to be the best source for estimating investor growth rates.[442]

But Dr. Avera provides no evidence to back up this claim. Additionally, most data on Value Line and Yahoo is historical data. By Dr. Avera's own admission, investors ignore this.[443] Dr. Woolridge alternatively testified that the DCF model should incorporate the dividend growth rate, not the earnings growth rate.[444] And Dr. Woolridge presented evidence, in the form of studies that concluded that relying on analysts' growth rate forecasts leads to an upward bias in cost of equity capital estimates.[445]

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[439] See, e.g., *Martha Coakley, Massachusetts Attorney General et al. v. Bangor Hyrdro-Electric Co.*, et al., Docket No. EL11-66-01, Opinion No. 531, Order on Initial decision at ¶122 (June 19, 2014).

[440] OCC Ex. 12 at 62 (Woolridge).

[441] AEP Ohio Brief at 112.

[442] Id.

[443] AEP Ohio Ex. 19 at 25. (Avera).

[444] OCC Ex. 12 at 6 (Woolridge).

[445] See OCC Ex. 12, Appendix B (Woolridge).

AEP Ohio also defends Dr. Avera's equity risk premium approach, which it offers as an alternative benchmark to show that his discounted cash flow analysis is reasonable. AEP Ohio describes Dr. Avera's approach as "straightforward." [446] AEP admits that Dr. Avera's analysis is based on historic authorized ROEs, which then serve as a basis for the future expected growth rate. But, as Dr. Woolridge testified, Dr. Avera's approach overstates the equity cost rate in several ways.[447] The base yield is in excess of investor return requirements. Dr. Avera's method produces an inflated measure of risk premium because it relies on historic yields and not projected yields.[448] Most importantly, the risk premium approach used by Dr. Avera measures commission behavior and not investor behavior.[449]

AEP Ohio also supports Dr. Avera's flotation cost estimate, describing it as being derived from a "very conventional and conservative method."[450] Dr. Avera's flotation cost estimate is part of the risk premium approach that Dr. Avera uses as a benchmark to show that his recommended ROE is reasonable. Dr. Avera made an upward adjustment to the cost of equity of 0.12%. This unreasonably increased the cost of equity under the risk premium approach.

Dr. Woolridge testified that such an adjustment is erroneous for a number of reasons.[451] First, Dr. Avera did not identify any flotation costs for AEP Ohio. Second, Dr. Woolridge testified that the market-to-book ratios for electric companies suggest a

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[446] AEP Ohio Brief at 112.

[447] OCC Ex. 12 at 76-77 (Woolridge).

[448] Id.

[449] Id.

[450] AEP Ohio Brief at 113.

[451] OCC Ex. 12 at 78 (Woolridge).

flotation cost reduction (not an increase) to the equity cost rate.[452] Third, there is no need for flotation costs when shareholders are realizing an increase in the book value per share of their investment, not a decrease. Fourth, flotation costs are not expenses that must be collected through the regulatory process.[453] And while AEP Ohio believes it should be compensated for transaction costs like flotation costs, it has not accounted for other transaction costs (i.e. like brokerage fees) that would lead to downward adjustments to the equity cost rate.[454]

Finally, AEP Ohio's contention that Dr. Woolridge's recommendation is "inordinately low" is inconsistent with the current market data. There are three facts that support this observation. First, as Dr. Woolridge demonstrates, there has been a downward trend in authorized ROEs for electric utilities in recent years. In 2013, the average ROE for electric utilities was 9.8%.[455] Second, Dr. Woolridge highlights that his recommendation of 9.0% is in line with the average ROEs earned by the Electric and Avera Proxy Groups. These groups are currently earning 9.1% and 8.2%, respectively.[456] Finally, Dr. Woolridge also demonstrates that Utilities have been the best performing sector in the S&P 500 in 2014, with returns in excess of 11% while the S&P 500 has been relative flat.[457] The earned ROEs for the proxy groups, in combination with the outstanding stock market performance of utilities, clearly demonstrates the reasonableness of the 9.0% ROE recommended by Dr. Woolridge. A 9.0%

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[452] OCC Ex. 12 at 79(Woolridge).

[453] Id. at 79-80.

[454] Id.

[455] Id. at 56.

[456] Id. at 59.

[457] Id. at 58.

recommendation is "more than adequate" and meets investors' expectations. AEP Ohio has not refuted any of these observations.

2. If a carrying charge is approved for AEP Ohio's riders, customers should be protected from paying excessive charges by basing the carrying charge on the most recent PUCO-determined cost of long-term debt, not on the weighted average cost of capital.

OCC recommends the PUCO adopt a carrying cost rate of 5.34% for all riders (except the DIR, if approved) approved by the PUCO in this proceeding with capital investments and deferral balances.[458] The 5.34% is the cost of long-term debt for the AEP Ohio approved by the PUCO in its most recent distribution rate case.[459] The 5.34% carrying charge is applicable to the following riders if they are approved by the Commission: the gridSMART Rider, the ESSR, the NCCR, the SDR, and the NCCR.

OCC's recommended 5.34% carrying charge rate is based on PUCO precedent.[460] Accepting a lower carrying charge than that proposed by AEP Ohio will lower the amount of money the utility is collecting from customers who are already paying the highest electricity bills in Ohio. OCC's recommendation in setting the carrying charge at the approved cost of long-term debt is reasonable and should be approved. OCC's recommendation is consistent with what the PUCO decided in AEP Ohio's last ESP case. And, the PUCO's own Staff also recommended setting a carrying charge based on the latest approved cost of long-term debt.[461]

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[458] OCC Brief at 146.

[459] Id. at 143.

[460] See, e.g., *In the Matter of the Application of The Dayton Power and Light Company for Authority to Modify its Accounting Procedure for Certain Storm-Related Service Restoration Costs,* Case No. 12-3281-EL-AAM, Finding and Order at ¶7 (Dec. 19, 2012).

[461] PUCO Staff Brief at 57.

AEP Ohio's request that a WACC (Weighted Average Cost of Capital) be used as for riders designed to recover capital investments and deferred expenses is unreasonable and should be rejected by the PUCO.[462] First of all, it is contrary to precedent established in numerous PUCO cases.[463] While AEP Ohio seeks to distinguish this case from its ESP II case (where the PUCO ruled that the financing costs should be based on long-term debt), it does not succeed in doing so. Its assertion that a lingering recession is the only reason that the PUCO adopted the cost of long-term debt as the carrying charge in the ESP II case is simply not true.[464] In many cases before and after the AEP Ohio's ESP II case, the PUCO routinely ordered the carrying charges be set at the most recently approved cost of long-term debt.[465]

Second, AEP Ohio completely ignored the significantly additional costs that customers would pay if the carrying charge rate is increased from 5.34% to 10.86%. This is especially troublesome given that AEP Ohio's customers are already paying the highest monthly electricity bill in Ohio.[466]

It would appear that AEP Ohio is not concerned about the detrimental effect of its proposed carrying charge rate for its customers. For example, AEP Ohio argued that the impact of the proposed ESP will have on customers' total bills should be ignored in

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[462] AEP Ohio Brief at 105.

[463] OCC Brief at 143-145.

[464] AEP Ohio Brief at 114.

[465] See, e.g., *In the Matter of the Application of The Dayton Power and Light Company for Authority to Modify its Accounting Procedure for Certain Storm-Related Service Restoration Costs*, Case No. 12-3281-EL-AAM, Finding and Order at ¶7 (Dec. 19, 2012), and *In the Matter of the Application of Duke Energy Ohio, Inc., for an Increase in its Electric Distribution Rates*, Case No. 12-1682-EL-AIR et al., Opinion and Order at 6 (May 1, 2013).

[466] OCC Brief at 144.

setting the ROE, a component of the weighted average cost of capital. [467] According to AEP Ohio, under the calculation provided by AEP Ohio Witness Roush, this is a non-issue because customers' total bills would actually be declining in most cases.[468] This is a half-truth given that many new cost items (such as the Purchase Power Agreement Rider) are ignored in his analysis.[469] AEP Ohio's estimated total bill impact also does not include any estimate of any final reconciliation of over/under recoveries (as of May 31, 2015) for any riders that will be ending such as the FAC or the Transmission Cost Recovery Rider ("TCRR").[470]

Nevertheless, assuming there is a decline in customers' bills, it cannot be ignored that the decline comes from moving to market-based power procurement. As a result of a significantly lower market rate for power, a customer's total monthly bill may be declining. This is forecasted by AEP Ohio to occur despite the numerous cost increases associated with the many riders it proposes. AEP Ohio essentially seeks to deny customers the cost savings from a lower market rates by proposing a higher financing costs through a carrying charge of 10.86%. AEP Ohio also argues that a higher ROE, which is used to calculate the carrying charge, is justified because "the incremental cost of the Company's proposed ROE compared to OCC's proposal (of a lower ROE) is not large."[471] This is another half-truth because the quote describes the impact of the higher ROE on only one rider. The fact of the matter is that when the weighted average cost of

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[467] AEP Ohio Brief at 110.

[468] Id.

[469] AEP Ohio Exhibit 12 at 3; DMR-1 (Roush).

[470] Id. at 3.

[471] AEP Ohio Brief at 110.

capital ("WACC") is applied to the numerous riders and to untold amount of deferred expenses, the additional costs to AEP Ohio's customers would be quite significant.[472]

Third, AEP Ohio's citation to two U.S. Supreme Court cases and various financial theories in its brief does not support its position.[473] These two U.S. Supreme Court cases address the return on and return of the rate base items (or permanent properties or assets). They have nothing to do with the setting of a reasonable return (or carrying charge) on the regulatory assets created through deferred expenses.

AEP Ohio apparently does not understand that a regulatory asset created though a deferral of expenses is not a rate base item and does not earn a return equal to the WACC. In other words, the risk to an investor for providing funds for approved deferred expenses is significantly less than the risk for funding the construction of a power plant. Consequently, the allowed returns on deferred expenses should be much lower than the allowed return on the construction of a power plant. A reasonable WACC can be applied to the permanent properties (or assets) of AEP Ohio. But an approved cost of long-term debt is appropriate for calculating the carrying charge of deferred expenses.

OCC's recommendation to use a 5.34% carrying cost rate should be adopted by the PUCO. It makes sense and will not burden customers with undue and unwarranted financing costs.

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[472] OCC Brief at 144.

[473] AEP Ohio Brief at 114-116.

3. The threshold for protecting customers from Significantly Excessive Earnings should remain at 12% or be lowered, not raised to 15% as requested by AEP Ohio.

R.C. 4928.143(F) allows utilities to keep excessive earnings. Customers are protecting from paying "significantly excessive earnings." The PUCO has generally established, on a case by case basis, a method for setting a threshold that measures whether the earnings are significantly excessive. If the earnings (as measured by ROE) are above the adopted threshold, they must be returned to customers. On the other hand, if the earnings are below the ROE threshold the utility gets to keep them. The higher the SEET threshold the greater earnings the Utility retains. But from a customer's perspective the lower the SEET threshold, the more opportunity customers have for getting a refund back from the utility.

In its brief, AEP Ohio claims that a 15% SEET threshold (as measured by ROE) would be consistent with the SEET threshold that the PUCO set for AEP Ohio in previous proceedings and at least one other EDU, Duke Energy Ohio.[474] However, AEP Ohio conveniently ignored the fact that the PUCO has set a **current** SEET threshold of 12% for AEP Ohio that applies to 2013 to 2015.[475] AEP Ohio also has ignored the fact another Ohio EDU, Dayton Power and Light Company, has a **current** SEET threshold of 12%. This was approved in DP&L's most recent ESP proceeding, PUCO Case No. 12-

[474] AEP Ohio Brief at 146-147.

[475] *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Authority to Establish a Standard Service Offer Pursuant to Section 4928.143, Revised Code, in the Form of an Electric Security Plan*, Case No. 11-346-EL-SSO, Opinion and Order at 37 (Aug. 8, 2012).

0426-EL-SSO et al.[476] In the DP&L ESP decision, the PUCO specifically cited to the 12% threshold established in AEP Ohio's ESP II case.[477]

And, AEP Ohio has not demonstrated that a 12% SEET threshold should be increased to 15%. Instead, given that AEP Ohio has completed its corporate separation and transferred all its generation assets (with the exception OVEC), its SEET threshold should be reduced. AEP Ohio is now a wires-only electric utility. Therefore, its business and financial risk have decreased considerably, and its risk should decrease further in the future.[478] Given AEP Ohio's lower risk exposure now and in the future, any SEET threshold applicable to the proposed ESP should be lowered from, or at most, kept at its current level of 12%.[479]

AEP Ohio has not demonstrated that an increase in the SEET threshold from 12% to 15% is warranted. AEP Ohio's proposed SEET threshold should be rejected. Otherwise, AEP Ohio would be given a "much-too-expansive opportunity to charge customers for excessive profits."[480]

H. AEP Ohio Did Not Prove A Need For A Late Payment Charge That Would Impose More Costs On Customers, Making Retail Electric Service Even More Expensive For Customers, Especially Low Income And At-Risk Customers. The PUCO Should Reject The Late Payment Charge.

OCC opposed the AEP Ohio's first-ever proposal to charge its customers a late payment charge. There were a number of reasons why the PUCO should reject the

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[476] *In the Matter of the Application of The Dayton Power and Light Company for Approval of its Electric Security Plan*, PUCO Case No. 12-426-EL-SSO et al., Opinion and Order at 26 (Sept. 4, 2013) .

[477] Id.

[478] Id.

[479] OCC Brief at 148.

[480] Id.at 147.

proposal. First, AEP Ohio did not demonstrate a need for the charge. OCC pointed out that AEP Ohio did not provide any supporting documentation to demonstrate the number of customers that paid their bills late, how late those customers' payments were, or the financial impact caused by such late payments.[481]

Additionally, OCC noted its concerns that the late payment charge would have a negative impact on low income and at-risk customers because it would increase their electric rates that are already the highest rates in the state.[482] Customers that already struggle to afford their electric service would only be further negatively impacted by the addition of a late payment charge. This would especially impact low income and at risk customers that struggle to pay their bills on time due to financial constraints.

OPAE and APJN also opposed the late payment charge because it would be detrimental for customers on the Graduate PIPP program if they were not expressly exempted from paying this charge.[483] OPAE and APJN explained the purpose for the Graduate PIPP program was to help low income customers transition out of the PIPP program to a point where they do not need assistance in paying their utility bill.[484] The Graduate PIPP program serves an important public policy goal as well as helping to provide customers with affordable service. As noted by OCC Witness Williams, a late payment charge would only add to the already high priced electric service that AEP Ohio provides (the highest priced electric service in the State).[485]

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[481] OCC Brief at 150.

[482] OCC Brief at 150.

[483] OPAE and APJN Brief at 22.

[484] OPAE and APJN Brief at 22-23.

[485] OCC Ex. 11 at 4-7, 27-28 (Williams).

Although AEP Ohio proposed the late payment charge in direct testimony,[486] the Utility did not address the late payment charge in its Brief, and did not demonstrate a need for such a charge in this case. The lack of support for the Late Payment Charge in the Utility's brief illustrates the absence of backing for its proposal. AEP Ohio did not present any information regarding the number of customers that allegedly pay their bills late, how late those payments might be and the impact, if any, on the Utility's finances. The PUCO should reject the Late Payment Charge.

III. CONCLUSION

The overwhelming evidence adduced at the evidentiary hearing shows that AEP Ohio's Modified ESP does not pass the statutory test. Because of this, the Commission should modify the ESP and approve it. The Commission can also modify the ESP even if it determines that the statutory test is met, so long as the modifications are supported by the record.

OCC recommends numerous modifications to Ohio Power's ESP. These modifications include, but are not limited to, rejecting the PPA, declining to adopt the excessive charges associated with generation rates such as the Distribution Investment Rider, the Bad Debt Rider, NERC, Cybersecurity Rider, and the Sustained and Skilled Workforce Rider. The PUCO should also decline to impose on customers a late payment charge and the POR charge.

The PUCO should also reject excessive financing costs related to an overstated return on equity (10.65%) and a weighted cost of capital for carrying cost on investment and deferrals should be rejected. And the PUCO should reject

[486] AEP Ohio Ex.3 (Spitznogle).

the Utility's proposed 15% threshold for the significantly excessive earnings test. There should be no cost premium assigned to residential customers from the SSO auction. If the PUCO approves the Utility's proposed new distribution riders, it should allocate them according to tested and fair cost causation factors.

The modifications proposed by OCC are intended to ensure that the base generation rates of residential customers are reasonably priced, consistent with this policy objective under R.C. 4928.02(A). Reasonably priced electric service, in keeping with R.C. 4928.02(A), should be the end goal.

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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing Reply by the Office of the Ohio Consumers' Counsel has been served upon those persons listed below via electronic transmission this 15th day of August, 2014.

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