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

APPLICATION FOR REHEARING
BY
THE OFFICE OF THE OHIO CONSUMERS' COUNSEL

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March 27, 2015

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APPLICATION FOR REHEARING BY THE OFFICE OF THE OHIO CONSUMERS' COUNSEL

The Office of the Ohio Consumers' Counsel ("OCC") files this application for rehearing to oppose, inter alia, the newest utility claim for customers to subsidize power plants that are no longer regulated by the government.[1] In its Opinion and Order of February 25, 2015, the Public Utilities Commission of Ohio ("Commission" or "PUCO") approved a mechanism (a power purchase agreement rider) that could require customers to pay hundreds of millions of dollars to fund uneconomic generation. The PPA rider is unlawful and unreasonable under Ohio law. And the PUCO is preempted by the Federal Power Act from approving the Power Purchase Agreement.

The Opinion and Order approved, with modifications, Ohio Power's electric security plan ("ESP"), filed in these proceedings on December 20, 2013. Under the

[1] OCC is authorized to file this application for rehearing under R.C. 4903.10 and Ohio Adm. Code 4901-1-35.

modified ESP Ohio Power will collect increased rates from customers for the period June 1, 2015 to May 31, 2018.

The Opinion and Order was unreasonable and unlawful in the following respects:

ASSIGNMENT OF ERROR 1: When the PUCO did not rule on the federal preemption argument, it violated R.C. 4903.09. It should have found AEP Ohio's proposed power purchase agreement is preempted under the Federal Power Act.

A. AEP Ohio's proposed PPA rider is field preempted under the FPA because it would establish the wholesale market price AEP Ohio would receive for its sales into the PJM wholesale markets of the energy, ancillary services and capacity.

B. The PPA rider is preempted by the FPA under the doctrine of conflict preemption because it would have anti-competitive effects on wholesale markets.

ASSIGNMENT OF ERROR 2: The Commission's approval of a placeholder for a power purchase agreement ("PPA") rider ("PPA Rider") is unreasonable and unlawful.

A. The determination that the proposed PPA Rider may be included in an ESP and charged to all distribution customers under R.C. 4928.143(B)(2)(d) as a "financial limitation on customer shopping" contravenes legislative intent and is unlawful.

B. The PPA rider is unlawful because it does not provide rate stability or certainty to customers as required by R.C. 4928.143(B)(2)(d).

1. The Commission's order is unlawful because it approves a placeholder PPA rider that customers would fund that is not based upon facts of record, as required by R.C.4903.09.

2. The theory upon which the Commission adopted the placeholder PPA Rider that customers would fund is flawed and unreasonable.

C. Shopping and SSO customers already have available to them solutions to hedge against price volatility.

D. The PPA Rider provides an anti-competitive subsidy funded by customers under R.C. 4928.02(H). R.C. 4928.02(H) prohibits the recovery of non-competitive generation related costs through distribution rates paid for by utility customers.

E. The PUCO approved the PPA Rider which could require customers to pay an enormous amount of money for lost revenues when the cost of generation purchased from AEP's affiliate (or OVEC) is too high to compete in the PJM market. As such the PPA Rider is an unlawful transition charge and must be disallowed under R.C. 4928.39.

F. The PUCO erred in ordering an asymmetric "severability provision" without requiring that the PPA rider be collected subject to refund to avoid prejudice to AEP Ohio's customers.

G. The factors the PUCO directed the Utility to address in its future PPA proceeding were incomplete and unreasonable because they are skewed in favor of approving the PPA without fully considering the impact of the PPA on customers.

ASSIGNMENT OF ERROR 3: The PUCO unreasonably and unlawfully found that AEP Ohio's electric security plan, as modified, is more favorable in the aggregate to customers than a market rate offer.

A. The PUCO unreasonably considered the extension of the residential distribution credit rider as a benefit to customers under an electric security plan.

B. The PUCO unreasonably failed to consider the distribution investment rider revenues as quantifiable costs to customers under an electric security plan.

C. The PUCO erred by approving a placeholder PPA and further erred by attributing no cost to the PPA when customers could end up paying millions of dollars.

D. The PUCO erred by unlawfully considering qualitative benefits as part of the ESP v. MRO test.

a. The PUCO erred in identifying factors under R.C. 4928.02 as qualitative benefits provided to customers under an electric security plan.

b. The PUCO erred in identifying the transition to market-based rates as a qualitative benefit to customers under an electric security plan.

c. The PUCO erred in ascribing customer benefits of the distribution investment rider only to the electric security plan and not the market rate offer.

ASSIGNMENT OF ERROR 4: The Public Utilities Commission erred when it ordered customers to fund excessive profits (a return on equity of 10.20 percent) for a distribution-only utility equal to those it ordered for the integrated utility four years ago.

A. The PUCO's determination was unreasonable because it did not lower customer-funded profits (return on equity) to account for the lower risks the Utility now faces. Those lower risks include the fact that AEP Ohio is now a distribution-only utility (without the more risky generation business) and collects virtually all of its revenues from customers through riders. Additionally, interest rates and other costs of capital have declined in the last four years. These factors support a lower return on equity than the 10.2 percent return on equity granted.

B. The PUCO's order is unlawful because it is not based upon facts of record, as required by R.C. 4903.09.

C. The PUCO unreasonably relied upon an ROE for the Utility that was agreed to as part of a comprehensive settlement of a prior case.

D. The PUCO's determination was unreasonable because it failed to consider factors that merit reducing the profit that customers must fund. These factors include a $368 million windfall for AEP Ohio for POLR charges collected from customers during the ESP II period, $508 million in customer funded stability charges and capacity charges collected during the ESP II period, and $499 million in deferred capacity charges.

ASSIGNMENT OF ERROR 5: The Commission is a creature of statute and as such can exert no authority beyond that which it has been granted.

A. The PUCO erred in rewriting R.C. 4928.143(B)(2)(d) to permit a financial limitation on shopping.

B. The PUCO erred in allowing AEP Ohio to collect unlawful transition revenues in contravention of R.C. 4928.38.

C. The Commission exceeded its authority in performing the more favorable in the aggregate test, set forth in R.C. 4928.142.

D. The PUCO unlawfully relies upon state policy to consider qualitative benefits under the ESP vs. MRO test.

The reasons in support of this application for rehearing are set forth in the accompanying Memorandum in Support. The PUCO should grant rehearing and abrogate or modify its Opinion and Order as requested by OCC.

Respectfully submitted,

BRUCE J. WESTON
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MEMORANDUM IN SUPPORT

I. INTRODUCTION

Ohio Power's 1.4 million customers pay the highest electric rates in the state. Sadly, customers will pay even more because of the PUCO's decision in this case. The PUCO voted to approve, with modifications, Ohio Power's electric security plan.

While the PUCO did deny some of Ohio Power's many requests for customer funding, it nonetheless allowed the Utility to implement a costly electric security plan in lieu of a market-based plan. The approved electric security plan ("ESP") permits Ohio Power ("Utility") to collect excessive profits, based on a 10.2 percent return on equity. Yet, the electric security plan was shown to be more expensive to customers than a market-based approach or market rate offer ("MRO").[2]

And, if Ohio Power is successful in justifying the jewel of its case--a power purchase agreement--customers will potentially be facing hundreds of millions of dollars

[2] See OCC Ex. 13 at 25 (Kahal).

more in future rate increases because of the PUCO's decision. While the PUCO conceptually approved the power purchase agreement as a tool to stabilize customers' rates, the price tag of alleged (not proven) stability--hundreds of millions of dollars—is just too high for consumers. It's a bad deal for customers, which unnecessarily enriches the Utility's shareholders.

OCC applies for rehearing on these issues and asks the PUCO to grant rehearing so that customers can get some relief from the exorbitant electric rates they are paying—rates higher than the rates paid by customers in thirty two other states.[3]

II. STANDARD OF REVIEW

Applications for rehearing are governed by R.C. 4903.10. The statute allows that, within 30 days after issuance of a PUCO order, "any party who has entered an appearance in person or by counsel in the proceeding may apply for rehearing in respect to any matters determined in the proceeding." OCC filed a motion to intervene in this proceeding on December 24, 2013, which was granted by Entry dated April 24, 2014. OCC also filed testimony regarding the Application and participated in the evidentiary hearing on the Application.

R.C. 4903.10 requires that an application for rehearing must be "in writing and shall set forth specifically the ground or grounds on which the applicant considers the order to be unreasonable or unlawful." In addition, Ohio Adm. Code 4901-1-35(A) states: "An application for rehearing must be accompanied by a memorandum in support, which shall be filed no later than the application for rehearing."

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[3] EIA Table 5.6b.

In considering an application for rehearing, R.C. 4903.10 provides that "the commission may grant and hold such rehearing on the matter specified in such application, if in its judgment sufficient reason therefor is made to appear." The statute also provides: "[i]f, after such rehearing, the commission is of the opinion that the original order or any part thereof is in any respect unjust or unwarranted, or should be changed, the commission may abrogate or modify the same; otherwise such order shall be affirmed."

The statutory standard for abrogating some portions of the Order and modifying other portions is met here. The Commission should grant and hold rehearing on the matters specified in this Application for Rehearing, and subsequently abrogate or modify its Opinion and Order of February 25, 2015.

III. ARGUMENT

ASSIGNMENT OF ERROR NO. 1: When the PUCO did not rule on the federal preemption argument, it violated R.C. 4903.09. It should have found AEP Ohio's proposed power purchase agreement is preempted under the Federal Power Act.

The PUCO should reconsider and reverse its rulings approving AEP Ohio's proposed Purchased Power Agreement ("PPA") Rider as a placeholder because the proposal is preempted by the Federal Power Act. The exercise of state authority in violation of the federal act is a violation of the Supremacy Clause of the U.S. Constitution, Article 6, c. 2. The PUCO's exercise of jurisdiction raises the same concerns that led the Third Circuit Court of Appeals in *PPL EnergyPlus, LLC, et al. v. Solomon*, 766 F.3d 241 (3rd Cir. 2014) ("*Solomon*") and the Fourth Circuit Court of Appeals in *PPL EnergyPlus, LLC, et al. v. Nazarian,* 753 F.3d 467 (4th Cir. 2014)

("*Nazarian*") to strike down the New Jersey and Maryland contracts for differences programs under the doctrine of field preemption.

In its February 25, 2015 Opinion and Order in this proceeding ("Opinion and Order"), the Commission authorized AEP Ohio to establish a placeholder PPA Rider. It approved the rider at an initial rate of zero, for the term of the ESP. It did so, finding that there "may be value for consumers in a reasonable PPA rider proposal that provides for a significant financial hedge that truly stabilizes rates, particularly during periods of extreme weather." Opinion and Order at 25. The Commission left the door open for AEP Ohio to submit a revised proposal in a future proceeding. *Id.* The Commission then noted that several parties raised federal preemption concerns, but declined "to address constitutional issues raised by the parties in these proceedings, as, under the specific facts and circumstances of these cases, such issues are best reserved for judicial determination." *Id.* at 26.

The threshold question that any agency must ask is whether it has the legal authority to act on the matter before it. The United States Court of Appeals for the Sixth Circuit found that:

> The APA establishes a scheme of "reasoned decision making." *Motor Vehicle Mfrs. Ass'n of United States, Inc. v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 52, 103 S.Ct. 2856, 77 L.Ed.2d 443 (1983). "*Not only must an agency's decreed result be within the scope of its lawful authority,* but the process by which it reaches that result must be logical and rational." *Allentown Mack Sales and Service, Inc. v. National Labor Relations Bd.*, 522 U.S. 359, 374, 118 S.Ct. 818, 139 L.Ed.2d 797 (1998).

Coalition for Government Procurement, et al. v. Federal Prison Industries, Inc., 365 F.3d 435, 475 (6th Cir. 2004) (Emphasis added).

The federal preemption concerns raised by OCC, IEU-Ohio, and others present this very threshold question with respect to the PPA Rider in this proceeding. But the PUCO sidestepped this important issue. Nonetheless, the PUCO asserted jurisdiction over the PPA rider. OCC and others are left to sort out the seminal question, with no ruling from the PUCO: is the PUCO's exercise of jurisdiction preempted, inter alia, by Federal Power Act, through the supremacy clause of the U. S. Constitution? The PUCO's failure to address those questions is contrary to R.C. 4903.09.

That statute prohibits the PUCO from issuing summary rulings and conclusions that do not develop the supporting rationale or record. *MCI Telecommunications Corp. v. Pub. Util. Comm*, (1987), 32 Ohio St.3d 306, 312, 313 N.E.2d. 803; *Indus. Energy Users-Ohio v. Pub. Util. Comm.*, 117 Ohio St.3d 486, 2008-Ohio-990, ¶30. Where contested cases are heard, R.C. 4903.09 requires the PUCO to address material issues raised by parties, including jurisdictional allegations. See e.g., *In the Matter of the Complaint of Westside Cellular, Inc., v. GTE Mobilnet Inc.*, Case No. 93-1758, Entry on Rehearing at ¶7 (Apr. 13, 1995); accord, *In re: Columbus S. Power Co.*, 128 Ohio St.3d 512, 2011-Ohio-1788, 947 N.E.2d 655, ¶71.

This jurisdictional issue was a material matter in this case. It is reversible error for the PUCO to not address whether its exercise of jurisdiction is precluded by federal acts or the U.S. Constitution. Because the federal preemption issues go to the heart of this Commission's authority to approve the PPA Rider at the outset, the Commission should reconsider its decision not to address those questions.

On reconsideration, the Commission should find that AEP Ohio's proposed PPA Rider is preempted under the Federal Power Act, 16 U.S.C. § 824d (2006) ("FPA"). This is because both the field and conflict federal preemption doctrines preclude the PUCO's exercise of jurisdiction. This would be consistent with the Third and Fourth Circuit Court rulings in *Solomon* and *Nazarian* respectively.

Field preemption applies when "Congress has legislated comprehensively to occupy an entire field of regulation, leaving no room for the States to supplement federal law." *Nazarian* at 474. The Fourth Circuit Court determined that the regulatory scheme for wholesale energy transactions set forth in the FPA "leaves no room either for direct state regulation of the prices of interstate wholesales of [energy], or for state regulations which would indirectly achieve the same result." *Id.* at 475*, citing N. Natural Gas Co. v. State Corporation Comm'n*, 372 U.S. 84, 91 (1963). Conflict preemption applies "where under the circumstances of a particular case, the challenged state law stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." *Nazarian* at 478, *citing Crosby v. Nat'l Foreign Trade Council*, 530 U.S. 363, 373 (2000).

Although the *Solomon* Court did not address the conflict preemption issue raised in the challenges to the New Jersey contract for differences program, (*Solomon* at 254-55), the Fourth Circuit did address that issue in *Nazarian*. There it found the contract for differences program in Maryland to be conflict preempted as well as field preempted under the FPA. *Nazarian* at 479. The Fourth Circuit reasoned that a state law may pose an obstacle to federal purposes "by interfering with the accomplishment of Congress' actual objectives, or by interfering with the methods that Congress selected for meeting those legislative goals." *Id.* at 478, *citing College Loan Corp. v. SLM Corp.*, 396 F.3d 588, 596 (4th Cir. 2005). It also determined that the Maryland program sought to directly override FERC's explicit policy choice regarding the provision of incentives for new entry under long-term contracts. *Id.*

The PPA Rider proposed by AEP Ohio seeks to accomplish similar objectives. It functions to override federal policy objectives: seeking to set the price for wholesale market transactions and to retain only economic generation in those markets. The PUCO's action is preempted under both the field and conflict preemption doctrines.

A. AEP Ohio's proposed PPA rider is field preempted under the FPA because it would establish the wholesale market price AEP Ohio would receive for its sales into the PJM wholesale markets of the energy, ancillary services and capacity.

The Courts in *Solomon* and *Nazarian* determined that the New Jersey and Maryland contract for differences programs "functionally set" wholesale capacity prices by determining the wholesale price to be paid under the contracts for differences. Thus the Courts determined that those programs were field preempted under the FPA. *Solomon* at 250, *Nazarian* at 476. The Fourth Circuit court found that the Maryland contract for differences program "supplant[s] the rate generated by the auction with an alternative rate preferred by the state." *Nazarian* at 476. The New Jersey and Maryland state programs required their electric public utilities to enter into 15 to 20-year contracts with a selected generator that would guarantee a fixed price for construction of a new generating plant. *Solomon* at 248, *Nazarian* at 473-74. The generator was obligated to bid the capacity into the PJM capacity auctions so that the resource cleared the auction. *Solomon* at 252; *Nazarian* at 473-74.

The contract for differences between the utilities and the generator required make-whole payments or credits for the capacity. *Id.* If the guaranteed contract price fell below the PJM capacity auction clearing price, the generator would provide the utilities with a make-whole credit to ensure that the generator received only the guaranteed contract price. *Id.* If the guaranteed contract price exceeded the PJM capacity auction clearing price, the utilities provided the generator with a make-whole payment to ensure that the generator received the guaranteed contract price. *Id.* The state programs then required the utilities to collect from their retail customers the make-whole payments made to the generator. Alternatively the state programs required the utilities to flow through to their retail customers the credits received from the generator to ensure that the utilities incurred no additional costs and no profit under the contracts for differences. *Id.*

The proposed AEP Ohio PPA Rider program works in substantially the same way. The Commission's approval of the PPA and the PPA Rider together comprise a program that contemplates AEP Ohio bidding the products purchased under the affiliated PPA with OVEC into the PJM auctions. This program would accomplish the same objective found preempted in the contracts for differences programs in *Solomon* and *Nazarian:* supplementing the PJM wholesale auction clearing prices with the revenues secured through out-of-market state subsidies. Moreover, in the case of the AEP Ohio PPA Rider, the "generator" is an affiliate. This raises additional concerns about cross-subsidization of AEP Ohio's marketing affiliates and the transfer of their business risks to Ohio consumers.

The only difference between the AEP Ohio proposed PPA Rider program and the state contract for differences programs found field preempted in *Solomon* and *Nazarian* is the identity of the entity that would bid the product into the PJM auction. In *Solomon* and *Nazarian*, that entity was the generator. In the PPA Rider program, the entity is the state-jurisdictional utility. That difference is irrelevant. The AEP Ohio PPA Rider, like the contract for differences in *Solomon* and *Nazarian,* ensures that the market participant would receive a customer-funded fixed payment for its sale into the PJM markets regardless of the PJM capacity auction clearing prices.

There is no merit to AEP Ohio's effort to shift the focus from its sales of the PPA products into the PJM wholesale markets, to the wholesale price set in the PPA for the sale by OVEC to AEP Ohio. It is not the PPA wholesale price that runs afoul of the FPA. Instead the issue is the effect of the retail rate rider programs on the PJM wholesale auction clearing prices for the energy, ancillary services and capacity products. Thus, there is no merit in AEP Ohio's argument that the PPA Rider simply reflects appropriate state regulation.[4] AEP Ohio argued that the PPA is a retail rate recovery mechanism that offsets the demand charges under the PPA with revenues received from "liquidating the power it purchased at FERC-approved rates from OVEC," and "is a common retail ratemaking technique."[5] However, the PPA rider does much more than offset demand charges under the PPA. It exists solely to supplement the revenues AEP Ohio will receive from bidding the products purchased under the PPA into the PJM markets.

Nor is there merit in AEP Ohio's argument that the PPA Rider program, unlike the state programs in *Solomon* and *Nazarian,* is a voluntary program that does not compel

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[4] Ohio Power Reply Brief at 51 ("Here, the Ohio Commission's order in this proceeding will have no effect on . . . the rates that AEP Ohio will receive when it resells that power to PJM"). Nothing could be further from the truth – Rider PPA is explicitly designed to supplement AEP Ohio's receipt of revenues from the PJM wholesale markets in order to ensure that AEP Ohio recovers all of its costs under the PPA.

[5] Ohio Power Reply Brief at 53-54.

a sale into the PJM markets.[6] The issue of whether the state compels the utility to enter into a contract, or simply sanctions a program proposed by the jurisdictional utility that supplements PJM market revenues with state commission-approved retail subsidies, is irrelevant. Regardless of whether the state compels the sale, or simply sanctions a retail subsidy for that sale, the effect on the PJM clearing prices is the same. The Commission's sanctioning of the program is preempted here.

It is by no means clear that AEP Ohio would have accepted the risk for the resale into the PJM wholesale markets of the energy, ancillary services and capacity purchased under the affiliated PPA had it been at risk for recovery of all or a portion of the associated costs. The PPA Rider would supplant the outcome of the PJM auctions with the revenues recovered under the rider in order to guarantee that AEP Ohio would fully recover its costs under the affiliated PPA. Just as the Fourth Circuit found in *Nazarian*, this state-sanctioned program "ensures that CPV [the market participant bidding the capacity into the PJM market under the Maryland program] receives a fixed price for every unit of energy and capacity it sells into the PJM auction, regardless of the market price." *Nazarian* at 476-77. It would supersede the PJM rates that the market participant would otherwise receive. The AEP Ohio PPA Rider is an attempt to set wholesale market prices. Who receives the subsidized payment (the utility or the generator) is not a distinguishing or determinative factor.

[6] Ohio Power Reply Brief at 51 (". . . it has not forced AEP Ohio (or any other local Ohio utility or retail supplier) to enter into a wholesale contract); *see also* Ohio Power Reply Brief at 54 ("Fourth, the PPAs are not the product of a state-initiated process or regulatory mandate like the programs that the courts addressed in Nazarian and Hanna [Solomon]. . . . the states initiated the programs, and ultimately legally compelled the local utilities (EDCs" to enter into the contracts as issue.").

B. The PPA rider is preempted by the FPA under the doctrine of conflict preemption because it would have anti-competitive effects on wholesale markets.

The proposed PPA Rider also is preempted under the conflict preemption doctrine. This is because the rider would affect PJM wholesale market clearing prices by allowing uneconomic generation (that would otherwise retire) to participate in the PJM auctions. This would undermine the competitive incentives FERC sought to facilitate in its wholesale market regime.[7]

OCC's witness James Wilson testified that his analysis of the $116 million net cost of the program suggests that the OVEC plants "may no longer be economic to operate" and that "the plants (or some units) should instead be retired or repowered."[8] Mr. Wilson also testified that the generation cost of one of the OVEC plants is in excess of AD Hub forward prices for off-peak hours in most months of the ESP Period, as shown in Exhibit JFW-4. He testified that this plant might be uneconomic, and called to run only infrequently, during off-peak hours in the coming years.[9] The IEU-Ohio likewise argued that the PPA Rider would insulate Ohio Power from market price risks, and place unregulated generation providers at a competitive disadvantage.[10]

The PPA Rider simply is not consistent with competition in the PJM wholesale power markets. It would constitute a subsidy analogous to the subsidies found to be

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[7] *Wholesale Competition in Regions with Organized Electric Markets*, Order No. 719 at P 1, FERC Stats. & Regs. ¶ 31,281 (2008) ("National policy has been, and continues to be, to foster competition in wholesale electric power markets."), *order on reh'g*, Order No. 719-A, FERC Stats. & Regs. ¶ 31,292; *order on reh'g*, Order No. 719-B, 129 FERC ¶ 61,252 (2009).

[8] *In the Matter of the Application of Ohio Power Company for Authority to Establish a Standard Service Offer Pursuant to R. C. 4928.143, in the Form of an Electric Security Plan*, PUCO Case No. 13-2385-EL-SSO *et al.*, OCC Initial Post-Hearing Brief at 69 (July 23, 2014), *citing* OCC Ex. 15A at 26-27 (Wilson).

[9] *Id.*

[10] Initial Brief of Industrial Energy Users-Ohio at 33 (July 23, 2014).

preempted in New Jersey and Maryland. It would make it difficult or impossible for generating units without subsidies to compete in the market. It would suppress prices in the PJM energy markets and negatively affect incentives for non-subsidized resources to build new generation in the region.[11]

The proposed narrow PPA Rider in AEP Ohio's case to recover only the costs associated with the relatively small OVEC entitlements is the tip of the iceberg as the industry struggles to retain base load resources (coal and nuclear) in an environment where future investment is steered toward lower-cost natural gas-fired resources. FirstEnergy's more expansive filing in Case No. 14-1297-EL-SSO seeking the costs associated with affiliated nuclear and coal generating facilities, if approved, would open the door to additional filings in Ohio (and perhaps other states).

But the concept should be rejected. The costs associated with uneconomic generation are a risk that was intended to be borne by market participants, not retail consumers.[12] AEP Ohio's PPA Rider, like the Maryland program in *Nazarian*, would "erode the effect of FERC determination and undermine FERC's exclusive jurisdiction." *Nazarian* at 477, *citing Appalachian Power Co. v. Pub. Serv. Comm'n.*, 812 F.2d 898, 904 (4th Cir. 1987).

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[11] The testimony of PJM's Independent Market Monitor, Dr. Joseph Bowring, in the FirstEnergy Operating Companies' ESP filing in *In the Matter of the Application 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 R. C. 4928.143, in the Form of an Electric Security Plan*, PUCO Case No. 14-1297-EL-SSO *et al.*, supports OCC's testimony regarding the deleterious effects of subsidizing uneconomic generation in wholesale markets. *See* Direct Testimony of Joseph E. Bowring on Behalf of the Independent Market Monitor for PJM at 3-4, filed in Case No. 14-1297-EL-SSO on December 22, 2014.

[12] *See, e.g.*, Order No. 719 at P 1 ("Effective wholesale competition protects consumers by providing more supply options, encouraging new entry and innovation, spurring deployment of new technologies, promoting demand response and energy efficiency, improving operating performance, exerting downward pressure on costs, *and shifting risk away from consumers*.") (Emphasis added).

The PPA Rider program will adversely affect bidding behavior in the wholesale competitive markets. The generators challenging the New Jersey and Maryland programs in *Solomon* and *Nazarian* were concerned that those programs would allow the subsidized generator to bid into PJM's capacity auctions at a price below the generator's actual cost. This would upset the intent of PJM's FERC-approved market rules to encourage new entry to bid at its cost of new entry. The generating facilities at issue in the AEP Ohio proposal are not new, but are existing facilities that are allowed to bid into PJM's capacity and energy markets at zero. There is no doubt that these out-of-market PPAs and the retail rate rider subsidies will disrupt PJM's wholesale markets and price formation rules which are designed to encourage bids at marginal costs and to deter uneconomic generation from participating in those markets. Allowing subsidized uneconomic generation to remain in the market will directly affect both the wholesale market clearing prices and the incentives for unsubsidized generators to invest in new generation in the region.

AEP Ohio proposed not to use the PPA purchases to supply Ohio retail customers in the state SSO competitive solicitation auctions, presumably so as to ensure a fully competitive auction process for SSO supply.[13] However, AEP Ohio does not explain why or how this purchased power would not adversely affect wholesale competitors and prices when it implicitly acknowledges the anticompetitive effects the purchases would have on retail competitors. The retail rate rider programs are in every respect the type of subsidy

[13] AEP Ohio Application at 8 (The energy and capacity associated with the Company's OVEC entitlement will simply be sold into the PJM market. Coupled with the non-bypassable nature of the rider, this will ensure that his provision of the Company's proposed ESP will have no adverse impact on the SSO auction or the ability of CRES providers to compete for customers on a level playing field.").

that merchant generators and the Market Monitor in PJM have often railed against – subsidies antithetical to the FERC wholesale market regime.

C. There is also no merit to AEP Ohio's miscellaneous arguments against federal preemption.

There is no merit in AEP Ohio's attempt to distinguish the proposed PPA Rider program from the state programs found preempted in *Solomon* and *Nazarian.* AEP Ohio argues that unlike the New Jersey and Maryland programs, the PPA Rider is not intended to incent investment in new generation. According to AEP, the proposed PPA Rider would encourage retention of existing plants through subsidized retail payments for energy and capacity. AEP comments that this differs from the New Jersey and Maryland programs in *Solomon* and *Nazarian* because those sought to encourage construction of new power plants through subsidized retail payments for capacity.

But the distinction between new and existing plants is irrelevant. The goal of both programs is to encourage investment in efficient and economic capacity, whether new or existing. Both goals are primary objectives of FERC's wholesale capacity and energy market regimes. To the extent that AEP Ohio's PPA Rider seeks to encourage retention of inefficient and uncompetitive existing facilities by supplementing the wholesale market prices with state retail revenues, it directly conflicts with the same federal wholesale market objectives recognized in the Maryland program. And the Fourth Circuit found the Maryland program was conflict preempted.

Nor can *Solomon* and *Nazarian* be distinguished from the PPA rider on the basis that those programs involved PJM's capacity market rather than PJM's energy market. While it is true that only capacity issues were before the Courts in *Solomon* and *Nazarian,* AEP's PPA Rider proposes to encompass sales into the PJM wholesale capacity market as well as into the wholesale energy and ancillary services markets. Moreover, the logic of the field and conflict preemption analyses is the same regardless of whether the market covers capacity or energy transactions. These are still wholesale market transactions subject to FERC's exclusive price-setting jurisdiction and FERC's policies underpinning the competitiveness of the wholesale markets.

AEP's argument that neither *Solomon* nor *Nazarian* prohibit all forms of state subsidies to encourage investment in generation is also mistaken. The Fourth Circuit determined that while states retain the right to encourage investment through subsidies, Maryland had chosen an "impermissible" approach of incentivizing generation "by setting interstate wholesale rates." *Nazarian* at 477-78. The PPA Rider similarly would encourage retention of existing generation by functionally setting the wholesale rate received by the utility bidding into the PJM wholesale markets the capacity, energy and ancillary services received under the PPA. The PPA Rider is no less disruptive and antithetical to the PJM wholesale markets than were the Maryland and New Jersey programs found preempted in *Solomon* and *Nazarian*. The PPA would allow uneconomic generation to participate in those markets contrary to FERC's policy objectives,

The Third Circuit also rejected in *Solomon* an argument similar to that raised by AEP Ohio --that the PPA Rider is merely a risk-hedging tool to protect Ohio retail consumers against the volatility of wholesale market prices.[14] The Third Circuit focused instead on the fact that the contracts set wholesale capacity prices. *Solomon* at 252. Moreover, the Third Circuit rejected arguments similar to that raised by AEP Ohio that there can be no conflict between the state and federal regulatory regimes because the PPA

[14] AEP Application, Case No. 13-2385-EL-SSO, Direct Testimony of Pablo A. Vegas in Support of AEP Ohio's Electric Security Plan at 13, ll. 13-17.

is a wholesale contract subject to FERC oversight. [15] The Court there reasoned that the argument conflated the inquiry into the field of regulation with an inquiry into the reasonableness of the contract prices. It found that what matters is not the reasonableness of the price, but the fact that the state program set the price in the first place. *Solomon* at 253.

Finally, there is no merit to AEP Ohio's argument in its Reply Brief that the PPA does not raise affiliate abuse concerns under FERC's affiliate restriction regulations.[16] The subsidized, out-of-market contract between AEP Ohio and its affiliate runs afoul of FERC's affiliate abuse restrictions. AEP Ohio argued to the Commission that FERC's criteria for analysis of affiliate abuse concerns do not apply to the PPA because OVEC is not controlled by the sponsoring companies in the same manner as the affiliate relationships underlying FERC's criteria.[17] Although in 2011 FERC did accept a contract between AEP Ohio and OVEC for the purchase by AEP Ohio of its OVEC entitlements to supply AEP Ohio's retail consumers, the current circumstances represent a significant departure from those present in 2011. Here, unlike the circumstances at stake in 2011, AEP Ohio plans not to supply its retail load with the energy, ancillary services and capacity purchased under the PPA. Rather it plans to subsidize its affiliate's generating facilities. That fundamental change in the nature of the contract warrants Commission reconsideration of the affiliate transaction issues. The PUCO should have addressed

[15] AEP Ohio Reply Brief at 5 3 ("Second, the contract between AEP Ohio and OVEC is already valid and accepted as a just and reasonable wholesale power contract under the Federal Power Act.").

[16] AEP Ohio Reply Brief at 55.

[17] AEP Ohio Reply Brief at 55-56.

concerns that approval of the PPA and the PPA Rider together, as a consolidated program, will run afoul of FERC's policy objectives rendering the program preempt under the FPA.

The Commission erred in failing to consider arguments challenging its legal authority to approve the PPA Rider. That rider, like the programs before the Third and Fourth Circuit Courts of Appeal in Solomon and Nazarian, seek to supplement the Utility's PJM market clearing revenues with subsidies garnered from a state-sanctioned program funded by customers. This means setting wholesale market prices and subverting FERC's policy objectives of encouraging investment in efficient and economic generation in wholesale markets. The Commission should find that its authority to approve the PPA Rider is preempted by the FPA under both the field and conflict preemption doctrines, through the supremacy clause of the U.S. Constitution. Rehearing should be granted and the PUCO's order abrogated or modified.

ASSIGNMENT OF ERROR 2: The Commission's approval of a theoretical placeholder power purchase agreement is unreasonable and unlawful.

A. Introduction

The most controversial portion of this proceeding was AEP Ohio's proposal to include, as a part of its ESP, a rider to require its customers to pay a return of and on its investment in the Ohio Valley Electric Corporation ("OVEC"). Specifically, AEP Ohio proposed to enter into a power purchase agreement with OVEC, under which it would purchase its share of OVEC power produced (the "OVEC Entitlement") and sell it into PJM Interconnection, LLC ("PJM"). AEP Ohio then would charge all of its distribution customers, through the PPA Rider, the difference between the PJM market value of its OVEC entitlement and its share of OVEC costs.

The evidence of record shows that, during the three-year ESP, the PPA Rider could cost Ohio consumers up to $116 million[18] -- in addition to the cost of their electric power supply secured from competitive retail electric service ("CRES") providers, or the standard service offer ("SSO"). Confronted with overwhelming evidence that the PPA Rider could result in significantly higher costs to consumers, the Commission rejected the PPA Rider for OVEC based on the record in this proceeding.[19] Specifically, the Commission found that the record did not support that the proposed rider would promote rate stability or benefit the public.[20]

Nevertheless, the Commission found that "the proposed PPA Rider would, ***in theory***, have the effect of stabilizing or providing certainty regarding retail electric service."[21] On this basis, it approved a "placeholder PPA Rider, at an initial rate of zero, for the term of the ESP."[22] The Commission instructed AEP Ohio to make a future filing "to justify any requested cost recovery,"[23] and offered advice on what that "future filing" should address.[24]

The Commission supported its determination by finding that a PPA Rider could theoretically meet the criteria of R.C. 4928.143(B)(2)(d). That provision identifies one of the provisions of an electric security plan as:

> Terms, conditions, or charges relating to limitations on customer shopping for retail electric generation service, bypassability, standby, back-up, or supplemental power service, default service,

[18] Order at 23; OCC Ex. (Wilson) 15A at 7; OCC Ex. 17.

[19] Order at 24-26.

[20] Order at 24.

[21] Order at 21 (Emphasis added).

[22] Order at 25.

[23] *Id*.

[24] *Id*.

> carrying costs, amortization periods, and accounting or deferrals, including future recovery of such deferrals, as would have the effect of stabilizing or providing certainty regarding retail electric service.

Specifically the Commission found that, in theory, a PPA Rider could meet these specific statutory requirements, in that the proposed PPA Rider would be:[25]

> (1) a charge,
>
> (2) relating to limitations on customer shopping,
>
> (3) as would have the effect of stabilizing or providing certainty regarding retail electric service.

OCC does not contest that the proposed PPA Rider would be a "charge" to consumers. However, OCC seeks rehearing of the Commission's determinations that the proposed PPA Rider relates to "limitations on customer shopping," and that the proposed PPA Rider would stabilize or provide certainty regarding retail electric service to customers.

B. The determination that the proposed PPA Rider may be included in an ESP and charged to all distribution customers under R.C. 4928.143(B)(2)(d) as a "financial limitation on customer shopping" contravenes legislative intent and is unlawful.

1. Background

AEP Ohio's proposed PPA Rider has nothing to do with stabilizing the rates of its customers. Instead, it has everything to do with the utility's attempt to make more money by continuing to require its customers to provide a return of and on its OVEC investment. By way of background, it should be noted that, because the contract to provide OVEC-generated power to the federal government was terminated in 2003, AEP Ohio's share of OVEC's output has been dedicated to supplying its SSO service.[26] However, in recent

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[25] Order at 20-22.

[26] AEP Ohio Initial Brief at 23; AEP Ohio Ex. 7 at 8-9 (Allen).

proceedings, AEP Ohio committed to divest its generating facilities[27] and provide 100 percent of its SSO supply through a competitive bid process ("CBP").[28] In its application in this proceeding, AEP Ohio kept its pledge to supply 100 percent of the SSO through a CBP. However, it did not divest all of its generating facilities because it retained its entitlement to a share of the OVEC power. Because its SSO now will be fully supplied by the CBP under R.C. 4928.143(B)(1), AEP Ohio no longer has statutorily prescribed authority to collect its share of OVEC generation from ratepayers. As a result, it attempts to argue that its share of OVEC power will not serve as a "physical" hedge to the supply of electric generating service under R.C. 4928.143(B)(1), but as a "financial" hedge. From there, AEP Ohio makes a leap of logic and claims that this financial hedge is authorized under R.C. 4928.143(B)(2)(d) under the fiction that it constitutes a "financial limitation on customer shopping."[29] And the PUCO took the leap as well.

2. The origin of the fictional "financial limitation on customer shopping."

Although the General Assembly permits items other than the supply of electric generating service under R.C. 4928.143(B)(1) to be included in an ESP, the Ohio Supreme Court limits such additional items to those expressly listed in R.C. 4928.143(B)(2)(a)-(i).[30] Notably, AEP Ohio failed to articulate in its application and direct testimony the express provisions of R.C. 4928.143(B)(2) under which it sought approval of the PPA Rider. Only on brief, did AEP Ohio offer that its PPA Rider was

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[27] *In Re Ohio Power Company*, Case No. 12-1126-EL-UNC, Finding and Order (October 17, 2012).

[28] *In Re Columbus Southern Power Company and Ohio Power Company*, PUCO Case No. 11-346-EL-ESP, Opinion and Order (August 8, 2012).

[29] AEP Ohio Initial Brief at 28.

[30] *In re Columbus S. Power Co.*, 128 Ohio St.3d 512, 2011-Ohio-1788, 947 N.E.2d 655 ("Columbus Southern").

permitted as a "limitation on customer shopping" under R.C. 4928.143(B)(2)(d).[31] Even then, it relied on the testimony of Ohio Energy Group ("OEG") witness Taylor for the proposition that Ohio's statutes permitted the PPA rider as a "***financial***" limitation on customer shopping.[32] Interestingly, AEP Ohio reached this determination despite the testimony of its own witness (Mr. Allen) who testified the PPA Rider was not a limitation on shopping.[33]

OEG witness Taylor's analysis is based upon his experience in the California electric markets.[34] In his direct testimony, he reasoned that a 100 percent reliance on a "marginal-cost electricity market"[35] (*e.g.*, a CBP) is unwise, and notes that California standard service supply portfolios are a balanced blend of "market purchases" (*e.g.*, competitive bids) from existing capacity and "purchased power agreements" with new capacity sources. [36] However, OEG witness Taylor's analysis of a blended supply portfolio offers nothing new to Ohio – this "physical" blend (or hedge) could have been obtained under R.C. 4928.143(B)(1), had AEP Ohio not committed to procure 100 percent of its supply through a CBP.[37] However, on cross-examination, OEG witness

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[31]AEP Ohio Initial Br., at 28. Indeed, on cross examination, AEP Ohio witness Allen agreed that the PPA rider was "clearly not" a limitation on customer shopping. Tr. II, at 566.

[32] AEP Ohio Initial Br., at 28. Tr. XI, (Taylor) at 2539, 2559 (Emphasis added).

[33]Tr. II at 566.

[34] OEG Ex. 1 (Taylor), at 6-11).

[35] OEG Ex. 1 (Taylor), at 7.

[36] OEC Ex. 1 (Taylor), at 7, 10-11). Significantly, according to Mr. Taylor's testimony, the purchased power agreements by California utilities to secure new capacity are entered subject to requests for proposals ("RFPs"). The RFPs permit the utilities to "evaluate responses, and negotiate contracts for best resources." *Id*. at 10. For this reason, AEP Ohio's theoretical PPA rider would be unreasonable and unlawful under R.C. 4928.02(A)(1), if it would permit AEP Ohio to enter into cost-plus contracts with its affiliates without an RFP.

[37] R.C. 4901.143(B)(1).

Taylor characterized what AEP Ohio has described as a "financial hedge,"[38] and a "financial limitation on customer shopping,"[39] without further explanation.

Nevertheless, the Commission adopted OEG witness Taylor's position. In doing so, it distinguished between a "physical" limitation on customer shopping (*i.e.*, a constraint on a customer's ability to switch generation service to a CRES provider), and a "financial" limitation. The Commission reasoned that under the PPA rider, five percent of a customer's bill would be based on the cost of service of the OVEC units and 95 percent on the "retail market."[40] Thus, relying on OEG witness Taylor's analysis, the Commission considers a "financial limitation on customer shopping" to occur when customers' bills do not reflect pricing that relies 100 percent on the competitive retail market. The Commission explained, "[e]ffectively * * * the proposed PPA rider would function as a "***financial restraint on complete reliance on the retail market"*** for the pricing of retail electric generation service.[41]

3. Common usage of the term "customer shopping" is synonymous with the term "customer switching" and reveals the General Assembly's intent under R.C. 4928.143(B)(2)(d) only to permit provisions in an ESP that would physically limit customer switching.

Key to the determination whether the PPA Rider constitutes a "limitation on customer shopping" is the interpretation of this phrase and, specifically, whether the phrase contemplates a "physical" or a "financial" limitation on customer shopping.

[38] Tr. I at 28 (Vegas).

[39] Tr. XI at 2539, 2559 (Taylor).

[40] Order at 22.

[41] Order at 22.

Resolution requires a determination of legislative intent. In this regard, R.C. 1.42 provides:

> Words and phrases shall be read in context and construed according to the rules of grammar and common usage. Words and phrases that have acquired a technical or particular meaning, whether by legislative definition or otherwise, shall be construed accordingly.

Initially, it must be observed that the Ohio Revised Code, as well as the Commission's and Ohio Supreme Court's precedent, are replete with references that use the term "shopping" synonymously with the word "switching."[42] Common usage dictates that the term "customer shopping" refers to customers who physically "switch" to CRES providers.

To accept OEG witness Taylor's interpretation, the Commission is required to read the word "financially" into the statute. Indeed, in an attempt to make any sense of Mr. Taylor's interpretation, the Commission was required to change the entire wording of the statute from permitting "limitations of customer shopping" to permitting a "***financial restraint on complete reliance on the retail market.***"[43]

Recently addressing the rules of statutory construction in Commission proceedings, the Ohio Supreme Court stated:

> When interpreting a statute, a court must first examine the plain language of the statute to determine legislative intent. *Cleveland Mobile Radio Sales, Inc. v. Verizon Wireless*, 113 Ohio St.3d 394, 2007-Ohio-2203, 865 N.E.2d 1275, ¶ 12. The court must give effect to the words used, ***making neither additions nor deletions from the words chosen by the General Assembly***. *Id. See, also, Columbia Gas Transm. Corp. v. Levin*, 117 Ohio St.3d 122, 2008-Ohio-511, 882 N.E.2d 400, ¶ 19. Certainly, had the General

[42] See, e.g., R.C. 4928.40(A)(1); *In Re Ohio Consumers' Counsel*, 109 Ohio St.3d, 206-Ohio-2110, 847 N.E.2d 1184, ¶ 21; *In Re Elyria Foundry*, 114 Ohio St.3d 305, 2007-Ohio-4146, 871 N.E.2d 970, at ¶ 72.

[43] Order, at 23.

> Assembly intended to require that electric distribution utilities prove that carrying costs were "necessary" before they could be recovered, it would have chosen words to that effect.[44] [Emphasis added.]

The Commission's addition of the word "financial" to the statute contravenes its plain meaning and the intent of the General Assembly to provide the Commission only with the authority to limit customer switching to CRES providers. Thus, the proper interpretation of the phrase at issue is that an ESP may include a provision relating to limitations on customers switching to a CRES provider. The Commission's determination that the phrase permits a "financial" limitation on customer shopping contravenes legislative intent, as determined by R.C. 1.42, and is unlawful. Moreover, without its express inclusion in the items listed in R.C. 4928.143(B)(2)(a)-(i), such a financial limitation is forbidden by *Columbus Southern*.

A general overview of the history of Ohio's attempts to deregulate its electric market confirms this legislative intent. Am. Sub. Senate Bill 3 ("SB 3"), enacted in 1999, was Ohio's first attempt at deregulation. That legislation required electric distribution utilities ("EDUs") to file electric transition plans and after a market development period, customers were to receive electricity from the competitive market. As a part of the legislation, the General Assembly enacted R.C. 4928.40(A)(1), which permitted the Commission to include in an EDU's electric transition plans:

> …such <u>***shopping incentives***</u> by customer class as are considered necessary to induce, at the minimum, a twenty per cent load <u>***switching rate by customer class***</u> halfway through the utility's market development period but not later than December 31, 2003. (Emphasis added).

[44] *In Re Columbus S. Power*, 138 Ohio St.3d 448, 2014-Ohio-462, 9 N.E.3d 1064, ¶ 26.

The Commission approved a stipulation adopting the FirstEnergy EDUs' electric transition plan, which provided for incentives to shoppers in the form of shopping credits and deferred the amount of the credit for subsequent collection by the EDUs. However, the stipulation also provided that, if more than a 20 percent shopping level were attained by the residential class of customers, the shopping credit incentives "may be adjusted in subsequent years as deemed appropriate to by the Commission to minimize deferrals." [45] In other words, the Commission had the ability to reduce the level of the shopping credit to limit the number of customers switching to CRES providers and, thus, limit the level of deferrals.

On July, 1, 2003, the FirstEnergy EDUs filed an application with the Commission to lower the shopping credits to limit shopping because of unexpectedly high deferrals. The Commission denied the request and instructed the FirstEnergy EDUs to file an application addressing the level of 2005 shopping credits for the post-market development period. It further encouraged the EDUs "to consider and develop plans for 2005 and beyond, which balance three objectives: ***rate certainty***, ***financial stability*** for the electric distribution utilities and competitive market development."[46]

The FirstEnergy EDUs filed their post-market development plan, known as a Rate Stabilization Plan ("RSP") on October 21, 2003, to encompass the period from 2006 through 2008.[47] Other EDUs subsequently followed suit. Subsequently, the Ohio Supreme Court, after reviewing a number of RSPs, recognized that the competitive

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[45] See, e.g., *In Re Ohio Consumers' Counsel*, 109 Ohio St.3d 328, 2006 –Ohio-2110, 847 N.E.2d 1184, ¶¶ 29-31.

[46] See, e.g., *In Re Ohio Consumers' Counsel*, 109 Ohio St.3d 328, 2006 –Ohio-2110, 847 N.E.2d 1184, ¶ 3. (Emphasis added).

[47] *In Re Ohio Edison Company, et al*., PUCO Case No. 03-2144-EL-ATA (Opinion and Order, June 9, 2004).

marketplace had not developed as expected under SB 3. It gently reminded the Commission of its duty to share its evaluations and reports on the effectiveness of competition with the General Assembly, so that it could evaluate the need for further legislation.[48]

Further legislation (SB 221) was enacted in 2008 that addressed changes to the competitive market, permitted EDUs to file ESPs, and permitted those ESPs to contain various provisions expressly listed in R.C. 4928.143(B). Not surprisingly, those provisions drew upon the regulatory experiences of the prior eight years and, germane to this proceeding, permitted "limitations on customer shopping…as would have the effect of stabilizing or providing certainty regarding retail electric service." In essence, R.C. 4928.143(B)(2)(d) merely codified the authority the Commission previously exercised in the post-market development period to limit customer switching to CRES providers.

This history, and the analysis under R.C. 1.42, clearly demonstrates the General Assembly's intent in permitting an ESP to limit customer switching to CRES providers. The Commission's interpretation, on the other hand, seeks to do something quite different by attempting to limit customers' exposure to the retail market, by including the OVEC cost of service as part of customers' bills. Had the General Assembly intended that R.C. 4928.143(B)(2)(d) have that effect it certainly knew how to fashion the language necessary to provide the PUCO such authority. For example, in designing the market rate offer ("MRO") contained in R.C. 4928.142, the General Assembly specifically provided

[48] *In Re Ohio Consumers' Counsel*, 114 Ohio St.3d 340, 2007-Ohio-4276, 872 N.E.2d 269, ¶41.

for the blending of the competitive bid price for a portion for the EDU's load with the EDUs generation service price for the remaining SSO load.[49]

The Commission's determination that R.C. 4928.143(B)(2)(d) permits a "financial" limitation on customer shopping contravenes legislative intent, as determined by R.C. 1.42, and is unlawful. Moreover, without its express inclusion in the items listed in R.C. 4928.143(B)(2)(a)-(i), such a financial limitation on customer shopping is forbidden by *Columbus Southern*.

C. The PPA Rider is unlawful because it does not provide rate stability or certainty to customers as required by R.C. 4928.143(B)(2)(d).

The Commission's order is internally inconsistent as to its finding that the proposed PPA Rider would have the effect of stabilizing or providing certainty regarding retail electric service for customers. On the one hand, it found that the proposed rider "in theory" would have the effect of stabilizing or providing certainty regarding retail electric service. In doing so, it relied on the testimony of AEP Ohio witness Vegas, who claimed that the rider would serve as a financial hedge to smooth out fluctuations in market prices because it would rise or fall opposite the direction of market prices.[50]

On the other hand, the Commission found that it was "unclear, based on the record evidence…how much the proposed PPA rider would cost customers and whether customers would even benefit from the financial hedge."[51] It disallowed the proposed PPA Rider, finding:

> The Commission must base our [sic] decision on the record before us [sic]. *Tongren v. Pub. Util. Comm.*, 85 Ohio St.3d 87, 706

[49] R.C. 4928.142(D).

[50] Order at 21.

[51] Order at 23.

> N.E.2d 1255 (1999). With that in mind, we are not persuaded that the PPA rider proposal put forth by AEP Ohio in the present proceedings would, in fact, promote rate stability, as the Company claims, or that it is in the public interest. There is considerable uncertainty with respect to pending PJM market reform proposals, environmental regulations, and federal litigation, as AEP Ohio acknowledges, and, in light of this uncertainty, the Commission does not believe that it is appropriate to adopt the proposed PPA rider at this time.[52]
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> * * *
>
> We conclude that AEP Ohio has not demonstrated that its PPA rider proposal, as put forth in these proceedings, should be approved under R.C. 4928.143(B)(2)(d).[53]

Yet, the Commission found:

> Nevertheless, the Commission does believe that a PPA rider proposal, if properly conceived, has the potential to supplement the benefits derived from the staggering and laddering of the SSO auctions, and to protect customers from price volatility in the wholesale market.[54]

As a result, the Commission authorized AEP Ohio to establish a "placeholder PPA [R]ider, at an initial rate of zero, for the term of the PPA." The Commission directed AEP Ohio to justify its PPA rider proposal in a "future filing," and proceeded to advise AEP Ohio of numerous criteria the proposal must address.[55]

1. The Commission's order is unlawful because it approves a placeholder PPA rider that customers would fund that is not based upon facts of record, as required by R.C.4903.09.

The factual record in this proceeding shows, and the Commission explicitly found, that AEP Ohio failed in its burden to show that its proposed PPA Rider would

[52] Order at 24.

[53] Order at 25.

[54] Order at 25.

[55] Order at 25.

provide rate stability or certainty for customers as required by R.C. 4928.143(B)(2)(d).[56] Nevertheless, it approved a "placeholder PPA [R]ider"[57] under the "theory"[58] that a "properly conceived"[59] PPA Rider proposal in a "future filing"[60] could meet the statutory requirements. Obviously, this record does not disclose the facts to be derived in the "future filing." Because the placeholder PPA is supported only by theory, and not facts admitted into the record in this proceeding, it violates R.C. 4903.09. *Tongren v. Pub. Util. Comm*., 85 Ohio St.3d 87, 706 N.E.2d 1255 (1999); *Ideal Transp. Co. v. Pub. Util. Comm.*, 42 Ohio St.2d 195, 326 N.E.2d 861 (1975), paragraph 2 of the syllabus ("The Public Utilities Commission must base its decision in each case upon the record before it."). Thus, it was unlawful for the Commission to adopt the placeholder PPA Rider that is premised on "theory" not facts in evidence.

Ohio's residential consumers are severely prejudiced by the Commission's approval of the placeholder PPA Rider in this proceeding because they are denied the factual information upon which to contest approval of the rider under R.C. 4928.143(B)(2)(d), either upon rehearing or appeal. Moreover, the rider currently is set at zero and the Commission intends to permit cost recovery in a "future proceeding" during this ESP's three-year term. As a result, Ohio's residential consumers currently are precluded from considering the rider's costs and other attributes in contesting, under R.C. 4928.143(C)(1), that the ESP is more favorable than a market rate offer ("MRO"). For

[56] Order at 25 ("We conclude that AEP Ohio has not demonstrated that its PPA rider proposal, as put forth in these proceedings, should be approved under R.C. 4928.143(B)(2)(d).").

[57] Order at 25.

[58] Order at 21.

[59] Order at 25.

[60] Order at 25.

this reason, as discussed subsequently, AEP Ohio cannot maintain its burden of proving its proposed ESP is more favorable than an MRO.

Accordingly, the placeholder PPA Rider must be denied. Additionally, if any subsequent rider is proposed, it must be filed and considered within the context of a subsequently filed ESP proceeding to permit the proper statutory evaluation under R.C. 4928.143(C)(1).

2. The theory upon which the Commission adopted the placeholder PPA Rider that customers would fund is flawed and unreasonable.

The PUCO found that the proposed PPA rider, in theory, would have the effect of stabilizing or providing certainty regarding retail electric service provided to customers. Of the erroneous opinion that OVEC costs are mostly fixed and stable,[61] the Commission found, in theory, that the PPA rider would create a credit when OVEC's costs are below wholesale market revenues, and would produce a charge when OVEC's costs are above wholesale market revenues. The Commission concluded that the rider would mitigate the effects of market volatility and provide customers with more stable pricing.[62]

None of AEP Ohio's witnesses presented any examples of the claimed price stability effect of the PPA Rider as part of the ESP application or in their direct testimony.[63] And AEP Ohio witness Allen specifically admitted that he had made no analysis of how much PJM wholesale prices had moved from year-to-year.[64]

[61] As stated below, this opinion contradicts the Commission's findings on the ***facts*** of record that it is unable to reasonably predict OVEC's costs (Order, at 24), particularly considering the uncertainty surrounding pending PJM market reform proposals, environmental regulations, and federal litigation. *Id*.

[62] Order at 21.

[63] OCC Ex. 15A at 29 (Wilson).

[64] Tr. XIII at 3295 (Allen).

Rather, in adopting its theory the Commission relied on a single, anecdotal example presented by AEP Ohio witness Allen on rebuttal as to the rider's effect. Mr. Allen testified that upon a $5.00/MWh change in market prices, the PPA rider would result in a $0.35/MWh credit – or charge – to consumers.[65] The record simply contains no evidence that the projected PJM market prices during the ESP period would be more volatile than the projected costs of OVEC.

Moreover, Mr. Allen's example, and the Commission's resulting theory, are expressly refuted by the evidence of record which shows that (1) OVEC's costs are not fixed and stable, do not remain constant over time, and will provide no incentive for OVEC to minimize its generation costs if a PPA rider is adopted; (2) the proposed PPA rider will not rise and fall in the opposite direction of the market, but is just as likely to move in the same direction of the market, resulting in even greater price volatility; and (3) that shopping and SSO customers already have available to them solutions to hedge against price volatility, rendering the PPA Rider needless and costly.

a. OVEC's costs are not fixed and stable and thus would not have the effect of stabilizing or providing certainty to customers.

As stated above, the Commission based its approval of the PPA rider, in theory, on its finding that OVEC's mostly fixed costs will remain relatively stable.[66] Indeed, AEP Ohio witness Allen's anecdotal example of how the proposed rider would operate assumed that OVEC costs remain constant. However, the evidence of record shows that

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

[66] Order at 21.

OVEC costs are sensitive to many factors, including plant outages, weather, soft energy prices, and general economic conditions.[67] Indeed, the record reveals a dramatic swing in OVEC costs from 2011 to 2012 of approximately 24 percent, from $50.86/MWh to $62.86 MWh.[68] These facts, coupled with the Commission's own admission that OVEC costs could be affected by yet-unknown changes to environmental regulations,[69] among other pending matters, conclusively demonstrate that the Commission's theory that OVEC costs remain stable is not supported by the record. Furthermore, if the proposed PPA rider is adopted, there will be no incentive for OVEC to control or minimize its costs of generation. This is because all costs of OVEC, no matter how high in comparison to the PJM market price, will be passed along and collected from AEP Ohio's customers.[70] This is bad news for customers.

b. The PPA Rider will not rise and fall in the opposite direction of the market, thus stability and certainty of rates for customers has not been proven

AEP Ohio witness Vegas testified that "OVEC's costs compared to market-based costs would smooth out market fluctuations as the rider will rise or fall in a direction opposite that of the market."[71] However, OCC witness Wilson explained that the one-year lag associated with PPA rider's reconciliation component to true up actual historical costs and revenues is about as likely to move in the same direction of the forecasted

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[67] Tr. II at 544-549; Order at 24.

[68] IEU Ex. 6 at 2; IEU Ex. 1B at EX. KMM-3 at 2.

[69] Order at 24.

[70] OCC Ex. 15A at 36-39 (Wilson).

[71] AEP Ohio Ex. 2 at 13 (Vegas).

PPA Rider as to move in the opposite direction.[72] The likelihood that the rider will move in the same direction of market prices will only exacerbate price volatility for consumers, rather than produce rate stability. Indeed, AEP Ohio witnesses Vegas[73] and Allen[74] agreed that the reconciliation component doesn't necessarily move counter to the market.

Nevertheless, the Commission approved the placeholder PPA Rider under the theory that, "[a]t its core, the PPA [R]ider is expected to move in the opposite direction of wholesale market prices."[75] The Commission's finding was based upon no comprehensive analysis of market trends or pricing, but only on the flawed, anecdotal example provided by AEP Ohio witness Allen.[76] But OVEC costs are subject to considerable variability. And there is not incentive to control costs by OVEC. Additionally, the true-up mechanism will add to the volatility of the PPA rider. Thus, it is illogical to conclude that there is any trend in OVEC costs relative to market pricing, much less that they move in opposite directions. To confirm as much, one need only to look at the wide range projected for the rider's cost to consumer – from a net credit of $8.4 million to a net cost of $116 million over the three-year ESP.[77] Indeed, AEP Ohio's own conflicting projections swung wildly. Its initial projection showed a net cost of $52 million during the ESP. Its revised analysis, based upon market data only one month

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[72] OCC Ex. 15A at 31 (Wilson).

[73] Tr. I at 50 (Vegas).

[74] Tr. II at 517 (Allen).

[75] Order at 21.

[76] Order at 21.

[77] Order at 23-24.

more recent, reflected an $8.4 million net credit.[78] Projections of the customer impacts of the proposed PPA Rider would be even more difficult, if not impossible, over a term longer than a three-year ESP.

D. Shopping and SSO customers already have available to them solutions to hedge against price volatility

The Commission also found that the proposed PPA Rider, in theory, would stabilize rates by smoothing out the market rates paid by shopping customers and the market-base rates paid by SSO customers. This finding is based on AEP Ohio's faulty premise that these customers are and will always be subject to the fluctuations of the hourly and day-ahead energy markets. This premise ignores that shopping customers can secure long-term contracts of up to three years at a fixed rate,[79] and SSO customers' rates already are stabilized by the laddering and staggering of the CBP.[80] They simply are not subject to the hourly and day ahead markets as AEP-Ohio assumes. Absent the PPA Rider, these market fluctuations would not affect their established rates.[81] Thus, the PPA Rider is not needed because CRES providers can provide products by which customers can elect the amount of price risk they wish to undertake, and the PUCO can address price volatility through the terms of the SSO product approved.

Considering all of the above, the PPA Rider would not have the effect of stabilizing or providing certainty for customers. Instead it could produce greater instability and higher prices for all customers. It thus fails to satisfy the requirements

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[78] Ohio Manufacturers' Association Energy Group ("OMAEG") Ex. 3; Tr. I at 110, Tr. II at 508-509 (Allen).

[79] AEP Ohio Ex. 33 at Ex. WAA-R-3; Tr. XIII at 3284-3285.

[80] Tr. XIII at 3279-3280.

[81] OCC Ex. 15A at 29-32 (Wilson).

under R.C. 4928.143(B)(2)(d), and cannot be authorized by the PUCO as part of AEP Ohio's ESP.

E. The PPA Rider is unlawful because it requires customers to fund an unlawful, anti-competitive subsidy under R.C. 4928.02(H).

On brief, OCC and other intervenors argued that the proposed PPA Rider violated R.C. 4928.02(H). That law prohibits anti-competitive subsidies flowing between competitive and non-competitive services. Familiarity with the history of this statutory provision is necessary for the proper determination of this issue.

This provision initially was enacted in 1999 as R.C. 4928.02(G) as a part of SB 3 and provided that it was the policy of this state to:

> Ensure effective competition in the provision of retail electric service by avoiding anticompetitive subsidies flowing from a noncompetitive retail electric service to a competitive retail electric service or to a product or service other than retail electric service, and vice versa.

Under SB 3, all generation service, including the generation service offered under the SSO, was considered to be competitive[82] and was exempted from the Commission's regulation.[83]

SB 221 changed this regulatory paradigm. It provided EDUs with the option to provide their electric supply through a competitive bid process under a market rate offer,[84] or by an ESP.[85] If an ESP was requested, the utility must prove that the price of

[82] R.C. 4928.03.

[83] R.C. 4928.05(A)(1).

[84] R.C. 4928.142.

[85] R.C. 4928.143(B).

its energy supply[86] and other terms and conditions[87] were more favorable in the aggregate than an MRO.[88]

Significantly, the General Assembly also revised R.C. 4928.05(A)(1). It removed generation from the services exempted from Commission regulation in the event the Commission exercised authority over the service under R.C. 4928.141 through 4928.144. It recognized that some generation service could be considered to be non-competitive. Accordingly, R.C. 4928.02(G) was amended (as R.C. 4928.02(H)), by adding the emphasized phrase below to make clear that it is unlawful (1) for a competitive generation service to subsidize a non-competitive generation service, or vice versa and (2) for "any" generation service rates – competitive or non-competitive – to be collected through distribution or transmission rates. R.C. 4928.02(H) now provides that it is the policy of this state to:

> Ensure effective competition in the provision of retail electric service by avoiding anticompetitive subsidies flowing from a noncompetitive retail electric service to a competitive retail electric service or to a product or service other than retail electric service, and vice versa, ***<u>including</u> by prohibiting the recovery of <u>any</u> generation-related costs through distribution or transmission rates.*** [Emphasis supplied.]

Thus, it is immaterial whether the PPA Rider is classified as a generation rate (as AEP Ohio and the PUCO contend) or a distribution rate (as OCC and many intervenors contend). No matter its classification, the PPA Rider is unlawful under R.C. 4928.02(H), as an anti-competitive subsidy.

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[86] R.C. 4928.143(B)(1).

[87] R.C. 4928.143(B)(2).

[88] R.C. 4928.143(C)(1).

1. **R.C. 4928.02(H) prohibits the recovery of non-competitive generation related cost through distribution rates paid for by utility customers.**

Although the PUCO (and AEP Ohio) characterize the PPA rider as a generation rate, it actually is a distribution rate under the authority of *In Re Ohio Power Company*, Case No. 10-1454-EL-RDR Finding and Order (January 11, 2012) ("*Ohio Power*"). In *Ohio Power,* AEP Ohio sought to recover the closing costs associated with its Sporn Unit 5 generating facility through a stand-alone rider, the Plant Closure Cost Recovery Rider ("PCCRR"). The costs included the unamortized plant balance that remained on AEP Ohio's books (approximately $56.1 million). Thus, the PCCRR rider clearly was a rate to recover the costs of generation-related service. However, AEP Ohio sought to recover the charge from all distribution customers as a non-bypassable charge, and it characterized the PCCRR rider in its application as a "distribution" charge. As discussed in more detail below, the PUCO denied AEP Ohio's request.

The PUCO attempts to distinguish this proceeding from *Ohio Power* solely on the basis that in *Ohio Power,* AEP Ohio classified the PCCRR as a distribution rate, while in this proceeding AEP Ohio has classified the PPA Rider as a generation rate. AEP Ohio's self-serving choice of nomenclature is not determinative of this issue. Indeed, in *Ohio Power*, the Commission recognized that whether a charge is to be classified as a distribution rate is dependent upon the class of customers to which it is applied. If a charge is applied to all distribution customers, it is considered a distribution rate. In *Ohio Power*, the Commission disallowed the PCCRR, finding:

> Additionally, the Commission notes that [AEP Ohio's] recovery of the closure costs would be contrary to the state policy found in Section 4928.02, Revised Code. That policy requires the Commission to avoid subsidies flowing from a noncompetitive retail electric service to a competitive retail electric service***. [AEP***

> ***Ohio] seeks to establish a nonbypassable charge that would be collected from all distribution customers by way of the PCCRR***.[89]

In this proceeding, under the *Ohio Power* rationale, the nonbypassable PPA Rider would also be charged to all distribution customers and, thus, be considered a distribution charge. The plain language of R.C. 4928.02(H) prevents the Commission from allowing recovery of ***<u>any</u>*** generation-related costs (be they competitive or non-competitive) through distribution rates. Because the PPA Rider charges all distribution customers for the cost of OVEC generation, it is a distribution rate and is prohibited by R.C. 4928.02(H).[90]

2. The subsidy customers are being asked to pay is anti-competitive.

Whether the PPA Rider is considered to be a generation rate or a distribution rate, it creates an anti-competitive subsidy by requiring AEP Ohio's customers to underwrite the costs of OVEC's generation. The PPA Rider requires ratepayers to guarantee that OVEC generation earns a profit by covering the difference in the revenues from the sale of the power and the cost of generation. This guarantee is a benefit to OVEC and AEP because AEP owns a large percentage of OVEC. In other words, it's a subsidy to AEP Ohio regardless of whether it produces a credit for retail customers in any particular year. It is a benefit that other competitive retail or wholesale providers do not enjoy, and thus is anti-competitive.[91]

Moreover, Staff witness Choueiki and OCC witness Wilson recognize other anti-competitive consequences of the PPA Rider. Each witness explains that the rider could

[89] *Ohio Power*, at 19 (Emphasis added).

[90] See *In Re Elyria Foundry Company*, 114 Ohio St.3d 305, 2007-Ohio-4164, 871 N.E.2d 1176.

[91] Constellation Ex. 1 at 12-14.

incent AEP Ohio to cause lower-cost OVEC power to be withheld from the market to the benefit of AEP Ohio's affiliate's unregulated generation in PJM.[92]

Whether considered a generation rate or a distribution rate, the PPA Rider is unlawful. It requires customers to provide an anti-competitive subsidy to OVEC and ultimately to AEP Ohio. OCC seeks rehearing to reject the PPA on this basis.

F. The PUCO approved the PPA rider that could require customers to pay an enormous amount of money for lost revenues when the cost of generation purchased from AEP's affiliate (or OVEC) is too high to compete in the PJM market. As such the PPA rider is an unlawful transition charge and must be disallowed under R.C. 4928.39.

In addition to providing AEP Ohio with an unlawful, anti-competitive subsidy, the PPA rider guarantees that AEP Ohio will collect from its customers a return of and on its investment associated with affiliate-owned generation (and OVEC). As OCC witness Wilson explained, these costs are considerable and for OVEC alone could amount to approximately $116 million during the term of a three-year ESP. This guarantee, which is meant to shelter AEP's generation from the realities of the competitive marketplace, constitutes an unlawful transition charge under R.C. 4928.38. In essence, it is a crutch for AEP Ohio to use at a time when Ohio law explicitly requires AEP Ohio to be "on its own in the competitive market."[93]

Unfortunately, the Commission's order devoted only a single sentence to this issue. It merely stated, "[n]either do we agree with the assertion that the PPA rider would permit AEP Ohio to collect untimely transition costs in violation of R.C. 4928.38."[94] The

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[92] OCC Ex. 15A at 38 (Wilson); Staff Ex. 18 at 13 (Choueiki).

[93] R.C. 4928.38.

[94] Order, at 26.

PUCO's failure to set forth the reasons prompting its decision on this issue, based upon findings of fact, violates R.C. 4903.09. Moreover, it prejudices consumers' ability to prosecute this application for rehearing and appeal, because they are unable to decipher the reasons behind the Commission's finding.

Nevertheless, the PPA rider clearly is a transition charge because it requires AEP Ohio's consumers to pay for AEP Ohio's (and its generation affiliate's) lost revenues. The lost revenues are created when the cost of OVEC generation (or other affiliated generation subject to a PPA) is higher than what it can be sold for in the PJM market.

When SB 3 was enacted in 1999, it permitted Ohio's electric utilities the opportunity to collect "transition revenues"[95] to "assist it in making the transition to a fully competitive retail electric generation market."[96] However, the recovery of transition charges was permitted for only a limited period of time.[97] Utilities could collect certain transition costs until the end of the market development period, which ended December 31, 2005.[98]

Moreover, the General Assembly emphatically provided that the Ohio electric utility was "wholly responsible for whether it is in a competitive position after the market development period," and further proclaimed that after the market development period concluded, the utility "shall be fully on its own in the competitive market."[99] In fact, R.C. 4928.38 prohibits the PUCO from authorizing transition revenues or "any equivalent revenues" except as provided by statute. And if this authority is not clear enough, R. C.

[95] "Transition revenues" are defined under R.C. 4928.39.

[96] R.C. 4928.37.

[97] R.C. 4928.38.

[98] R.C. 4928.38.

[99] R.C. 4928.38.

4928.141 also explicitly declares that a standard service offer, such as that which AEP Ohio seeks approval in this proceeding, "shall exclude any previously authorized allowances for transition costs."

The tens of millions of dollars that AEP Ohio could collect under the PPA Rider are transition revenues (or the equivalent of transition revenues) that the PUCO cannot impose on customers after the end of the statutory market development period, December 31, 2005.

AEP Ohio has had over 15 years, since the enactment of SB 3, to accept its responsibility to prepare for market. Indeed, it is only with this ESP proceeding that it seeks to procure its SSO electric supply 100 percent through a CBP for the term of the ESP. After this prolonged transition, it is more than time for AEP Ohio "to be on its own" with respect to the risks and rewards of all of its generating units as the General Assembly intended in the 1999 law. Accordingly, OCC seeks rehearing of the Commission's Opinion and Order that permits the PPA rider to function as an unlawful transition charge.

G. The PUCO erred in approving a "severability provision" without requiring that the PPA Rider be collected subject to refund to avoid prejudice to AEP Ohio's customers.

Under the PUCO's Order, AEP is required to commit in a future filing that, if a court invalidates the PPA Rider in a subsequent proceeding, all other provisions of the ESP will remain in effect. With this provision, the Commission (as well as many intervenors at hearing and on brief) recognize that the proposed PPA Rider is controversial and, if approved, will be challenged and is subject to reversal at the state and federal levels. Indeed, the Commission refused to pass on the considerable federal preemption and constitutional issues presented, in favor of subsequent judicial determination.

This places AEP Ohio's consumers in an untenable position if cost recovery is approved through the "future filing" and consumers are required to pay the PPA rider. If the rider is subsequently invalidated, customers may have no means to collect a refund, due to the Ohio Supreme Court's prohibition against retroactive ratemaking.[100] Accordingly, fairness to AEP Ohio's consumers requires that if PPA Rider cost recovery is approved, the rider should be collected subject to refund. Such a condition should not be objectionable to AEP Ohio who believes that it is possible for the PPA Rider to produce a credit, and undoubtedly would be looking for a means to take back from its customers unlawful credits. OCC seeks rehearing on this issue.

H. The factors the Commission ordered AEP Ohio to include in its "future filing" are unreasonable to the extent that they are biased toward supporting the Utility-proposed PPA Rider. The Commission must order AEP Ohio to include factors in a future filing that also assess the rider's benefits (or detriments) to AEP Ohio's consumers.

As stated previously, in approving the placeholder PPA Rider, the Commission advised AEP Ohio as to additional factors to include in a "future filing" for a PPA rider. The factors include:[101]

1) Financial need of the generating plant;
2) Necessity of the generating facility, in light of future reliability concerns and, including supply diversity;
3) Description of how the generation plant is compliant with all pertinent environmental regulations and its plan for compliance;

[100] See, e.g., *Keco Industries, Inc. v. Cincinnati & Suburban Bell Tel. Co.*, 166 Ohio St. 254, 141 N.E.2d 465 (1957) and its progeny.

[101] Order at 25.

4) The impact that a closure of the generating plant would have on electric prices and the resulting effect on economic development.

The factors that the Commission ordered AEP to include in a future filing appear to be biased toward building a case that would support approval for the Utility-proposed PPA Rider. Although the PUCO indicated that the PPA Rider must be shown to be reasonable and of benefit to customers,[102] it failed to require the Utility to address factors that would enable it to assess the benefits (or detriment) to customers. The Commission's list of factors is thus incomplete and unreasonable. It is skewed in favor of approving the PPA Rider without fully considering the PPA's impact on customers. Accordingly, OCC seeks rehearing in order that the PUCO, in fairness to consumers, order AEP Ohio to include the following factors in any "future filing:"

1) The total costs of the PPA Rider to the customers who are being asked to pay it (including bill impact statements through the entire period the PPA is in effect).

The Commission should consider the PPA Rider's impact on customers' bills before making a decision that imposes the costs of the PPA on customers. Additionally, the Commission should require AEP Ohio to provide alternatives to the PPA Rider that could be less costly or more beneficial (*i.e.*, less harmful) to customers than the PPA Rider.

2) The PPA's impact on PJM's competitive markets, including short-term markets, day-ahead and real-time markets, long-term markets, and the capacity market, as well as generation facility investment decisions.

[102] Order at 23.

As the record reflects, when plants are subsidized in a competitive market, the market can be detrimentally affected.[103] If the competitive market does not function properly, customers may lose the benefits they are entitled to under the law, including the benefit of reasonably priced retail electric service).[104] AEP Ohio should be required to address market effects of subsidized plants, including the impact on the plants' various bidding commitments and/or strategies on existing resources and the impact on investors' willingness to invest in new generation. AEP Ohio should present an independent analysis of these impacts on the generation rates customers will pay

3) The magnitude and value of the hedge to customers and its expected impact on the stability of customers' rates.

Before approving a PPA Rider, AEP Ohio must provide the Commission with this information in order to ensure that the PPA Rider will in fact, not just in "theory," meet the statutory criteria of R.C. 4928.143(B)(2)(d), *i.e.*, that it has the effect of stabilizing rates (in more than a de minimus amount) or providing certainty regarding retail electric service. Additionally, the Utility must show that the PPA Rider is reasonable and benefits customers.

4) Evidence that AEP Ohio's customers would be willing to pay higher rates in return for a modest increase in rate stability.

In evaluating electric security plans, the Commission has required that proponents of a provision demonstrate that it benefits consumers and is in the public interest.[105]

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[103] OCC Ex. 15A at 38 (Wilson); Staff Ex. 18 at 13 (Choueiki).

[104] R.C. 4928.02(A).

[105] See *In the matter of the Application of Columbus Southern Power Company and Ohio Power Company for Authority to Establish a Standard Service Offer Pursuant to §4928.143, Ohio Rev. Code, in the Form of an Electric Security Plan,* Case No. 11-346-EL-SSO et al., Entry on Rehearing at ¶19 (Jan. 23, 2012).

Determining customers' willingness to pay higher rates for modest increases in rate stability would assist the Commission in ensuring that the PPA Rider benefits consumers and is the public interest. Moreover, assessment of customers' willingness would help satisfy the state policy that "provides consumers with the supplier, price, terms, conditions, and quality options they elect to meet their respective needs."[106]

5) When presenting the economic development impact of plant closure, the impact on customers of increased rates to support the PPA Rider also should be presented.

This information would assist the PUCO in determining whether the PPA benefits consumers and the public interest. Consistent with these filing requirements, the Commission should conduct its own a study to examine the economic impacts on the state of Ohio and its electric utility customers. Such a study should evaluate the impacts of potential long-term subsidization of financially challenged generation facilities in contrast to deploying natural gas fueled generation units along with expanded distributed generation and energy storage in the state.

6) Environmental impacts of subsidizing select plants.

The subsidization of a utility's plants included under a PPA could affect a utility's decision to run plants that should otherwise not be dispatched. Such a decision has economic as well as environmental implications. Those implications must be fully disclosed and analyzed in order to show that the PPA Rider is reasonable.

7) Incentives to control costs.

Because the PPA rider permits a 100 percent pass through of actual plant fixed and variable (fuel) cost (net of revenues) there is no incentive to control these costs. This

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

information should be part of AEP Ohio's future filing to assist the PUCO in fulfilling state policy to ensure reasonably priced service is available to all customers in Ohio.[107]

8) Incentives to maximize market value/wholesale generation revenues.

Similarly to 7) above, with 100 percent pass through of all earned revenues there is no incentive to keep the plants operating, minimize outage time, offer the plants at efficient prices, etc. In order to assist the Commission in fulfilling state policy,[108] this information should be part of AEP Ohio's future filing.

9) Incentives to make rational end-of-life decisions.

When a plant no longer appears likely to cover its going forward costs over any future time frame (short or long), the owner should retire or repower it. Any proposed PPA Rider should be evaluated based on whether it provides incentives for owners to make sensible retirement decisions. As stated above, a 100 percent pass through provides no incentive for rational decision-making.

Incorporating these factors into a future PPA filing will help ensure that the PUCO has before it all the information it needs to determine whether the PPA is reasonable, benefits customers, and is in the public interest. The PUCO should abrogate its Opinion and Order and require utilities to address these additional factors.

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[107] R.C. 4928.02(A).

[108] R.C. 4928.02(A).

ASSIGNMENT OF ERROR 3: The PUCO unreasonably and unlawfully found that AEP Ohio's electric security plan, as modified, is more favorable in the aggregate to customers than a market rate offer.

A. AEP Ohio's proposed ESP is not more favorable than an MRO under the Commission's traditional application of the statutory test.

In this proceeding, the Commission performed its traditional analysis of the ESP v. MRO test,[109] which considers three elements: (1) the SSO price of generation to customers,[110] (2) other quantifiable provisions,[111] and (3) qualitative provisions. These three elements, combined, are compared to the results that would be obtained under R.C. 4928.142, if the SSO were proposed in the form of an MRO. From this comparison, the PUCO makes its determination whether the proposed ESP, in the aggregate, is more favorable than an SSO offered through an MRO.

In addressing the test's first element, the Commission found that the SSO price of generation to customers would be established through the competitive bid process and would be equivalent to the results that would be obtained under the MRO provided in R.C. 4928.142.[112] OCC does not dispute this Commission finding.

Under the second element, the Commission found that the Residential Distribution Credit ("RDC") rider provided the sole quantifiable benefit in AEP Ohio's ESP, in the amount of $44,064,000. OCC seeks rehearing on this finding because RDC rider was a benefit already recognized by AEP Ohio's prior ESP.[113] Moreover, although the Commission rejected AEP Ohio's proposed PPA Rider (quantified at a cost of up to

[109] R.C. 4928.143(C)(1).

[110] R.C. 4928.143(B)(1).

[111] R.C. 4928.143(B)(2).

[112] Order at 94.

[113] OCC Ex. 13 at 28 (Kahal).

$116 million), it approved a placeholder PPA rider. The Commission established an initial rate of zero for the rider and invited AEP Ohio to seek recovery of PPA costs in a future filing during the term of this ESP.[114]

OCC seeks rehearing on this issue on several bases. First, the placeholder PPA Rider should be denied because it is not an item expressly listed in R.C. 4928.143(B)(2). Second, if the placeholder is approved at a rate of zero, but costs are expected to be recovered during the ESP, a determination cannot be made on this record whether the ESP is more favorable than an MRO. Absent costs being assigned, the Commission should find that AEP Ohio has failed in its burden of proving the ESP is more favorable. Alternatively, the Commission should prevent PPA costs from being collected from customers during the ESP's term. In addition, OCC seeks rehearing on the Commission's failure to recognize the costs associated with Distribution Investment Rider ("DIR").

As to the third element, qualitative benefits should not be included and considered a part of the ESP v. MRO test. The Ohio Supreme Court has limited the items that can be included in an ESP to those expressly listed in R.C. 4928.143(B),[115] and the Court subsequently found that each of those items were "categories of cost recovery."[116] The categories of cost recovery do not include qualitative factors. The question whether it is lawful to include and consider qualitative provisions in the statutory test currently is pending before the Ohio Supreme Court.[117] Assuming arguendo that qualitative factors

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[114] Order at 25.

[115] *In Re Application of Columbus Southern Power Co., et al*., 128 Ohio St.3d 402, 2011-Ohio-958, 945 N.E.2d 501 (hereinafter, "*CSP I*").

[116] *In Re Application of Columbus Southern Power Co., et al*., 128 Ohio St.3d 512, 2011-Ohio-1788, 945 N.E.2d 655.

[117] See *In the Matter of Northeast Ohio Public Energy Council*, Appeal No. 2013-0513.

can be properly considered in this proceeding as a part of the ESP v. MRO test, OCC seeks rehearing because none of the factors identified provide Ohio consumers a benefit.

OCC asks the Commission to find that the proposed ESP is less favorable than an MRO and deny AEP Ohio's application. Alternatively, the Commission should further modify the ESP consistent with this application for rehearing.

The following analysis addresses in more detail the elements of the statutory test and the issues on which OCC seeks rehearing.

1. The Test's first element: determination of the SSO generation price.

As stated above, the SSO generation price would be determined by essentially the same competitive bid process under either the proposed ESP or an MRO. Thus, the SSO generation price would be quantitatively equal under either form of SSO.

2. The Test's Second Element: Cost Quantification of ESP provisions.

OCC seeks rehearing of the Commission's determination that the RDC rider is a quantifiable benefit, its failure to quantify the DIR rider, and its approval of the placeholder PPA Rider with an initial rate of zero.

3. The PUCO unreasonably considered the extension of the residential distribution credit rider as a benefit to customers under an electric security plan.

The RDC rider was approved in AEP Ohio's last distribution rate case,[118] which coincided with AEP Ohio's prior ESP case.[119] The rider was established to address potential double recovery of distribution costs approved in the rate case ($46.7 million)

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[118] *In Re Columbus Southern Power Company and Ohio Power Company*, Case No. 11-351-EL-AIR, Opinion and Order (December 14, 2001).

[119] *In Re Columbus Southern Power Company and Ohio Power Company*, Case No. 11-346--EL-SSO, Opinion and Order (August 8, 2012).

and the ESP under the DIR rider.[120] In other words, it was the combination of the authorized distribution rate increase coupled with the DIR that created this excess cost collection problem. The RDC rider established an annual credit of $14.688 million and was set to expire on May 31, 2015.[121] In this ESP proceeding the DIR will collect $543.2 million during the ESP's term. However, AEP Ohio proposes to extend the rider to May 31, 2018, only at its current level, $14.688 million annually (or $44,064,000 over the ESP's term).[122] The Commission found that this extension was a quantifiable benefit[123]

The continuation of the static annual credit of $14.688 million, in combination with the DIR, should not be considered a benefit of this ESP. It provides consumers no new benefit. Indeed, AEP Ohio continues to collect the $46.7 million annual revenue increase from its last distribution case and will collect even more revenues under the DIR--$543.2 million. This increase creates the real probability of double recovery of AEP Ohio's distribution costs, and places Ohio's residential consumers in a worse position than in the prior ESP. Thus, continuation of the RDC rider is merely a mechanism to mitigate the excess revenue collection under the DIR and is not a benefit offered by this ESP.

a. The PUCO unreasonably failed to consider the distribution investment rider revenues as quantifiable costs to customers under an electric security plan.

[120] OCC Ex. 13 at 19 (Kahal Direct).

[121] OCC Ex. 13 at 19 (Kahal Direct).

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

[123] Order at 94.

OCC witness Kahal demonstrated that revenues associated with the DIR, ESSR and other distribution riders were quantifiable costs of the ESP.[124] However, the PUCO refused to quantify these costs as a part of the ESP v. MRO test, finding that "the revenue requirements associated with the recovery of incremental distribution investments should be considered to be the same whether recovered through the ESP or ***through a distribution rate case conducted in conjunction with*** an MRO."[125]

As a threshold matter, the Commission's finding misstates the statutory test found in R.C. 4928.143(C)(1), which requires the Commission to compare "the electric security plan so approved…to the expected ***results that would otherwise apply under section 4928.142 of the Revised Code***." Emphasis added. The plain meaning of the statute clearly limits the Commission's analysis to the "expected results" of R.C. 4928.142, and does not contemplate consideration of the results of a distribution rate case.[126]

Moreover, the Commission's interpretation requires one to read into the statute words to the effect that the approved ESP should be compared to the expected results under R.C. 4928.142 **and a distribution rate case**. In considering the rules of statutory construction, the Ohio Supreme Court has found:

> When interpreting a statute, a court must first examine the plain language of the statute to determine legislative intent. *Cleveland Mobile Radio Sales, Inc. v. Verizon Wireless*, 113 Ohio St.3d 394, 2007-Ohio-2203, 865 N.E.2d 1275, ¶ 12. The court must give effect to the words used, ***making neither additions nor deletions from the words chosen by the General Assembly***. *Id. See, also, Columbia Gas Transm. Corp. v. Levin*, 117 Ohio St.3d 122, 2008-Ohio-511, 882 N.E.2d 400, ¶ 19. Certainly, had the General Assembly intended to require that electric distribution utilities prove that carrying costs were "necessary" before they could be

[124] OCC Ex. 13 at 23-24 (Kahal Direct).

[125] Order at 94 (Emphasis added).

[126] R.C. 1.42.

> recovered, it would have chosen words to that effect.[127] (Emphasis added).

Clearly, the Commission's interpretation of the statute adds to the words chosen by the General Assembly. Had the General Assembly intended to include the expected results of a distribution rate case in the statutory test, it would have. It did not.

In addition, the Commission's finding is based on its prior determination in the *FirstEnergy ESP III* case.[128] In that case, FirstEnergy quantified (for purposes of the statutory test) the accelerated recovery of revenues under the ESP's distribution rider, *i.e.*, because the ESP provides for accelerated recovery of distribution costs, customers would pay more distribution charges during the ESP's term than they would under a traditional rate case because of regulatory lag. Nevertheless, the Commission refused to quantify these accelerated revenues, finding that, over a period of time extending beyond the ESP's term, the revenues collected under the ESP and rate case would be a "wash."[129]

FirstEnergy ESP III misstates the statutory test that requires that the ESP "so approved" be compared to the expected results of an MRO.[130] In *FirstEnergy ESP III*, the ESP approved was for a period of three years and the Commission erred by extending its consideration to the longer, indefinite period of time. Thus, in this proceeding, the Commission may not lawfully extend its consideration of distribution revenues collected beyond the ESP's three-year term. Accordingly, if the Commission determines that it

[127] *In Re Columbus S. Power*, 138 Ohio St.3d 448, 2014-Ohio-462, 9 N.E.3d 1064, ¶ 26.

[128] *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company, The Toledo Edison 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. 12-1230-EL-SSO Opinion and Order (July 18, 2012) ("*FirstEnergy ESP III*").

[129] *FirstEnergy ESP III* at 55.

[130] R.C. 14928.143(C)(1).

lawfully may consider the results of a distribution rate case as a part of the statutory test (which it cannot, as stated above), then the Commission at least must include in its comparison the additional revenues collected by the DIR rider as compared to collections it would have received under a distribution rate case.

b. The PUCO erred by approving a placeholder PPA and further erred by attributing no cost to the PPA when customers could end up paying millions of dollars.

As stated previously, only those items that are expressly listed in R.C. 4928.143(B) may be included in an ESP. The Commission approved the placeholder PPA, in theory, based upon R.C. 4928.143(B)(2)(d), finding that it was a charge relating to "limitations on customer shopping" and that it would have the effect of "stabilizing or providing certainty regarding retail electric service." OCC has demonstrated in this application for rehearing that the proposed PPA Rider does not meet the elements of R.C. 4928.143(B)(2)(d). Thus, it should be disallowed. No value can be assigned to it for purposes of this ESP v. MRO test.

However, the Commission has approved the rider as placeholder, with an initial rate of zero, and has invited AEP Ohio to seek subsequent recovery of PPA costs during the term of this ESP. These costs can be reasonably expected to reach $116 million.[131] Because the rider currently is set at zero and the Commission intends to permit cost recovery in a "future proceeding" during this ESP's three-year term, Ohio's residential consumers currently are precluded from considering the rider's costs. Without presently knowing how the rider may be quantified in the future, they cannot reasonably contend, under R.C. 4928.143(C)(1), that the ESP is more favorable than an MRO. Thus, the

[131] OCC Ex. 15A, at 7, OCC Ex. 17; Order at 23.

Commission has unreasonably and unlawfully sheltered review of the PPA Rider costs to be collected during the ESP's term for purposes of the statutory test. Moreover, the Commission's approval of the placeholder rider prevents AEP Ohio from sustaining its burden of proof that the ESP is more favorable than an MRO under R.C. 4928.143(C)(1). Accordingly, approval of the placeholder PPA Rider requires the Commission to reject AEP Ohio's proposed ESP in its entirety.

Alternatively, the Commission may modify the ESP such that AEP Ohio cannot collect PPA revenues for the term of the ESP.

4. The PUCO erred by unlawfully considering qualitative benefits as part of the ESP v. MRO test.

As stated above, qualitative benefits are not properly considered a part of the ESP v. MRO test. The Ohio Supreme Court has limited the items that can be included in an ESP to those expressly listed in R.C. 4928.143(B),[132] and the Court subsequently found that each of those items were "categories of cost recovery."[133] The statutory test, as confirmed by judicial interpretation, is meant to serve as a consumer protection provision. It limits the rates that consumers pay under an ESP to less than those they would otherwise pay at market under an MRO. It is improper and unlawful to permit amorphous qualitative benefits to override the quantitative analysis that R.C. 4928.143(C)(1) expressly requires.

Nevertheless, in this proceeding, the Commission has found that several qualitative factors provide a benefit under the ESP. OCC seeks rehearing as to each on

[132] *In Re Application of Columbus Southern Power Co., et al*., 128 Ohio St. 3d 402, 2011-Ohio-958, 945 N.E.2d 501 (hereinafter, "*CSP I*").

[133] *In Re Application of Columbus Southern Power Co., et al*., 128 Ohio St.3d 512, 2011-Ohio-1788, 945 N.E.2d 655 (hereinafter, "*CSP I*").

the basis that they may not lawfully be considered by the Commission and that they provide no benefit at all.

a. The PUCO erred in identifying factors under R.C. 4928.02 as qualitative benefits provided to customers under an electric security plan.

The Commission relies on R.C. 4928.02 as independent authority to consider qualitative benefits under the ESP v. MRO test. Unfortunately, the Commission fails to identify which ESP provisions advance what policy,[134] contrary to R.C. 4903.09. Regardless, the Commission, itself, has admitted that only items expressly listed in R.C. 4928.143(B) may lawfully be considered in an ESP.[135] While the Commission must review an ESP to ensure that its provisions do not violate the state policies contained in R.C. 4928.02, only those items expressly listed in R.C. 4928.143(B) can be considered a part of the ESP for purposes of the test performed under R.C. 4928.143(C)(1).

b. The PUCO erred in identifying the transition to market-based rates as a qualitative benefit to customers under an electric security plan.

The Commission found that AEP Ohio's full transition (finally) to market-based rates is a benefit of this ESP proceeding. However, AEP Ohio made that commitment in its prior ESP proceeding.[136] As such, this binding commitment to transition cannot be considered a benefit of this proceeding. The Commission has held that if a benefit is approved in a prior ESP proceeding, it cannot again be considered a benefit in a subsequent ESP case. See *FirstEnergy ESP III* at 55 (refusing to recognize a benefit to forego transmission costs that had been agreed to in a prior proceeding); *In Re Ohio*

[134] Order at 95.

[135] Order at 20.

[136] IEU Ohio Ex. 1b at 24 (Murray).

Power, Case No. 11-346-El-SSO, Opinion and Order, at 30 (December 14, 2011) (refusing to recognize the removal of provider of last resort charges, when removal was mandated by a prior proceeding).

c. The PUCO erred in ascribing customer benefits of the distribution investment rider only to the electric security plan and not the market rate offer.

In its order, the PUCO found that the DIR and related distribution riders (collectively "DIR") provide a qualitative benefit over an MRO. Specifically, it found that approval of the DIR "***should*** enable the Company to hold base rates constant over the ESP period" while making improvements to the distribution infrastructure and improving system reliability.[137]

The Commission's relies on the testimony of AEP Ohio witness Allen in making its finding. Mr. Allen's testimony elaborates on and separates the DIR's qualitative benefits into three components (1) the DIR will permit AEP Ohio to make significant investments in infrastructure, (2) "will" keep base distribution rates constant over the ESP, and (3) the "streamlined" DIR process will improve the reliability of the system more quickly and at less cost than under a traditional base rate case.[138]

As to the first component of Mr. Allen's analysis, there is no dispute among the parties that AEP Ohio could make significant investments in its distribution infrastructure under either the DIR or a base rate proceeding. The significance of the amount is immaterial considering that consumers will be required to support it under either an ESP

[137] Order at 95 (Emphasis added).

[138] AEP Ohio Ex. 7, at 4 (Allen); Tr. II, at 611-613 (Allen).AEP Ohio Initial Br. at 141. AEP Ohio has provided no analysis of what savings, if any, it would incur through the DIR process and have failed to sustain its burden on this point. OCC Ex. 13 at 29 (Kahal).

or MRO. Indeed, the enormity of this investment (up to $543.2 million), granted outside of the comprehensive review of a base rate proceeding, must be considered a qualitative detriment to Ohio's residential consumers.

As to the second element of Mr. Allen's analysis, the statement in his direct testimony that the DIR "will" permit AEP Ohio to keep base rates constant is incorrect, or at least misleading.[139] On cross-examination, Mr. Allen admitted that AEP Ohio had made no commitment to freeze base rates during this ESP, but only expected that a rate case would be unnecessary if all of the elements of the ESP are approved.[140] Absent a commitment to freeze base rates, the benefit of maintaining constant base rates is illusory. Moreover, considering that Ohio's residential ratepayers will be required to pay for this infrastructure investment in any event, they receive no benefit whether paying it through the DIR or a base rate case. Indeed, as explained previously, consumers will suffer because they will be required to make these payments sooner under the "streamlined" DIR than they would have through base rates.

Considering that the first two components of Mr. Allen's analysis provide absolutely no benefit (and in fact are detriments) to consumers, the heart of his testimony lies in the fact that the "streamlined" DIR process will improve the reliability of the system more quickly.[141] This analysis shows how unreasonable (and unfair) Mr. Allen's analysis is to AEP Ohio's consumers. The analysis considers the qualitative benefit of consumers receiving infrastructure improvements more quickly under the DIR process, but (as explained above) refuses to recognize that consumers must also pay for these

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

[140] Tr. II at 612 (Allen).

[141] AEP Ohio Ex. 7 at 4 (Allen); AEP Ohio Initial Br. at 141.

improvements sooner. Instead, AEP Ohio (and the PUCO) considers this accelerated payments under the DIR as a "wash" with the payments under a base rate proceeding over an indefinite period of time.

AEP Ohio can't have its cake and eat it too. Clearly, if the DIR provides accelerated benefits then customers incur accelerated costs. It is unreasonable for the Commission to consider benefits while ignoring the costs that customers pay for them. If the Commission is to consider the DIR to be a benefit because it accelerates infrastructure reliability, it must recognize the accelerated payments that provide for that benefit. Otherwise, the Commission should find that the infrastructure improvements made through the DIR will "wash" over time, which they certainly will, if made pursuant to a base rate proceeding.

ASSIGNMENT OF ERROR 4: The Public Utilities Commission erred when it ordered customers to fund excessive profits (a return on equity of 10.20 percent) for a distribution-only utility equal to those it ordered for the integrated utility four years ago.

AEP Ohio requested authority to charge customers for profit at a rate of return based on a 10.65 percent equity cost rate.[142] But OCC Witness Woolridge urged the PUCO to adopt a return on equity of 9 percent.[143] Dr. Woolridge testified that there are a number of reasons why a 9 percent ROE is appropriate and fair for AEP Ohio in this case. Two factors in particular strongly support the 9 percent ROE: (1) AEP Ohio is now a distribution-only electric utility with a significantly reduced risk than it had as an integrated generation, transmission, and distribution owner; (2) AEP Ohio also currently collects a large portion of its rates through rate mechanisms called "riders" also lowering its risk.

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

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

At the same time, there has been a decline of interest rates and other costs of capital in the last four years. This decline in capital costs has been recognized by other state commissions in setting authorized ROEs for electric utilities, and especially for distribution-only electric utilities. Walmart Ex. 1 at 7-10. Dr. Woolridge testified that based on these three factors, AEP Ohio's risk is lower than other electric utilities,[144] justifying customer funded profits at a 9.0 percent ROE.

While the PUCO agreed that AEP's recommended 10.65 percent ROE was too high (Opinion and Order at 84), it nonetheless authorized an excessive ROE of 10.2 percent. *Id*. The 10.2 percent ROE was adopted based on the mere fact that it was the ROE for Ohio Power (the merged entity) that was ordered in the Utility's distribution rate case four years ago. *Id*. The PUCO's decision in this regard was unjust and unreasonable.

A. The PUCO's determination was unjust and unreasonable because it did not lower customer-funded profits (return on equity) to account for the lower risks the utility now faces. Those lower risks include the fact that AEP Ohio is now a distribution only utility (without the more risky generation business) and collects virtually all of its revenues from customers through riders. Additionally, interest rates and other costs of capital have declined in the last four years. These factors support a lower return on equity than the 10.2 percent return on equity granted.

Four years ago, as part of a comprehensive case settlement, stipulating parties agreed to a 10.2 percent ROE for Ohio Power. At that time the Utility was an integrated utility that provided generation, transmission, and distribution service. But on January 1, 2014, Ohio Power became a wires-only entity when it completed its corporate separation and divested its generation assets, after PUCO approval.[145]

[144] OCC Ex. 12 at 59 (Woolridge).

[145] See *In the Matter of the Application of Ohio Power Company for Approval of an Amendment to its Corporate Separation Plan*, Case No. 12-1126-EL-UNC, Finding and Order (Oct. 17, 2012).

As a wires-only entity, Ohio Power has less risk than it had four years ago when it was an integrated utility. Consequently, the Utility's profits should be reduced accordingly. Dr. Woolridge testified that in recent years, the authorized ROEs for electric distribution utilities (wires-only) have been lower than those of integrated electric utilities. OCC Ex. 12 at 54. And for a utility with lower risks, investors typically demand a lower return on equity.[146] Additionally, as discussed in the testimony of AEP witness Andrea Moore, virtually 100 percent of the Utility's projected revenues under the proposed ESP, with the exception of base distribution rates, are collected through riders. See AEM-1, listing fourteen current riders, and nine proposed riders (seven of which were approved by the PUCO); OCC Ex. 12 at 54-55). While many electric utilities have riders that adjust rates between rate cases, Dr. Woolridge testified that AEP Ohio has a more comprehensive set of riders that would lower the Utility's risk. OCC Ex. 12 at 55.[147] The PUCO, in fact, acknowledged Ohio Power has reduced exposure to risk from regulatory lag in light of the distribution investment rider and numerous other riders.[148]

The Commission's decision also failed to consider the decline of interest rates and other costs of capital in the last four years. This decline in capital costs has been recognized by other state commissions in setting authorized ROEs for electric utilities, and especially for distribution-only electric utilities. For example, Dr. Woolridge concluded that "authorized ROEs for electric utilities further declined to below 10.0 percent in 2013 and have continued to decline in 2014." OCC Ex. 12 at 6. Wal-Mart

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[146] Tr. V at 1286 (Avera).

[147] Walmart witness, Steve W. Chriss, also recognized this and pointed out the Utility's proposed ROE is excessive, especially given its proposal to continue and/or expand the use of DIR and other riders to reduce its regulatory lag on a significant amount of its revenue that would otherwise be collected through base rates. See Walmart Ex. 1 at 7.

[148] Opinion and Order at 84.

witness Steve Chriss calculated that "the average authorized ROE for distribution only utilities in 2012 was 9.75 percent, in 2013 was 9.37 percent, and so far in 2014 is 9.46 percent." Wal-Mart Ex. 1 at 9.

But despite these factors, the PUCO gave Ohio Power the same ROE as it ordered four years ago when the utility had more, not less risk, than today. The PUCO's decision is unreasonable, and contrary to the weight of evidence. The evidence supports an ROE less than 10.2 percent, as evidenced by the testimony of OCC Witness Woolridge (and Walmart Witness Chris).[149] There is no evidence to support the PUCO's contrary conclusion that a 9.0 percent ROE is not enough profit to enable AEP to maintain its financial integrity and protect its ability to attract capital.[150]

B. The PUCO's order is unlawful because it is not based upon facts of record, as required by R.C. 4903.09.

The PUCO's decision to maintain the same ROE as it granted the Utility four years ago disregards the evidence produced in this case. Instead the PUCO mistakenly relies upon a ROE recommendation that is four years old and was made for a more risky entity—not the wires-only entity that Ohio Power has morphed into.

But under R.C. 4903.09, the PUCO must make findings of fact based on the record before it. It cannot resort to information outside the record. *Tongren v. Pub. Util. Comm.*, 85 Ohio St.3d 87, 706 N.E.2d 1255 (1999); *Ideal Transp. Co. v. Pub. Util. Comm.*, 42 Ohio St.2d 195, 326 N.E.2d 861 (1975), paragraph 2 of the syllabus. Thus, it was unlawful for the PUCO to adopt a ROE of 10.2 percent based solely on a ROE reached

149 Walmart Ex. 1 at 7-10.

150 Opinion and Order at 84.

in the Utility's distribution rate case four years earlier. The PUCO should grant rehearing and abrogate its finding.

C. The PUCO unreasonably relied upon an ROE for the utility that was agreed to as part of comprehensive settlement of a prior case.

Additionally, the 10.2 percent ROE was but one provision in a comprehensive settlement of an entire case. The 10.2 percent ROE from the prior case does not stand on its own as a reasonable ROE—it can only be viewed in the context of the entire stipulation, which as a package was determined to be reasonable. The Stipulation itself, which the PUCO approved expressly, conveys this:

> This Stipulation contains a combination of outcomes that reflects an overall compromise involving a balance of competing positions and it does not necessarily reflect the position that one or more of the Signatory Parties would have taken on any individual issue. Rather the Stipulation represents a package that, taken as a whole, is acceptable for the purposes of resolving all contested issues without resorting to litigation. The Signatory Parties believe that this Stipulation, taken as a whole, represents a reasonable compromise of varying interests.

The PUCO misuses one component of the Stipulation to the detriment of customers who will now be forced to pay millions more in profits to the utility. This is unreasonable and unjust.

Additionally, the terms of the Stipulation expressly prohibit the PUCO from using one component of the stipulation as precedent for its decision in "any future proceeding," including this one. That stipulation included the provision that "except for enforcement purposes or to establish that the terms of the Stipulation are lawful, neither this Stipulation nor the information and data contained herein or attached hereto shall be cited as a precedent in any future proceeding for or against any signatory party, or the Commission itself, if the

Commission approves the Stipulation."[151] The Stipulation, in its entirety, was approved by the PUCO.[152]

While the PUCO avers that this limitation extends only to the parties, and not to the Commission itself (Opinion and Order at 84), the language is not so limited. The PUCO is bound by the language. It cannot use the terms of the Stipulation, including the 10.2 percent ROE as precedent. To permit the PUCO to disregard a crucial element of the stipulation that parties considered an integral underpinning of the agreement is unjust and unreasonable.

The PUCO's interpretation is contrary to the inherent nature of a stipulation. It violates the terms expressly agreed upon by the parties who signed the Stipulation. It will have a chilling effect on the willingness of parties to enter into future negotiations. If the Commission wishes to encourage future settlements and encourage respect for terms of past settlements, it should abrogate its order. Rehearing should be granted.

D. The PUCO's determination was unreasonable because it failed to consider factors that merit reducing the profit that customers must fund. These factors include a $368 million windfall for AEP Ohio for POLR charges collected from customers during the ESP II period, $508 million in customer funded stability charges, and $ 499 million in capacity charges.

The Ohio Supreme Court issued a decision earlier this year that permitted AEP Ohio to keep $368 million[153] in unwarranted POLR charges collected from its customers during the ESP II period, despite the fact that there was no evidence to justify the costs.[154]

[151] *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, Joint Stipulation and Recommendation at 14 (Nov. 23, 2011).

[152] Id., Opinion and Order (December 14, 2011).

[153] There are also tens of millions of dollars in carrying charges permitted to be retained by the Utility.

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

While the Court recognized that its decision was a "windfall for AEP" and that "this particular outcome is unfair" for customers, it nonetheless considered itself bound by the no-refund rule in the *Keco* decision.[155] This windfall to AEP, funded by customers, should have been recognized by the PUCO as a factor for reducing the profit that the PUCO sets for AEP to charge customers.[156]

And there are yet other factors as well that the PUCO should have considered but did not. AEP has received and continues to receive (through May 31, 2015) hundreds of millions of dollars ($508 million in total) in customer-funded rate stability revenues and capacity charges. These stability charges and capacity charges were approved by the PUCO in AEP's last electric security plan proceeding.[157] These hundreds of millions of dollars in revenues are being collected from AEP's customers to provide the Utility "financial stability."

And it doesn't end there. Once the current electric security plan ends, the Utility plans to collect, starting June 1, 2015, yet more from its customers—this time $499 million through a customer funded capacity charge deferral plus carrying charges. That capacity charge deferral was approved by the PUCO[158] and was intended to make the Utility whole. Under the capacity charge customers pay the utility for PUCO-determined fully embedded cost of capacity[159] and marketers (CRES providers) receive the capacity

[155] Id.

[156] 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).

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

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

[159] The utility believes its fully embedded cost of capacity is greater than the PUCO determined cost.

at the PJM market price. Giving the utility its fully embedded cost of capacity (through customer funding) will also assure that the utility is "made whole."

Both of these PUCO Orders should have been recognized as factors for reducing the profit that the PUCO sets for AEP to charge customers in this proceeding. But these streams of income and the reduced risks flowing from revenue guarantees for the Utility were ignored by the PUCO when the PUCO set the 10.2 percent ROE. The PUCO's failure to consider these factors and lower the profits that customers must fund was unjust and unreasonable.

There is precedent that supports adjusting a utility's return on equity for qualitative factors beyond the various formulae. These factors are issues that affect customers and include the quality of the utility's management practices, the efficiency of its delivery of service to customers, its future capital needs, and other factors in the PUCO's discretion.[160]

There have been numerous decisions over the years where the PUCO has chosen a lower rate of return, based on qualitative factors affecting consumers. For instance the PUCO has lowered the rate of return granted to utilities based on poor quality of service.[161] The PUCO has also permitted adjustments to the rate of return to address poor

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[160] Id.

[161] *Ohio Utilities Company*, Case No. 81-426-WW-AIR, Opinion and Order (June 7, 1982); *In the Matter of the Application of General Telephone Company of Ohio for Authority to Increase and Adjust its Rates and Charges and to Change Regulations and Practices Affecting the Same,* Case No. 84-1026-TP-AIR, Opinion and Order at 12-16 (July 23, 1985); *In the Matter of the Application of The Ohio Bell Telephone Company for Authority to Amend Certain of its Intrastate Tariffs to Increase and Adjust its Rates and Charges and to Change its Regulations and Practices Affecting the Same*, Case No. 84-1435-TP-AIR, Opinion and Order at 96, 206-212 (Dec. 10, 1985).

management decisions, such as “inadequate” decision-making and lack of commitment to demand side management activities.[162] Additionally, the PUCO has lowered the rate of return in response to actions taken by a utility, including a case where the utility took the “unprecedented act” of putting proposed rates into effect prior to the issuance of a PUCO order.[163] The PUCO has also considered the frequency with which a utility goes to market with equity issues as a consideration in selecting a point within the rate of return range.[164]

Beyond considering the factors discussed above for setting profit, there is precedent for more. For example, the PUCO increased the utility’s rate of return for risk[165] when the Supreme Court of Ohio reversed a PUCO decision that allowed charging customers for cancelled nuclear power plants. Interestingly, the PUCO noted that the increase in the rate of return was enough to allow the utility to collect from customers the “unamortized balance” of approximately what the Court had disallowed in rate base.[166] Given that the PUCO noted, in 1982, that its rate of return adjustment essentially allowed for making the utility whole (despite the Supreme Court’s reversal of the PUCO’s

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[162] *In the Matter of the Application of The Cincinnati Gas & Electric Company for an Increase in Electric Rates in its Service Area*, Case No. 91-0410-EL-AIR, Opinion & Order at 180-181, 206-212 (May 12, 1992)(selecting a return on equity in the first quartile of the range). See also *In re Ohio Edison*, Case No. 89-1001-EL-AIR, Opinion and Order at 88 (Aug. 16, 1990) putting all jurisdictional utilities on notice than an “applicant’s efforts in pursuing demand side management initiatives” would be utilized as one criteria in determining the appropriate point within the rate of return range).

[163] *In the Matter of the Applications of Columbia Gas of Ohio, Inc. to Establish a Uniform Rate for Natural Gas Service within the Company's Northwestern Region, Lake Erie Region, Central Region, Eastern Region, and Southeastern Region*, Case No. 89-616-GA-AIR, Opinion & Order at 123-130 (April 5, 1990) (In determining the appropriate rate of return, the PUCO also considered the utility’s attempt to shield services provided under contract from Commission review).

[164] *In re: Columbia Gas of Ohio*, Case No. 81-1024-GA-AIR, Opinion and Order at 5 (Sept. 9, 1982).

[165] *In re: Cleveland Electric Illuminating Co.* Case No. 81-146-EL-AIR, Opinion and Order at 115-117 (Mar. 17, 1982) (finding that the Ohio Supreme Court decision in *Consumers’ Counsel v. Public Utilities Commission*, 67 Ohio St. 2d 153 (1981) should be taken into account when selecting a rate of return within the range recommended).

[166] Id. at 79-80.

decision), symmetry suggests that the "unfairness" to customers (through the "windfall") and the enormous sums of customer funded make whole payments to AEP are reasons to limit AEP Ohio's excessive profits.

The PUCO should grant rehearing and reassess the ROE that should be set for Ohio Power. Considering the evidence in the record and the factors discussed here, the PUCO should abrogate its order and instead find that an appropriate ROE is 9 percent, not 10.2 percent.

ASSIGNMENT OF ERROR 5: The Commission is a creature of statute and as such can exert no authority beyond that which it has been granted.

It is unrefuted that the PUCO is a creature of statute, and is not authorized to act except by and through the authority granted to it under Ohio statutes. See, e.g., *Canton Storage and Transfer Co. v. Public Util. Comm.* (1995), 72 Ohio St.3d 1, 647 N.E.2d 136. In this proceeding, the PUCO exceeded that authority in at least four ways in the Opinion and Order that is the subject of this rehearing request.

A. The PUCO erred in rewriting R.C. 4928.143(B)(2)(d) to permit a financial limitation on shopping.

As argued above, the PUCO added the word "financial" to the statute. This contravenes its plain meaning and the intent of the General Assembly to provide the Commission only with the authority to limit customer switching to CRES providers. This reworking of the statute to justify the PPA Rider was unlawful. The PUCO should grant OCC's rehearing request.

B. The PUCO erred in allowing AEP Ohio to collect unlawful transition revenues in contravention of R.C. 4928.38.

While the PPA Rider was set at zero, the PUCO provided AEP Ohio with the opportunity through a "future filing," to collect costs. This subsequent cost recovery, as argued above, must be considered a form of transition revenues. Notably, the Commission's order devoted only a single sentence to this issue. It merely stated, "[n]either do we agree with the assertion that the PPA rider would permit AEP Ohio to collect untimely transition costs in violation of R.C. 4928.38."[167] Nevertheless, the PPA rider clearly is a transition charge because it requires AEP Ohio's consumers to pay for AEP Ohio's (and its generation affiliate's) lost revenues. The lost revenues are created when the cost of OVEC generation (or other affiliated generation subject to a PPA) is greater than the market price derived through the PJM market. Rehearing should be granted.

C. The Commission exceeded its authority in performing the more favorable in the aggregate test, set forth in R.C. 4928.142.

The intention of the mandated test in R.C. *4928.142* is to assure that the results of the ESP are more favorable to customers in the aggregate that the results otherwise obtained through an MRO. As argued above, the plain meaning of the statute clearly limits the Commission's analysis to the "expected results" of R.C. 4928.142, and does not contemplate consideration of the results of a distribution rate case.[168]

Moreover, the Commission's interpretation requires one to read into the statute words to the effect that the approved ESP should be compared to the expected results under R.C. 4928.142 and a distribution rate case. Clearly, the Commission's interpretation of the statute adds to the words chosen by the General Assembly. Had the General Assembly intended to include the expected results of a distribution rate case in the statutory test, it would have so stated. It did not. This misapplication of the statute

[167] Order at 26.

[168] R.C. 1.42.

results in the PUCO exceeding its authority under the statute. OCC's rehearing request should be granted.

D. The PUCO unlawfully relies upon state policy to consider qualitative benefits under the ESP vs. MRO test.

As argued above, the PUCO relies on R.C. 4928.02 as independent authority to consider qualitative benefits under the ESP v. MRO test. Unfortunately, the Commission fails to identify which ESP provisions advance what policy,[169] Regardless, the Commission itself, (as well as the Court)[170] has admitted that only items expressly listed in R.C. 4928.143(B) may lawfully be considered in an ESP.[171] While the Commission must review an ESP to ensure that its provisions do not violate the state policies contained in R.C. 4928.02, only those items expressly listed in R.C. 4928.143(B) can be considered a part of the ESP for purposes of the test performed under R.C. 4928.143(C)(1). The PUCO's willingness to stray outside the statutory lines to achieve the desired result is unlawful and unreasonable. The PUCO should grant OCC's rehearing request.

IV. CONCLUSION

The PUCO should grant rehearing on OCC's claims of error and modify or abrogate its February 25, 2015 Opinion and Order. Granting rehearing as requested by OCC is necessary to ensure that AEP Ohio customers are not subject to unreasonable and unjust charges. Otherwise Ohio consumers could end up paying for a whole host of unreasonable and unlawful charges, including excessive profits, an ESP plan that does not produce lower prices than a market plan, and a government ordered subsidy of utility

[169] Order at 95.

[170] CSP I.

[171] Order at 20.

power plants by customers that under the law should be fending for themselves in the competitive generation market.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing Application for Rehearing by the Office of the Ohio Consumers' Counsel was served via electronic transmission, to the persons listed below, on this 27th day of March, 2015.

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