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BEFORE THE
PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Adoption of Rules for Standard Service Offer, Corporate Separation, Reasonable Arrangements, and Transmission Riders for Electric Utilities Pursuant to Sections 4918.14, 4928.17 and 4905.31, Revised Code, as amended by Amended Substitute Senate Bill 221	)))))))	**Case No. 08-777-EL-ORD**

COLUMBUS SOUTHERN POWER COMPANY'S AND OHIO POWER COMPANY'S APPLICATION FOR REHEARING

Pursuant to §4903.10, Ohio Rev. Code, Columbus Southern Power Company and Ohio Power Company (AEP Ohio) file this application for rehearing of the Commission's September 17, 2008 Finding and Order in this docket. The Commission's order adopted rules concerning filing requirements for Electric Utility Standard Service Offer applications (Chapter 4901:1-35); Transmission Cost Recovery (Chapter 4901:1-36); Corporate Separation (Chapter 4901:1-37); and Reasonable Arrangements (Chapter 4901:1-38). These rules, in part, are unlawful and/or unreasonable in the specifics and for the reasons set out in the following memorandum in support and should be modified on rehearing.

MEMORANDUM IN SUPPORT OF REHEARING

Chapter 4901:1-35: Electric Utility Standard Service Offer

This chapter sets out rules addressing procedural and content requirements governing the filing of either an Electric Security Plan (ESP) or Market Rate Offer (MRO) to establish an electric utility's Standard Service Offer (SSO). The following provisions of this chapter should be modified on rehearing in the following manner:

4901:1-35-01 (K): The definition in the rule of "rate plan" differs from the statutory definition of that term in §4928.01 (A) (33), Ohio Rev. Code. The definition in the rule focuses on rates established "at the expiration of ... the market development period." The statutory definition, which must be controlling, focuses on the SSO "in effect on the effective date" of S.B. 221. In order to avoid confusion, the Commission should adopt the statutory definition of "rate plan."

4901:1-35-03 (B) (1): The requirements for a MRO filing should be consistent with §4928.142, Ohio Rev. Code. Unfortunately, provisions within subdivision (B) contain significant variances from the controlling statutory language. For example, the language in subpart (B)(1)(a) regarding alternative conditions including non-pancaked rates, open access by generation suppliers and full interconnection with the distribution grid expands the narrower statutory language requiring comparable and nondiscriminatory access. *See* §4928.142(B)(1), Ohio Rev. Code. Similarly, there is no apparent statutory basis for the language in subpart (B)(1)(c) regarding publicly available pricing information being independent and sufficiently reliable; available for any product or service necessary for a winning bidder to fulfill the contractual obligations resulting from the competitive bidding process (CBP); representative of prices and changes in prices in the electric utility's market; and that such information be updated monthly by the publication. Wherever possible, the rules should either repeat the exact statutory language or simply refer to the applicable statute. The competitive market test was central to the debate and deliberations of the General Assembly and additional requirements should not be grafted onto the governing statutory language.

4901:1-35-03 (B)(2)(b) and (c): In subpart (B)(2)(b) and (c), it is not clear why the proposed rule includes submission of pro forma financial projections of the CBP plan's implementation upon transmission and distribution operations and upon transmission and distribution rate impacts. The MRO only encompasses pricing for generation service and is not tied to the price of transmission or distribution operations or rates. These provisions should only refer to generation operations and rates.

4901:1-35-03 (B)(2)(d) and (n): The Commission modified the proposed rule regarding the role of state policies under §4928.02, Ohio Rev. Code, in an ESP proceeding. The proposed rule would have required a showing of how an ESP would "achieve" those policies. The Commission, "recognizing the need for flexibility in attempting to satisfy those policies" (Finding and Order, p.3), stated that it was inserting the words "consistent with" for the word "achieve."

The adopted rule, however, uses the phrase "consistent with *and advances," (emphasis added).* The words "and advances" not only are inconsistent with the Commission's discussion of this rule, but raise the same problems indentified in comments concerning the word "achieves." (See AEP Ohio's Initial Comments pp. 5,6). Requiring that an ESP not only is consistent with fourteen different, broadly-stated and sometimes conflicting state policies, but actually *advances* each policy fails to recognize the need for flexibility in attempting to satisfy those policies. The phrase "consistent with" should be used as indicated in the Finding and Order.

4901:1-35-03 (C) (2): This provision unlawfully requires the filing of pro forma financial projections with an ESP application. As AEP Ohio explained in its Initial Comments, the requirement is without basis in S.B. 221. A prospective review of

significantly excessive earnings is relevant only in the context of an ESP that extends beyond a three-year period, and then only when going into the fourth year of the ESP. (See, Initial Comments, p. 14).

The Commission explains its retention of this requirement as follows:

> An ESP is quite complex, with many aspects to be decided, and these decisions should be made in the context of all available information. The Commission, throughout its history, has been charged with consideration and balancing of the understanding of the possible effects of decisions on various parties. AEP Ohio's argument would have the Commission, and the public, flying blind in this regard, and could jeopardize the sense of fairness and legitimacy of the process. We would also observe that none of the other electric utilities objected to this provision or interpreted it as an excess earnings test.

Making decisions based on all available information and considering and balancing competing interests of stakeholders, based on the possible effects of decisions on parties, must be viewed in the context of the applicable statutory authority. Just because information is available does not mean that the Commission is free to consider it. For instance, when setting the SSO for the AEP Ohio companies, the Commission would not base its decision on the SSO authorized for the FirstEnergy companies, even though that information might be available.

Similarly, the balancing of competing interests of stakeholders must be based on the balancing of those interests in a manner consistent with S.B. 221. The General Assembly conducted extensive hearings and deliberated at length before enacting S.B. 221. That legislation sets forth the balance of interests struck by the legislative process. This is not a mere detail but goes to the core of the partial re-regulation methodology reflected in S.B. 221.

S.B. 221 rejects the traditional process for setting rates for the SSO. That traditional process, while using historic data, is forward looking in nature. It endeavors to set rates that will be reasonable on a going-forward basis, based in large part on a representative level of expenses. There is no opportunity for customer refunds if it turns out that the returns were higher than anticipated. In that context, standard filing requirements which include pro forma financial data is appropriate because there is no retroactive ratemaking and no customer refunds based on a subsequent finding that rates have become unjust or unreasonable.

In sum, traditional ratemaking involves a "bottom up" approach that builds rates based on cost. An ESP under S.B. 221, however, does not set the SSO on a cost-based analysis and is ultimately governed by a "top down" retrospective excessive earnings review. §4928.143 (C) (1), Ohio Rev. Code, is very clear -- the Commission "shall approve or modify and approve [an ESP] if it finds that the [ESP] ... is more favorable in the aggregate as compared to the expected results that would otherwise apply under section 4928.142 of the Revised Code."

Traditional rate making is based on a current assessment of the reasonableness of the rates going forward and a determination that the expenses are representative of the expected level to be incurred. Once set those rates remain in effect until replaced. There is no periodic review with a refund potential. SSO rates set by an ESP are set in the context of a comparison to SSO rates set by an MRO. Perhaps the most important distinction in comparing traditional ratemaking to an ESP under S.B. 221 is the excessive earnings test. Unlike traditional rate making where such an approach would be considered unlawful retroactive ratemaking, the ESP under S.B. 221 requires an annual,

after-the-fact review with the potential for refunds to customers. In imposing this provision, however, the General Assembly made it clear that the excessive earnings test would only be applied retroactively, not prospectively, to an ESP with a term of three years or less. Moreover, because the excessive earnings test is strictly one-sided and does not offer any after-the-fact earnings increases, ESP rates should not be established based on a prospective estimate of what earnings might be. Instead, ESP rates are to be prospectively judged by what MRO rates would be during the same term.

The Commission's rule, unlawfully blends the two rate making processes. In addition to the sole test for judging an ESP set out in S.B. 221, it would overlay its traditional approach to rate making. In so doing, the Commission would consider the reasonableness of earnings at both ends of the rate making cycle -- considering its own extra-statutory earnings analysis as a factor in setting the SSO, in addition to the annual after-the-fact earnings analysis required by the General Assembly.

The Commission states that "AEP Ohio's argument would have the Commission, and the public, flying blind in this regard, and could jeopardize the sense of fairness and legitimacy of the process." (Finding and Order p.5). AEP Ohio believes that rather than "flying blind" its argument is that the Commission must stay on the course set for it by the General Assembly. The fairness and legitimacy to which the Commission refers is addressed by the annual after-the-fact review of possible significantly excessive earnings. That is the fail safe provision adopted by the General Assembly. This rule unlawfully imposes an up-front earnings analysis while S.B 221 provides for only an after-the-fact earnings analysis. This aspect of the rule should be deleted on rehearing.

4901:1-35-03 (C) (8): As discussed above in connection with Rule 4901:1-35-03(B)(2)(d) and (n), the phrase "consistent with" should be used instead of "achieves" or "advances," as indicated in the Finding and Order.

4901:1-35-03 (C) (9) (a): This rules relates to ESP filing requirements pertaining to the proposed automatic recovery of fuel, purchased power and certain other specified costs. While filing requirements concerning how the proposed cost recovery mechanism would work are appropriate, other requirements are appropriate only for subsequent Commission proceedings involving the review of the actual operation of the cost recovery mechanism. For instance, the reasonableness of the utility's procurement policies and procedures regarding such costs will be judged in the context of the circumstances at the time the cost recovery is being reviewed. The decision to include an automatic cost recovery mechanism in an ESP should not be made on whether the Commission agrees today with, for instance, the degree on which the electric utility relies on spot market purchases versus long-term contracts or with the other aspects of the electric utility's procurement policies and procedures. Consequently, the reference to the electric utility's procurement policies and procedures should be deleted as an ESP filing requirement from (a) (i).

Similarly, the ESP proceeding is not the time or place to review whether costs were prudently incurred. ((a) (iii)). Rule 4901:1-35-09 (C), which is being adopted by the Commission, recognizes that "costs incurred and recovered through quarterly adjustments shall be reviewed in a separate proceeding outside of the automatic recovery provision of the electric utility's ESP." The reference in §4928.143 (A) (2) (a), Ohio Rev. Code, to costs "prudently incurred" limits the automatic recovery to prudent costs,

the determination of which will be made throughout the life of the cost recovery mechanism. That reference does not require a demonstration *in the ESP proceeding* that all costs that will pass through the cost recovery mechanism actually are prudent. Consequently, (a) (iii) should be deleted as an ESP filing requirement.

4901:1-35-03 (C) (9) (b): This rule addresses filing requirements associated with recovery of an allowance for construction work in progress (CWIP) and of a nonbypassable surcharge for the life of an electric generating facility under §4928.143 (B) (2) (b) and (c), respectively, Ohio Rev. Code. The Commission stated its belief that "the impetus for these provisions of S.B. 221 was a concern that the market might not provide sufficient means for the creation of additional generation resources which might be needed in the future." (Finding and Order, p. 5). Unfortunately, certain of the adopted filing requirements are inconsistent with those statutory provisions.

Subdivision (b) (i) requires that the need for the proposed facility must have already been reviewed and determined by the Commission through an integrated resource planning process under another Commission rule. The statute, however, does not require a prior determination of need. In fact, the statute provides that the Commission must "first determine *in the proceeding* that there is need for the generating facility based on resource planning projections submitted by the electric distribution utility." (§4928.143 (B) (2) (b), Ohio Rev. Code, emphasis added). This subdivision of the rule should be modified to conform to the statute. Subdivision (b) (ii) of the rule also is inconsistent with the applicable statute. That rule would require that the competitive bidding process for construction of the facility must be approved by the Commission. The statute states that no CWIP allowance "shall be authorized unless the facility's construction was

sourced through a competitive bid process, regarding which process the commission may adopt rules." (*Id.*). The problem with the proposed rule is twofold. First, a case-by-case approval of the bidding process is contrary to the statute which contemplates a generic rule applicable to all electric utilities and to all construction projects. A generic rule would enable the electric utility to conduct its bidding process *before* filing its ESP. With the case-by-case approach resulting from the rule, the electric utility will not have the results of its bidding process until *after* the ESP is ruled upon.

That leads to the second problem. Subdivision (b) (i) (iii) (iv) and (v) requires the submission of data dependent on the projected cost of the project. Obviously, construction is an important component of that projection. While the rule speaks to a previous approval of the competitive bidding process for the specific facility, no procedure for obtaining such approval is set out in the rule. Even if such a procedure were available, the electric utility, the Commission and interested parties would need to engage in two separate proceedings -- the prior approval of the process and the ESP proceeding. That kind of two-step process is inefficient and should be avoided. Further, if the Commission has in mind a specific competitive bidding process it should set out those processes for comment in a separate rule making. Once such a rule is adopted, as contemplated by S.B. 221, electric utilities can submit their competitive bidding processes in conformance with those rules. There would be no need for case-by-case evaluation of the proposed bidding process. Consequently, the reference in subdivision (b) (ii) to Commission approval of the bidding process should be deleted.

4901:1-35-03 (9) (c) (i): This rule requires the electric utility to include in its filing a list of all components of the ESP which would have the effect of preventing,

limiting, inhibiting or promoting customer shopping for a competitive retail electric service. As noted in AEP Ohio's initial comments (pages 15, 16) such a list is so subjective that the filing requirement itself is overbroad and ambiguous. It may be tempting to say that the electric utility should use its best judgment in compiling the list and the required related information (explanation of the component, descriptive rationale and quantitative justification). However, since the list and related information is a filing requirement, the electric utility will run the risk of having its ESP filing rejected if the Commission agrees with an intervenor's subjective analysis that additional ESP components will prevent, limit, inhibit or promote customer shopping. This filing requirement could be complied with if it were limited to those components the *filing utility believes* would have the stated effect. That concept should be incorporated into the rule on rehearing. Such a modification would eliminate the exposure to the significant consequences (rejection of the ESP filing) of being second guessed, while still permitting intervenors to challenge components of the ESP which they believe improperly restrict or promote customer shopping.

4901:1-35-03 (9) (g): This rule addresses an extensive list of information that must be filed in conjunction with an infrastructure modernization plan which is included in the ESP. The required information is so extensive as to create a barrier to proposing such a plan. For instance, the rule requires such information as societal benefits (distinct from customer benefits), service disruptions associated with implementation of the plan, the number of customers impacted by the plan and the timing of the impacts. When the five paragraphs of detailed information requirements are reviewed, not on the basis of whether the information is relevant in an evidentiary sense, but rather on the basis of

every requirement having to be submitted with the ESP application, the burden of such a filing requirement is apparent. As filing requirements, the questions of whether the electric utility has addressed in sufficient detail a description of the plan, the benefits, the costs, the proposed cost recovery mechanism and the alignment of the plan with customers' reliability and power quality expectations places in jeopardy whether the ESP filings or that portion of the filing will be accepted. On rehearing the Commission should require a more general discussion of these five aspects of the plan and leave to the Staff and intervenors to request the information relevant to the particular infrastructure modernization plan.

4901:1-35-06 (A): This rule places on the electric utility the burden of proving that the ESP is consistent with state policies under §4928.02, Ohio Rev. Code. AEP Ohio noted its concern that such a requirement would add ESP approval standards beyond the MRO comparison adopted by the General Assembly. (See AEP Ohio's Initial Comments, pp. 5, 6). While the Commission has tempered its reference to the significance of the state policies in an ESP proceeding, it still appears that the Commission intends to require that the ESP *must be* consistent with these state policies in order to be approved. Such a requirement is inconsistent with the limited MRO comparison test set out in §4928.143 (C) (1), Ohio Rev. Code, for approval of an ESP. The Commission should delete any reference to proving an ESP is consistent with state policy.

This rule layers yet another requirement for approval of an ESP -- the "just and reasonable" standard. As AEP Ohio explained in its Initial Comments, this standard typically is associated with traditional cost-based rate regulation.

The evolution of S.B. 221 demonstrates the impropriety of including a just and reasonable test (and consistency with state policy test) in the ESP process. While prior versions of the legislation did include both the 4928.02 policy mandates and the "just and reasonable" test within the standard to be applied in approving an ESP, the version of S.B. 221 adopted by the General Assembly did not. *See e.g.*, Sub. S.B. 221 (As Passed by Senate) §4928.14 (D) (6) (a), http://www.legislature.state.oh.us/bills.cfm?ID=127_SB_221_PS. Given this history, it is clear that this division would adopt tests that were rejected by the General Assembly. Accordingly, the last sentence of this division should be deleted on rehearing.

4901:1-35-09 (D): This rule addresses the hiring of consultants to conduct prudence and financial reviews of fuel/purchased power adjustments. On rehearing, the Commission should specify that the cost of hiring such consultants is recoverable through the cost recovery mechanism being reviewed. Such recovery is consistent with the reference in §4905.31 (E), Ohio Rev. Code, to recovering costs of complying with government mandates.

4901:1-36: Transmission Cost Recovery

4901:1-36-03 (C): This rule addresses the hiring of consultants to conduct prudence and/or financial reviews of costs incurred and recovered through the transmission cost recovery rider. On rehearing, the Commission should specify that the cost of hiring such consultants is recoverable through the cost recovery mechanism being reviewed. Such recovery is consistent with the reference in §4905.31 (E), Ohio Rev. Code, to recovering of costs of complying with government mandates.

4901:1-37: Corporate Separation

4901:1-37-04 (D) (1): This rule prohibits the release of proprietary customer information without the customers' authorization, except as required by a regulatory agency or court of law. On rehearing the rule should be modified to explicitly clarify that a properly issued subpoena is one of the bases for releasing such information in the absence of customer authorization.

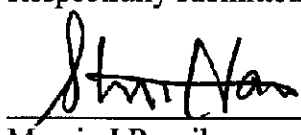
4901:1-37-09 (F): This rule provides for Staff's access to the books, accounts and other records kept by the transferor and transferee as related to the application to sell or transfer generating assets. The meaning of the phrase "as related to the application is unclear. The rule, however, appears to provide for perpetual access to a transferee's books, accounts and other records, regardless of whether those materials included information beyond the scope of the transaction, and whether the transferee is an affiliate of the transferor.[1] On rehearing, the Commission should modify this rule to make clear that access to the transferee's books, accounts and other records is only for the period prior to the actual transaction and only for information related to the transaction.

[1] If the transferee is an affiliate of the transferor, the Staff will have access to its books, accounts and other records pursuant to Rule 4901:1-37-07 (A).

CONCLUSION

For the foregoing reasons, the rule provisions discussed above should be reconsidered and modified by the Commission on rehearing.

Respectfully submitted,



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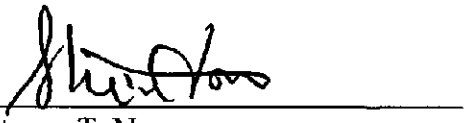
CERTIFICATE OF SERVICE

I hereby certify that a copy of Columbus Southern Power Company's and Ohio Power Company's Application for Rehearing was served by US Mail upon counsel for parties that filed comments.



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