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BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of the Columbus Southern Power Company for Approval of its Electric Security Plan; an Amendment to its Corporate Separation Plan; and the Sale or Transfer of Certain Assets.	)))))	Case No. 08-917-EL-SSO
In the Matter of the Application of the Ohio Power Company for Approval of its Electric Security Plan; an Amendment to its Corporate Separation Plan; and the Sale or Transfer of Certain Assets.	)))))	Case No. 08-918-EL-SSO

BRIEF OF THE OHIO HOSPITAL ASSOCIATION

I. INTRODUCTION

A. The Ohio Hospital Association.

The Ohio Hospital Association ("OHA") is a private, nonprofit trade association with 178 hospitals and 40 healthcare system members that have more than 700 electricity accounts statewide. Collectively, OHA members annually spend well in excess of $150 million for electric services, about $4,500 per staffed bed. A significant amount of that expenditure is for electric service provided by the Columbus Southern Power Company ("CSPC") and the Ohio Power Company ("OPC") (collectively, "AEP" or the "Company") to the approximately 50 OHA member hospitals in the service territories of AEP's operating companies. For example, in the Central Ohio area, the OhioHealth hospital organization (an active OHA member) spent approximately $8.6 million on electricity in 2008.[1]

Hospitals and healthcare systems have a unique profile on the electric grid. Their loads

[1] OHA Exhibit 5, p. 2, lines 39-40.

vary from smaller medical office buildings and outpatient centers operating during normal business hours, to traditional hospitals providing inpatient acute care on a 24-hour basis every day of the year. Major hospital facilities must operate around the clock, 365 days each year, thereby requiring that they have a continual supply of electricity from the local utility or on-site generation facilities.[2] These facilities (during 2006) provided inpatient care for 1.5 million people, outpatient care for 32.7 million people, and emergency room care for 933,000 uninsured people, 74,670 of whom were admitted after their initial emergency room visit. For example, in AEP's Central Ohio service territory, OhioHealth anticipates having around 100,000 inpatient admissions and over 2,200,000 outpatient and emergency visits in 2009.[3] In financial terms, Ohio hospitals provided $1.8 billion in community benefits, including $868 million in charity care in 2006 alone.[4]

The outcome of this proceeding will have a substantial impact on the operation of the OHA members' facilities and the cost at which they provide their essential services to the communities within the AEP service territories. Every patient's health (and possibly life) would be at a significantly greater risk were there disrupted and/or unavailable electric service.[5] For everything "[f]rom the lighting, heating and cooling of the facilities, to the high technology diagnostic and treatment equipment that are used to treat these patients, electricity is integral" to the services provided by OHA-member hospitals.[6]

It is highly significant that the OHA's members have a number of things in common with AEP. As a regulated local distribution utility, AEP is an essential backbone of the Ohio

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2 *Id.* at p. 2, lines 22-25.

3 *Id.* at p. 3, lines 4-5.

4 OHA Website at http://www.ohanet.org/benefit/default.htm.

5 OHA Exhibit 5 at p. 3, lines 5-6.

6 *Id.* lines 7-9.

communities it serves. Hospitals, too, serve an essential function within their communities. There is a strong element of mutual dependence at work between the hospitals and AEP: hospitals are dependent on utility service, and the operating companies are dependent upon the hospitals that provide essential health care services to those companies' employees.

The relationship between AEP, its Ohio employees, the hospitals and the communities they serve runs deep. AEP employees and officers are community leaders, some possibly sitting on the boards of OHA member hospitals. Because of this symbiosis, the OHA clearly understands the importance of a viable, financially-healthy electric utility in their communities. The OHA wants AEP to succeed financially and recognizes the importance of that success to the communities in which OHA members are a part.

Nevertheless, the hospitals within the communities served by AEP must be able to thrive in order to continue to provide health care services in their communities. This need goes beyond the ability to obtain reasonably priced electric service for their own operations. Perhaps more importantly, the businesses within their communities must be able to continue to operate in order to employ the residents of those communities. Employers are the primary source of private health insurance for patients, which hospitals depend upon for their financial viability. When jobs are lost from the community, the hospitals still provide necessary health care, but now without the financial support of employer-provided insurance. This presents an unsustainable situation. The health of the local economy is tied to—in a very direct way—the health of the community. Hospitals need a healthy economy in order to survive, just as AEP needs a healthy local economy in order to recover its costs of providing necessary services.

It is from this perspective that the OHA urges the Public Utilities Commission of Ohio ("Commission") to modify AEP's proposed electric security plan ("ESP"), as argued by the

Commission Staff and intervening parties. AEP's proposal would place an intolerable burden on the economic health of the communities that it serves which would in turn upset the balance of these mutual dependencies.

Under more favorable economic circumstances this case might call for a different outcome. This is certainly not the time to incur the very real risk of pushing the economy of Ohio further into a recessionary spiral, thereby endangering hospitals and their ability to serve communities and patients, including the employees of AEP.

II. BACKGROUND

A. Procedure.

On July 31, 2008, AEP filed its application for authority to establish their Standard Service Offer ("SSO") ("Application"), as required by Ohio Revised Code Section ("R.C.") 4928.141. This application was docketed as Case Nos. 08-917-EL-SSO and 08-918-EL-SSO.

On August 20, 2008, OHA filed its motion to intervene in these cases. That motion was granted by Attorney Examiner Entry dated September 19, 2008. The following parties were also granted intervenor status in this case: American Wind Energy Association/Wind on the Wire/Ohio Advanced Energy ("AWEA"); Constellation NewEnergy, Inc. and Constellation Energy Commodities Group, Inc. ("Constellation"); Dominion Retail, Inc.; Industrial Energy Users-Ohio ("IEU-Ohio"); Integrys Energy Services. Inc. ("Integrys"); Morgan Stanley Capital Group; National Energy Marketers Association ("NEMA"); Natural Resources Defense Council; Office of the Ohio Consumers' Counsel ("OCC"); Ohio Association of School Business Officials, the Ohio School Boards Association and the Buckeye Association of School Administrators; Ohio Energy Group ("OEG"); Ohio Environmental Council; Ohio Farm Bureau; Ohio Manufacturers' Association ("OMA"); Direct Energy Services, LLC; Ormet Primary

Aluminum Corporation; ConsumerPowerline; Ohio Partners for Affordable Energy ("OPAE"); The Kroger Company; The Sierra Club, Ohio Chapter; and The Commercial Group, Wal-Mart Stores East LP, Sam's Club East, LP, Macy's Inc., and BJ's Wholesale Club, Inc. Evidentiary hearings were held in the case from November 17, 2008 through December 2, 2008. Over the course of 14 days of hearings, testimony was elicited from approximately 43 witnesses resulting in an extensive record having been compiled.

In addition to the evidentiary hearing, five local public hearings were held pursuant to order of Attorney Examiner Greta See dated September 24, 2008. These hearings commenced on October 14, 2008 and continued through October 27, 2008 in locations across the state.

B. Amended Senate Bill 221.

Amended Senate Bill 221 ("SB 221") is a complex new law that vests the Public Utilities Commission of Ohio (the "Commission") with considerable authority and discretion to regulate the provision of electric service in Ohio. SB 221 gives the Commission an opportunity to set the tone for the Ohio economy and decide whether the state of Ohio, its residents, its industries, its hospitals, its employers and employees, or its electric distribution utilities will be better off under market rates or an ESP designed by AEP and approved by the Commission.

Under SB 221, as codified in R.C. 4928.141(A), an electric distribution utility has an obligation to provide a standard service offer ("SSO") to its customers beginning January 1, 2009. The utility can satisfy its obligation to provide an SSO to customers in one of two ways—through a market rate offer ("MRO") under R.C. 4928.142, or an ESP under R.C. 4928.143. More specifically, SB 221 contains a number of requirements relating solely to a utility's first post-SB 221 application filed with the Commission for generation service rates. In particular,

the first filing of a utility must be an ESP regardless of whether an MRO also is submitted.[7] In simpler terms, if the utility's first SSO application is for an MRO, that application must include an ESP proposal as well.

As part of its initial SSO application, and pursuant to R.C. 4928.143, AEP submitted an ESP. The purported benefit of an ESP is that it provides the Commission with assurances that customers will receive stable, reasonably-priced electric service for the plan's duration when compared to an MRO. The question now before the Commission is whether the plan proposed by the Companies satisfies the requirements of SB 221. The Companies have interpreted SB 221 to not require cost justification or quantitative analysis of the ESP's proposed generation rates and charges. AEP proposes to use its application in this proceeding to increase its revenues by as much as $686,412,652 over the course of three years, raising rates substantially to certain customers.

Because AEP has not yet filed an application for authority to establish an MRO pursuant to R.C. 4928.142, which would serve as an alternative to its ESP proposal—and a fallback option should its ESP proposal be denied—AEP's ESP application represents its first rate offering under SB 221.

The Commission must correct the glaring deficiencies in AEP's ESP proposal in order to protect Ohio consumers, the fifty hospitals served by AEP, and the Ohio economy. The OHA thereby respectfully submits its brief opposing the ESP proposed by AEP.

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[7] R.C. 4928.141(A). This provision states:

> the electric distribution utility shall apply to the public utilities commission to establish the standard service offer in accordance with section 4928.142 [4928.14.2] or 4928.143 [4928.14.3] of the Revised Code and, at its discretion, may apply simultaneously under both sections, except that the utility's first standard service offer application at minimum shall include a filing under section 4928.143 [4928.14.3] of the Revised Code.

III. LAW AND ARGUMENT

A. R.C. 4928.143: The standard for Commission-approval of an Electric Security Plan.

R.C. 4928.143 sets forth the requirements for the approval of an ESP. The following is a non-exhaustive list of items an ESP may provide for:

- Automatic recovery of certain costs (i.e., fuel costs incurred in generating electricity supplied under the plan; costs of purchased power supplied under the offer; emission allowance costs; and cost associated with carbon or energy taxes);[8]
- Reasonable "allowance for construction work in progress" or "for an environmental expenditure *** incurred *** on or after January 1, 2009," provided the Commission determines there is "need for the facility" and construction was "sourced through a competitive bid process;"[9]
- "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, carrying costs, amortization periods, and accounting or deferrals;"[10]
- "Automatic increases or decreases in any component of the standard service offer price;"[11]
- Provisions allowing for the securitization of any "phase-in," and the recovery of costs associated with securitization;"[12]
- "Provisions relating to transmission, ancillary, congestion, or any related service required for the standard service offer, including provisions for the recovery of any cost of such service that the electric distribution utility incurs on or after that date pursuant to the standard service offer;"[13]
- "Provisions regarding the utility's distribution service, including *** single issue ratemaking, a revenue decoupling mechanism or any other incentive

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

9 R.C. 4928.143(B)(2)(b). "An allowance approved under division (B)(2)(b) of this section shall be established as a *nonbypassable* surcharge for the life of the facility."

10 R.C. 4928.143(B)(2)(d).

11 R.C. 4928.143(B)(2)(e).

12 R.C. 4928.143(B)(2)(f).

13 R.C. 4928.143(B)(2)(g).

ratemaking, and provisions regarding distribution infrastructure and modernization incentives for the electric distribution utility," but only after the Commission makes sure that "customers' and the electric distribution utility's expectations are aligned and that the electric distribution utility is placing sufficient emphasis on and dedicating sufficient resources to the reliability of its distribution system;"[14] and

- "Provisions under which the electric distribution utility may implement economic development, job retention, and energy efficiency programs."[15]

Perhaps most importantly, the Commission can only approve an ESP application if it determines that the ESP, "including its pricing and all other terms and conditions, including any deferrals and any future recovery of deferrals, ***is more favorable in the aggregate*** as compared to the expected results that would otherwise apply under section 4928.142 of the Revised Code." (emphasis added.) In simpler terms, the ESP must put customers in a better position than they would be under the same utility's MRO established pursuant to R.C. 4928.142.

1. The "more favorable in the aggregate" test.

The Commission has wide discretion and flexibility in applying the statutory test reflected in SB 221. It is the Commission's task to sort through the considerations that make an ESP application "more favorable in the aggregate" than an MRO. Exactly how the Commission should undertake this exercise is anything but clear.

AEP witness Baker suggests that if ESP *rates* are more favorable to customers than market rates under an MRO, then this is, by itself, a meaningful standard that may be applied by the Commission without reference to other considerations.[16] But this is *not* the standard contained in SB 221. The test to be applied by the Commission must take into account not only pricing, but *all other terms and conditions* of the proposed ESP, compared to the "expected

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14 R.C. 4928.143(B)(2)(h).

15 R.C. 4928.143(B)(2)(i).

16 Company Exhibit 2 at p. 3.

results" that would otherwise apply under section 4928.142. It is the totality of the circumstances presented by both the ESP application and the totality of the expected results of an MRO that must be weighed by the Commission. Unlike traditional ratemaking, the legislature did not provide the Commission with a clear formula as to *how* it should arrive at a reasonable determination. In the absence of constraining direction by the legislature, the Commission must rely on the broad guidance that the legislature *did* provide.[17]

2. The Commission must not lose sight of the public interest in evaluating the merits of AEP's ESP proposal.

In carrying out its responsibilities under Chapter 49 of the Ohio Revised Code, the Commission cannot lose sight of its primary function of serving the public interest, including the interests of the 50 hospitals served by AEP.[18] Section 4928.02 sets forth the important state policies underlying the regulation of electric utilities in the state of Ohio, including the following:

> (A) Ensure the availability to consumers of adequate, reliable, safe, efficient, nondiscriminatory, and reasonably priced retail electric service;
> (B) Ensure the availability of unbundled and comparable retail electric service that provides consumers with the supplier, price, terms, conditions, and quality options they elect to meet their respective needs;
> ***
> (G) Recognize the continuing emergence of competitive electricity markets through the development and implementation of flexible regulatory treatment;
> (H) Ensure effective competition in the provision of retail electric service by avoiding anticompetitive subsidies flowing from a noncompetitive retail electric service to a competitive retail electric service or to a product or service other than retail electric service, and vice versa, including by prohibiting the recovery of any generation-related costs through distribution or transmission rates;

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17 *Cf., Columbus Southern Power v. PUC,* (1993) 67 Ohio St. 3d, 535, 537.

18 In fact, the Commission's own mission statement defines its primary goal as "to assure all residential and business consumers access to adequate, safe and reliable utility services at fair prices, while facilitating an environment that provides competitive choices." (Emphasis added.) http://www.puco.ohio.gov/PUCO/about/mission.cfm.

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(N) Facilitate the state's effectiveness in the global economy.

As emphatically stated in the Commission's recent Opinion and Order in the FirstEnergy case:

> The Commission believes that the state policy codified by the General Assembly in Chapter 4928, Revised Code, sets forth important objectives which the Commission must keep in mind when considering all cases filed pursuant to that chapter of the code. Therefore, in determining whether the ESP meets the requirements of Section 4928.143, Revised Code, the Commission takes into consideration the policy provisions of Section 4928.02, Revised Code, and we use these policies as a guide in our implementation of Section 4928.143, Revised Code.[19]

It is because of these policy considerations that the Commission must view the "more favorable in the aggregate" standard through the lens of the overriding "public interest." The public interest cannot possibly be served by an outcome that is not also reasonable. Even the Company acknowledges that R.C. 4928.02(A) requires a reasonable outcome in this case.[20] While it may be the case that SB 221 does not contemplate a return to the "just and reasonable" standard under traditional rate-base-rate-of-return regulation, it is equally clear that the legislature has not determined that the market will necessarily produce a reasonable outcome; otherwise the Herculean efforts that went into the passage of SB 221 would not have been necessary. The earnings test provisions of SB 221 would not be necessary if the legislature was placing its faith in market outcomes. An outcome in this case that *increases* an already very healthy return on equity to the shareholders of AEP at the time of a major economic downturn in the greater Ohio economy cannot pass a test of "reasonable" under any circumstances. As

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19 *Ohio Edison Company, Cleveland Electric Illuminating Company and Toledo Edison Company*, Case No. 08-935-EL-SSO (*Opinion and Order* dated December 19, 2008) (hereinafter referred to as "FirstEnergy Order").

20 Company Exhibit 2 at p. 3.

Kroger witness Higgins aptly opined, "I do not believe it would be in the public interest to knowingly adopt an ESP proposal that was expected to fail a Significantly Excessive Earnings Test."[21] This point should guide the Commission in its evaluation of the terms and conditions of AEP's ESP.

B. AEP has the burden of proof in this ESP proceeding.

As set forth in R.C. 4928.143(C)(1), the burden of proof in this proceeding lies solely with AEP. AEP must demonstrate that the ESP, as proposed, including its pricing and all other terms and conditions, including any deferrals and any future recovery of deferrals, is more favorable in the aggregate to customers[22] than the expected results of an MRO alternative.[23] AEP has touted the benefits of the overall package of the ESP as making it more favorable in the aggregate than the expected results of an MRO.[24] To the contrary, and as discussed in detail below, the proposed ESP fails to mitigate the harmful effects of the creation of new regulatory assets and deferrals, and the effects of the substantial rate increases confronting hospitals on January 1, 2009. Accordingly, this ESP proposal does not provide benefits that make it more favorable than a simple MRO.[25]

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21 Kroger Exhibit 1 at p. 6, lines 1-2.

22 The question of "more favorable to whom" is not explicitly addressed in the statute. The OHA read Section (C)(1) to require the ESP to be more favorable to customers in the aggregate, and therefore include this language in addressing the applicants' burden of proof.

23 R.C. 4928.143(C)(1).

24 See, e.g., Application, p. 3.

25 In light of the numerous parties that have intervened in this proceeding and contributed to the development of a record which shows AEP's application may be deficient in multiple areas, the OHA will only address the application as it most substantially affects its members' interests. This should not be construed as support for other provisions of the application not discussed by the OHA. These other provisions likely will be addressed by other parties, and will provide an additional basis for the Commission to determine that AEP's application, as proposed, and without any modifications, should not be approved under the "more favorable in the aggregate" test.

C. The unreasonable non-FAC increases must be eliminated, or at a minimum, reduced as recommended by the Staff.

As part of its ESP application, AEP proposes to increase non-FAC base generation rates by 3% and 7% each year for the life of the ESP for CSPC and OPC respectively.[26] These increases are composed of "non-specific, non-FAC-related generation charges" designed to cover environmental "2009 carrying costs associated with 2001-2008 environmental investments"[27] and increases in labor and material costs.[28] Furthermore, AEP attempts to justify these increases on the grounds they are "consistent with the percentages that were used to adjust total rates in the RSP, so we believe customers are familiar with that."[29]

Based upon Exhibit DMR-1 provided by AEP, the results of this proposal will be unjustified increases of "$14.209 million in 2009, $14.636 million in 2010 and $15.075 million in 2011 for CSP[C]"[30] and "47.771 million in 2009, $44.695 million in 2010 and 47.824 million in 2011 for OPC."[31] According to AEP Exhibit JCB-2, the total increase over the three-year life of the ESP will be "$87 million" for CSPC and "$263 million" for OPC.[32]

AEP, however, provided no cost basis in support of these arbitrary rate increases.[33] AEP witness Baker explained that the "3[%] and 7[%] increases in the generation cost, non-FAC generations costs, are **not cost based**."[34] (Emphasis added.) Expounding on this point, AEP

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26 Company Ex. 1, Exhibit DMR-1.

27 Tr. Vol. XI, p. 220, lines 9-11.

28 Tr. Vol. IX, p. 92, line 13 through p. 93, line 12.

29 OCC Exhibit 10 at pp. 9-10, citing to the Deposition of J. Craig Baker, October 25, 2008 at 56.

30 OEG Exhibit 3 at p. 18, lines 14-16.

31 *Id.*, lines 18-20.

32 *Id.*, lines 16-17 and 19-20.

33 *Id.*, line 23 through p. 19, line 1.

34 Tr. Vol. XI, p. 87, lines 9-10. See also Tr. Vol. XI, p. 139, lines 6-10. See also OCC Ex. 10, p. 9, lines 19-21 (explaining that AEP has "not provided any analysis to justify these percentage increases, and in fact state that these increases are not based on costs").

witness Baker engaged in the following exchange with counsel:

> Q. And yet these are specific increases upon which you -- specific items upon which you base this increase; isn't that correct?
>
> A. I believe what I have said in a deposition, in response to a question you made earlier, and in response to my counsel was that these are not cost-based increases.
>
> Q. And didn't you also say in your deposition that there's no specific cost justification for these increases and that you don't think any is required?
>
> A. That, to me, is a definition of noncost based.[35]

Not surprisingly then, Staff witness Cahaan proved unable to answer a question regarding what actual costs were included in his recommendation to cut in half the proposed non-FAC generation rate increases, because "the 3[%] and 7[%] that was in the RSP was not cost based. The 3[%] and 7[%] that's in the ESP is, to my understanding, not a regulatory type, traditional regulatory type cost-based number."[36]

Furthermore, there is no support anywhere in SB 221 that would support an arbitrary rate increase with absolutely no supporting basis.[37] As Staff witness Cahaan pointed out, the rate increases "may have been a reasonable expectation of cost increases at the time that the ESP was contemplated, but not now."[38] Simply put, we are now in a "financial crisis, we are entering a recessionary, and possibly deflationary, period, and any expectations of price increases need to be **revised downwards**."[39] (emphasis added.)

As OCC witness Smith explained:

> there are specific allowances in SB 221 regarding the MRO, and those

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35 Tr. Vol. XI, p. 230, lines 10-22.

36 Tr. Vol. XII, p. 209, lines 18-21.

37 OEG Exhibit 3 at p. 19, lines 3-6.

38 Staff Exhibit 10 at p. 4, lines 9-10.

39 *Id.*, lines 11-12.

> allowances would not include an increase to the non-FAC portion of the generation rate. So the company's approach of increasing the non-FAC portion of the ESP is saying that, well, we're buying slightly less power from the SSO in the MRO and we're buying slightly more in the ESP and somehow that gives us the right to increase the base portion of the generation rate. That strikes me as just an irrational position.[40]

Furthermore, customers are unable to seek a reduction in the non-FAC generation rates during the three-year term of the ESP.[41]

If, however, the Commission deems it appropriate to increase AEP's non-FAC generation rates by some amount, the OHA could endorse the recommendation of Staff witness Cahaan that the arbitrary non-FAC generation rate increases be cut in half, meaning more reasonable increases would be 1.5% for the Columbus Southern Power Company and 3.5% for the Ohio Power Company.[42] Nevertheless, under current economic conditions, it is difficult to imagine how such a purely gratuitous increase in electric rates could be justified.

D. AEP must not be allowed to recover its POLR costs through nonbypassable charges.

Ohio electric distribution utilities retain a POLR obligation by virtue of R.C. 4928.141. However, as Staff witness Cahaan noted: "We have had discussions about POLR for a number of years now and I got to admit that **the concept is about as slippery as anything I've ever seen in public utility regulation**, it changes and morphs depending upon who's talking about it when and how."[43] (Emphasis added.)

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40 Tr. Vol. VI, p. 89, line 19 through p. 90, line 3.

41 Id., p. 180, lines 15-18.

42 Tr. Vol. XI, p. 209, lines 9-14.

43 Tr. Vol. XII, p. 257, lines 7-12.

As part of its ESP application, AEP proposed a "non-bypassable Provider of Last Resort (POLR) Rider"[44] purportedly designed to compensate it for the risks arising from its status as a POLR supplier of generation service. These risks are that "customers would ... chose market at a time when market prices are lower than SSO and ... come back when that condition changes."[45] In simpler terms, the risk is twofold: (1) that customers may leave SSO service and (2) customers may return to SSO service.[46] AEP acknowledged that at least for the Columbus Southern Power Company, the POLR charge itself represents one of the two largest sources of the overall rate increase proposed by AEP.[47] In total, the POLR charge will result in increased POLR revenues of $93 million between 2009 and 2011 for the Columbus Southern Power Company alone.[48]

OHA strongly supports the position of the Commission Staff that the "AEP companies not be allowed their requested provider of last resort (POLR) charge."[49]

First, and foremost, SB 221 does not mandate that the Commission compensate AEP (or any electric distribution utility) for POLR risks. Not only is SB 221 silent, but these very risks for which AEP seeks to be compensated for are mitigated by statute—specifically, R.C. 4928.142. Therefore, AEP has no entitlement to compensation as part of its proposed SSO rates, or a separate rider, for the very POLR risks it alone must bear. Revised Code 4928.141 imposes a regulatory obligation on Ohio electric distribution utilities to provide SSO service. As the Company persuasively argues through Mr. Baker's rebuttal testimony, SB 221 is not a return to

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44 Application, p. 7. Making this POLR charge nonbypassable means that customers will pay the charge regardless of whether they actually shop. Tr. Vol. XI, p. 19, lines 2-5.

45 Tr. Vol. III, p. 151, lines 9-13 (AEP witness Hamrock).

46 Tr. Vol. VI, p. 215 line 24 through p. 216, line 7.

47 Tr. Vol. IX, p. 193, lines 3-9.

48 Id., p. 196, lines 1-3.

49 Staff Exhibit 1 at p. 4, lines 3-4.

rate of return regulation.[50] But neither does SB 221 contain any particular standard of compensation for the obligations that it imposes, except where there are explicit references to cost recovery. The POLR risk is not one of those enumerated costs. In theory, this leaves the constitutional standards applicable to takings as the absolutely clear threshold that the Commission must meet with respect to compensating the Company for its POLR risk. As the corpulent returns now enjoyed by AEP attest, there is little foreseeable risk that the Fifth Amendment's capital attraction test[51] is implicated by the Commission's elimination of AEP's requested POLR charge. SB 221 provides ample benefits to the electric distribution utilities, such as relief from the provisions of R.C. 4909; but along with those benefits come corresponding burdens. The POLR obligation is one of those burdens. No direct compensation is necessary, nor would it be fair.

Furthermore, AEP's "POLR charge is a charge to all customers."[52] More specifically, AEP is "proposing that each customer be required to purchase an option that will give such customer the right (in economic terms) to either leave SSO service for a lower market price or return from the market to a lower SSO price (the ESP tariff)." As OEG witness Baron notes:

> if customers elect to waive their rights to shop during the three year ESP term, then there is no risk to the Companies from customer switching and no basis for the Companies [AEP] to impose the POLR option charge. Simply put, if a customer decides to not buy the "option," then there should be no charge. Customers should not be "forced" to purchase an option if they make a three year binding commitment to waive their shopping rights.[53]

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50 Company Exhibit 2 at p. 3.

51 *Duquesne Light Co. v. Barasch*, 488 U.S. 299 (1989).

52 Tr. Vol. I, p. 188, lines 15-16.

53 OEG Exhibit 2 pp. 11-12.

However, even AEP admits that there is virtually no shopping in AEP's Ohio territories.[54] Further expounding on this proposition, Kroger witness Higgins explains:

> AEP is proposing to increase dramatically the rates charged for POLR service based on an analysis of option pricing using the Black-Scholes model presented by Mr. Baker. The Company's position is that this approach properly values the risk AEP faces with respect to shopping customers returning to utility service at times when market prices increase. The POLR charge proposed by AEP for the three-year duration of the ESP is in excess of $500 million for the two utilities. This strikes me as rather stiff premium for utility customers to pay when few customers have actually shopped in the AEP Ohio service territories since the onset of direct access.[55]

E. The distribution service issues addressed in AEP's proposal merit further scrutiny, but not in this accelerated ESP case.

The record in this case reflects the fact that the distribution prong of AEP's electric service deserves further Commission scrutiny--but not in the context of this accelerated ESP proceeding. Unlike most ESP filings in Ohio, SB 221 required that the first post-SB 221 ESP filing be ruled upon by the Commission "150 days after the initial application filing date."[56] It would be a "disservice to the customers, including OHA, to rush this proceeding without a thorough and complete review" of all documents supporting AEP's proposal.[57]

With such an "aggressive" time frame imposed by SB 221,[58] the Commission should not force distribution-related issues into this ESP proceeding when the Commission would be better served doing so in the context of a separate rate case. In fact, the Commission did just that in the FirstEnergy ESP case (08-935) by stating that "the Commission declines to resolve in this [ESP]

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54 Tr. Vol. XI, p. 46, lines 8-12.

55 Kroger Exhibit 1 at p. 11, lines 6-14.

56 OHA Exhibit 3 at p. 13, lines 17-18 (referencing R.C. 4928.143(C)(1).

57 *Id.* at p. 17, lines 13-14.

58 *Id.* at p. 14, lines 1-2. See also OHA Exhibit 3 at p. 15, lines 10-11 (explaining his concern that "OHA is being rushed to judgment on what its position should be on the reasonableness and accuracy of the [ESP] filing").

case the substantive issues of the FirstEnergy Distribution Rate Case."[59] Therefore, OHA supports the recommendation of the Commission Staff that AEP "file a base rate case in 2009 to recover the costs" associated with the various distribution-related programs in its ESP proposal.[60]

1. AEP is due for a base distribution rate case.

Furthermore, AEP is due for a base distribution rate case. The last distribution rate case filed by the Columbus Southern Power Company was 17 years ago, and the last one for the Ohio Power Company was 14 years ago.[61] In the past 15 years, the electric distribution industry has undergone "tremendous changes."[62] The most glaring change has been the fact that AEP "unbundled the rates from a vertically integrated utility to a distribution utility."[63] Staff concluded that this change alone warrants the filing of a separate distribution rate case.[64]

2. A distribution rate case is necessary to publicly discuss AEP's distribution system, which has been scrutinized in recent years.

In addition to the fact that AEP is due for a distribution rate case, there are a number of issues that need to be addressed in a public setting in which AEP, the Commission, and members of the public can "air" their grievances. As Staff witness Hess explained, "[t]here have been a lot of accusations and public discussions about the AEP companies management of its distribution system specifically as it related to the costs of the 2004/2005 ice storms and the 2008 hurricane damage."[65] In fact, as part of PUCO Case No. 06-622-EL-SLF, the Commission, AEP,

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59 FirstEnergy Order at p. 35.

60 Staff Exhibit 1 at p. 5, lines 18-21. See also Tr. Vol. XIII, p. 78, lines 16-21, and p. 81, lines 22-23.

61 *Id.* at p. 6, lines 2-3.

62 *Id.*, lines 3-4. More specifically, Staff witness Hess explains that authorized rates of return, rate base investments, operation and maintenance expenses, sales levels, taxes and a number of the other components of the revenue requirement are different. Staff Exhibit 1 at p. 6, lines 6-8.

63 *Id.* at p. 6, lines 10-11.

64 *Id.*

65 Hess Testimony, p. 6, lines 14-17.

and the public engaged in lengthy formal and informal discussions relating to problems involving the management of AEP's distribution systems.[66] A separate distribution rate case would provide the perfect setting for this dialogue--and help AEP regain the public's trust.

3. AEP's proposed enhanced service reliability plan (ESRP) is deficient and should be rejected.

The OHA is very much concerned with service reliability and the overall condition of AEP's distribution network. As explained above, the critical function of hospitals is dependent on reliable electric service. The OHA supports AEP's efforts to improve its distribution system reliability and OHA members expect to pay for the services they receive from AEP. But those rates are still subject to the provisions of R.C. 4909 and the consumer protections of the traditional ratemaking structure that ensure just and reasonable rates.

Through the testimony of Karl G. Boyd, AEP categorizes the major programs it uses to "maintain its distribution infrastructure," including: (1) distribution asset management programs (i.e. overhead line inspections); (2) major distribution reliability improvements and capacity additions (i.e. "distribution circuit reconfigurations" or "adding new substations and associated lines"); and (3) a distribution vegetation management program (i.e. trimming, moving and herbicide applications).[67] Many of these programs were adopted as part of the Commission's ongoing investigation into AEP's electric distribution service reliability problems.[68] In fact, as recently as October 2006, AEP filed an "Enhanced Distribution Reliability Plan" that "expanded on the Company's base distribution reliability programs, added incremental reliability programs, and provided for increased funding by ratepayers of the Company's reliability-related

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66 Tr. Vol. XIII, p. 79, line 7 through p. 80, line 11.

67 Company Exhibit 11 at p. 5, lines 3-9, and p. 7, lines 6-18.

68 See OCC Exhibit 13 at pp. 17-21 (explaining AEP's continuing struggle to implement the Commission's recommendations relating to distribution service reliability between 2003 and 2006).

programs."[69]

As part of its ESP proposal, AEP presented the three-year ESRP,[70] which contains the following "enhancements":

- Additional overhead line inspection programs;
- Additional vegetation management programs (i.e. clearing of rights-of-way); and
- Targeted underground distribution cable replacement and/or rejuvenation.[71]

It is this plan that AEP touts as the "means by which the Company can reach the next level of reliability."[72]

AEP, however, fails to demonstrate how these "enhanced" programs "go beyond what it should be doing on a normal basis."[73] The majority of the ESRP consists of activities AEP should already be doing.[74] Simply stated, reliability programs that allow AEP to "'catch-up' because its reliability programs were inadequate are not 'enhancements.'"[75] AEP "has not shown that the additional investment it has proposed as part of its ESRP will noticeably enhance distribution system reliability."[76] The Commission must hold AEP accountable for "achieving the projected reliability improvements associated" with these programs[77]--and that can best be done in a separate rate case.

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69 *Id.* at p. 20, lines 14-15 and p. 21, lines 5-8.

70 Tr. Vol. V, p. 166, lines 1-2. See also Company Exhibit 11 at p. 3, lines 6-7.

71 Tr. Vol. V, p. 178 line 24 through p. 179, line 5. See also Company Exhibit 11 at p. 17, lines 9-14.

72 OCC Exhibit 13 at p. 28, lines 20-21.

73 *Id.* at p. 30, lines 5-6.

74 Tr.Vol. VII, p. 65, lines 18-20.

75 OCC Exhibit 13 at p. 30, lines 9-11.

76 Tr. Vol. VII, p. 61, lines 9-16. See also OCC Exhibit 13 at p. 8, lines 13-15.

77 Staff Exhibit 2 at p. 19, lines 10-11.

i. The "enhanced" overhead line inspection program is not significantly different from AEP's current program.

AEP's overhead line inspection proposal "is not truly enhanced."[78] In fact, the overhead line inspection program is not significantly different from AEP's current program.[79] Instead, the proposed "enhancements" simply reflect the fact that AEP should have, and "should now begin[,] following good industry practice as required by Rule 27 of ESSS [Electric Service and Safety Standards] – which it should have been doing in the normal course of business."[80]

ii. The "enhanced" vegetation management program actually represents the amount of additional work necessary to allow AEP to catch-up to normal industry standards.

The "proposed Vegetation Management Programs, while an improvement over its current performance based program, is not an enhancement but rather a reflection of additional tree trimming needed as a result of their prior program."[81] The prior, performance-based programs allocated resources solely to areas where a vegetation-related outage occurred.[82] As a result, only "those distribution circuits that exhibit especially poor electric service reliability due to tree-related faults probably comes at a cost to overall system reliability."[83] Because tree trimming is a "meat and potatoes" type of activity that has been around for, and completed by utilities, for a

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78 OCC Exhibit 13 at p. 9, lines 12-16. See also Tr. Vol. VII, p. 66, lines 17-19 ("I think the programs in a broad sense are things that I would expect AEP to be doing as a part of providing reliable service").

79 Tr. Vol. VII, p. 79, lines 7-12. For example, AEP's proposed accelerated replacement of certain equipment does not constitute an enhancement as it simply represents AEP's late decision to follow "good industry practices." OCC Exhibit 13 at p. 9, lines 19-20.

80 OCC Exhibit 13 at p. 9, lines 12-16. See also Tr. Vol. VII, p. 66, lines 17-19 ("I think the programs in a broad sense are things that I would expect AEP to be doing as a part of providing reliable service").

81 OCC Exhibit 13 at p. 9, lines 4-7.

82 Company Exhibit 11 at p. 27, lines 15-18.

83 OCC Exhibit 13 at p. 32, lines 5-7. Minimizing vegetation management of the whole circuit "leaves a lot of vegetation in close proximity to circuits, which also tends to increase the tree-related problems that occur during storms." OCC Exhibit 13 at p. 32, lines 7-9. Furthermore, the uncleared parts of the circuit might not be "cleared end-to-end for some number of years." Company Exhibit 11 at p. 27, lines 15-18.

long time,[84] AEP should not be lauded for its untimely decision to implement vegetation management programs that simply bring them into compliance with the orders of the Commission.

4. AEP's Proposed Alternate Feed Service tariff requires further scrutiny

AEP included alternate feed service ("AFS") in its tariff revisions as a part of its ESP application. The OHA supports AEP's efforts in this regard because OHA members have encountered problems with AEP's prior, ad hoc approach to imposing AFS charges on customers where no apparent basis for such charges existed. The OHA believes that AFS should be a tariffed offering with clearly defined terms and conditions. Further, while the OHA does not take issue with the overall structure of AEP's proposed AFS tariff provisions, it does take issue with two aspects of AEP's proposal.

OHA witness Solganick testified to the shortcomings of AEP's proposed AFS structure as they impact hospitals. In particular, Mr. Solganick explained that the six-month notice provision included in AEP's tariff is inadequate because it does not allow customers to adequately consider alternatives to full or partial AFS.[85] For critical use customers like hospitals, changes to their electric supply infrastructure requires a degree of analysis and lead time in order to ensure that its power needs are met in the most cost-effective and reliable manner possible. Mr. Solganick testified that a 24-month planning horizon would be the appropriate interval for AFS planning purposes.[86]

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[84] Tr. Vol. VII, p. 85, line 11 through p. 86, line 3.

[85] OHA Exhibit 4 at p. 16.

[86] Id., at p. 17.

Because this question involves the overall management and cost of operating AEP's distribution system, the OHA urges the Commission to defer treatment of AEP's proposed AFS until AEP's next distribution rate case, where the opportunity of more deliberate treatment will be available, rather than through this highly complex, 150-day case.

While OHA members do not object to paying for the increased reliability that AFS provides, the OHA wants to be assured that the recurring rate structure for that service is correct. Because AEP's proposed rate for AFS service cannot receive the scrutiny that it deserves in the context of this "first" ESP proceeding, AEP's proposed AFS tariff language should not be approved in the context of this proceeding, but rather should follow the other distribution-related features of AEP's application into AEP's next distribution rate case.

5. Schedule NEMS-H is unduly restrictive and should be modified.

AEP included a new tariff provision intended to address SB 221's requirements for hospital-specific net metering. Hospitals, by virtue of the fact that they are required by law to maintain an emergency generation system,[87] are keenly interested in participating in the net metering programs of electric distribution utilities. Net metering and distributed generation, in general, are intended to play a prominent role in supplying the electric needs of Ohio consumers into the future.[88] While AEP's proposed tariff language is faithful to the requirements of R.C. 4928.67(A)(2), certain provisions of AEP's underlying net metering tariff are dated and should be revised in order to make AEP's net metering program more customer-friendly.

OHA witness Solganick raised two important flaws in AEP's net metering tariff that should be corrected by the Commission. First, Mr. Solganick pointed out that AEP's net

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87 OHA Exhibit 5, p. 2.

88 R.C. 4928.02(F).

metering schedules contain facility ownership requirements that have no basis in law.[89] While it may be the case that hospitals have historically owned the generation facilities that they use for emergency purposes, the fact remains that owning and operating electrical generation facilities is not the primary business of hospitals, and as the economics of installing more sophisticated and efficient generating equipment become more favorable, it may be the case that it is in the interest of the hospital to contract with a third party to own, operate and maintain that equipment.[90] The ownership requirements in AEP's net metering schedules would disqualify such an arrangement – needlessly. AEP's proposed Schedule NEMS-H is based upon its pre-existing Schedule NEMS, dating from 2005,[91] prior to the Commission's review of its net metering rules in Case No. 05-1500-EL-COI. The ownership restriction in AEP's proposed Schedule NEMS-H should not be approved by the Commission as it is incompatible with state and federal policies encouraging net metering arrangements and distributed generation generally.

The second issue raised by OHA witness Solganick concerned the payment structure reflected in AEP's Schedule NEMS-H. Mr. Solganick explained that AEP's payment structure for electricity delivered into its distribution system through a net metering arrangement may not properly reflect the benefits received by AEP through the net metering arrangement, particularly with respect to avoided transmission costs.[92] This issue, as raised by Mr. Solganick, serves to underscore the need for a further examination of AEP's rates and tariffs, outside the context of a "first time" ESP proceeding, as recommended by Staff witness Hess. The OHA urges the Commission to refrain from approving Schedule NEMS-H in this proceeding and instead defer

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89 OHA Exhibit 4 at pp. 8-10.

90 Id.

91 Tr. Vol IX, p. 17, lines 11-17.

92 Id., at p. 12.

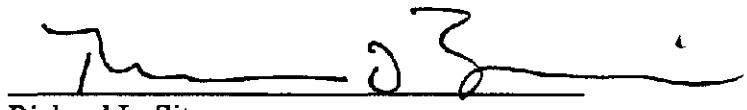
consideration of AEP's Schedule NEMS-H until the next base rate case.

IV. CONCLUSION

The hard reality is that AEP, OHA's member hospitals, Ohio businesses, and their respective communities exist in a symbiotic relationship. This complicated mutual dependence requires a balancing of interests in order to ensure the social and economic well-being of all involved. Promoting the interests of AEP to the serious detriment of the greater community will not only adversely affect the health of Ohioans, but ultimately will damage the financial and physical health of AEP's Ohio and its employees.

For all of the reasons set forth above, OHA respectfully requests that the Commission reject the application of AEP and craft a more reasonable and justified resolution to the setting of new electric rates.

Respectfully submitted on behalf of
OHIO HOSPITAL ASSOCIATION



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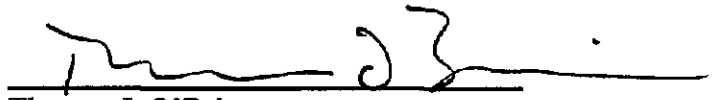
CERTIFICATE OF SERVICE

I hereby certify that the BRIEF OF THE OHIO HOSPITAL ASSOCIATION was served by electronic mail on the parties of record listed below this 30th day of December 2008.



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