

FILE

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Committees

Energy & Public Utilities – Chair
Ways and Means and Economic Development
– Vice Chair
Finance and Financial Institutions
Insurance, Commerce and Labor

May 13, 2009

Alan R. Schriber – Chairman
Ohio Public Utilities Commission
180 E. Broad St.
Columbus, Oh 43215

Dear Chairman Schriber,

Enclosed you will find a letter sent to my office from Mr. Thomas Froehle of the Industrial Energy Users of Ohio. He is writing in regards to concerns his organization has on the subject of a March 18, 2009 order issued by the Public Utilities Commission of Ohio.

Mr. Froehle outlines several concerns the IEU has about the order and informs me that they have filed an application for rehearing with the PUCO to protest this order. I would like to see this situation resolved in a timely and amicable manner.

As such, I would appreciate it if you would review Mr. Froehle's letter, and please respond with your thoughts on the concerns of the IEU. I appreciate your attention in this matter, and I look forward to your response.

Sincerely

Chris Widener
State Senator
10th Senate District

CC: Tom Froehle

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April 16, 2009

Senator Chris Widener
Ohio Senate
Statehouse Rm. 041
Columbus, Ohio 43215

Dear Senator Widener:

On March 18, 2009, the Public Utilities Commission of Ohio ("PUCO") issued an order in a case initiated by Ohio Power Company ("OP") and Columbus Southern Power Company ("CSP") under the new electricity law (SB 221) enacted by the General Assembly and signed by the Governor last year.¹ Today, the Industrial Energy Users-Ohio ("IEU-Ohio")² filed an application for rehearing with the PUCO to protest the PUCO's March 18, 2009 order because the order is unreasonable and unlawful. The PUCO's rate increasing order is also stunningly excessive when compared to the expectations set by the PUCO during presentations to the General Assembly.³ According to the utilities' interpretation of the PUCO's order, they will collect an additional \$1.5 billion during 2009, 2010 and 2011.

Below is a summary of some of the PUCO's determinations that IEU-Ohio has asked the PUCO to reevaluate for the purpose of producing an outcome that better balances the interests of consumers and the utilities.

¹ The order was signed and supported by Chairman Schriber, Commissioner Centolella, Commissioner Lemmie and Commissioner Roberto. Commissioner Fergus did not participate in the decision.

² IEU-Ohio's members include commercial and industrial customers located throughout Ohio including areas served by OP and CSP. Information about IEU-Ohio is available via the Internet at <http://www.ieu-ohio.org>.

³ During the course of recent testimony before the Finance and Appropriations Committee on the Commission's budget, PUCO Chairman Alan Schriber specifically addressed the current difficulties customers are having. In response to an observation made by Representative Yates that "The ordinary citizen feels like they're taking it on the chin," Chairman Schriber stated, "We are very intent, in this day and age, to mitigate rate increases," adding that the Commission's goal is to have "virtually no increase in utility rates." Chairman Schriber went on to say, "I think we're doing a pretty decent job this year of doing that. This is not the year when you want to increase rates. There is no question that, over time, rates are going to go up." Gongwer News Service, Gongwer House Activity Report (March 5, 2009) (Attachment A to IEU-Ohio's application for rehearing).

- Contrary to general expectations created by the PUCO and the language in the PUCO's order, the rate increases the PUCO allowed to go into effect in 2009 exceed the 7 percent to 8 percent total bill increase limitations that the PUCO ordered CSP and OP to observe. The rates that the utilities filed with the PUCO after the PUCO's order made it clear, prior to the PUCO's approval of the rates, that customers would see rate increases significantly above these percentage amounts in 2009. Billing calculations based on the rates filed by the utilities indicated that most, if not all, customers would get double digit percentage increases and that some larger customers would get increases above the 15 percent level that the PUCO rejected because it said rate increases at or above the 15 percent level would impose a severe hardship on customers. To try to correct this mismatch, IEU-Ohio and other parties advised the PUCO that the rates filed by OP and CSP pursuant to the PUCO's order exceeded the total bill increase limitation established by the PUCO. But the PUCO did nothing to stop the 2009 excessive increases from going into effect.
- The PUCO's order authorized CSP and OP to bill and collect electric rates that cram 12 months of rate increases into about 9 months of electric bills making the 2009 rate increase effects even harder on customers. According to press reports, the PUCO explained its choice to, in effect, retroactively increase rates as being necessary because the PUCO was unable to complete its work on time.
- Even though there has been no customer switching in OP's service area and de minimus customer switching in CSP's service area, the PUCO's order gave the utilities rate increases that provide for the recovery of \$152 million annually (\$456 million over the three-year electric security plan period) in compensation for the hypothetical risk of customer switching. **Over the objections of all consumer representatives, the PUCO authorized this rate increase by relying on the same economic model (the Black-Scholes Model) used by the financial community to value and sell the mortgaged backed securities responsible for the largest financial collapse since the Great Depression.** In contrast, a week later the PUCO approved a negotiated settlement for FirstEnergy that eliminated any charges for this hypothetical risk.
- For benchmarking purposes, the PUCO's order appears to have relied on an electricity market price developed by one of its Staff members who acknowledged that the price was high when it was developed and that electric prices had declined after the number was developed. The market price used by the PUCO for purposes of the OP and CSP rate increase order is higher than the market price which the PUCO adopted for

purposes of modifying FirstEnergy's electric pricing proposal in December 2008. And, information which AEP has used in presentations to the financial community shows that AEP agrees that market prices declined sharply during 2008. It is common knowledge that electric prices post-2008 have declined further as conditions in the general economy worked their way into wholesale electric prices. Despite the Staff number being high at the time it was developed and the sharply downward price trends afterwards, the PUCO appears to have picked a high market price number to make its rate increase order look like it is "better in the aggregate" than the statutory alternative. Also for benchmarking purposes, the PUCO appears to have assumed the maximum market purchases blending percentages permitted by Ohio law (Section 4928.142, Revised Code) even though the General Assembly clarified the law, at the Governor's urging, to make it absolutely clear that the PUCO was not required to do so. The use of the maximum blending percentages also appears to have been designed to make the PUCO's rate increase order look like it is "better in the aggregate" than the statutory alternative.

- The PUCO's order increases rates in 2009 and thereafter by \$120 million based on a claim that certain costs of generating assets and contract entitlements in other generation which CSP wanted to sell were not in current rates. In other words, the PUCO selectively applied cost-based ratemaking to increase rates.
- The PUCO's order increased distribution rates by \$34.8 million in 2009 for, among other things, a not-ready-for-prime-time gridSMART proposal. The PUCO apparently believes that allowing AEP to gamble with customers' money may result in the development of a ready-for-prime-time proposal some day in the future. In the meantime, electric rates have increased to fund a gridSMART-to-nowhere without the PUCO applying the cost benefit test established by the General Assembly and without prudent measures of performance accountability on the part of the utilities.
- Despite repeated calls for process transparency by Ohio's leaders, the PUCO's order fails to explain how the PUCO reached its rate increase conclusions even though it is required to provide such reasons according to Ohio statutory law and decisions by the Ohio Supreme Court. The findings of fact and conclusions of law section of the PUCO's order contains not one substantive determination. The PUCO's inability or unwillingness to transparently explain its reasoning makes it even harder for members of the public to understand how the PUCO could order large rate increases while claiming that it has a goal of virtually no increases

and harder for the General Assembly to evaluate the PUCO's implementation of this new law.

- The PUCO's order was issued in a case where, unlike every other similar case over the last nine months, the PUCO made no attempt to encourage and promote settlement negotiations. In two other similar cases in which the PUCO has taken action (Duke and FirstEnergy), the PUCO encouraged settlement negotiations and eventually approved settlements supported in whole or part by almost all the parties. A settlement is pending in the third case (DP&L). The PUCO's order allows for rate increases for items which consumer representatives were able to defeat through good faith settlement negotiations in other cases.
- In addition to large rate increases in 2009, 2010 and 2011, the PUCO's order allows OP and CSP to defer additional increases that, once the PUCO-approved interest charges are added, will likely produce additional non-bypassable rate increases during the period 2012 to 2018. Because the PUCO included an equity return allowance for purposes of calculating interest charges, the interest rate will cause the deferred balances to grow at the annual compound rate of 11.15 percent. The PUCO refused to calculate interest charges based on much less expensive debt financing used in other cases. Based on information OP and CSP provided to the PUCO, their average cost of debt financing is about 5.7 percent.
- The PUCO's order makes it clear that OP's and CSP's rates will increase even further in 2010 and 2011. It appears that the PUCO will allow OP and CSP to collect, in the aggregate, about **1.5 billion rate increase dollars** from their customers during this three-year period. But the PUCO has not required OP and CSP to give customers the information customers need to predict their 2010 and 2011 electric bills. While the PUCO has repeatedly expressed a desire to provide Ohio electric consumers with predictable and stable rates, OP's and CSP's customers cannot predict what electric bills they will be paying in 2010, a little less than nine months from now.

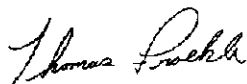
The PUCO has 30 days to act on the application for rehearing (copy attached) which IEU-Ohio has filed. We expect other parties will also file rehearing requests. Recently, the PUCO has extended this statutory deadline by granting rehearing requests for the purpose of giving itself more time to consider rehearing requests. IEU-Ohio's rehearing request urges the PUCO to make a substantive ruling within the 30-day period because otherwise the PUCO has the ability to stymie efforts to secure review of its actions by the Ohio Supreme Court. On an interim basis, IEU-Ohio has also asked the PUCO to limit total bill increases for 2009 to the percentage amounts contained in the PUCO's

order so that customers are not burdened by more than the PUCO-specified increase amounts at a time when economic hardship has blanketed Ohio.

As if things were not bad enough for OP and CSP customers, on April 8, 2009, AEP filed an application to make it even harder on customers who have become more vulnerable as a result of conditions in the general economy. Under the proposal submitted by OP and CSP in PUCO Case No. 09-308-EL-WVR, the utilities are seeking the PUCO's permission to bypass a PUCO rule that states when and to what extent utilities may demand non-residential customers to make deposits to secure bill payments. IEU-Ohio has asked the PUCO to deny this application and require OP and CSP to work proactively with their customers to work through the difficult issues presented by conditions in the general economy. In the meantime, IEU-Ohio has also suggested that neither the utilities nor the PUCO are helping to reduce bill collection risk by imposing double digit percentage electric rate increases on customers.

If you have any questions regarding this letter, the attached application for rehearing or what you might do to help make sure that electric rate increases are kept as low as possible during this difficult time, please call me at your earliest convenience.

Sincerely,



Thomas L. Froehle

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