BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Ormet Primary Aluminum Corporation for Approval of Unique Arrangement with Ohio Power Company and Columbus Southern Power Company	)))))	Case No. 09-119-EL-AEC

POST HEARING BRIEF OF THE KROGER CO.

I. INTRODUCTION

The Kroger Co. is one of the largest grocers in the United States. The Kroger Co.'s grocery and related businesses require the use of substantial amounts of electric power. The Kroger Co. has facilities in the service territories of both Ohio Power ("OP") and Columbus Southern Power ("CSP") that collectively consume over 230 million kWh per year.

In the above captioned matter, Ormet Primary Aluminum Corporation ("Ormet") filed an Application for approval of a ten-year unique arrangement ("Application") with CSP and OP (collectively "AEP"). The Unique Arrangement seeks to tie the price of electricity paid by Ormet to the worldwide price of aluminum as established on the London Metal Exchange ("LME"). The unique arrangement also asks that AEP be permitted to recover delta revenues that result from Ormet paying electric rates below AEP's tariff rate. The recovery of delta revenues from the unique arrangement could cost AEP ratepayers more than $200 million annually.[1]

[1] The Ohio Energy Group ("OEG") Comments at p. 3

Generally, The Kroger Co. does not oppose reasonable and cost effective assistance to aid an ailing business when such assistance is prudent. However, the Commission must balance all costs of the assistance, with the benefits of assuming those costs. Further, the Commission must not expose ratepayers to unreasonable and unlimited risk. Any unique arrangement approved by the Commission must satisfy these principles. Specifically, a unique arrangement must include:

- Reasonable protections for AEP Ratepayers;
- The exclusion of the POLR charges from the amount of delta revenue AEP recovers; and
- A greater share in the benefit with AEP ratepayers in the event that LME prices rise above Ormet's target price.

Further, before approving a unique arrangement for Ormet, the Commission should investigate whether assistance to Ormet is better addressed through other economic development or legislative means. All alternative avenues of funding should be exhausted before AEP ratepayers are required to bear the high cost and risk that are inherent in this Application.

II. ARGUMENT

A. A Unique Arrangement Must Have Reasonable Protections.

Under Section 2.03 of the proposed Power Sales Contract ("Section 2.03") between Ormet and AEP, the Commission may not modify Ormet's unique arrangement before the year 2016 unless the cumulative net discount to Ormet is more than 50% of AEP's tariff rate.[2] At hearing, Ormet's Witness Fayne admitted that under the proposed Power Sales Contract it is

[2] Application, Attachment A, p. 9.

possible for Ormet to pay well below 50% of AEP's tariff rate for a year or more before the Commission had the opportunity to modify the unique arrangement.[3] Even if Ormet's net cumulative discount is more than 50% of AEP's tariff rate, the Commission *may* modify the unique arrangement, but is not required to. Other than Section 2.03, there is no limit in the Application on the amount of subsidy Ormet may receive.

The proposed unique arrangement does not offer AEP ratepayers sufficient protection. Before a unique arrangement can be approved, there must be a reasonable and definite floor on the cost to customers. Further, the Commission must have the ability to periodically review, and if necessary modify the unique arrangement. Finally, the unique arrangement must last only the amount of time necessary to ensure Ormet can continue operations.

The unique arrangement, as proposed, will likely cost AEP ratepayers substantial sums of money. If the LME price of aluminum stays at its current rate, under the proposed unique arrangement, AEP will collect from customers over $200 million in delta revenues annually.[4] To put this in context, the total retail electric sales for both OP and CSP for the year 2008 were approximately $3.3 billion.[5] $200 million in delta revenues is the equivalent of an approximate 6% rate increase for customers. This additional cost, on top of the most recent rate increase authorized by the Commission, would create an unbearable burden for AEP ratepayers.

In order to protect customers against unjustifiably high electric rates, the Commission must place a definitive limit on the cost customers are required to pay. For instance, the Commission could limit the discount Ormet receives to a certain percentage below AEP's tariff

[3] Transcript Volume I, p. 213, lines 13-17.
[4] OEG estimates that at the current LME price Ormet would receive electricity at a 100% discount, which amounts to a $206 million subsidy to Ormet under the terms of the proposed power sales contract. This is despite the fact that the total compensation Ormet pays to Ohio workers is only $56 million annually. OEG Comments, Attachment 3.
[5] AEP 2008 Form 10-K, at p. 4.

rate. In the alterative, the Commission could place a dollar limit on the amount of delta revenues AEP may recover annually from the unique arrangement.

The cost must also be limited to a reasonable amount. Ormet is not the only company that will request approval of a unique arrangement. In fact, Eramet Marrietta, Inc. ("Eramet") has just filed an application for unique arrangements requesting that CSP ratepayer pay the cost of a substantial discount on Eramet's electric rates.[6] If the Commission does not put a reasonable limit on the cost to customers, the rate increases that result from unique arrangements with individual companies will dwarf the rate increase from AEP's most recent ESP.

The Commission also must have the ability to periodically review, and if necessary modify the unique arrangement. As noted herein, Section 2.03 attempts to limit the Commission's ability to modify the unique arrangement until 2016. RC 4905.31, which authorizes unique arrangements, requires that every unique arrangement "shall be under the supervision and regulation of the commission, and *is subject to change, alteration, or modification by the commission*." Clearly it is unlawful to restrict the Commission from modifying the unique arrangement until 2016.

Not only does Section 2.03 violate Ohio statute, it would be unwise to restrict the Commission's ability to modify a unique arrangement. It is possible that long-term changes in market fundamentals could decrease the demand for aluminum and thus lower the market price for aluminum. The decrease in demand and price could occur irrespective of economic conditions. Restricting the Commission's ability to modify the unique arrangement until 2016 exposes customers further to the risk of the volatile aluminum market.

[6] See PUCO Case No. 09-516-EL-AEC.

Finally, there must be a reasonable time limit on the unique arrangement approved by the Commission. As proposed, AEP will supply Ormet with electricity under the unique arrangement until 2019. Ten years is an unreasonable amount of time to expose ratepayers to the risk and cost of a unique arrangement. At times it may be prudent to offer temporary assistance to an ailing business; however, it is not good policy to create a permanent subsidy. The time of the unique arrangement should be limited to the minimum amount of time necessary to prevent Ormet from ceasing operations. To continue the unique arrangement any further will only enrich Ormet shareholders at the expense of AEP ratepayers.

B. POLR Charges Should Be Excluded From Delta Revenue Recovery.

The unique arrangement, as proposed, allows AEP to recover 100% of the delta revenues that result from Ormet paying a price for electricity below AEP's tariff rate. The proposed unique arrangement also makes AEP the exclusive electric supplier to Ormet's Hanibal facility. If a unique arrangement is approved, the Commission must require that AEP share the cost of the subsidy to Ormet to reflect the benefits of the unique arrangement to AEP.

In AEP's most recent ESP, the Commission approved a Provider of Last Resort ("POLR") rider to compensate AEP for assuming risk that customers might select an alternative service provider of electricity.[7] Because Ormet is contractually obligated to receive electricity from AEP under the proposed unique arrangement, there is no risk that Ormet will purchase electricity from an alternative electric provider. Under the proposed unique arrangement, AEP would still receive all the compensation for being POLR supplier without incurring POLR costs. This double recovery would give AEP a financial windfall at the expense of already burdened

[7] Opinion and Order Approving AEP's ESP, at p. 40 (March 18, 2009) PUCO Case No. 08-917-EL-SSP.

customers. Any unique arrangement approved by the Commission must not allow AEP to recover Ormet's POLR charge.

Even if AEP actually faced POLR risk, the pricing of that risk would be substantially lower according to the Black-Scholes model, which was used by AEP to calculate the cost of POLR risk. Under the Black-Scholes model, as AEP's electric prices increase, the cost of AEP's POLR risk also increases. This is because if AEP charges a customer a higher price for electricity, it is more likely that an alternative service provider can sell that customer electricity at a lower rate, and thus more likely that a customer will shop.[8] Under a unique arrangement, Ormet's rate for electricity is likely to be much lower than AEP's tariff rate; therefore it is less likely that an alternative service provider could offer electricity at a lower rate. As The Kroger Co. explains above, AEP does not actually face POLR risk because Ormet cannot shop for electricity; however, if the Commission allows AEP to collect Ormet's POLR charge, the POLR charge should be repriced to reflect Ormet's discounted rate.

Finally, because AEP financially benefits from continued Ormet operation, AEP should be required to share the cost to discount Ormet's electric use. AEP receives substantial revenues due to Ormet's electric consumption. If Ormet were to ceases operations, AEP would lose those revenues permanently. Accordingly, the Commission must require that AEP pay for a certain percentage of the overall subsidy Ormet receives to reflect the great benefit to AEP from a unique arrangement with Ormet.

[8] Testimony of J. Craig Baker, at p. 31-32 (July 31, 2008) PUCO Case No. 08-917-EL-SSP (explaining that the cost of fulfilling AEP's POLR obligations are less when the price of competitive electric services is much higher than the price AEP offers for electricity).

C. Customers Must Share the Benefit If Aluminum Prices Increase.

Under the unique arrangement, Ormet seeks to tie the price that it pays for electricity to the LME price of aluminum. As noted herein, the unique arrangement that Ormet proposes could require customers to pay Ormet's entire cost of electricity. However, the proposed unique arrangement only requires Ormet to pay a maximum of 105% of AEP's tariff rate in the event the price of aluminum increases.[9] If Ormet is entering into a unique arrangement in order to maintain enough cash flow to sustain operations, there is no legitimate reason why the maximum price Ormet pays for electricity should be capped at 5% above AEP's tariff when aluminum prices rise. Ratepayers are asked to bear the risk of declining aluminum prices, and therefore should also receive a reasonable return in the event aluminum prices rebound. A potential 5% gain is not nearly enough return to compensate ratepayers for the risk and cost of bailing out Ormet. If the Commission is to approve a unique arrangement for Ormet, the Commission must allow ratepayers to share in a larger portion of the up side if aluminum prices rise.

D. Assistance Should Be Sought Through Other Means.

It may be possible for Ormet to obtain assistance through other economic development or legislative means. Payment directly from a government entity rather than from AEP ratepayers may be desirable for several reasons. First, a direct payment from the government will more likely address Ormet's specific problems, rather than a broad subsidy from ratepayers.[10] The savings from a blanket reduction of costs on the other hand may or may not be used to make Ormet more competitive in the long run. Second, direct government assistance is more likely to include the types of protections for ratepayers that The Kroger Co. has asked for, such as explicit

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[9] Application, at p. 6.

[10] For instance, if Ormet faces a disproportionate burden due to its legacy costs (i.e. pensions and healthcare), government assistance can go directly to alleviating that burden.

limits on the amount of subsidy and additional oversight mechanisms. Finally, assistance directly from the government will more evenly distribute the cost to all taxpayers rather than just AEP ratepayers.

For these reasons, The Kroger. Co. asks that before a unique arrangement is approved, the Commission submit this matter to Governor Strickland with a request to investigate whether assistance to Ormet is better addressed through other economic development or legislative means. Ormet may also be eligible for federal stimulus money to address many of the problems cited in the Application. All alternative avenues of funding should be exhausted before AEP ratepayers are required to bear the high cost and risk that are inherent in this Application.

III. CONCLUSION

The Kroger Co. respectfully requests that if the Commission approves a unique arrangement for Ormet, the Commission amend Ormet's modifications to take into consideration the changes The Kroger Co. has proposed.

Respectfully submitted,

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CERTIFICATE OF SERVICE

The undersigned hereby certifies that the preceding pleading was served this 1st day of July, 2009 upon the parties of record at the addresses listed below via electronic mail or U.S. Regular mail, postage prepaid.

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