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BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO **PUCO**

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|---|---|------------------------|
| In the Matter of the Application of |) | |
| Columbus Southern Power Company and |) | |
| Ohio Power Company for Authority to |) | Case No. 11-346-EL-SSO |
| Establish a Standard Service Offer |) | Case No. 11-348-EL-SSO |
| Pursuant to §4928.143, Ohio Rev. Code, |) | |
| in the Form of an Electric Security Plan. |) | |
| | | |
| In the Matter of the Application of |) | |
| Columbus Southern Power Company and |) | Case No. 11-349-EL-AAM |
| Ohio Power Company for Approval of |) | Case No. 11-350-EL-AAM |
| Certain Accounting Authority. |) | |

SUPPLEMENTAL DIRECT TESTIMONY OF
LAURA J. THOMAS
ON BEHALF OF
COLUMBUS SOUTHERN POWER COMPANY
AND
OHIO POWER COMPANY

Filed July 6, 2011

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LAURA J. THOMAS

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BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO
SUPPLEMENTAL DIRECT TESTIMONY OF
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COLUMBUS SOUTHERN POWER COMPANY
AND
OHIO POWER COMPANY

1 **PERSONAL DATA**

2 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

3 A. My name is Laura J. Thomas. My business address is 1 Riverside Plaza, Columbus,
4 Ohio 43215.

5 **Q. DID YOU PREVIOUSLY FILE DIRECT TESTIMONY IN THIS**
6 **PROCEEDING?**

7 A. Yes, I filed direct testimony on January 27, 2011 in this proceeding regarding the
8 subjects of the Market Rate Offer (MRO) price test, Provider of Last Resort (POLR),
9 Facility Closure Cost Recovery Rider, and the Generation NERC Compliance Rider.

10

11 **PURPOSE OF SUPPLEMENTAL DIRECT TESTIMONY**

12 **Q. WHAT IS THE PURPOSE OF YOUR SUPPLEMENTAL DIRECT**
13 **TESTIMONY IN THIS PROCEEDING?**

14 A. The purpose of my supplemental direct testimony is to provide additional information
15 in support of the Company's proposed charges for Provider of Last Resort (POLR) as
16 the result of the Commission's June 9, 2011 entry in these cases. For convenience, I
17 also present two corrections to my direct testimony as filed on January 27, 2011.

18 **Q. WHAT EXHIBITS ARE YOU SPONSORING IN THIS PROCEEDING?**

1 A. I am sponsoring Supplemental Exhibits LJT-1 through LJT-4.

2

3 **DIRECT TESTIMONY CORRECTIONS**

4 **Q. PLEASE EXPLAIN ANY CORRECTIONS THAT YOU HAVE TO YOUR**
5 **DIRECT TESTIMONY AS FILED ON JANUARY 27, 2011.**

6 A. I have two corrections to my direct testimony. First, Page 8, line 22 should be
7 corrected because the Company used the first week of each quarter for 2010 in
8 developing the Simple Swap (SS) component of the Competitive Benchmark.
9 Accordingly, the corrected sentence, beginning on line 2, should read as follows:

10 "To avoid the issue of selecting data that produce a pre-determined result, an
11 average of the forward prices from the first week of each quarter of 2010 were
12 used to develop the SS component of the Competitive Benchmark."

13 Second, on Page 16, line 9, the word "increasing" should be changed to "decreasing".

14 Accordingly, the corrected sentence should read as follows:

15 "Further, as discussed below, during the term of the 2009-2011 ESP, customer
16 switching has been increasing significantly in response to decreasing market
17 rates."

18

19 **PROVIDER OF LAST RESORT**

20 **Q. PLEASE DEFINE THE PRODUCT OR SERVICE THAT CUSTOMERS**
21 **RECEIVE IN EXCHANGE FOR PAYING POLR CHARGES.**

22 A. In exchange for the payment of POLR charges, customers receive the option or right,
23 but not the obligation, to switch suppliers and return to service from the Company at
24 SSO generation rates when they choose to do so, subject to the switching limitations

1 contained in the Company's tariffs. This is a valuable service to customers provided
2 by the Company.

3 **Q. PLEASE DESCRIBE THE POLR OBLIGATION FOR THE COMPANY.**

4 A. As described in my direct testimony, the Company incurs a POLR obligation because
5 all customers are free to switch to generation service from a CRES (Competitive
6 Retail Electric Service) provider, either on an individual basis or as part of
7 governmental aggregation. In addition, customers are free to return to receiving SSO
8 generation service from the Company when they so choose. The Company must then
9 serve such customers whether it is the choice of the customer to return or if the CRES
10 provider or supplier to the governmental aggregation group were to default in its
11 service obligation. Consequently, the Company's generation obligation is subject to
12 significant volatility.

13 The flexibility or options provided to customers are an obligation of the
14 Company which is put in the position of losing customers when the competitive
15 market price is low, but is required to stand ready to serve that load again when
16 market prices increase and customers return. As explained by Company witnesses
17 Dr. LaCasse and Dr. Makhija, there is a definite and significant cost to the Company
18 associated with providing customers with this flexibility.

19 **Q. IS THE POLR OBLIGATION UNIQUE TO OHIO ELECTRIC**
20 **DISTRIBUTION COMPANIES?**

21 A. Yes, only Ohio electric distribution utilities (EDUs) incur the POLR obligation and
22 the associated risks regardless of whether or not they are currently serving a
23 customer. CRES providers do not have such an obligation and are free to choose the

1 customers they serve, the length of time they provide service, and the pricing and
2 terms and conditions of such service. However, the EDU has no such choices and,
3 instead, must serve any customer in their service territories, at standard service offer
4 (SSO) generation rates, that CRES providers choose not to serve or choose to stop
5 serving. Customers have the right to rely on the EDU for SSO generation service at
6 regulated rates and the Company must be appropriately compensated for this option
7 that its is required to provide.

8 **Q. DO ALL OHIO EDUs HAVE A POLR OBLIGATION?**

9 A. Yes. The statements above were intended to distinguish between the Company and
10 CRES providers when it comes to POLR service. However, as discussed by
11 Company's witness Dr. LaCasse, EDUs (like the FirstEnergy EDUs¹) who
12 competitively bid out their load, transfer the majority of their POLR risk to the
13 winning suppliers. Such EDUs still maintain the obligation to provide SSO
14 generation service in the event one or more of the winning suppliers defaults on its
15 load obligations. However, the FirstEnergy EDUs also have tariff mechanisms in
16 place to cover the cost of any such defaults.

17 **Q. IS THE SSO GENERATION OBLIGATION OF THE COMPANY THE SAME**
18 **AS THE OBLIGATION REQUIRED OF THE FIRSTENERGY EDUs?**

19 A. No. The Company is in a different situation than are the FirstEnergy EDUs which do
20 not have generation assets. If the Company did not own generation assets and had an
21 SSO where the price and sources of generation were established through a competitive

¹ The Cleveland Electric Illuminating Company, Ohio Edison Company and The Toledo Edison Company.

1 bid process, then the SSO generation obligation would be comparable in this regard.
2 However, under the Company's ESP, SSO generation service is provided by the
3 Company's generation and is not supplied by the generation of competitive suppliers
4 and therefore is not comparable.

5 **Q. IS THE SSO GENERATION OBLIGATION OF THE COMPANY THE SAME**
6 **AS THE OBLIGATION REQUIRED OF WINNING BIDDERS IN AN SSO**
7 **AUCTION?**

8 A. No. Bidders in an SSO auction have the freedom to bid for the amount of load they
9 choose. They also bid at prices to compensate themselves for the risk they are willing
10 to take, including the migration risk both away and back to its SSO generation
11 service. However, the Company does not have such freedoms nor is it able to choose
12 the level of risk it desires for serving customers. Instead, it must provide SSO
13 generation or POLR service to all customers that elect such service, up to 100% of its
14 customers, including those customers it is currently serving.

15 **Q. DO CRES PROVIDERS HAVE A POLR OBLIGATION?**

16 A. No, they do not. This is a key distinction between EDUs and CRES providers.
17 CRES providers are free to select what ever customers they choose to serve and for
18 what ever time they choose to serve those customers. CRES providers may also
19 adjust their rates under terms and conditions of their own choosing and design and are
20 not obligated to offer the equivalent of SSO generation rates to anyone. The
21 Company is not a competitive entity that is equivalent to a CRES provider because
22 they have very different obligations to provide service to customers. These are

1 reasons that an EDU's POLR charges are not included in the customer's price to
2 compare and must be non-bypassable.

3 **Q. DOES THE COMPANY HAVE A POLR OBLIGATION TO ALL**
4 **CUSTOMERS REGARDLESS OF WHETHER THEY HAVE SWITCHED TO**
5 **A CRES PROVIDER YET?**

6 A. Yes, any customer taking service at SSO generation rates at any time is taking POLR
7 service from the Company. POLR service does not begin when a customer leaves the
8 Company and then returns. Even if the customers who have switched to a CRES
9 provider never return to the Company, the Company is providing POLR service to all
10 those customers who have not chosen a CRES provider. Accordingly, migration must
11 be considered in both directions (away from the Company and returning to the
12 Company) because the POLR service the EDU is required to provide under SSO
13 generation rates exists for all customers regardless of when or if they choose another
14 supplier. The Commission's 2009 decision in the Company's 2009-2011 ESP case
15 properly recognized both components of POLR risk. Any exclusion of one
16 component or the other would grossly understate the Company's POLR cost.

17 **Q. DOES THE COMPANY FACE INCREASED RISK DUE TO THE PRIORITY**
18 **OF CUSTOMER PAYMENTS?**

19 A. Yes. When customers receive a consolidated bill from either the Company or a
20 CRES provider, and customers pay less than the total amount owed, the CRES
21 provider is paid first for any past due charges included in the bill. A CRES provider
22 may also discontinue service to customers with poor payment history and such
23 customers would then return to the Company. The Company has no such alternatives

1 and must follow the rules in place for payments and disconnection of service.
2 Accordingly, the Company has a greater risk of not being paid for its generation
3 service, or of being paid at a significant lag, than a CRES provider who is paid first
4 and may elect to discontinue service to customers with poor payment history. CRES
5 providers may also limit their risk by choosing not to serve specific customers or by
6 excluding groups of customers from participation in their aggregation programs. This
7 additional risk was not included in the Company's POLR cost.

8 **Q. DOES HAVING A POLR CHARGE PREVENT CUSTOMERS FROM**
9 **SWITCHING?**

10 A. No, as stated in my direct testimony, a POLR charge does not keep customers from
11 shopping. On the contrary, the POLR option provides customers with the option to
12 shop and return to the Company under regulated, stable SSO generation rates. Under
13 the POLR charges and provisions approved by the Commission in its 2009 decision,
14 when a customer considers shopping, they may either 1) switch suppliers, continue to
15 pay the POLR charge, and retain the right to return to the Company at SSO
16 generation prices or 2) switch suppliers, waive paying the POLR charge, and commit
17 to pay market prices if they return to service from the Company. Paying the POLR
18 charge until such a commitment is made is appropriate because only upon a switching
19 customer's commitment to market pricing is the Company partially relieved of its
20 POLR obligation. The term "partial" is used because the Company is still required to
21 serve the customer, only the issue of price has been resolved.

1 **Q. HAVE CUSTOMERS RECOGNIZED THE BENEFIT OF RETAINING THE**
2 **OPTION TO RETURN TO SERVICE FROM THE COMPANY AT SSO**
3 **GENERATION PRICES?**

4 A. Yes. As of July 1, 2011, of the customers that have selected service from a CRES
5 provider and receive distribution service from the Company, approximately 98% have
6 elected to continue to pay the POLR charge rather than face the prospect of returning
7 to the Company at market rates. Customers have elected to continue to pay this
8 relatively small charge (compared to the total price for SSO generation service) in
9 order to preserve their option of returning at stable SSO generation rates from the
10 Company. Therefore, based on actual customer behavior when faced with this
11 choice, it is clear that customers place significant value on the option to return to
12 service at stable SSO generation rates.

13 **Q. DOES THE LEVEL OF CUSTOMER SWITCHING HAVE AN IMPACT ON**
14 **THE NEED FOR A POLR CHARGE?**

15 A. No, the actual level of switching is not a determining factor regarding the need for a
16 POLR charge. The Company incurs a POLR obligation regardless of who is
17 currently serving a customer in the Company's service territory since a customer can
18 either stay with the Company's POLR service at regulated, stable SSO generation
19 rates or switch and then return to that service. Material levels of switching have
20 occurred for AEP Ohio and therefore any debate about whether actual switching
21 levels should affect the need for a POLR charge is moot, in any event, because actual
22 customer behavior has shown significant switching.

1 **Q. WHAT IS THE RISK THAT SWITCHING LEVELS WILL CHANGE**
2 **DURING THE PERIOD OF THE PROPOSED ESP AND EVEN BEFORE**
3 **THE 2012-2014 ESP BEGINS?**

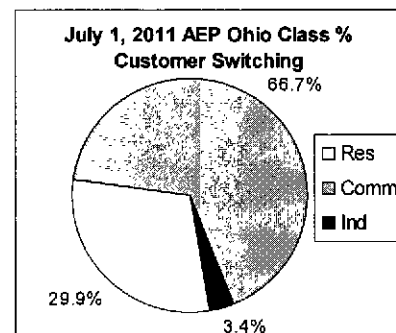
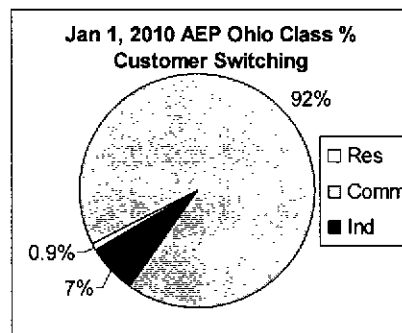
4 A. There is a high likelihood that switching levels will continue to significantly increase
5 based on the continued growth of switching that has occurred in the past year. As
6 shown in the exhibits to my direct testimony filed on January 27, 2011, which
7 reflected data through year end 2010, approximately 3.8% of AEP Ohio load had
8 switched to an alternative provider as of December 31, 2010. As shown in
9 Supplemental Exhibit LJT-1, Page 1, switching levels (MWH) have continued to
10 increase each month for AEP Ohio. As of June 30, 2010, only 6 months later, that
11 percentage has now increased to approximately 9.3%.

12 Likewise, the number of customers that have switched to an alternative
13 supplier continues to grow. Supplemental Exhibit LJT-1, Page 2, shows the total
14 number of AEP Ohio customers that have switched to CRES providers as of July 1,
15 2011. The total customers that have switched as of July 1, 2011 represents
16 approximately a 300% increase over the number of customers that switched to CRES
17 providers as of January 1, 2011 – only six months prior.

18 **Q. FOR AEP OHIO, WHICH CUSTOMER CLASSES ARE EXPERIENCING**
19 **THE MOST SIGNIFICANT GROWTH IN THE NUMBER OF CUSTOMERS**
20 **SWITCHING?**

21 A. Initially, the commercial class experienced the most switching. However, in recent
22 months, it is the AEP Ohio residential class that has experienced the greatest growth
23 in switching. As shown in the graph below, the customer class percentages of those

1 customers served by CRES providers have changed dramatically. As of January 1,
2 2011, residential customers represented less than 1% of the customers switching. As
3 of July 1, 2011, residential customers make up approximately 30% of all customers
4 switching.



5

6 **Q. WHAT HAS CAUSED THIS SIGNIFICANT INCREASE IN THE NUMBER**
7 **OF RESIDENTIAL CUSTOMERS THAT ARE NOW SERVED BY CRES**
8 **PROVIDERS?**

9 A. The significant increase in residential customer switching is the result of increasing
10 aggregation in many places in the AEP Ohio service territory. This is significant
11 because customers (and their loads) may switch suppliers in large numbers when
12 aggregation opportunities are offered. Consideration of these recent trends leads to
13 the conclusion that customer switching will continue to increase for AEP Ohio. For
14 example, currently, at least six entities (municipalities, townships, etc.) have provided
15 notice of opt-out aggregation that is under way for their customers. Such customers
16 are only partially reflected in the load data shown in Supplemental Exhibit LJT-1
17 because aggregation is under way and not all customers will switch at the same time.
18 Also, there is a lag regarding when switched usage is reflected in Supplemental
19 Exhibit LJT-1, page 1 because customers who have actually switched may not yet

1 have been billed for usage provided by their new supplier. The testimony of
2 Company witness Dr. LaCasse also addresses the significance of opt-out aggregation
3 with regard to the POLR cost.

4 **Q. ARE THESE TRENDS FOR AEP OHIO CONSISTENT WITH THE**
5 **SWITCHING THAT OCCURRED ELSEWHERE IN THE STATE?**

6 A. Yes, the AEP Ohio trends are consistent with the trends across the state. A review of
7 these switching trends also across the state shows how quickly the level of switching
8 can change. Supplemental Exhibit LJT-2, Page 1 shows the updated levels of
9 switching that have occurred for each of the other Ohio utilities for the period Q1
10 2009 through Q1 2011. As shown by the data, the percentage of customer switching
11 can change significantly in a short period of time. AEP Ohio is experiencing the
12 same increases in switching which have occurred for the other utilities.

13 **Q. WHAT HAS BEEN THE STATE'S EXPERIENCE WITH AGGREGATION?**

14 A. Based on Ohio's switching statistics as published by the PUCO², nearly all residential
15 and commercial customers who have switched suppliers did so under some form of
16 aggregation. This significant level of aggregation indicates that such customers are
17 likely to switch suppliers in large numbers, and therefore the opportunity for
18 aggregation makes it more difficult for the Company to plan for and determine the
19 impact of customer switching.

20 **Q. WHAT CONCLUSIONS CAN YOU DRAW FROM THIS PATTERN OF**
21 **SWITCHING FOR AEP OHIO?**

² www.puco.ohio.gov/puco/?LinkServID=07ECCC22-E8B3-39E3-D6243E2482FA17CF

1 A. The switching pattern for AEP Ohio only reaffirms the position stated in my direct
2 testimony – that actual customer switching is not a determining factor regarding the
3 need for a POLR charge for all customers. What is determinative is that customers
4 can switch suppliers at any time, subject to the switching constraints.

5 **Q. IN THE CALCULATION OF THE AVERAGE POLR CHARGE TO**
6 **CUSTOMERS, DID THE COMPANY EXCLUDE ANY CUSTOMERS OR**
7 **THEIR ASSOCIATED ENERGY USAGE?**

8 A. No. Perhaps the Company could have excluded two classes of customers – 1)
9 customers who are not able to shop due to the provisions of their special
10 arrangements with the Company as approved by the Commission, and 2) customers
11 who may not be able to shop due to certain rules or other provisions. However, the
12 removal of such customers would either have little impact on the POLR charge or
13 would actually increase the average POLR charge for the remaining customers.

14 **Q. PLEASE EXPLAIN THE IMPACT ON THE POLR CHARGE IF**
15 **CUSTOMERS WITH THESE TYPES OF SPECIAL ARRANGEMENTS**
16 **WERE ACCOUNTED FOR.**

17 A. There are presently two customers with these types of special arrangements approved
18 by the Commission – Ormet Primary aluminum Corp. (Case No. 09-119-EL-AEC)
19 and Eramet Minerals, Inc. (Case No. 09-516-EL-AEC). If these customers are
20 excluded, then the industrial MWH are reduced by approximately 4.8 million MWH.
21 Assuming that the load shape of these customers is similar to that of the remaining
22 industrial customer class, there is no impact on the POLR cost for the industrial class
23 because there is no change in any of the five inputs to the POLR model. Accordingly,

1 because there is no change in POLR cost for any of the classes (residential,
2 commercial and industrial), removal of the MWH for these customers will affect the
3 averaging of the rates that results in the overall proposed POLR charge. Specifically,
4 the impact of removing such MWH from the POLR calculation would be to increase
5 the average POLR rate for the remaining customers by \$0.03.

6 **Q. WHAT WOULD BE THE IMPACT OF REMOVING RESIDENTIAL**
7 **CUSTOMERS UNDER THE PERCENTAGE OF INCOME PAYMENT PLAN**
8 **(PIPP) FROM THE POLR CALCULATION?**

9 A. First, such a calculation would not be appropriate. While some may characterize
10 PIPP customers as not being able to shop, it is not that simple. The restriction is that
11 a customer cannot receive PIPP assistance and choose a CRES provider at the same
12 time. However, if it is in the customer's economic interest to shop because the
13 savings create a lower bill than the customer's PIPP payment, a customer is likely to
14 take the greater savings. In addition, this addresses only the limitation on PIPP
15 customers shopping as individuals. PIPP customers are "coordinated exclusively by
16 the Ohio department of development." As a result, the Ohio department of
17 development may aggregate these customers and shop their load to a CRES provider;
18 this could occur at any time. Therefore, it is not correct to state that PIPP customers
19 cannot shop.

20 However, for illustrative purposes, if one assumes that PIPP customers have
21 no ability to shop, the removal of PIPP customers results in a reduction of only
22 approximately 1 million MWH (3% of residential MWH) for the purposes of
23 weighting the residential, commercial and industrial POLR charges. This has

1 minimal impact, reducing the POLR charge by only \$0.01/MWH. Note that this is
2 far less than the opposite impact of removing special arrangement customers who are
3 more restricted in terms of their ability to shop than are PIPP customers. Therefore,
4 even if one assumes that PIPP customers have no ability to shop, and should pay no
5 POLR charges, the impact of that assumption on the POLR charge for all remaining
6 customers is negligible.

7 **Q. HAVE YOU PREPARED AN EXHIBIT WHICH DETAILS THE IMPACTS**
8 **DISCUSSED ABOVE?**

9 A. Yes, Supplemental Exhibit LJT-3 details the impacts of removing certain customers
10 from the POLR weightings as discussed above. If adjustments are made to the POLR
11 calculation to remove those customers who may have limited ability to shop (and
12 eliminate their requirement to pay POLR costs), then all such customers must be
13 considered and the net impact is to raise the POLR charge for the remaining
14 customers, but only by \$0.02/MWH. Therefore, while the constrained option model
15 used to determine the Company's POLR cost does not specifically address special
16 arrangement or PIPP customers, the impact favors customers by producing a POLR
17 rate that is lower than it otherwise would be if these customers were excluded from
18 the POLR rate calculation.

19 **Q. WHAT HAPPENS IF A CUSTOMER SHOPS AND SUBSEQUENTLY**
20 **BECOMES A PIPP CUSTOMER?**

21 A. If a customer shops and subsequently becomes approved as a PIPP customer, the
22 customer "shall be dropped by the electric utility to standard offer service..." This
23 requirement adds risk to the Company. In addition, the Company has a greater risk of

1 being paid for generation service, or of being paid at a significant lag, due to the
2 priority of customer payments. When customers receive a consolidated bill from
3 either the Company or a CRES provider, and customers pay less than the total amount
4 owed, the CRES provider is paid first for any past due charges included in the bill.

5 **Q. HAS THE COMPANY INCLUDED THIS INCREASED RISK IN ITS**
6 **PROPOSED POLR CHARGE?**

7 A. No, the Company's proposed POLR charge is conservative in that it did not include
8 the increased risk related to the priority of payments or the fact that customers can be
9 dropped to the EDU to be served under SSO generation rates if they become a PIPP
10 customer.

11 **Q. ARE THERE ADDITIONAL WAYS IN WHICH THE COMPANY'S**
12 **PROPOSED POLR CHARGE IS CONSERVATIVE?**

13 A. Yes, in addition to the above item related to the priority of payments, the Company
14 treated all commercial customers as if they were subject to the switching rules
15 applicable to the larger commercial customers. In reality, a significant portion of
16 commercial customers face less restrictive switching constraints. The impact of
17 differentiating the constraints for various commercial customers would result in a
18 higher POLR charge than proposed by the Company and, therefore, the Company was
19 conservative in its estimate.

20 **Q. DOES THE COMPANY'S CONSTRAINED MODEL USED TO DETERMINE**
21 **THE COMPANY'S POLR COST ACCOUNT FOR CERTAIN NON-PRICE**
22 **FACTORS?**

1 A. Yes, in addition to the switching restrictions explicitly included in the model as
2 explained in my direct testimony, other restrictions such as 90-day notice for certain
3 customers are implicitly accounted for. When a customer provides a 90-day notice to
4 switch suppliers, they have made a decision based on forward-looking information
5 regarding the pricing, terms and conditions that they will be served under by a CRES
6 provider. Otherwise, they would not provide the Company with a notice of
7 switching. Because the model assumes that customers will switch when it is to their
8 economic advantage to do so, this is no different than the assumption that the
9 customer who must provide a 90-day notice is switching because they have enough
10 forward-looking information to determine that it is in their economic interest to
11 switch suppliers.

12 **Q. DOES THE CUSTOMER BENEFIT FROM THE POLR CHARGE EVEN IF**
13 **THE POLR CHARGE INCREASES DUE TO CHANGES IN MARKET**
14 **PRICES?**

15 A. Yes. The customer always benefits from the POLR charge because, in exchange for
16 the payment of POLR' charges, customers receive the option or right, but not the
17 obligation, to switch suppliers and return to service from the Company at stable SSO
18 generation rates when they choose to do so, subject to the switching limitations
19 contained in the Company's tariffs. This is a valuable service to customers provided
20 by the Company.

21 As explained in my direct testimony, it is the relative differential between the
22 market price and the ESP price that is significant. As market prices move, the POLR
23 cost to the Company changes. When there are significant movements in market price

1 or greater price volatility, the greater the benefit to the customer of having a stable
2 SSO price. If market prices decrease, the customer becomes more likely to exercise
3 the option to switch to another supplier. This also means that less future market price
4 movement (or volatility) is then needed for the customer to desire to use the safety net
5 or POLR by returning to SSO generation service. Because of the Competitive
6 Benchmark (market) price to ESP price relationship, as stated in my direct testimony,
7 the Company has proposed to provide final POLR charges that reflect the final ESP
8 rates, Competitive Benchmark price and switching rules.

9 **Q. WHY DOES THE POLR CHARGE NEED TO BE SET AT THE BEGINNING**
10 **OF THE ESP PERIOD?**

11 A. The POLR charge must be set at the beginning of the ESP period because that is
12 when the Company makes its commitment to providing regulated, stable SSO
13 generation rates for the entire ESP period. If customers know the POLR cost up
14 front, then they are able to plan accordingly by determining their switching options
15 and savings. It also enables them to evaluate their option to continue to pay the
16 POLR cost which entitles them to return to SSO generation rates if they so choose
17 and their option to waive paying POLR in exchange for returning to the Company at
18 market-based rates.

19 **Q. WHAT ADDITIONAL INFORMATION SHOULD BE CONSIDERED**
20 **REGARDING THE VOLATILITY OF MARKET PRICES AS USED IN THE**
21 **CONSTRAINED OPTION MODEL USED TO DETERMINE THE**
22 **COMPANY'S POLR COST?**

1 A. As explained in my direct testimony, the Company used a three-year average annual
2 volatility percentage as an input to the constrained option model to determine the
3 Company's POLR cost. This was a simplifying and reasonable assumption -
4 applying the annual average volatility to the total Competitive Benchmark (market)
5 price. However, a much more detailed approach could have been used. Such an
6 approach would have used higher (monthly) volatilities applied to the SS-related
7 (simple swap-related) components which comprise approximately 65% of the total
8 Competitive Benchmark price. Additional variation would also have applied to the
9 seasonal shape of market prices and a lower volatility may have applied to other
10 components (approximately 35%) of the Competitive Benchmark price. In any event,
11 a more detailed approach would simply have included additional, but offsetting
12 information without material impact.

13 **Q. WHY WOULD IT BE MORE APPROPRIATE TO USE MONTHLY**
14 **VOLATILITIES FOR THE SS (SIMPLE SWAP)-RELATED COMPONENTS**
15 **OF THE MARKET PRICE?**

16 A. It would be more appropriate to use a monthly volatility for the energy or SS-related
17 components because customers generally face monthly decisions as to whether or not
18 they will switch to another supplier. It is the customer's switching ability that is
19 relevant and not whether a specific CRES provider offers prices that change that
20 frequently or not. In any event, it would not be appropriate to use a 3-year annual
21 average volatility if only the SS-related components of the Competitive Benchmark
22 price are considered.

1 **IMPACT OF POLR RATES ON THE MARKET RATE OFFER TEST**

2 **Q. THE MRO TEST, AS PROVIDED IN DIRECT TESTIMONY EXHIBIT LJT-**
3 **2, PAGE 1 OF 1, DID NOT INCLUDE ANY POLR CHARGES. PLEASE**
4 **EXPLAIN THE REASON FOR EXCLUDING POLR CHARGES FROM THE**
5 **MRO TEST.**

6 A. POLR charges were not included in the MRO test because, generally, their existence
7 does not impact the results of the test. This is because the POLR charges would exist
8 under either an ESP or MRO. Adding the same charge to both sides of an equation or
9 comparison would not change the end result. However, the Company has proposed a
10 decrease in the POLR charge and there continues to be a net ESP benefit shown under
11 the MRO test.

12 **Q. WHY ARE PROPOSED POLR CHARGES THE SAME UNDER EITHER AN**
13 **ESP OR MRO?**

14 A. Proposed POLR charges are the same under an ESP or MRO because of how these
15 POLR charges are derived and the fact that either the Company or the competitive
16 bidders incurs the POLR cost, i.e., the cost of providing POLR service to customers at
17 SSO generation rates. Under an ESP, the Company bears 100% of the POLR risk.
18 Under an MRO, the Company only bears the POLR risk for the portion of load which
19 is not competitively bid and the winning bidders bear the POLR risk for the portion of
20 load which they serve. For example, in Year 1 of an MRO, the Company bears 90%
21 of the POLR risk and winning bidders will bear 10% of the POLR risk.

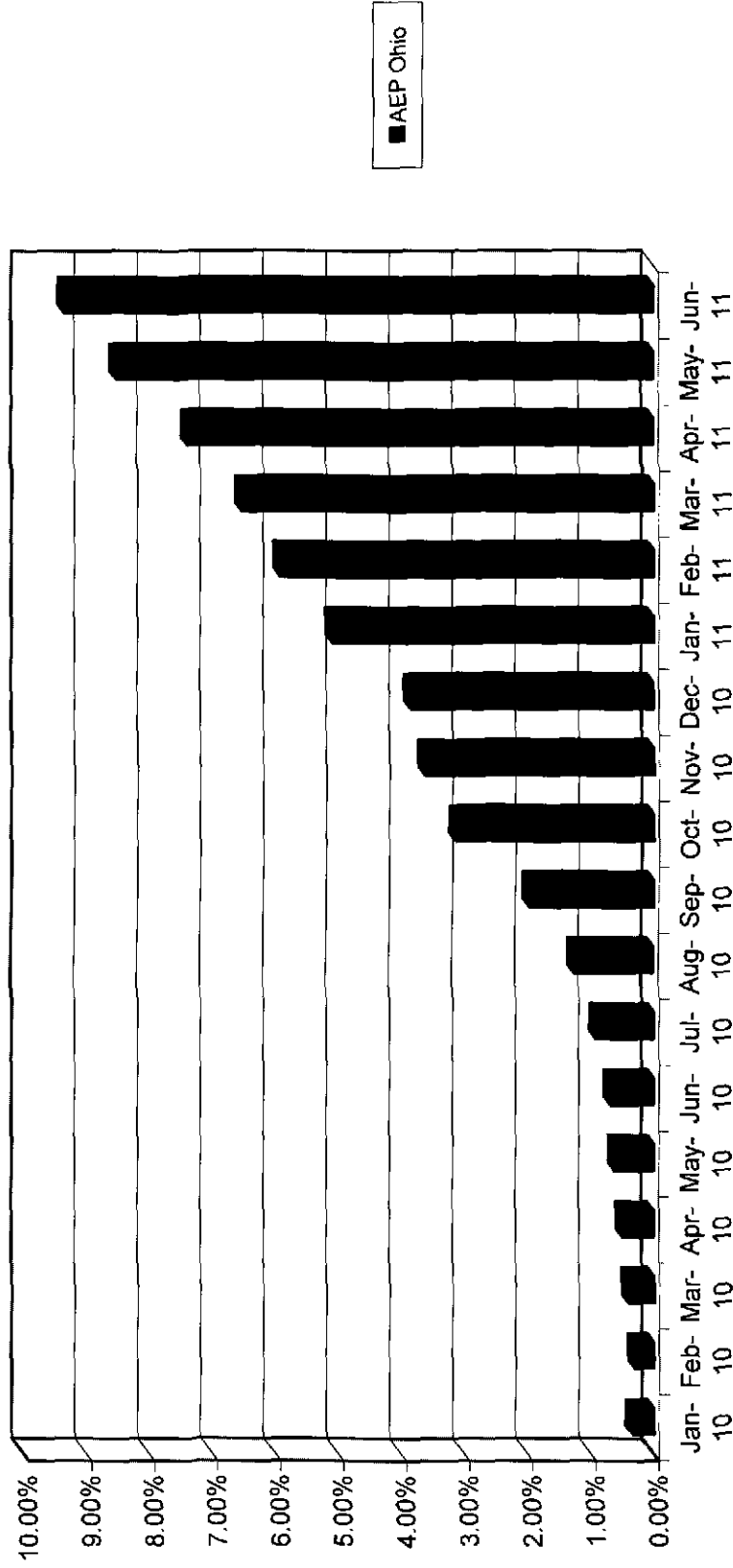
1 **Q. HAVE YOU PREPARED AN EXHIBIT TO DEMONSTRATE HOW THE**
2 **MRO TEST IS AFFECTED BY INCLUSION OF THE COST OF THE POLR**
3 **RISK?**

4 **A.** Yes. Supplemental Exhibit LJT-4 is the same as Exhibit LJT-2, filed on January 27,
5 2011 except that it includes the cost of the POLR risk as part of the Generation
6 Service Price. For simplicity and for purposes of this illustration, no additional
7 POLR costs were added to the Competitive Benchmark Price. This provides a
8 conservative assumption in that no adjustments are made to the Competitive
9 Benchmark Price to account for POLR. As shown by this supplemental exhibit, the
10 impact of including the cost of the POLR risk in the Generation Service Price is to
11 show that the ESP is still more beneficial than an MRO.

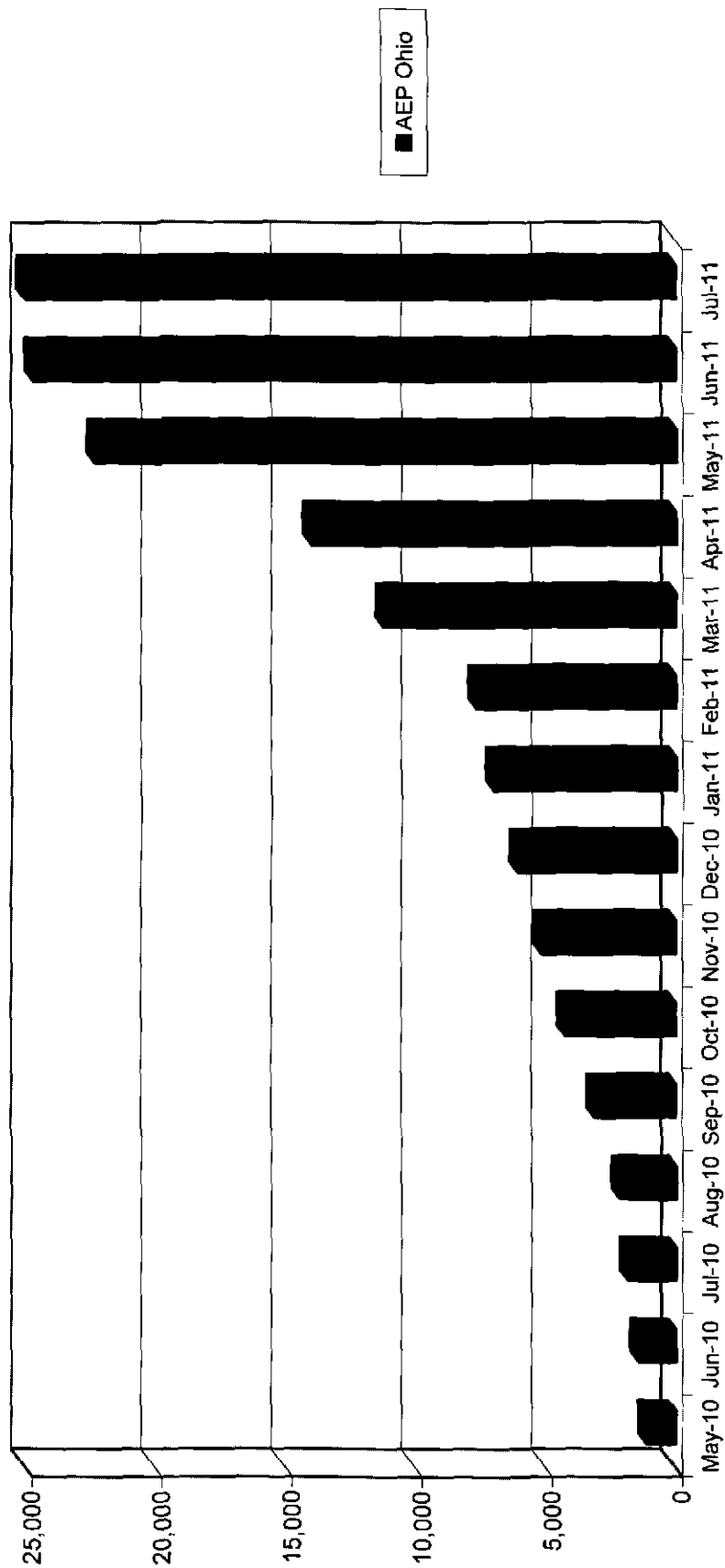
12 **Q. DOES THIS CONCLUDE YOUR SUPPLEMENTAL DIRECT TESTIMONY?**

13 **A.** Yes it does.

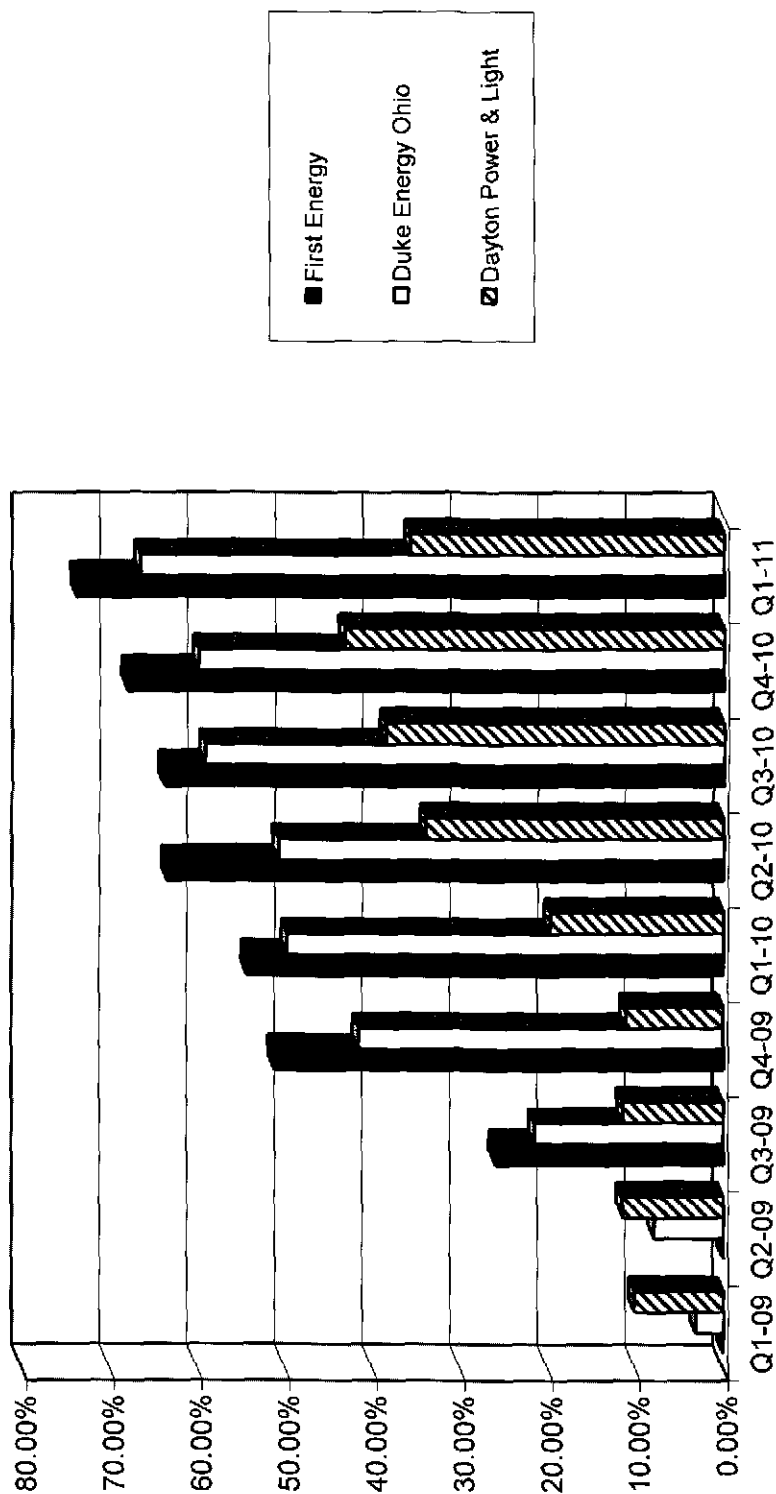
Columbus Southern Power Company and
Ohio Power Company
Percentage of Load Served by Competitive Suppliers



Columbus Southern Power Company and
Ohio Power Company
Number of Customers Served by Competitive Suppliers



First Energy, Duke Energy Ohio and
Dayton Power & Light
Percentage of Load Served by Competitive Suppliers



AEP Ohio
Electric Security Plan
Impact of PIPP and Special Arrangements on POLR

| | Residential | Commercial | Industrial | Total |
|--|-------------|------------|------------|-------|
|--|-------------|------------|------------|-------|

Impact of PIPP on POLR

| | | | | |
|--|------------|------------|------------|-------------|
| Total MWH | 35,810,900 | 33,338,600 | 44,226,800 | 113,376,300 |
| Estimated PIPP MWH (3% of Residential) | 1,074,327 | 0 | 0 | 1,074,327 |
| Total MWH Excl PIPP | 34,736,573 | 33,338,600 | 44,226,800 | 112,301,973 |
| POLR (\$/MWH) | \$3.94 | \$2.59 | \$2.13 | \$2.83 |

Impact of Special Arrangements on POLR

| | | | | |
|-------------------------------------|------------|------------|------------|-------------|
| Total MWH | 35,810,900 | 33,338,600 | 44,226,800 | 113,376,300 |
| Special Arrangement MWH | 0 | 0 | 4,500,000 | 4,500,000 |
| Total MWH Excl Special Arrangements | 35,810,900 | 33,338,600 | 39,726,800 | 108,876,300 |
| POLR (\$/MWH) | \$3.94 | \$2.59 | \$2.13 | \$2.87 |

Cumulative Impact of PIPP and Special Arrangements on POLR

| | | | | |
|--|------------|------------|------------|-------------|
| Total MWH | 35,810,900 | 33,338,600 | 44,226,800 | 113,376,300 |
| Estimated PIPP MWH (3% of Residential) | 1,074,327 | 0 | 0 | 1,074,327 |
| Special Arrangement MWH | 0 | 0 | 4,500,000 | 4,500,000 |
| Total MWH Excl PIPP & Special Arrangements | 34,736,573 | 33,338,600 | 39,726,800 | 107,801,973 |
| POLR (\$/MWH) | \$3.94 | \$2.59 | \$2.13 | \$2.86 |

AEP Ohio
Electric Security Plan
Market Rate Option Test

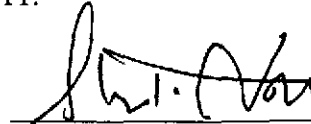
| | | 2012 | Jan 2013 - May 2014 | Wtd Average (3) = weighted (1) and (2) |
|-----------------------------------|--|-------|------------------------|--|
| <u>Generation Service Price</u> | | (1) | (2) | (2) |
| 1 | 2011 Base ESP 'g' Rate | 23.15 | 23.07 | 23.10 |
| 2 | 2011 Full Fuel* | 32.86 | 32.86 | 32.86 |
| 3 | 2011 Environmental Compliance Costs ** | 0.90 | 0.90 | 0.90 |
| 4 | Total Generation Service Price | 56.91 | 56.82 | 56.86 |
| 5 | 2011 POLR Cost | 3.07 | 3.07 | 3.07 |
| 6 | Total Generation Service Price + POLR | 59.98 | 59.89 | 59.93 |
| <u>Expected Bid Price</u> | | | | |
| 7 | Competitive Benchmark | 77.91 | 82.90 | 80.83 |
| <u>MRO Pricing</u> | | | | |
| 8 | Generation Service Price | 59.98 | 59.89 | 59.93 |
| 9 | Generation Service Weight | 90% | 77% | |
| 10 | Expected Bid Price | 77.91 | 82.90 | 80.83 |
| 11 | Expected Bid Weight | 10% | 23% | |
| 12 | MRO Annual Price | 61.77 | 65.18 | 63.76 |
| <u>MRO - ESP Price Comparison</u> | | | | |
| 13 | MRO Annual Price | 61.77 | 65.18 | 63.76 |
| 14 | Proposed ESP Price | 58.42 | 60.82 | 59.82 |
| 15 | Proposed POLR Cost | 2.84 | 2.84 | 2.84 |
| 16 | Proposed ESP Price + POLR Cost | 61.26 | 63.66 | 62.66 |
| 17 | ESP Price Benefit | 0.51 | 1.52 | 1.10 |

* Includes "Renewable and Energy Efficiency Adjustment"

** Assumes no lag in recovery or 2009-2011 carrying costs

CERTIFICATE OF SERVICE

The undersigned hereby certifies that a true and correct copy of the foregoing Columbus Southern Power Company's and Ohio Power Company's Supplemental Direct Testimony of Laura J. Thomas has been served upon the below-named counsel via First Class mail, postage prepaid, this 6th day of July, 2011.



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