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Ohio | **Public Utilities Commission**

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September 15, 2011

Betty McCauley, Secretary
The Public Utilities Commission of Ohio
180 East Broad Street, 12th Floor
Columbus, Ohio 43215

Re: Ohio Power Company
Case No. 11-352-EL-AIR, et al.

Dear Honorable McCauley:

Attached please find a section of the Ohio Power Company's Staff Report that was inadvertently omitted. Page 29 of the Staff Report should be replaced by the attached Section.

Very truly yours,

Jodi Bair

Jodi Bair
Director of Utilities

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RATES AND REVENUE ANALYSIS

Rate and Revenue Guidelines

General guidelines or objectives are followed in Staff's review of rate schedules and design. The applicable schedules should provide the utility the opportunity of recovering an authorized revenue. The various schedules should represent a reasonable distribution of revenue between and among the various customer groups. The particular schedules should be equitable and reasonable, should provide for customer understanding and continuity of rates and should cause minimal customer impact.

Rate design criteria are to be viewed as a package, in that they are interrelated. Although each item can be separately identified and applied to rate schedule determinations, no single standard is overriding in determining proper rate design. The rate schedules which comprise a particular utility's tariff should provide for recovery of expenses found proper in the course of a regulatory proceeding. If the rate schedule is designed on the basis of cost causation, it will provide for expense recovery in the long term, given changes in the customer consumption characteristics. Normally, and to the extent sufficient information is available, cost of service studies and related expense analyses are necessary to determine the appropriate level of revenue to be generated and the appropriate recovery of such revenue.

The rate schedules should be designed to be equitable and reasonable to the customers served pursuant to their applicability. The criterion involves several considerations. The rate schedules should, to the extent practicable, be predicated upon the cost associated with a particular service rendered. Customers receiving like services should be facing the same charges and provisions. Also, differences in applicable charges should be representative of differences in costs.

From a practicable rate design standpoint, absolute equality between costs and revenues may be difficult to achieve in the short term. While it may be viewed as equitable to set rates at cost, if there is a substantial divergence in the current rates, the resulting impact on individual customers may be viewed as unreasonable. While desiring cost supported charges, Staff considers such items as resulting typical billings and resulting revenue increases which would necessarily occur. These tests help provide benchmarks with regard to reasonableness of charges in rate forms. While it is Staff's position that rate schedules reflect costs, it is also important to consider the continuity associated with current and proposed pricing structures. This may result in movement towards more closely aligning revenue with costs rather than an absolute match at a particular time period.

When employing these standards to develop and design rates, the results should be understandable to all the customers billed under the schedule.

Cost of Service Analysis

Cost of service studies approximate the costs incurred by a utility in providing service and identifies costs causation. The allocation of costs is determined by assigning costs relative to what each class imposes on the system. There are several steps involved, as listed below:

- Functionalization: The separation of costs according to production, transmission or distribution function.

- Classification: The separation of the customer, demand or energy related costs. Customer costs are independent of customer usage characteristics and are costs which are associated with customer service connections to the system and vary with the number of customers served. Demand and capacity costs are those expenses which vary with the rate in which the service is used, such as the cost of meeting peak demand. Energy costs are the costs which vary according to the volume of energy consumed, or the customer's kilowatt-hour consumption.

- Allocation: The last step is the allocation of costs to each customer class. This is determined by a combination of the number of customers, class demands, and energy usage.

The Cost of Service Study (COSS) filed by the Applicant is an embedded fully allocated cost of service study by rate class for the test period ended May 31, 2011. The COSS allocates distribution related items such as plant investment, operating expenses and taxes to the various customer classes. These costs are then classified as customer-related or demand related. The final step calculates the revenue responsibility of each class required to generate the Applicant's recommended rate of return.

The Applicant delineated distribution plant costs by sub-functionalizing assets through the identification and separation of primary and secondary voltages. The voltage peaks are based on the combined average of the three summer coincident months (June, July, August) and three winter coincident months (December, January, February and are used in allocating primary plant costs. Secondary voltages were separated using the combination of each class' 12-month maximum demand and the summation of individual customers' annual maximum demands in each class. COSS results are presented on Tables 1 and 2.

Table 1 represents the Current, Applicant-proposed and Staff-proposed distribution related Rates of Return and Indices for the customer classes.

Table 1

Cost of Service Results

Rate of Return

	Current Rate of Return		Applicant Proposed Rate of Return		Staff Proposed Rate of Return	
Class	%	Index	%	Index	%	Index
RS	4.15%	0.88	8.43%	1.00	8.18%	0.97
GS-1	5.18%	1.10	8.43%	1.00	8.63%	1.02
Secondary	2.16%	0.46	8.43%	1.00	7.29%	0.86
Primary	4.14%	0.88	8.43%	1.00	8.17%	0 .97
Sub/Transmission	8,367.54%	(1771.14)	8.43%	1.00	3,727.25%	(442.03)
OL	-1.05%	(0.22)	8.43%	1.00	5.86%	0.69
SL	4.73%	1.00	8.43%	1.00	8.44%	1.00
Total	4.72%	1.00	8.43%	1.00	8.43%	1.00

Table 2 represents the Applicant's proposed revenue increase based upon COSS levelized rates of returns for Ohio Power (OP), in contrast to the actual revenues made by the Applicant as shown in the E-4 schedules. The 5 million dollar variance is a result of the Applicant assigning a portion of Ohio Power's (OP) revenue increase to CSP.

Table 2
COSS/Schedule E-4.1
Comparisons (Dollars)

Class	COSS	Proposed E-4.1 Schedule Increase	Variance
RS	38,098,517	38,770,327	671,810
GS-1	1,608,812	1,450,737	(158,075)
Secondary	26,871,524	22,680,138	(4,191,386)
Primary	5,810,612	4,596,884	(1,213,728)
Sub/Transmission	(19,102,751)	(18,574,235)	528,516
OL	3,505,089	2,843,134	(661,955)
SL	845,487	654,672	(190,815)
	57,637,290	52,421,657	(5,215,633)

Note: Table includes only base rates.

Revenue and Revenue Distribution

Current, Applicant-proposed and Staff-proposed revenue distribution are presented on Table 3.

Table 3
Cost of Service Results
Revenue Distribution (Dollars)
Excluding Fuel

Class	Current Revenue Distribution	COSS Levelized Revenue Distribution	Applicant Proposed Revenue Distribution	Staff Proposed Revenue Distribution
RS	187,678,408	225,776,925	226,448,735	223,446,163
GS-1	11,379,917	12,988,729	12,830,654	13,100,523
Secondary	69,786,357	96,657,881	92,466,495	91,685,218
Primary	25,391,002	31,201,614	29,987,886	30,841,210
Sub/Transmission	21,095,582	1,992,831	2,521,347	10,499,088
OL	5,088,054	8,593,143	7,931,188	7,632,780
SL	3,954,167	4,799,654	4,608,839	4,800,645
Total	324,373,487	382,010,777	376,795,144	382,005,627

Note: Table includes only base rate revenues (cust. chgs, volumetric chgs.).

Revenue and Revenue Distribution

The OP's COSS shows a $57,637,290 increase. The Applicant assigned $5 million of the $57 million to CSP customers based upon a proposed merger. At the conclusion of Staff's review, the commission had not approved AEP's merger, therefore, Staff is assigning OP's costs on a stand alone basis. Staff established a "target" of moving the rate of return index for each customer class at least three-fourths of the way to 1.00 (levelized rate of return index). Once the target was established, rates were designed taking into account the standards previously described. Therefore, Staff recommends its proposed revenue distribution be approved. Staff-proposed revenue distribution is presented (excluding fuel) in Tables 4 and 5.