

**BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO**

In the Matter of the Application of Ohio Power Company and Columbus Southern Power Company for Authority to Merge and Related Approvals.))))	Case No. 10-2376-EL-UNC
In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Authority to Establish a Standard Service Offer Pursuant to §4928.143, Ohio Rev. Code, in the Form of an Electric Security Plan.))))))	Case No. 11-346-EL-SSO Case No. 11-348-EL-SSO
In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of Certain Accounting Authority.))))	Case No. 11-349-EL-AAM Case No. 11-350-EL-AAM
In the Matter of the Application of Columbus Southern Power Company to Amend its Emergency Curtailment Service Riders.))))	Case No. 10-343-EL-ATA
In the Matter of the Application of Ohio Power Company to Amend its Emergency Curtailment Service Riders.)))	Case No. 10-344-EL-ATA
In the Matter of the Commission Review Of the Capacity Charges of Ohio Power Company and Columbus Southern Power Company.))))	Case No. 10-2929-EL-UNC
In the Matter of the Application of Columbus Southern Power Company for Approval of a Mechanism to Recover Deferred Fuel Costs Ordered Under Ohio Revised Code 4928.144.)))))	Case No. 11-4920-EL-RDR
In the Matter of the Application of Ohio Power Company for Approval of a Mechanism to Recover Deferred Fuel Costs Ordered Under Ohio Revised Code 4928.144.)))))	Case No. 11-4921-EL-RDR

INITIAL BRIEF OF INDUSTRIAL ENERGY USERS-OHIO

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TABLE OF CONTENTS

	<u>Page No.</u>
I. INTRODUCTION	1
II. BACKGROUND	5
III. EVALUATION CRITERIA FOR SETTLEMENT	6
IV. IEU-OHIO'S MOTION TO DISMISS	7
V. THE STIPULATION DOES NOT ADVANCE THE PUBLIC INTEREST, BENEFIT CONSUMERS, OR SATISFY LEGAL OR POLICY REQUIREMENTS NECESSARY FOR APPROVAL OF THE STIPULATION	18
A. The ESP is Not More Favorable than an MRO	19
1. All witnesses agree that prices under the proposed ESP are not more favorable than prices under an MRO	19
2. The ESP versus MRO analysis performed by Companies' witness Thomas and Staff witness Fortney are flawed and cannot be relied upon for anything other than confirming that the ESP fails the statutory test	21
3. The ESP non-price and qualitative benefits claimed by the Companies and Staff do not exist or are entirely speculative	27
B. Generation Rate Structure	29
C. Rate Increases	34
D. Shopping Limits	37
1. The two-tiered capacity price frustrates customer choice	38
2. The two-tiered capacity price imposes an unreasonable and discriminatory condition on the resale of electric service	43
E. Generation Resource Rider ("GRR")	46
1. The GRR is not justified	46
2. Authorizing the GRR without accounting for the likely cost improperly biases the ESP versus MRO analysis	49

F.	Combined Heat and Power Provisions	50
G.	Distribution Investment Rider	50
H.	Pool Modification or Termination Rider	58
I.	Phase-In Recovery Rider (“PIRR”)/Securitization	60
J.	Timber Road Renewable Energy Purchase Agreement and Shale Gas FAC Review	64
K.	Corporate Separation.....	66
L.	Summary	68
VI.	THE STIPULATION IS NOT THE PRODUCT OF SERIOUS BARGAINING.....	68
VII.	MODIFICATION OF THE STIPULATION	72
VIII.	CONCLUSION.....	74

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INITIAL BRIEF OF INDUSTRIAL ENERGY USERS-OHIO

I. INTRODUCTION

In the pages that follow, the Industrial Energy Users-Ohio (“IEU-Ohio”) presents legal, policy and other arguments in support of the position that the Public Utilities Commission of Ohio (“Commission”) must, as a matter of law, reject the Stipulation and Recommendation (“Stipulation”) and the electric security plan (“ESP”) illegally, vaguely and confusingly recommended therein. Combined, these arguments reveal the Stipulation’s most fundamental defect: It is a bad deal measured by everything the Commission is obligated to obey and respect.

The Stipulation recommends unjustified rate increases at a time when the Great Recession’s hold on Ohio’s economy and its citizens remains profound and unyielding. It then recommends that the Commission use its authority to permit Columbus Southern Power Company (“CSP”) and Ohio Power Company (“OP”) (collectively, the “Companies”) to erect a monopoly toll booth in interstate commerce so that customers are captive to the rate increases the Companies demand but cannot justify. The timing of the toll booth provision in the Stipulation is not coincidental.

The toll booth’s proponents advance their recommendation just as the forces of competition have begun to provide customers with lower prices and better service in circumstances where customers have unfettered access to competitive retail electric service (“CRES”) suppliers including governmental aggregators. The proposed in-service date for the toll booth will allow the Companies to rain on the parade of

governmental aggregation programs that overwhelmingly were approved by voters throughout the Companies' service areas in the last few days.

All the evidence produced by parties supporting the Stipulation and those who took on the responsibility of demonstrating that the "emperor has no clothes" agree that the Stipulation cannot pass the price comparison test threshold which must be crossed before the Commission can approve an ESP presented through a settlement or otherwise. Yet, the parties that signed the Stipulation (after most of them conducted no independent analysis and failed to understand the real-time significance of the shopping limitations) persisted in their effort to secure the Commission's approval of their bad deal.

During the course of these proceedings, the Companies called often upon the roll of context as though context can operate as a substitute for procedural and substantive due process. Ironically, the historical context which precedes the Stipulation also demonstrates the fundamental unfairness of the outcomes recommended within the Stipulation.

Since 2006, the Companies' Standard Service Offer ("SSO") prices have increased annually and significantly.¹ The increases were in some cases illegal, but

¹ *In the Matter of the Applications of the Columbus Southern Power Company and the Ohio Power Company for Approval of a Post-Market Development Period Rate Stabilization Plan*, Case No. 04-169-EL-UNC, Opinion and Order at 9 (Jan. 26, 2005); *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of an Additional Generation Service Rate Increase Pursuant to Their Post-Market Development Period Rate Stabilization Plans*, Case No. 07-63-EL-UNC, Opinion and Order at 27-29 (Oct. 3, 2007); *In the Matter of the Application of Columbus Southern Power Company for Approval of an Electric Security Plan; an Amendment to its Corporate Separation Plan; and the Sale or Transfer of Certain Generating Assets*, Case Nos. 08-917-EL-SSO, *et al.*, Opinion and Order at 28 (Mar. 18, 2009), *affirmed in part and reversed and remanded in part*, *In re Application of Columbus S. Power Co.*, 128 Ohio St.3d 512 (2011).

nonetheless transferred hundreds of millions of dollars in consumers' wealth to the Companies. The steady stream of increases provided CSP with "significantly excessive earnings."² The steady stream of increases has given the Companies the highest gross margin per megawatt hour of any business division within American Electric Power ("AEP").³

During this history, the Companies repeatedly pointed to competitive benchmark prices and the bypassability of their SSO prices as justification for the significant year-to-year uptick in prices.⁴ The competitive benchmark prices strongly and uniformly supported over the years by the Companies were based on a capacity charge tied to the output of PJM Interconnection LLC's ("PJM") reliability pricing model ("RPM") and the competitive bidding process ("CBP") that PJM uses to establish capacity prices.⁵

Year after year and case after case, the Companies clung to RPM and beat back efforts, with the Commission's support, to install a cost-based system of measuring "just and reasonable" rates. Now the Companies, in their advocacy for the Stipulation, are leading an assault on the very methods they successfully leveraged in the past to significantly raise SSO prices. And the current assault is selective; the Companies'

² *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Administration of the Significantly Excessive Earnings Test Under Section 4928.143(F), Revised Code, and Rule 4901:1-35-10, Ohio Administrative Code*, Case No. 10-1261-EL-UNC, Opinion and Order at 35 (Jan. 11, 2011).

³ IEU-Ohio Exhibit 19 (at pages 11 and 13) contains AEP's documentation of the extent to which rates authorized by the Commission have produced financial results stunningly superior to the results in states that set rates for the Companies' affiliates based on a cost-of-service metric. Tr. Vol. XII at 2251-57 (Cross-examination of Philip Nelson).

⁴ IEU-Ohio Ex. 16 at 9, 11-14.

⁵ Tr. Vol. V at 811-12 (Cross-examination of Joseph Hamrock); IEU-Ohio Ex. 17, Attachment 1 at 2.

turnabout now invites the Commission to use either a cost-based yardstick or an arbitrary number to set the price for the capacity component of generation service. Yet they persist in their claim that the balance of their SSO price and the arbitrary increases in that price recommended by the Stipulation cannot and must not be subjected to cost-based evaluation.

The history that precedes these proceedings also documents the Companies' persistent support for a market-based system of setting SSO prices so long as the system worked to allow the Companies' rates to be lifted higher. For example, the Companies unabashedly and unequivocally supported reliance on a market-based approach and competition as the best means to advance Ohio's policies and secure useful outcomes for customers.⁶ They extolled the virtues of PJM's wholesale market and their use of a CBP to secure generation supply and establish retail prices for default service.⁷ More recently, the CBP used to set the default generation supply prices in the service areas of the Ohio operating companies of FirstEnergy Corp. confirm the power of competition to produce reliable service and stable lower prices.⁸ This historical context shows that, in these proceedings, the Companies are attacking the very

⁶ See Tr. Vol. V at 831 (administrative notice taken of *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Approval of a Competitive Bidding Process for Standard Service Offer Electric Generation Supply, Accounting Modifications Associated With Reconciliation Mechanism and Phase In, and Tariffs for Generation Service*, Case Nos. 07-796-EL-ATA, *et al.*, Comments of Columbus Southern Power Company and Ohio Power Company (Sep. 5, 2007) and Reply Comments of Columbus Southern Power Company and Ohio Power Company (Oct. 12, 2007)).

⁷ *Id.*

⁸ See Tr. Vol. XIII at 2340 (administrative notice taken of *In the Matter of the Procurement of Standard Service Offer Generation for Customers of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company*, Case No. 10-1284-EL-UNC, Finding and Order at 2 (Oct. 26, 2011)).

positions that they advanced previously to secure the Commission's approval of frequent, dramatic and, too often, illegal rate increases.

The arguments below identify specific provisions housed within the Stipulation that are unreasonable, illegal, or both. The discrete discussions of the evidence and propositions of law must not, however, obscure the more fundamental and fatally defective problem with the Stipulation. It is a bad deal for customers and Ohio.

II. BACKGROUND

On January 27, 2011, CSP and OP filed applications ("Application") to establish their second ESPs. In anticipation of evidentiary hearings on the Application, public hearings were held throughout the Companies' service territory. At those public hearings, consumers expressed concern about the Companies' proposals to increase rates and limit shopping for retail electric service.⁹

On the eve of the start of the evidentiary hearing on the Application, the Companies, the Staff of the Public Utilities Commission of Ohio ("Staff") and several intervenors indicated that they had reached an agreement regarding the Application and several other matters pending before the Commission. They signed and filed the Stipulation on September 7, 2011. Because the Stipulation recommends the approval of unjustified rate increases, limitations on the right of customers to obtain competitive retail electric service, unduly discriminatory rates, and other provisions that violate a host of legal requirements, IEU-Ohio, FirstEnergy Solutions ("FES"), Ormet Primary

⁹ See, e.g., Lima, Ohio Public Hearing, Tr. at 17-24 (June 8, 2011); Columbus, Ohio Public Hearing, Tr. at 27-30 (June 6, 2011); Canton, Ohio Public Hearing, Tr. at 16-20 (June 7, 2011).

Aluminum Corporation (“Ormet”), the Office of the Ohio Consumers’ Counsel (“OCC”), Ohio Partners for Affordable Energy (“OPAЕ”), and the Appalachian Peace and Justice Network (“APJN”) either did not sign or actively opposed the Stipulation. Given the opposition to the Stipulation, the Commission scheduled additional discovery, and hearings began October 4, 2011.

The nearly three weeks of hearings on what has already been described as a “bad deal” demonstrates that the proponents of the Stipulation have failed to satisfy the requirements necessary to demonstrate that the Commission may approve lawfully the ESP and the other matters the Stipulation attempts to resolve. The Stipulation fails to advance the public interest, contains patently illegal terms, and is not the product of serious bargaining within the bounds of the law. As a result, the Commission must reject the Stipulation. If the Commission instead chooses to control the damage that would otherwise be created by the Stipulation, it must make significant modifications to it to make the Stipulation both lawful and reasonable.

III. EVALUATION CRITERIA FOR SETTLEMENT

Before approving a contested settlement, the Commission must find that: (1) the settlement is a product of serious bargaining among capable, knowledgeable parties; (2) the settlement, as a package, benefits ratepayers and the public interest; and; (3) the settlement package does not violate any important regulatory principles or practices.¹⁰

¹⁰ *Consumers’ Counsel v. Pub. Util. Comm.*, 64 Ohio St.3d 123, 126 (1992). See, also, *AK Steel Corp. v. Pub. Util. Comm.*, 95 Ohio St.3d 81, 82-83 (2002).

A settlement is not evidence and it is not binding on the Commission. It is a recommendation by parties to a proceeding on how the Commission should address and resolve contested issues and nothing more.

A settlement cannot provide the Commission with authority to do what the Commission does not otherwise have authority to do or to disrespect procedural or substantive requirements established by the General Assembly or the Commission's rules. For example, Monongahela Power relied upon a settlement for its authority to end the five-year market development period early (a result which would have imposed "rate shock"). The Ohio Supreme Court ("Supreme Court") rejected the claim that the settlement provided support for the early termination, stating:

Nevertheless, to the extent that Section IV of the Stipulation approved by the commission in the ETP Order can be considered an order authorizing the early end of Mon Power's MDP, that order was premature. It was based upon an optimistic assumption that the requisite levels of the switching rate or effective competition would be achieved by December 31, 2003, an assumption that proved to be unwarranted, making any such order ending the MDP unenforceable **because the order exceeded the statutory authority of the commission**.¹¹

IV. IEU-OHIO'S MOTION TO DISMISS

At the close of the Companies' direct case, IEU-Ohio moved to dismiss the Application and the Stipulation.¹² OCC, APJN and FES joined IEU-Ohio's motion to dismiss.¹³ The Attorney Examiners took the motion to dismiss under advisement.¹⁴

¹¹ *Monongahela Power Co. v. Pub. Util. Comm.*, 104 Ohio St.3d 571, 2004-Ohio-6896 at ¶ 26 (2004) (emphasis added).

¹² Tr. Vol. VI at 956.

¹³ Tr. Vol. VI at 958.

Based on the law and facts associated with these proceedings, the motion to dismiss should be granted.¹⁵

Section 4928.143, Revised Code, is the exclusive statutory means by which an EDU may establish an ESP capable of satisfying the obligations imposed on an EDU by Section 4928.141, Revised Code. Section 4928.143(C), Revised Code, states that with regard to a proposed ESP the burden of proof shall be on the EDU.

Neither the Application filed on January 27, 2011 in Case Nos. 11-346-EL-SSO, *et al.*, nor the Stipulation proposes to establish an ESP for an EDU. Both propose an ESP for an entity named AEP-Ohio. CSP and OP are each an EDU in their own right as defined by Ohio law.¹⁶ AEP-Ohio is not a legal entity and is not an EDU.¹⁷

Section 4928.141, Revised Code, requires that an EDU apply to the Commission to establish a standard service offer (“SSO”). If the EDU elects to file an application for an ESP, the application is governed by Section 4928.143, Revised Code. Division (A) of that Section provides in relevant part:

[A]n **electric distribution utility** may file an application for public utilities commission approval of an electric security plan as prescribed under

¹⁴ Tr. Vol. VI at 961.

¹⁵ On May 10, 2011, IEU-Ohio filed a written Motion to Dismiss and Memorandum in Support in Case Nos. 11-346-EL-SSO, *et al.* The Motion and Memorandum are incorporated herein by reference as they relate to the failure by OP and CSP to each propose an electric distribution utility (“EDU”) ESP as required by Ohio law.

¹⁶ Tr. Vol. V at 783 (Cross-examination of Joseph Hamrock); *see also* Section 4928.01(A)(6), Revised Code.

¹⁷ Tr. Vol. V at 783-84 (Cross-examination of Joseph Hamrock). In fact, American Electric Power Company, Inc. has claimed that it is not a public utility and, as a result, the Commission lacks jurisdiction over it: “AEP posits that it is not a public utility as that term is defined in Section 4905.02, Revised Code, and therefore, the Commission lacks jurisdiction over AEP.” *In the Matter of the Complaint of Brian Tomlin v. Columbus Power Company*, Case No. 02-46-EL-CSS, Opinion and Order (Dec. 12, 2002).

division (B) of this section. The utility may file that application prior to the effective date of any rules the commission may adopt for the purpose of this section, and, as the commission determines necessary, **the utility immediately shall conform its filing to those rules upon their taking effect.**¹⁸

This division creates several mandatory requirements.

First, only an EDU can file an application for an ESP. “EDU” is a defined term. Section 4928.01(A)(6), Revised Code, defines “Electric distribution utility” as “an electric utility that supplies at least retail electric distribution service.” It further defines “Electric utility” as “an electric light company that has a certified territory and is engaged on a for-profit basis either in the business of supplying a noncompetitive retail electric service in this state or in the businesses of supplying both a noncompetitive and a competitive retail electric service in this state.”¹⁹ No entity other than an EDU is authorized to seek an ESP. OP and CSP are each an EDU.²⁰ Sections 4928.141 and 4928.143, Revised Code, confine the opportunity to seek and obtain an ESP to an EDU.

Second, the plan must relate to the terms of service of the EDU. Sections 4928.143(B)(2)(b) and (c), Revised Code, are limited to providing cost recovery for construction work in progress and generation facilities dedicated to Ohio customers by the EDU. Divisions (B)(2)(f), (g), (h), and (i) similarly are constrained by reference to the EDU. Although Divisions (B)(2)(d) and (e) do not specifically mention a limitation to

¹⁸ Section 4928.143(A), Revised Code (emphasis added).

¹⁹ Section 4928.01(A)(11), Revised Code.

²⁰ Tr. Vol. V at 783-84 (Cross-examination of Joseph Hamrock).

an EDU, they are limited to terms affecting the EDU's "retail electric service"²¹ and "standard service offer price," respectively.²²

Third, Section 4928.143(B)(2)(a)-(i), Revised Code, requires that the ESP relate specifically to services and charges of an EDU, and just as importantly, those subdivisions detail the exclusive list of what may be included in an ESP. As the Supreme Court has explained, "[b]y its terms, R.C. 4928.143(B)(2) allows plans to include only 'any of the following' provisions. It does not allow plans to include 'any' provision. So if a given provision does not fit within one of the categories listed 'following' (B)(2), it is not authorized by statute."²³

Fourth, an EDU's request for an ESP must conform to the Commission's filing requirements. The filing requirements are set out in Rule 4901:1-35-03, Ohio Administrative Code ("OAC"), and serve as the basis for the Commission to review²⁴ and the customers to understand the scope of the Companies' application. Of particular

²¹ Section 4928.01(A)(27), Revised Code, defines "retail electric service" as "any service involved in supplying or arranging for the supply of electricity to ultimate consumers in this state, from the point of generation to the point of consumption. For the purposes of this chapter, retail electric service includes one or more of the following service components: generation service, aggregation service, power marketing service, power brokerage service, transmission."

²² The relevant provisions of Sections 4928.143(C) and 4928.144, Revised Code, similarly apply to only an EDU. The EDU has the burden to demonstrate that the ESP meets the requirement that the ESP is better in the aggregate than the alternative under Section 4928.142, Revised Code, and only the EDU may withdraw an ESP if the Commission modifies and approves an ESP not to the EDU's liking. Section 4928.143(C), Revised Code. Finally, the provision regarding phase-in deferral recovery is similarly limited to the provision of a phase-in plan for an EDU. Section 4928.144, Revised Code.

²³ *In re Application of Columbus S. Power Co.*, 128 Ohio St.3d. 512, 520 (2011).

²⁴ The Commission is charged with evaluating the legitimacy of the terms and conditions of the plan in making a determination whether to approve, dismiss, or modify and approve an ESP application. Section 4928.143(C), Revised Code. *In re Application of Columbus Southern Power Co.*, 128 Ohio St.3d 402, 407 (2011) ("[I]n evaluating the favorability of a plan, the statute instructs the commission to consider 'pricing and all other terms and conditions.'").

importance to this motion to dismiss is subdivision (C)(2) which requires “[p]ro forma financial projections of the effect of the ESP’s implementation upon the electric utility” and subdivision (C)(3) which requires “[p]rojected rate impacts by customer class/rate schedules for the duration of the ESP.”²⁵ The Commission rules thus make it clear that “placeholders” are not appropriate in an ESP filing.

The Stipulation²⁶ envisions the use of “securitization” for purposes of addressing a phase-in deferral. Rule 4901:1-35-03(C)(9)(e), OAC, states (emphasis added):

Division (B)(2)(f) of section 4928.143 of the Revised Code authorizes an electric utility to include provisions for the securitization of authorized phase-in recovery of the standard service offer price. If a phase-in deferred asset is proposed to be securitized, the electric utility **shall** provide, at the time of an application for securitization, a description of the securitization instrument and an accounting of that securitization, including the deferred cash flow due to the phase-in, carrying charges, and the incremental cost of the securitization. The electric utility will also describe any efforts to minimize the incremental cost of the securitization. The electric utility **shall** provide all documentation associated with securitization, including but not limited to, a summary sheet of terms and conditions. The electric utility shall also provide a comparison of costs associated with securitization with the costs associated with other forms of financing to demonstrate that securitization is the least cost strategy.

None of the information required by Rule 4901:1-35-03(C)(9)(e), OAC, was filed with the Commission or made a part of the evidentiary record.

The Stipulation (Section IV.2.b) contains provisions that have the effect of preventing, limiting, or inhibiting customer shopping for retail electric generation service.

Rule 4901:1-35-03(C)(9)(c)(i), OAC, states (emphasis added):

²⁵ Rule 4901:1-35-03(C)(2) and (3), OAC.

²⁶ Stipulation at 25-26.

Division (B)(2)(d) of section 4928.143 of the Revised Code authorizes an electric utility to include terms, conditions, or charges related to retail shopping by customers. Any application which includes such terms, conditions or charges, shall include, at a minimum, the following information:

(i) A listing of all components of the ESP which would have the effect of preventing, limiting, inhibiting, or promoting customer shopping for retail electric generation service. Such components would include, but are not limited to, terms and conditions relating to shopping or to returning to the standard service offer and any unavoidable charges. For each such component, an explanation of the component and a descriptive rationale and, to the extent possible, a quantitative justification shall be provided.

The Companies have publicly admitted that the provisions in the Stipulation that impose a \$255 per megawatt-day capacity charge on CRES suppliers are designed to limit shopping for retail electric generation service.²⁷ Other witnesses testifying in support of the Stipulation confirmed that the Stipulation is designed to limit and will inhibit customer shopping for retail electric generation service.²⁸ The testimony of parties not supporting the Stipulation also confirms that the Stipulation is designed to limit customer shopping for retail electric generation service.²⁹ The information required by Rule 4901:1-35-03(C)(9)(c)(i), OAC, however, was not submitted.

Rules 4901:1-35-03(C)(6) and (7), OAC, state that an SSO application containing an ESP must include: “[a] description of how the electric utility proposes to address

²⁷ FES Ex. 1, TCB-8, TCB-9; IEU-Ohio Ex. 13; Tr. Vol. X at 1693-94 (Cross-examination of Robert Fortney); Tr. Vol. III at 395 (Cross-examination of William Allen); Tr. Vol. IV at 542-43 (Cross-examination of Teresa Ringenbach); Tr. Vol. VI at 970-71 (Cross-examination of David Fein).

²⁸ Tr. Vol. X at 1693-94 (Cross-examination of Robert Fortney); Tr. Vol. III at 395 (Cross-examination of William Allen); Tr. Vol. IV at 542-43 (Cross-examination of Teresa Ringenbach); Tr. Vol. VI at 970-71 (Cross-examination of David Fein); IEU-Ohio Ex. 9A at 9-21, 24; FES Ex. 1 at 4-6, 17-37; FES Ex. 14 at 4, 16-23, 31-32; FES Ex. 3 at 4-5, 35-37; 40-41.

²⁹ IEU-Ohio Ex. 9A at 9-21, 24; FES Ex. 1 at 4-6, 17-37; FES Ex. 14 at 4, 16-23, 31-32; FES Ex. 3 at 4-5, 35-37, 40-41.

governmental aggregation programs and implementation of divisions (I),³⁰ (J),³¹ and (K)³² of section 4928.20 of the Revised Code”; and, “[a] description of the effect on large-scale governmental aggregation of any unavoidable generation charge proposed to be established in the ESP”. Section 4928.20(K), Revised Code, requires the Commission to adopt rules to encourage and promote large-scale governmental aggregation and, in the context of a proposed ESP, the Commission must consider the effect of any provisions that would, if approved, impose non-bypassable generation charges, **“however collected”** on such large-scale aggregation programs. Common sense and the evidence supplied by parties opposing the Stipulation demonstrate that the Stipulation works against large-scale aggregation programs.³³ The information required by Rules 4901:1-35-03(C)(6) and (7), OAC, was not submitted.

Section 4928.40(D), Revised Code, states that “no electric utility in this state shall prohibit the resale of electric generation service or impose unreasonable or discriminatory conditions or limitations on the resale of electric generation service.” The Companies’ witness Nelson explained the Companies’ view that resale of electricity

³⁰ Section 4928.20(I), Revised Code, limits the amount of any non-bypassable charge associated with a Section 4928.144, Revised Code, phase-in that may be applied to customers that are part of a governmental aggregation program. The non-bypassable phase-in charge must not exceed an amount that is proportional to the benefits received by such customers. The phase-in recovery rider (“PIRR”) proposed in the Stipulation would, if approved, make CSP customers responsible for an OP phase-in deferral. Stipulation at 26. The PIRR is illegal on its face.

³¹ Section 4928.20(J), Revised Code, allows a governmental aggregation program to elect, on behalf of the program’s customers, to not receive and pay for standby service within the meaning of Section 4928.143(B)(2)(d), Revised Code. Upon such election, any program customer returning to the SSO shall pay the “market price” of power incurred by the EDU plus an allowance for the EDU’s cost of compliance with the portfolio requirements in Section 4928.64, Revised Code.

³² Section 4928.20(K), Revised Code, requires the Commission to adopt rules to encourage and promote large-scale governmental aggregation and to consider, in the context of a proposed ESP, the effect of any non-bypassable generation charges on such aggregation.

³³ IEU-Ohio Ex. 8 at 12-13; IEU-Ohio Ex. 9A at 21-22; FES Ex. 1 at 9,12-13, 18-20, 25-26, 31-35, 46, 56.

involves a wholesale transaction and the Stipulation's proposed \$255 per megawatt-day capacity charge is a wholesale charge involving a sale for resale.³⁴ The Stipulation recommends a discriminatory³⁵ capacity charge structure with CRES suppliers providing megawatt hours above the "caps" subjected to the \$255 per megawatt-day amount and the megawatt hours supplied below the "caps" paying the Commission-approved and current market-based capacity charge arising from PJM's wholesale auction process.³⁶ When questioned about the justification for the \$255 per megawatt-day capacity charge, the parties supporting the Stipulation uniformly stated that the \$255 per megawatt-day capacity charge was "negotiated" and provided no other basis to support its reasonableness or lawfulness.³⁷

As explained above, the bifurcated capacity charge structure in the Stipulation is designed to limit economically the opportunity for customers to act on their retail electric service preferences. On its face and with the understanding that the Companies' objective is to limit shopping, the bifurcated capacity charge structure offends the pro "customer choice" and supplier diversity policy goals set forth in Section 4928.02, Revised Code. Thus, the bifurcated capacity charge structure is discriminatory and unreasonable, a condition that is prohibited by Section 4928.40(D), Revised Code.

³⁴ Tr. Vol. XII at 2230 (Cross-examination of Philip Nelson).

³⁵ The definition of "standard service offer" in Rule 4901:1-35-01(L), OAC, highlights the importance of the role of the nondiscriminatory and comparable requirements that are imposed by Chapter 4928, Revised Code: "'Standard service offer' means an electric utility offer to provide consumers, on a comparable and nondiscriminatory basis within its certified territory, all competitive retail electric services necessary to maintain essential electric service to consumers, including a firm supply of electric generation service."

³⁶ Stipulation at 20-23.

³⁷ Tr. Vol. II at 191 (Cross-examination of Kelly Pearce); Tr. Vol. V at 737 (Cross-examination of Philip Nelson); Tr. Vol. V at 810, 845 (Cross-examination of Joseph Hamrock).

As also explained above, the design of the bifurcated capacity charge structure discriminates between shopping customers based on conditions that existed in the past and does so prior to the recommended effective date of the Stipulation's provisions containing the bifurcated capacity charge structure. Similarly, the design of the bifurcated capacity charge structure discriminates between CRES suppliers based on conditions that existed in the past and does so prior to the recommended effective date of the Stipulation's provisions containing the bifurcated capacity charge structure. The Stipulation retroactively and unlawfully imposes disabilities on customers' right to shop and the right of CRES suppliers to have comparable and non-discriminatory access to the retail market in the Companies' services areas.

Despite the prohibitions contained in Section 4928.40(D), Revised Code, and the burden of proof obligation contained in Section 4928.143(C), Revised Code, neither the Companies nor any party supporting the Stipulation offered any evidence to demonstrate that the bifurcated capacity charge structure recommended by the Stipulation can be lawfully approved by the Commission.

The Stipulation (Section IV.1.n) calls for the establishment of a distribution investment rider ("DIR") effective January 1, 2012 based on post-2000 investment and including components for certain taxes, depreciation, and an unsupported and high rate of return on plant. Rule 4901:1-35-03(C)(9)(g), OAC, states (emphasis added):

Division (B)(2)(h) of section 4928.143 of the Revised Code authorizes an electric utility to include provisions for alternative regulation mechanisms or programs, including infrastructure and modernization incentives, relating to distribution service as part of an ESP. While a number of mechanisms may be combined within a plan, for each specific mechanism or program, the electric utility **shall** provide a detailed description, with

supporting data and information, to allow appropriate evaluation of each proposal, including how the proposal addresses any cost savings to the electric utility, avoids duplicative cost recovery, and aligns electric utility and consumer interests. In general, and to the extent applicable, the electric utility **shall** also include, for each separate mechanism or program, quantification of the estimated impact on rates over the term of any proposed modernization plan. Any application for an infrastructure modernization plan **shall** include the following specific requirements:

(i) A description of the infrastructure modernization plan, including but not limited to, the electric utility's existing infrastructure, its existing asset management system and related capabilities, the type of technology and reason chosen, the portion of service territory affected, the percentage of customers directly impacted (non-rate impact), and the implementation schedule by geographic location and/or type of activity. A description of any communication infrastructure included in the infrastructure modernization plan and any metering, distribution automation, or other applications that may be supported by this communication infrastructure also shall be included.

(ii) A description of the benefits of the infrastructure modernization plan (in total and by activity or type), including but not limited to the following as they may apply to the plan: the impacts on current reliability, the number of circuits impacted, the number of customers impacted, the timing of impacts, whether the impact is on the frequency or duration of outages, whether the infrastructure modernization plan addresses primary outage causes, what problems are addressed by the infrastructure modernization plan, the resulting dollar savings and additional costs, the activities affected and related accounts, the timing of savings, other customer benefits, and societal benefits. Through metrics and milestones, the infrastructure modernization plan shall include a description of how the performance and outcomes of the plan will be measured.

(iii) A detailed description of the costs of the infrastructure modernization plan, including a breakdown of capital costs and operating and maintenance expenses net of any related savings, the revenue requirement, including recovery of stranded investment related to replacement of un-depreciated plant with new technology, the impact on customer bills, service disruptions associated with plan implementation, and description of (and dollar value of) equipment being made obsolescent by the plan and reason for early plant retirement. The infrastructure modernization plan shall also include a description of efforts made to mitigate such stranded investment.

The information required by Rule 4901:1-35-03(C)(9)(g), OAC, was not provided.

Section 4928.143(C)(1), Revised Code, imposes on the Companies the burden of proof. As part of that burden, an EDU must demonstrate that the proposed 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.” Neither the Companies nor any party supporting the Stipulation provided evidence showing that the ESP proposed in the Stipulation is more favorable in the aggregate than the expected results that would otherwise apply under Section 4928.142, Revised Code.

The Companies’ witness Hamrock acknowledged that many of the provisions in the Stipulation look to provisions in the ESP Application to identify the procedural and substantive significance of the provisions in the Stipulation.³⁸ No evidence was offered to support the ESP Application or any provisions in the ESP Application. In effect, the Stipulation proposes to amend an ESP which is not part of the record evidence and for which there is no evidentiary support.

A company’s failure to comply with the statutory requirements and administrative rules is ground for dismissing an EDUs proposed ESP. As the Commission recently determined in Duke Energy Ohio, Inc.’s SSO case:

As we stated throughout this order, the Commission finds that Duke’s application does not comply with the statute and, therefore, this case can not proceed as filed. **It is required that Duke provide the information dictated by the statute and delineated in the Commission’s rules, in order for the Commission to determine if the application satisfies the**

³⁸ Tr. Vol. V at 821-25 (Cross-examination of Joseph Hamrock).

statutory requirements. Duke readily concedes that it did not provide certain information because it was outside of its two-year proposal. **Accordingly, the Commission can not find that Duke satisfied the requirements set forth in Rules 4901:1-35-03 and 4901:1-35-11, O.A.C.**³⁹

For the reasons provided above (as examples of the many fundamental burden of proof failures, as well as violations of statutory provisions and the Commission's rules), it is IEU-Ohio's position that the Commission must dismiss the ESP Application filed in these proceedings on January 27, 2011 as well as the Stipulation.

V. THE STIPULATION DOES NOT ADVANCE THE PUBLIC INTEREST, BENEFIT CONSUMERS, OR SATISFY LEGAL OR POLICY REQUIREMENTS NECESSARY FOR APPROVAL OF THE STIPULATION

If the Commission does not dismiss the ESP proposed in the Stipulation as IEU-Ohio urges, the Commission must nonetheless reject the Stipulation as filed because it fails to satisfy the three-prong test for approval of a settlement. As discussed in the following subsections, the Stipulation fails to satisfy the statutory requirements for approving an ESP and contains several provisions that violate substantive provisions of the law, Commission rules, the state's energy policy, is devoid of any benefit for consumers, and violates the public interest.

³⁹ *In the Matter of the Application of Duke Energy Ohio, Inc., for Approval of a Market Rate Offer to Conduct a Competitive Bidding Process for a Standard Service Offer, Electric Generation Accounting Modifications and Tariffs for Generation Service*, Case No. 10-2586-EL-SSO, Opinion and Order at 49 (Feb. 23, 2011) ("*Duke SSO*") (emphasis added).

A. The ESP is Not More Favorable Than an MRO

In order to approve an ESP, the Commission is statutorily required to find that the ESP is more favorable in the aggregate than a market rate offer (“MRO”).⁴⁰ The Ohio General Assembly delegates authority to the Commission, and neither the Commission nor the parties to a stipulation and recommendation have the ability to change a law that the Ohio General Assembly has enacted.⁴¹ Thus, in the absence of affirmatively finding the ESP proposed by the Stipulation is more favorable in the aggregate than an MRO, the Commission must conclude the Stipulation violates an important regulatory principle (the Stipulation produces an unlawful result) and cannot be approved.

1. All witnesses agree that prices under the proposed ESP are not more favorable than prices under an MRO.

There is no disagreement that the SSO prices under the proposed ESP are not more favorable than the prices that would result under an MRO. Every witness who addressed the quantification of the MRO versus ESP test concluded that the cost to consumers of the proposed ESP exceeded the cost of an MRO.

After finally providing CSP- and OP-specific results in her rebuttal testimony, Companies’ witness Thomas, looking only at the period of January 2012 through May

⁴⁰ Section 4928.143(C)(1), Revised Code.

⁴¹ *Monongahela Power Co. v. Pub. Util. Comm.*, 104 Ohio St.3d 571 at ¶ 26 (2004); *In the Matter of the Application of Duke Energy Ohio, Inc. for Approval of an Electric Security Plan*, Case Nos. 08-920-EL-SSO, *et al.*, Opinion and Order at 34-37 (Dec. 17, 2008).

2015 and not the entire term of the proposed ESP, concluded that the ESP was less favorable than an MRO by \$0.33 per MWh for CSP and \$0.97 per MWh for OP.⁴²

Staff witness Fortney identified during cross-examination that the ESP versus MRO analysis in his prepared testimony did not reflect the effects of the Commission's remand order.⁴³ However, Mr. Fortney testified that if the effects of the Commission's remand order were considered, for the portion of the term he analyzed (the three years of 2012, 2013 and 2014), the proposed ESP would be less favorable than the MRO by \$276.6 million⁴⁴ or approximately \$2.12 per MWh for both CSP and OP combined.⁴⁵

FES' witness Schnitzer quantified the costs of the ESP under two scenarios. After correcting for errors that Mr. Schnitzer identified in the analysis performed by Companies' witness Thomas,⁴⁶ Mr. Schnitzer concluded the ESP was less favorable than an MRO by at least \$100-800 million.⁴⁷

IEU-Ohio witness Murray presented Exhibit KMM-11 to reflect the results of the Commission's remand order on his ESP versus MRO comparison. Mr. Murray also

⁴² Cos. Ex. 23, Revised Ex. LJT-R3 at line 16. As discussed *infra*, Ms. Thomas' analysis improperly excluded the last year of the Stipulation ESP and contains other flawed assumptions.

⁴³ Tr. Vol. X at 1696 (Cross-examination of Robert Fortney).

⁴⁴ *Id.* As discussed *infra*, Mr. Fortney's analysis improperly excluded seventeen months of the Stipulation ESP and contains other flawed assumptions.

⁴⁵ *Id.* at 1697.

⁴⁶ The errors Mr. Schnitzer identified in Ms. Thomas' analysis included failing to adjust fuel costs to reflect forecast fuel costs during the term of the ESP, ignoring potential costs associated with the GRR, ignoring potential pool termination costs, assuming capacity cost prices based on a CSP and OP cost-based rate rather than RPM, and understating the legacy ESP price by ignoring expected environmental investment costs. FES Ex. 3 at 14-28.

⁴⁷ *Id.* at 29.

made appropriate adjustments to the Stipulation ESP price to recognize expected costs under the generation resource rider (“GRR”) and to add additional distribution-related costs (the Enhanced Service Reliability Rider, the DIR, and gridSMART for CSP) that would not be permissible under an MRO. After removing provider of last resort (“POLR”) charges and making the adjustments to the ESP price the Companies failed to include, Mr. Murray concluded: (1) that OP’s proposed ESP is less favorable than an MRO by \$4.83 per MWh or \$556 million over the term of the proposed ESP, and (2) CSP’s proposed ESP is less favorable than an MRO by \$8.55 per MWh or \$660 million over the term of the proposed ESP.⁴⁸

2. The ESP versus MRO analysis performed by Companies’ witness Thomas and Staff witness Fortney are flawed and cannot be relied upon for anything other than confirming that the ESP fails the statutory test.

The ESP versus MRO analysis performed by Companies’ witness Thomas is flawed and cannot be relied upon. Ms. Thomas relied exclusively upon administratively-estimated market prices rather than the actual market transactions to establish her MRO benchmark price.⁴⁹ Ms. Thomas performed no investigation of her MRO benchmark prices to verify that her administratively-estimated prices were representative of real world offers made by suppliers.⁵⁰ When compared to current full requirements offers and properly adjusted for differences for such things as losses and

⁴⁸ Tr. Vol. VIII at 1531-32 (Direct examination of Kevin Murray).

⁴⁹ IEU-Ohio Ex. 9A at 26.

⁵⁰ IEU-Ohio Ex. 9B at 30-35; Tr. Vol. XIII at 2324.

various legal requirements, the administratively-determined prices suggested by Ms. Thomas are grossly overstated.⁵¹

Ms. Thomas made numerous erroneous assumptions in her analysis. The assumed capacity costs reflected in the benchmark price in her analysis are based upon a mathematical weighting of market-based capacity prices under PJM's RPM and the arbitrary capacity charge of \$255 per megawatt-day in Section IV.2.b.1 of the Stipulation.⁵² The defectively derived capacity price that Ms. Thomas applies to calculate a benchmark price significantly overstates the capacity price that would apply to the benchmark price associated with the MRO option. As a result, the benchmark prices in Ms. Thomas' analysis are too high by a very large margin, and she thus understates the amount by which the ESP fails the ESP versus MRO price comparison.

Ms. Thomas also failed to recognize that OP's and CSP's current ESP includes distribution rate riders (gridSMART⁵³ for CSP and the Enhanced Service Reliability Rider⁵⁴ for OP and CSP) that were approved pursuant to the single issue ratemaking provision of Section 4928.143(B)(2)(h), Revised Code. In projecting the cost of the Stipulation's ESP, she also ignored the DIR provided for pursuant to Section IV.1.n of

⁵¹ The results of a recent auction illustrate the amount of error contained in the Companies' benchmark price. While the hearing was proceeding, the results of the most recent auction for FirstEnergy were approved. The auction closed at a level well below Ms. Thomas' administratively-estimated price. Tr. Vol. XIII at 2341 (Attorney Examiner's administrative notice of results of FirstEnergy auction resulting in a clearing price of \$52.83 per MWh for June 1, 2012 to May 31, 2014. *In the Matter of the Procurement of Standard Service Offer Generation for Customers of Ohio Edison Company, the Cleveland Electric Illuminating Company, and the Toledo Edison Company*, Case No. 10-1284-EL-UNC, Finding and Order at 2 (Oct. 26, 2011)).

⁵² Tr. Vol. IV at 577 (Cross-examination of Laura Thomas).

⁵³ Tr. Vol. IV at 616-17 (Cross-examination of Laura Thomas).

⁵⁴ *Id.*

the Stipulation.⁵⁵ An MRO does not permit the inclusion of these riders or charges. Therefore, the ESP versus MRO comparison must recognize that the rates produced by the MRO would not include these riders or charges.⁵⁶ By failing to account for these differences, Ms. Thomas further understated the amount by which the proposed ESP is more expensive than the MRO.

Additionally, adoption of the Stipulation would result in approval of the GRR as a non-bypassable placeholder rider to be used to potentially collect costs associated with the Turning Point Solar Project and a hypothetical Muskingum River 6 (“MR6”) generating unit. Similarly, Section IV.2.c of the Stipulation obligates the Companies or the successor EDU to pursue development of up to 350 MW of customer-sited combined heat and power, waste energy recovery, and distributed energy resources, with costs to be recovered under an “appropriate rider.” The Stipulation does not identify any statutory basis for collection of the costs of these customer-sited generation facilities. Ms. Thomas assumed zero cost for the GRR⁵⁷ even though there are cost estimates for at least the Turning Point Solar Project project.⁵⁸ As to her decision to assign a zero value to the GRR, Ms. Thomas explained that she did so because the GRR was a placeholder.⁵⁹ Because she failed to include the revenue effects of at least

⁵⁵ Companies’ Ex. 5 at 16; Tr. Vol. IV at 593-94 (Cross-examination of Laura Thomas).

⁵⁶ These additional costs, which total \$524 million, need to be scored in the ESP versus MRO comparison. IEU-Ohio Ex. 9A at 45.

⁵⁷ *Id.*

⁵⁸ Tr. Vol. IV at 597.

⁵⁹ *Id.* at 596-97, 600 (Cross-examination of Laura Thomas).

the Turning Point Solar Project, her estimate of the cost of the proposed ESP was further understated.

In addition to the flawed assumptions in her ESP versus MRO analysis, Ms. Thomas ignores the entire last year of the proposed ESP. When questioned during cross-examination about her decision to exclude the period of June 2015 through May 2016 from her analysis, Ms. Thomas offered the view that since prices during the fifth year of the Stipulation ESP would be established through a CBP, it was not necessary or required to blend prices during the fifth year of the Stipulation ESP.⁶⁰ On that matter, Ms. Thomas was contradicted by Mr. Nelson, another Company witness, who recognized that the MRO was subject to a six to ten year transition period and she was wrong as a matter of law⁶¹

It is settled law that the first MRO application filed by an EDU that, as of July 31, 2008, directly owns, in whole or in part, operating electric generating facilities that had been used and useful in this state requires a blending of the portion of the SSO load price based upon the competitive bid with the remainder of the SSO load price based upon the legacy ESP price.⁶² Section 4928.142(D), Revised Code, requires the initial MRO application to blend the competitive bid price proportionally with the legacy ESP price over the initial five years.

⁶⁰ *Id.* at 607-611 (Cross-examination of Laura Thomas).

⁶¹ Tr. Vol. XII at 2265 (Cross-examination of Philip Nelson).

⁶² Section 4928.142(D), Revised Code.

The appropriate blending period has already been determined in a review of an application by Duke to establish Duke's first MRO.⁶³ Because Duke projected that expected market prices and its legacy ESP price would converge in the third year of the MRO, and because Duke proposed to transfer its legacy generation to an affiliate no later than the beginning of the third year, Duke proposed to end the blending period at the beginning of year three and make available to customers an ESP price exclusively based upon the market prices resulting from an auction.⁶⁴ Similarly, Ms. Thomas' MRO price in the fifth year of her ESP versus MRO comparison assumes that the competitive bid price applies to the entire SSO load with no blending of the legacy ESP rate.⁶⁵ In *Duke SSO*, the Commission determined that the initial five-year blending period is statutorily required and cannot be altered:

The Commission agrees with Staff that, under Sections 4928.142(D) and (E), Revised Code, as well as Chapter 4901:1-35, O.A.C., Duke was required to file a five-year blending plan and transition to market. Failure to do so renders Duke's proposed MRO application in noncompliance with the statutory requirements.⁶⁶

As a matter of law, the Companies are subject to the blending required by Section 4928.143.142(D), Revised Code. Ms. Thomas confirmed for the record that the Companies owned generation facilities at the time Section 4928.142, Revised Code,

⁶³ *Duke SSO*, Opinion and Order (Feb. 23, 2011).

⁶⁴ *Duke SSO*, Opinion and Order at 9.

⁶⁵ During his cross-examination, Staff witness Fortney acknowledged his understanding that an initial MRO application by a utility that owned generation assets requires blending of the competitive bid prices with the legacy ESP prices for a minimum of five years. Tr. Vol. X at 1739-41 (Cross-examination of Robert Fortney). Ohio Energy Group ("OEG") witness Stephen Baron previously submitted testimony supporting a five-year blending period, also. IEU-Ohio Ex. 2 at 2.

⁶⁶ *Duke SSO* at 23. In the *Duke SSO* Order, the Commission determined that Section 4928.142(E), Revised Code, could allow a party to propose prospectively an alteration of the blending percentages specified in Section 4928.142(D), Revised Code, after the first two years of an MRO. *Duke SSO* at 17.

was enacted.⁶⁷ Thus, by the requirements of Section 4928.142(D), Revised Code, an initial application to establish an MRO would require blending of the first five years of the proposal. Ms. Thomas instead chose to assume that the fifth year would not be blended with the legacy ESP price.⁶⁸ By assuming that the fifth year of the MRO does not involve blending with the legacy ESP price, Ms. Thomas grossly understated the relative amount by which the proposed ESP failed the MRO versus ESP test. Mr. Murray's testimony demonstrated that correcting her version of the test for the omission of the last year even while ignoring the many other errors in her calculation resulted in the ESP failing the MRO price comparison.⁶⁹

Although he did not make as many errors as Ms. Thomas, Mr. Fortney made some of the same errors contained in Ms. Thomas' version of the ESP versus MRO test. Mr. Fortney relied, in part, upon administratively-estimated market prices developed by Staff witness Johnson. Mr. Fortney did not prepare any analysis to consider the ESP versus the MRO result specifically for CSP or OP.⁷⁰ Mr. Fortney overlooked the additional costs over the term of the Stipulation ESP associated with the DIR (\$366 million), the gridSMART Rider (\$28 million specific to CSP), and the Enhanced Service Reliability Rider (\$130 million).⁷¹ Mr. Fortney also omitted (without explanation) the final seventeen months of the Stipulation ESP in his ESP versus MRO

⁶⁷ Tr. Vol. XIII at 2323-24 (Cross-examination of Laura Thomas).

⁶⁸ Cos. Ex. 23 at 10.

⁶⁹ IEU-Ohio Ex. 9A at 43-44.

⁷⁰ Tr. Vol. X at 1741 (Cross-examination of Robert Fortney).

⁷¹ IEU-Ohio Ex. 9A at 45.

analysis.⁷² Because Mr. Fortney failed to model the final seventeen months of the Stipulation ESP term in his ESP versus MRO analysis, his analysis is likewise fatally defective and cannot be relied upon by the Commission.

3. The ESP non-price and qualitative benefits claimed by the Companies and Staff do not exist or are entirely speculative.

Recognizing the Stipulation ESP failed the ESP versus MRO test, both the Companies and Staff turned to alleged non-price or qualitative benefits they claimed may result from the Stipulation ESP. The Companies' witness Allen testified the additional non-price benefits resulting from the Stipulation ESP would have a net present value of \$880 million, consisting of \$108 million in ESP non-price benefit for non-shopping customers, \$856 million value of discounted capacity to CRES suppliers, \$104 million in reduced PIRR carrying costs,⁷³ and \$27 million associated with the Partnership with Ohio and Ohio Growth Fund Initiatives.⁷⁴

In his effort to make the proposed ESP look better than it is, he attributed benefits to the Stipulation from the above market capacity charge by assuming that the Companies would have been successful in securing approval for a \$355 per megawatt-day capacity charge.⁷⁵ As Mr. Murray testified, however, customers and their CRES suppliers currently have access to capacity priced at RPM. Thus, taking away rights

⁷² Mr. Murray provided un rebutted testimony demonstrating that simply correcting the omission of the last year of Mr. Fortney's analysis and ignoring the other errors in his assumptions resulted in the ESP failing the MRO price comparison. IEU-Ohio Ex. 9A at 44-45.

⁷³ During his cross-examination, Mr. Allen acknowledged that the benefits associated with reduced carrying charges did not reflect the lower phase-in balance that will result from the Commission's remand order in Case Nos. 08-917-EL-SSO, *et al.* Tr. Vol. III at 425-430 (Cross-examination of William Allen).

⁷⁴ Cos. Ex. 4, Ex. WAA-6.

⁷⁵ Tr. Vol. II at 441-49 (Cross-examination of William Allen).

that currently exist and attempting to classify the action as a customer benefit is not logical or reasonable.⁷⁶ Staff witness Fortney likewise testified the presumed benefit was not meaningful and therefore not relevant in the ESP versus MRO comparison.⁷⁷

The majority of the other alleged benefits asserted by Mr. Allen are associated with the Stipulation's use of a debt-based carrying charge to amortize the phase-in deferral. It is a long-standing Commission policy that the carrying costs allowed when regulatory assets are being amortized should be based on no more than a long-term cost of debt.⁷⁸ Thus, Mr. Allen's claim associated with the reduction in carrying costs unreasonably assumes that the Commission would violate long-standing precedent but for the Stipulation.

Mr. Fortney testified that the Stipulation ESP has two other attributes that he believed would result in additional qualitative benefits that are difficult, if not impossible, to economically value.⁷⁹ According to Mr. Fortney, those attributes are the Companies' agreement to move to a CBP for SSO load in 2015 and the possible construction of a natural gas-fired generating facility (MR6).⁸⁰ However, Mr. Fortney conceded there are conditions precedent to a competitive bid in 2015 such that the competitive bid may not

⁷⁶ IEU-Ohio Ex. 9A at 48.

⁷⁷ Tr. Vol. X at 1707-08 (Cross-examination of Robert Fortney). Staff witness Choueiki testified that the appropriate capacity price to charge all CRES suppliers would be equal to the RPM price. See Staff Ex. 2.

⁷⁸ Where the Commission authorizes the creation of a regulatory asset including carrying charges, such charges are typically based on the utility's cost of long-term debt. *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Authority to Modify Their Accounting Procedure for Certain Storm-Related Services Restoration Costs*, Case No. 08-1301-EL-AAM, Finding and Order at 3 (Dec. 19, 2008).

⁷⁹ Tr. Vol. X at 1751-52 (Cross-examination of Robert Fortney).

⁸⁰ *Id.* at 1752 (Cross-examination of Robert Fortney).

occur,⁸¹ and the Stipulation does not require AEP's next ESP to include a CBP.⁸² Mr. Fortney also conceded that the construction of MR6 would have to satisfy other statutory requirements and that it is unclear when or if those conditions would ever be met.⁸³

Taken together, the Companies and the Signatory Parties did not demonstrate that the proposed ESP is more favorable, in the aggregate, than an MRO. On the mandatory price test, the MRO is superior; no witness claims otherwise. The claimed benefits of the capacity charge provisions and carrying charges on the deferrals do not exist. Nothing in this record supports a finding that the proposed ESP is statutorily permitted or benefits consumers and the public interest.

B. Generation Rate Structure

The Stipulation recommends that the Commission approve the Companies' proposed redesign of generation rates, in which demand-based generation charges would be eliminated for larger customers. It would establish a Market Transition Rider ("MTR") as a non-bypassable charge to reduce the impact of the move to the so-called market-based rates, but modify the levels from the Companies' original Application.⁸⁴ The Stipulation further provides that the MTR during 2012 is not revenue neutral;

⁸¹ *Id.* at 1762 (Cross-examination of Robert Fortney).

⁸² IEU-Ohio Ex. 9A at 7-8. Exelon witness Joseph Dominguez also conceded during his cross-examination that the Stipulation would not require a CBP for energy in the Companies' next ESP. Tr. Vol. VI at 1052 (Cross-examination of Joseph Dominquez).

⁸³ Tr. Vol. X at 1762-1763 (Cross-examination of Robert Fortney).

⁸⁴ Stipulation at 4-6.

instead it is designed to authorize up to \$24 million in additional revenue.⁸⁵ The Stipulation also introduces a Load Factor Provision (“LFP”) for GS2, GS3, and GS4 customers that appears designed to “fix” some of the problems created by the elimination of demand-based charges for larger customers, as a result of the Stipulation starting with the Companies’ proposal.⁸⁶ As described by the Companies, the proposed generation rate structure results in significant interclass shifts in revenue responsibility.⁸⁷ The rationale for these shifts is to make the rates more market-like.⁸⁸ In attempting to create these more “market-like” rates, the Companies used an administratively-constructed set of rates that were based in part on the blended capacity price the Stipulation illegally and unreasonably proposes.⁸⁹ The result of this exercise, however, would be illegal and unreasonable changes in rate design and revenue responsibility.

First, the claim that the Stipulation’s proposed rate structure and revenue distribution shares some rational connection to market or cost is not supported by the record in this case. As Mr. Murray testified, the rates resulting from the Companies’ approach fail to consistently trend seasonally or by time of day as market-based rates do.⁹⁰ The Companies provide no legitimate response to this evidence, but instead

⁸⁵ “The MTR is designed to produce a net charge of \$6 million quarterly until the end of 2012 or until securitization is completed, whichever is earlier, at which time the MTR is designed to produce a net charge of \$0 quarterly. Any over/under recovery will be reflected in the quarterly adjustment.” *Id.* at 5-6.

⁸⁶ *Id.* at 4-5.

⁸⁷ IEU-Ohio Ex. 9A at 19-20.

⁸⁸ Cos. Ex. 2 at 9.

⁸⁹ IEU-Ohio Ex. 9A at 19-20.

⁹⁰ *Id.* at 20-21.

improperly rely on rates established by a stipulation that created the FirstEnergy CBP to argue that proposed rates follow the same general structure resulting from the FirstEnergy auctions.⁹¹ The Companies do not suggest that the rates bear a relationship to costs, and in fact the resulting rates “defy any cost-based explanation.”⁹² The Staff also initially rejected the proposed changes to revenue distribution and rate design because a complete overhaul was not necessary, if at all, until the Companies were at actual market prices.⁹³

The more likely explanation for the so-called market based rates is that the rate design is an element in OP’s and CSP’s attempt to restrict choice by customers. As Dr. Lesser in direct testimony⁹⁴ and Ms. Ringenbach on cross-examination⁹⁵ noted, the design of the proposed rates would likely foreclose competition by lowering rates for those customers more likely to shop and raising rates for those less likely to shop. Ms. Ringenbach acknowledged that she believed that the Companies’ rate approach

⁹¹ The only response offered by the Companies is testimony by Mr. Roush that the resulting rates are similar to those resulting from the FirstEnergy auctions. Cos. Ex. 22 at 3. Mr. Roush, on cross-examination, offered that he was not relying on the stipulation in the FirstEnergy case that created the basis for the rates, but was relying on the published tariff rates that resulted from the stipulated ESP. Tr. Vol. XIII at 2308. Reliance on the rates resulting from the FirstEnergy stipulated ESP, however, is improper: the Stipulation cannot be used for precedent in any other matter. Tr. Vol. XIII at 2061.

⁹² FES Ex. 2 at 39; Tr. Vol. IV at 535 (Cross-examination of Teresa Ringenbach). As Dr. Lesser demonstrated, part of the problem with the Companies’ approach is that it is substantially driven by the value used to price capacity. The result is that as capacity numbers are substituted the rate relationships change. FES Ex. 2 at 40. The sensitivity of the relationships to changes in capacity prices is heightened when a non-market-based capacity price is used as is the case presented by the Stipulation. The results are tied to neither a market-based nor cost-based capacity charge.

⁹³ Tr. Vol. X at 1715.

⁹⁴ FES Ex. 2 at 39.

⁹⁵ Tr. Vol. IV at 532-34, 535, and 539 (Cross-examination of Teresa Ringenbach).

was part of a larger pattern to discourage shopping⁹⁶ and concluded that Senate Bill 221 would not support the rate approach the Companies were proposing.⁹⁷

Because of the negative effects on shopping, the proposed revenue distribution and rate design changes violate the state's policy to promote customer choice. The policy of the state is to take steps to encourage diversity of suppliers and supply "by giving consumers effective choices over the selection of those supplies."⁹⁸ Instead of promoting competition, the proposed rates would forestall competition relative to the status quo.

The Stipulation's proposal to mitigate the damage caused by the proposed revenue distribution and rate design through the MTR presents its own difficulties. As noted above, the proposed MTR is a non-bypassable generation-related⁹⁹ rider that rebalances some of the revenue shifts caused by the application of the proposed revenue distribution and rate design. As Dr. Lesser explained, the MTR is apparently designed to reduce the rate shock that is produced by other aspects of the Stipulation.¹⁰⁰ Yet, it also generates as much as \$24 million in additional revenue without any cost justification. Apart from the nonsensical logic of introducing the MTR to soften rate increases for which no justification has been provided, other provisions in the Stipulation propose to impose economic barriers to shopping thereby preventing

⁹⁶ *Id.* at 538 (Cross-examination of Teresa Ringenbach).

⁹⁷ *Id.* at 536 (Cross-examination of Teresa Ringenbach).

⁹⁸ Section 4928.02(C), Revised Code.

⁹⁹ Tr. Vol. VI at 967 (Cross-examination of David Fein) and 1039 (Cross-examination of Joseph Dominquez).

¹⁰⁰ FES Ex. 2 at 42.

customers from accessing the market which the proposed rates are claimed to mimic. If proposed rates were really market-based, the MTR accompanied by the shopping limits operate to distort competitive purchasing decisions.¹⁰¹ The fact that the rider is proposed to be non-bypassable adds to the potential distortion while inhibiting “customer choice”.

Further, the generation-related MTR standing alone has no valid basis in law. It is a non-bypassable rider; all customers will pay the charge regardless of whether they are shopping or SSO customers. As a result, the MTR operates effectively as a distribution charge. The result is that generation-related charges are being collected as if they were distribution or transmission charges, a violation of state policy.¹⁰²

Finally, the MTR is not allowable as a charge under Section 4928.143(B)(2), Revised Code. The recent Supreme Court decision concerning the Companies’ ESP approved in 2009 has made clear that only those riders that are permitted under that section may be authorized as a part of the ESP.¹⁰³ The Companies are not seeking a non-bypassable rider under those provisions (Sections 4928.143(B)(2)(b) and (c), Revised Code) that specifically provide for non-bypassable riders. The only other provision that they may point to is subdivision (B)(2)(d), but that provision requires some showing that the rider will have the effect of providing stability or certainty in the

¹⁰¹ *Id.* at 43; Tr. Vol. IV at 553 and 562 (Cross-examination of Teresa Ringenbach).

¹⁰² *Ohio Consumers’ Counsel v. Public Utilities Commission of Ohio*, 114 Ohio St. 3d 340 (2007) (unbundling is the cornerstone of electric deregulation begun with Senate Bill 3 (“SB 3”).)

¹⁰³ *In re Application of Columbus S. Power Co.*, 128 Ohio St.3d 512 (2011).

provision of retail electric service. There is no evidence in the record that supports any finding that the MTR would have that result.¹⁰⁴

In summary, the rate design and revenue distribution proposed by the Stipulation are irrational and inconsistent with “customer choice.” It shifts revenue responsibility between and within customer classes and creates rates that are disconnected from any cost or market-based justification. The “fixes” provided by the MTR actually increase the Companies’ revenue with no cost justification and further distort the so-called market basis for the rates. If customers had a choice of electric service providers, these charges might be less objectionable because customers could choose to avoid the unreasonable (and illegal) rates.¹⁰⁵ The Stipulation, however, proposes to stifle the amount of access customers have to suppliers offering real market-based rates. The proposal to redesign the rate structure and shift revenue responsibility thus fails to satisfy state policy requirements or benefit customers and should be rejected.

C. Rate Increases

The Stipulation proposes arbitrary automatic increases in the base generation rates raising the average rate to 2.45¢/kWh in 2012, 2.57¢/kWh in 2013, and 2.72¢/kWh in 2014 and the first five months of 2015. The Stipulation further provides that the rate increases are to be implemented pursuant to Section 4928.143(B)(2)(d), Revised

¹⁰⁴ The Stipulation states, “The MTR Rider is designed to provide rate certainty and stabilized pricing during the transition to deregulation of generation service pricing.” Stipulation at 5. That statement does not address the specific requirements of the statute. See Section 4928.143(B)(2)(d), Revised Code. Even if the statement did address the requirements, the Stipulation is not evidence. Thus, the assertion in the Stipulation does not provide any basis for the Commission to find that the rider may be approved under Section 4928.143(B)(2)(d), Revised Code.

¹⁰⁵ A representative of the CRES Signatory Parties indicated that there would be no need for an MTR if customers had the choice to move to a CRES supplier. Tr. Vol. IV at 562 (Cross-examination of Teresa Ringenbach).

Code.¹⁰⁶ However, there is no justification (based on increased costs or otherwise) for the proposed increases. These proposed increases without any cost justification violate well understood Commission policy, especially in light of the fact that the Stipulation proposes to significantly limit customers' ability to shop.

"It is the policy of this state to do the following throughout this state: (A) Ensure the availability to consumers of adequate, reliable, safe, efficient, nondiscriminatory, and reasonably priced retail electric service."¹⁰⁷ In assuring that retail electric service is reasonably priced, the General Assembly has provided that an EDU seeking to implement an ESP must demonstrate that in the aggregate the ESP is more favorable than an MRO.¹⁰⁸ As demonstrated above, the ESP proposed by the Stipulation fails to satisfy that test. As a starting point, therefore, it is apparent that the proposed rates will fail to satisfy State policy to ensure that rates are "reasonably priced."

Furthermore, the annual rate increases lack any cost justification. As indicated by the Companies' rate witness, there is no cost basis for the increase.¹⁰⁹ The only justification offered for the rate increases is that they were agreed to and are designed to better replicate market rates. (The latter argument cannot serve to justify rate increases and is a separate basis for rejecting the Stipulation discussed in the previous section.)

¹⁰⁶ Stipulation at 7.

¹⁰⁷ Section 4928.02(A), Revised Code.

¹⁰⁸ Section 4928.143(C), Revised Code.

¹⁰⁹ Tr. Vol. I at 113-14 (Cross-examination of David Roush).

The Staff, itself, has indicated that more justification for these proposed rate increases is necessary. In response to cross-examination, Mr. Fortney testified:

Q. Now, in your testimony filed [August 4, 2011] with respect to the ESP proposed by the company you also disagreed with the company's proposal to increase its generation rate, correct?

A. Correct.

Q. And the premise of your disagreement was that there was no cost-based rationale to the company's proposal, correct?

A. That was my initial testimony, yes.

Q. And because there was no cost-based rationale you testified that the staff had no reason to believe that such an increase in revenue was warranted at that time; is that correct?

A. I don't know. I assume you're reading from my initial testimony so yes.

Q. That is a correct assumption. Now, under the proposed stipulation there are increases in generation rates for each year of the years 2012 through 2015; are there not?

A. There are proposed increases in the base generation rates, but those base generation rates no longer represent what they initially did in the application.

Q. And these generation rate increases are not based on cost, are they?

A. Not to my knowledge.¹¹⁰

As Mr. Fortney testified, the Commission has not approved non-cost based increases.

Q. Can you identify, Mr. Fortney, any specific examples of Commission practice with respect to ESPs where the PUCO has allowed noncost-based elements or provisions in an electric security plan?

A. And, again, are we talking about distribution? Was that part of the question?

Q. Of an—an electric security plan of an electric utility.

¹¹⁰ Tr. Vol. X at 1716-17 (Cross-examination of Robert Fortney).

A. Not that I'm aware of. There have been several approvals of riders, but all of them have some cost-based mechanism for adjustment.¹¹¹

With regard to the Companies, Mr. Fortney's testimony reflects the Commission's position in the Companies' first ESP case. In that case, the Companies sought annual automatic increases in the base generation rates. The Commission rejected non-cost based increases because "the record is void of sufficient support to rationalize automatic, annual generation increases that are not cost-based, but that are significant, equaling approximately \$87 million for CSP and \$262 million for OP."¹¹²

Additionally, the Companies have failed to provide any demonstration that the rates satisfy state policy that rates be reasonable. The Companies have made no attempt to establish a cost basis or other basis for either the increase or the resulting level of rates and revenue. Under these circumstances, the Companies have failed to provide any basis for the Commission to determine, as it is required to do, that the rates are "reasonably priced." When this deficiency is added to the fact that the rates do not satisfy the ESP versus MRO test, it is readily apparent that the resulting rate increases cannot satisfy the requirements for approval of the proposed rates under either the statutory requirements or Commission policy.

D. Shopping Limits

Section IV.2 of the Stipulation addressed capacity charges applicable to CRES suppliers serving customers within the Companies' service areas. The Stipulation

¹¹¹ *Id.* at 1719 (Cross-examination of Robert Fortney).

¹¹² *In the Matter of the Application of Columbus Southern Power Company for Approval of an Electric Security Plan; an Amendment to its Corporate Separation Plan; and the Sale or Transfer of Certain Generating Assets*, Case No. 08-917-EL-SSO, Opinion and Order at 30 (Mar. 18, 2009) (citations omitted).

proposes the creation of a two-tiered system of capacity charges and limitations on the availability of the lower-priced capacity to CRES suppliers through predetermined set-asides or caps on shopping. Because the proposals violate several state policy goals, the Commission should reject or substantially amend this part of the Stipulation.

1. The two-tiered capacity price frustrates customer choice.

Since the adoption of SB 3, the state has pursued a policy of competition in the pricing and delivery of retail electric generation service. It is the policy of the state to “[e]nsure 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” and “[e]nsure diversity of electricity supplies and suppliers, by giving consumers effective choices over the selection of those supplies and suppliers.”¹¹³ The Companies have taken a position since the filing of the Application that they would seek to limit customer choice. In agreeing to the two-tiered pricing of capacity, the Signatory Parties substantially assisted the Companies in attaining their goal.

The Companies have made no secret of the fact that their goal through this ESP Application is to frustrate competition with their SSO. Michael Morris, the Chief Executive Officer of AEP, the parent of OP and CSP, stated soon after the ESP Applications were filed that he expected the Companies to be better able to retain customers under the new ESP.¹¹⁴ The filing of the Stipulation triggered another corporate declaration that the effect of the Stipulation would allow the Companies to

¹¹³ Sections 4928.02(B) and (C), Revised Code.

¹¹⁴ FES Ex. 1, Ex. TCB-7.

limit customer choice. Richard Munczinski, speaking on behalf of the Companies the day the Stipulation was filed with the Commission, was very clear that shopping under the Stipulation's two-tier capacity pricing scheme would be constrained:

What happens is those customers that get the discount as Brian [Tierny] mentioned are allowed—are priced out at the RPM prices. So the \$100, the \$16, and I think the \$26 going forward. Over those percentages, if you want to shop, you pay the full cost of \$255 per megawatt day. So the thought and the theory is that the shopping will be constrained to the RPM price.¹¹⁵

He continued, “So basically, we should see no more shopping than the 20%, 30%, 40% levels that are included in the stipulation.”¹¹⁶ Thus, it is clear that the Companies are seeking to use the Stipulation's two-tiered capacity pricing provisions with the set asides to limit the ability of customers to exercise their right to obtain competitive retail electric service from a supplier other than the Companies.

The Companies' ability to limit customer choice is practically guaranteed because of the way they will be able to control competitive retail electric service pricing under the Stipulation. Under the current Fixed Resource Requirements (“FRR”) election by the Companies, the Companies are required to assure that they will satisfy their total system capacity requirements to PJM.¹¹⁷ As a result, CRES suppliers serving retail customers in the Companies' service areas must rely upon capacity from OP or CSP until May 2015.

¹¹⁵ *Id.*, Ex. TCB-8.

¹¹⁶ *Id.*, Ex. TCB-9.

¹¹⁷ FES Ex. 2 at 8; Tr. Vol. IV at 541-42 (Cross-examination of Teresa Ringenbach).

Since CRES suppliers obtain capacity from the Companies, the Stipulation's proposed \$255 charge means that CRES suppliers will not be able to offer a competitively priced product to OP or CSP customers. Apart from an attempt by the Companies to demonstrate that there was some headroom for CRES, all reasonable projections in the record of this case and discussed below indicate that the two-tiered capacity pricing will limit customer choice to those customers who are successful in securing capacity under the RPM set-aside amounts.

As Mr. Schnitzer demonstrated, there are savings opportunities available to customers when RPM prices are available to CRES suppliers during the term of the proposed ESP through sometime in 2014. When CRES capacity is priced at \$255 per megawatt-day, however, there is no savings opportunity until sometime in 2014, and thereafter the amount of room to price competitive offers is minimal.¹¹⁸ Thus, setting the capacity price at \$255 per megawatt-day prevents shopping and customers are stuck with the unjustified and higher ESP prices in the Stipulation. As Mr. Schnitzer concluded, "[O]nce AEP Ohio no longer has to provide capacity to CRES suppliers at RPM market prices, the Stipulation effectively shuts down the opportunity for customers to shop by making it very difficult for customers to shop for price savings. Thus, the higher base generation rates and other 'bypassable charges' included in the Stipulation become non-bypassable in practical terms."¹¹⁹ Mr. Murray agreed. After describing the structure of capacity rates and set-asides proposed by the Stipulation, he concluded,

¹¹⁸ FES Ex. 3 at 34-36.

¹¹⁹ *Id.* at 36.

“This structure will effectively block shopping at the amounts that have access to market-based capacity price.”¹²⁰

The CRES Signatory Parties essentially agree with the analysis provided by Mr. Schnitzer and Mr. Murray. Ms. Ringenbach, on behalf of the Retail Energy Supply Association (“RESA”), for example, stated that increased capacity costs in the range of one and a half to two and a half times RPM would be significant and have the effect of deterring offers.¹²¹ Similarly, David Fein, testifying on behalf of Constellation NewEnergy, stated that an increase of two hundred percent in capacity prices over RPM prices, all else being equal, would adversely affect shopping.¹²²

Only the Companies offered testimony (in rebuttal) suggesting that there was headroom for competitive offers available to CRES suppliers paying \$255 per megawatt-day for capacity. To advance this contrarian view, Mr. Allen testified that he had taken the administratively-determined and defective benchmark price of Ms. Thomas and removed two components of that price (the Transaction Risk Adder and the Retail Administration costs) to come up with some headroom.¹²³ As demonstrated in the confidential version of his testimony, the amount of headroom is miniscule and in one year actually negative.¹²⁴ Additionally, his analysis simply does not make any sense.

¹²⁰ IEU-Ohio Ex. 9A at 17.

¹²¹ Tr. Vol. IV at 542-43 (Cross-examination of Teresa Ringenbach).

¹²² *Id.* at 971 (Cross-examination of David Fein).

¹²³ Cos. Ex. 20A at 7-9.

¹²⁴ *Id.* at 8.

The benchmark price administratively determined by Ms. Thomas was presented as the “all-in” requirements for a competitive price;¹²⁵ there was no proof that CRES suppliers would or could forgo a part of the price relied upon by Ms. Thomas and then arbitrarily reduced by Mr. Allen to find headroom.¹²⁶

Thus, the Companies, the opposing parties, and the CRES suppliers supporting the Stipulation all conclude that the provisions regarding capacity pricing would have the effect of blocking customer access to CRES suppliers offering better prices, and that blocking translates into real losses for customers. Just as the future competitive price is projected by the Companies to exceed the administratively-set ESP price, the Stipulation provides that all default service will be priced by an auction.¹²⁷ As Mr. Murray testified, “Most customers will be blocked from shopping at a time when ESP rates are above competitive retail price offers. Then, once market rates are forecasted to rise above the Stipulation ESP’s rates, the Stipulation will set default generation supply prices 100% on a CBP. For customers, the Stipulation provides a lose-lose proposition; customers pay SSO prices based upon the Stipulation or the CBP, whichever is higher.”¹²⁸ Under the circumstances described by Mr. Murray, the

¹²⁵ Cos. Ex. 5 at 4; Tr. Vol. XII at 2105 (Cross-examination of William Allen).

¹²⁶ Mr. Allen also suggested that CRES suppliers would either sell at a loss or below market rates. Without any basis in fact, he asserted that CRES suppliers will enter into contracts for substantial periods during part of which the CRES suppliers will suffer losses. Cos. Ex. 20A at 8-9. Alternatively, he assumed CRES suppliers will sell in an economically irrational manner at below market price that even he found difficult to explain. Tr. Vol. XII at 2107-09. Rather than relying on these contrived explanations, the Commission would do better by accepting the word of the Companies and signatory CRES suppliers that the higher capacity charges will limit consumer choice.

¹²⁷ IEU-Ohio Ex. 9A at 18.

¹²⁸ *Id.* at 18-19.

Stipulation proposes a result that violates an important regulatory principle or practice.¹²⁹

As noted previously, the state energy policy includes a goal of encouraging customer choice and reasonably priced retail electric service. Under the Stipulation, however, large numbers of customers are locked into above-market ESP rates.¹³⁰ The blocking of customer choice, furthermore, comes with an additional cost that customers will face because the Stipulation proposes that default service prices in the last year of the ESP be set by a CBP that can be expected to result in prices higher than the administratively-determined ESP price. Under these circumstances, the shopping limits in the Stipulation cannot be said to advance the public interest or generate lawful or reasonable rates.

2. The two-tiered capacity price imposes an unreasonable and discriminatory condition on the resale of electric service.

The state energy policy and its implementation through various sections in Chapter 4928 requires the Commission to ensure that rates are not discriminatory. Section 4928.02(A), Revised Code, provides that it is the State's policy to "[e]nsure the availability to consumers of ... nondiscriminatory ... retail electric service." Section 4928.40(D), Revised Code, states that "no electric utility in this state shall prohibit the resale of electric generation service or impose unreasonable or discriminatory conditions or limitations on the resale of electric generation service." Thus, the policy of

¹²⁹ *Id.* at 19.

¹³⁰ Section 4928.02, Revised Code.

the State to ensure non-discrimination and comparability in pricing applies whether one is addressing retail or wholesale transactions.

In the case of capacity, the Companies' witness Nelson explained the Companies' view that the resale of electricity involves a wholesale transaction, or sale for resale.¹³¹ By the terms of the Stipulation, some capacity will be charged at the RPM price; the balance will be priced at \$255 per megawatt-day.¹³² The Signatory Parties uniformly testified that the \$255 rate is not based on cost,¹³³ and it clearly is not based on market. As the testimony also demonstrated, whether a CRES supplier is charged the RPM price or \$255 depends on where and when its customer stands in the line created by the Stipulation and Appendix C's five classes of customers.¹³⁴ In all other respects, the products are identical.¹³⁵

Despite the statutory prohibition in Section 4928.40(D), Revised Code, the Stipulation recommends a non-comparable and discriminatory¹³⁶ capacity charge structure with CRES suppliers providing megawatt hours above the "caps" subjected to the \$255 per megawatt-day amount and the megawatt hours supplied below the "caps"

¹³¹ Tr. Vol. XII at 2184-85, 2230-31 (Cross-examination of Philip Nelson).

¹³² Stipulation at 20-21.

¹³³ Tr. Vol. II at 191 (Cross-examination of Kelly Pearce); Tr. Vol. V at 737 (Cross-examination of Philip Nelson); Tr. Vol. V at 810, 845 (Cross-examination of Joseph Hamrock).

¹³⁴ Tr. Vol. VI at 973 (Cross-examination of David Fein).

¹³⁵ *Id.* at 972 (Cross-examination of David Fein).

¹³⁶ The definition of "standard service offer" in Rule 4901:1-35-01(L), OAC, highlights the importance of the role of the nondiscriminatory and comparable requirements that are imposed by Chapter 4928, Revised Code: "'Standard service offer' means an electric utility offer to provide consumers, on a comparable and nondiscriminatory basis within its certified territory, all competitive retail electric services necessary to maintain essential electric service to consumers, including a firm supply of electric generation service."

paying the Commission-approved and current market-based capacity charge arising from PJM's wholesale auction process. The difference in pricing cannot be explained on any cost or market-based rationale. Instead, it is designed to limit the opportunity of customers to act on their preferences.

Despite the state policy contained in Section 4928.02(A), Revised Code, neither the Companies nor any party supporting the Stipulation offered any evidence to demonstrate that the bifurcated capacity charge structure recommended by the Stipulation can be lawfully authorized. As Mr. Fein offered during cross-examination:

Q. You also believe that the Commission should avoid discriminatory pricing policies; do you not?

A. I do.

Q. So similarly situated customers receiving the same service shouldn't be required to pay different prices for that service, correct?

A. That's correct.¹³⁷

Yet, under the Stipulation's capacity charge proposal, discrimination is guaranteed: similarly situated customers and suppliers will see two different prices based on nothing more than whether they took or signed up for competitive retail electric service soon enough. Given the state's policies that strongly support competition and comparable and non-discriminatory pricing of wholesale and retail electric service, the Stipulation effects a result that the Commission cannot authorize.

¹³⁷ Tr. Vol. IV at 971 (Cross-examination of David Fein).

E. Generation Resource Rider (“GRR”)

1. The GRR is not justified.

The Stipulation, if approved, would authorize the Companies to illegally establish a non-bypassable GRR as a “placeholder.”¹³⁸ During the term of the ESP, the Stipulation would allow the Companies to pursue recovery through the GRR of the costs associated with the Turning Point Solar Project and MR6 project, a new combined cycle plant to replace MR5 after it is retired.¹³⁹ The Commission should reject the GRR because the statutory requirements of Section 4928.143(B)(2)(c), Revised Code, that must be established to authorize a non-bypassable charge, have not been satisfied. Additionally, the GRR is simply a placeholder, and such placeholder riders are not statutorily authorized as part of an ESP.

The Companies have not identified any statutory basis that authorizes the inclusion of “placeholder riders” as part of an ESP. Section 4928.143(B)(2), Revised Code, states that “[t]he [electric security] plan may provide for or include, without limitation, any of the following,” and then lists nine provisions. Only one of the nine provisions mentions the possibility of a non-bypassable charge for a completed new generation facility. Section 4928.43(B)(2)(c), Revised Code, provides an ESP may include:

The establishment of a nonbypassable surcharge for the life of an electric generating facility that is owned or operated by the electric distribution utility, was sourced through a competitive bid process subject to any such rules as the commission adopts under division (B)(2)(b) of this section, and is newly used and useful on or after January 1, 2009, which surcharge shall cover all costs of the utility specified in the application, excluding

¹³⁸ Tr. Vol. IV at 569-70, 598 (Cross-examination of Laura Thomas).

¹³⁹ Stipulation at 6.

costs recovered through a surcharge under division (B)(2)(b) of this section. However, no surcharge shall be authorized unless the commission first determines in the proceeding that there is need for the facility based on resource planning projections submitted by the electric distribution utility. Additionally, if a surcharge is authorized for a facility pursuant to plan approval under division (C) of this section and as a condition of the continuation of the surcharge, the electric distribution utility shall dedicate to Ohio consumers the capacity and energy and the rate associated with the cost of that facility. Before the commission authorizes any surcharge pursuant to this division, it may consider, as applicable, the effects of any decommissioning, deratings, and retirements.

As set out above, Section 4928.143(B)(2)(c), Revised Code, includes several specific requirements that must be satisfied before the Commission can authorize a non-bypassable charge. There must be a finding that the generating facility for which a non-bypassable charge is sought was sourced through competitive bids. There must a finding by the Commission in the ESP proceeding that there is a need for the facility based on resource planning projections submitted by the EDU. There must be a finding by the Commission that the capacity, energy and the rate associated with the cost of that facility has been dedicated to Ohio consumers.

In this case, the Companies have made no attempt to justify the rider. When pressed, their witnesses stated that the GRR is a placeholder and pointed to the Stipulation's provision that the recovery under the rider will be the subject of additional Commission proceedings.¹⁴⁰ Thus, the Companies have offered nothing in the way of proof to support the creation of the GRR pursuant to Section 4928.143(B)(2)(c), Revised Code.

¹⁴⁰ Tr. Vol. IV at 598 (Cross-examination of Laura Thomas).

Since the GRR does not satisfy Section 4928.143(B)(2)(c), Revised Code, the only way the Commission could lawfully authorize the GRR would be to alternatively determine that one of the other eight categories of cost recovery under Section 4928.143(B)(2), Revised Code, creates an opportunity for the GRR. There has been no evidence presented in this proceeding that the proposed GRR falls within one of the other eight provisions under Section 4928.143(B)(2), Revised Code. On that point, recent guidance from the Supreme Court is instructive.

On March 18, 2009, the Commission issued its order on the Companies' current ESP.¹⁴¹ On appeal, one of the issues raised by OCC was whether Section 4928.143(B)(2), Revised Code, permitted the Companies to recover certain carrying costs associated with environmental investments. OCC argued that Section 4928.143(B)(2), Revised Code, must be narrowly read and authorizes the inclusion of provisions in an ESP that were listed in the statute. The Court agreed:

By its terms, R.C. 4928.143(B)(2) allows plans to include only “any of the following” provisions. It does not allow plans to include “any provision.” So if a given provision does not fit within one of the categories listed “following” (B)(2), it is not authorized by statute.

. . .

The plain language of the statute controls, and this interpretation leads to a reasonable result.¹⁴²

Including a placeholder rider as part of an ESP requires an assumption that the phrase “without limitation” allows unlisted items, a result contrary to the Supreme

¹⁴¹ *In the Matter of the Application of Columbus Southern Power Company for Approval of an Electric Security Plan; an Amendment to its Corporate Separation Plan; and the Sale or Transfer of Certain Generating Assets*, PUCO Case Nos. 08-917-EL-SSO, *et al.*, Opinion and Order (March 18, 2009).

¹⁴² *In re Application of Columbus S. Power Co.*, 128 Ohio St.3d at 520.

Court's determination. Because none of the other eight categories of costs allows the Commission to approve a placeholder rider, with specific costs to be determined at a later date, there is no statutory basis to approve the GRR.

2. Authorizing the GRR without accounting for the likely cost improperly biases the ESP versus MRO analysis.

As previously discussed, if the GRR is authorized by the Commission, the Commission must account for the likely revenue to be recovered through the GRR as a cost of the ESP for the purpose of conducting the ESP versus MRO test. The failure to do so results in an unreasonable portrayal of the ESP (as compared to the MRO) because the full cost of the ESP would be understated.

As discussed above, although Section 4928.143(B)(2)(c), Revised Code, creates the possibility that an ESP could include a non-bypassable charge for a new generating facility, provided other statutory criteria are met, there is no similar provision in Section 4928.142, Revised Code, that allows such a non-bypassable charge in an MRO. Therefore, in the ESP versus MRO analysis, the likely costs associated with the GRR must be recognized as additional cost of the ESP.

Other than the Companies, the witnesses in this case properly recognized that the Stipulation's GRR creates an ESP cost that must be counted in the ESP versus MRO test. Staff witness Fortney, FES witness Schnitzer and IEU-Ohio witness Murray all testified that it was necessary to adjust the projected ESP price to recognize the additional costs associated with the GRR.¹⁴³ Ms. Thomas incorrectly omits the

¹⁴³ Staff Ex. 4, Attachment A; FES Ex. 4, Ex. MMS-2; IEU-Ohio Ex. 9A, Ex. KMM-11.

additional costs associated with the GRR in her ESP versus MRO analysis.¹⁴⁴ Her error results in an understatement in the costs of the ESP and makes the ESP seem more favorable on paper than it would be once implemented. The Companies' attempt to execute the test without making an allowance for the GRR, therefore, is unreasonable and unlawful.

F. Combined Heat and Power Provisions

Section IV.2.c of the Stipulation requires the Companies to pursue the development of up to 350 megawatt (MW) of customer-sited combined heat and power, waste energy recovery, and distributed energy resources in their service territories, with the costs to be recovered through an "appropriate" rider. Here again, the Stipulation creates a placeholder rider that cannot be lawfully authorized as part of an ESP.¹⁴⁵ The costs of customer-sited combined heat and power, waste energy recovery, and distributed energy resources are not mentioned within any of the nine provisions that may be addressed pursuant to Section 4928.143(B)(2), Revised Code. Additionally, as is the case with the GRR and for all of the same reasons, the failure to attribute likely costs associated with these 350 MW of customer-sited resources unreasonably biases the ESP versus MRO analysis in favor of the ESP proposed in the Stipulation.

G. Distribution Investment Rider

As previously noted, the Supreme Court has clearly stated that an ESP cannot include provisions that are not expressly authorized by statute.¹⁴⁶ Despite this

¹⁴⁴ See, for example, Cos. Ex. 5, Ex. LJT-3, page 1 of 1.

¹⁴⁵ See discussion, *supra*.

¹⁴⁶ *In re Application of Columbus Southern Power Co.*, 128 Ohio St.3d 512 (2011).

requirement, neither the Stipulation nor the prefiled direct testimony of the Companies or the other Signatory Parties explained which provision of Section 4928.143(B)(2), Revised Code, authorized the Commission to establish the DIR. In rebuttal testimony, the Companies and Staff offered testimony suggesting that Sections 4928.143(B)(2)(d) and (h), Revised Code, supported inclusion of the DIR. The Commission must reject the Companies and Staff's arguments because Subsection (d) does not authorize the DIR and the requirements of Subsection (h) have not been satisfied.

Section 4928.143(B)(2)(d), Revised Code, requires that the Companies demonstrate that charges would have the effect of stabilizing or providing certainty regarding retail electric service. The Companies, however, have provided no evidence to demonstrate that the DIR will satisfy those requirements. As discussed below, the Companies could make no investment or improvement in distribution service and still collect the DIR. Thus, the Commission cannot authorize the DIR pursuant to Section 4928.143(B)(2)(d), Revised Code.

Although charges specific to distribution may be authorized by the Commission under Section 4928.143(B)(2)(h), Revised Code, if detailed requirements are satisfied, the Companies and Signatory Parties failed to provide any evidence that supported the lawful authorization of the DIR under that section. For example, the Companies have not undertaken a reliability study in this proceeding, and the Staff has not independently undertaken that analysis. Cross-examination of the only Staff witness (Mr. Hecker) to testify regarding the distribution system in the Signatory Parties' direct case also revealed that Staff has not analyzed the reliability of the distribution system for this proceeding:

Q. Did you perform any analysis regarding the current [re]liability [sic] of AEP Ohio's distribution system?

A. No, I did not.¹⁴⁷

Staff witness Fortney also stated that Doris McCarter, the other Staff member with responsibility regarding the DIR, had not analyzed the reliability of the distribution system.¹⁴⁸ As noted by IEU-Ohio witness Bowser, “the Stipulation is unaccompanied by any examination of reliability of the utility’s distribution system or the other requirements in Section 4928.143(B)(2)(h), Revised Code.”¹⁴⁹

In an apparent attempt to remedy the fact that their direct case failed to address the statutory requirements of Section 4928.143(B)(2)(h), Revised Code, the Companies and Staff submitted rebuttal testimony that referenced reliability standards that were established in a 2009 proceeding pursuant to a stipulation.¹⁵⁰ Even assuming that it is proper to violate the terms that restrict the use of the Stipulation in the *2009 Reliability Standards Proceeding* as precedent,¹⁵¹ the statutory requirements remain unsatisfied. Staff witness Baker (in the Staff’s rebuttal testimony) admitted that he had not analyzed the impact that the DIR would have on the reliability of the distribution system:

¹⁴⁷ Tr. Vol. IX at 1656.

¹⁴⁸ Tr. Vol. X at 1730 (Cross-examination of Robert Fortney).

¹⁴⁹ IEU-Ohio Ex. 8 at 7; see also IEU-Ohio Ex. 8 at 6-7.

¹⁵⁰ *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of Proposed Reliability Standards*, Case No. 09-756-EL-ESS, Opinion and Order (Sept. 8, 2010) (“*2009 Reliability Standards Proceeding*”).

¹⁵¹ The stipulation specifically states that “[e]xcept for purposes of enforcement of the terms of this Stipulation, this Stipulation, the information and data contained therein or attached and any Commission rulings adopting it, shall not be cited as precedent in any future proceeding for or against any Party or the Commission itself.” *2009 Reliability Standards Proceeding*, Case No. 09-756-EL-ESS, Stipulation and Recommendation (July 22, 2010).

Q. Are there any projected improvements to reliability that you are aware of that are tied to the distribution investment rider associated with the stipulation in this proceeding?

A. I'm not aware of any but I only did one brief review of the stipulation. I'm not familiar with it.¹⁵²

The Companies also failed to demonstrate that customers' and the Companies' expectations are aligned with respect to the distribution system for each customer class. The Companies did not present any testimony on this issue in their direct case. The Staff, likewise, did not provide any evidence to demonstrate that customers' and the Companies' expectations are aligned on cross-examination.

Q. Did you perform any assessment of whether customers' expectations and AEP Ohio's expectations are aligned?

A. No, sir.¹⁵³

In rebuttal testimony, the Companies and Staff again attempted to paper over the problems with their legal theory by relying on customer surveys¹⁵⁴ from the *2009 Reliability Standards Proceeding*.¹⁵⁵ The surveys, however, do not demonstrate a majority of customers' expectations are aligned with the Companies' regarding the need

¹⁵² Tr. Vol. XIII at 2377 (Cross-examination of Peter Baker).

¹⁵³ Tr. Vol. IX at 1657 (Cross-examination of Jeffrey Hecker).

¹⁵⁴ Of the 500 residential and 300 commercial customers who participated in the survey, only 16% of residential and 19% of commercial participants anticipated that their reliability expectations would increase over the next five years. Conversely, 77% of residential participants and 79% of commercial participants anticipated that their reliability expectations would stay the same or decrease over the next five years. OCC Ex. 10; Tr. Vol. XII at 2016 (Cross-examination of Joseph Hamrock). Surveys in 2010 yielded similar results. Tr. Vol. XII at 2022-25 (Cross-examination of Joseph Hamrock).

¹⁵⁵ Cos. Ex. 19 at 4 (Hamrock rebuttal); Staff Ex. 5 at 2-5.

for additional investment in distribution facilities.¹⁵⁶ Moreover, the surveys the Companies relied upon did not include any information regarding the expectations of the industrial class.¹⁵⁷ Thus, the statutory requirement was not satisfied as there is insufficient or no information available regarding the expectations of any class of customers.

The failure of proof extended to other areas as well. Rule 4901:1-35-03(C)(9)(g), OAC, specifically requires a detailed description of the infrastructure plan, the benefits that will result, and the costs that will be incurred. Neither the Stipulation nor the testimony offered in support of the Stipulation contains an analysis of the assets that would be replaced, a concrete methodology to target the asset improvement/replacements, any expected improvement to reliability measured by customer outages or power quality indices, or the cost of the program. During cross-examination, Companies' witness Hamrock admitted that the Companies simply do not have specific details:

Q. So you do not know yet what you will be fixing as a result?

A. We know it will be some combination of the types of programs I've already referred to. The exact specific mix of those programs will depend on the results of these analyses.

Q. So you could not give me a projection of cost yet?

¹⁵⁶ Only 20% of residential and 21% of commercial customers reported that their reliability expectations would increase over the next five years. Cos. Ex. 19 at 4 (Hamrock rebuttal); Tr. Vol. XII at 2022-25 (Cross-examination of Joseph Hamrock).

¹⁵⁷ *Id.* See also 2009 Reliability Standards Proceeding, Case No. 09-756-EL-ESS, Stipulation and Recommendation (July 22, 2010).

A. Not a specific projection of cost, no.¹⁵⁸

The Companies have also failed to describe, as required by Rule 4901:1-35-03(C)(9)(g), OAC, how the DIR does not result in double recovery. Section IV.1.n of the Stipulation states that the rider will be based on carrying charges on “post-2000 investment.”¹⁵⁹ In the Companies’ distribution rate cases, however, August 31, 2010 was used as the date certain to value plant-in-service.¹⁶⁰ The date certain includes post-2000 investment that would be recovered through the DIR. Thus, the Stipulation, if approved, will result in double recovery once base distribution rates are approved in Case Nos. 11-351-EL-AIR, *et al.*, and no amount of explanation will prevent that result, absent some Commission-authorized contortion to the base distribution case.¹⁶¹

Apparently recognizing that authorization of the DIR would result in double recovery, Companies’ witness Allen offered an unsupported conclusion: “Any costs recovered through the Companies’ base distribution rates would not be recovered through the DIR.”¹⁶² During cross-examination, Mr. Allen explained that a provision that provided for the identification and exclusion of riders for distribution capital additions prevented double recovery.¹⁶³ Since base distribution rates are not collected through a

¹⁵⁸ Tr. Vol. XII at 1995 (Cross-examination of Joseph Hamrock); Tr. Vol. X at 1724 (Cross-examination of Robert Fortney).

¹⁵⁹ Stipulation at 8.

¹⁶⁰ Tr. Vol. III at 315-317.

¹⁶¹ The Companies have filed testimony in the rate case urging the Commission to consider a revenue credit if the DIR is approved, an explicit admission that the DIR will double recover. Tr. Vol. XII at 2055.

¹⁶² Cos. Ex. 22A at 5.

¹⁶³ Tr. Vol. XII at 2142.

rider, nothing in the Stipulation requires the Companies or the Commission to adjust the DIR to prevent double recovery. Mr. Allen's answer, thus, does not address the double recovery that will likely occur in base distribution rates and the DIR.

Moreover, any recovery under the proposed DIR will be excessive. OP and CSP currently have applications to increase distribution rates pending in Case Nos. 11-351-EL-AIR, *et al.*, and the date certain which has been approved by the Commission for purposes of identifying the rate base valuation is August 31, 2010. The Staff Reports of Investigation ("Staff Report") address the Rider DIR proposal contained in the Companies' ESP Application and contain a recommendation that a plant investment baseline for the year 2000 not be used until the Commission renders a decision in the 11-351-EL-AIR, *et al.* distribution rate case.¹⁶⁴ The Staff Reports also find that CSP's current distribution rates are too high (by between \$2.3 million and \$9.5 million) and that OP's current distribution rates could be increased. On a net and combined basis, the Staff Reports recommend that any distribution rate increase should be between about \$13.7 million and \$29.6 million, based on the net distribution rate base "used and useful" as of August 31, 2010 (the date certain). Based on the findings in the Staff Reports, the DIR rate increases called for by the Stipulation starting at \$86 million in 2012 are clearly excessive, unjust, and unreasonable.¹⁶⁵

Even if the Commission were to approve the DIR, certain other features of the DIR violate regulatory principles. Particularly, the Stipulation includes an excessive carrying cost for the DIR. As provided by the Stipulation, the DIR carrying charges will

¹⁶⁴ IEU-Ohio Ex. 8 at 9 (October 13, 2011).

¹⁶⁵ IEU-Ohio Ex. 8 at 10.

include property taxes, commercial activity tax, associated income taxes, and a return on and of investment; and the rate of return on common equity is proposed to be set arbitrarily at 10.5%.¹⁶⁶ Carrying cost rates, however, should compensate a utility only in accordance with its risks.¹⁶⁷ In this case, the DIR is proposed to be a single-issue non-bypassable rider, and the carrying costs are applied to investments that have already been made. A full carrying charge based on the weighted average cost of capital (“WACC”) is excessive in light of the fact that the DIR reduces the Companies’ financial and business risk below the risks for which a full WACC-based carrying charge would be appropriate.¹⁶⁸ A carrying cost based on the cost of debt would be more commensurate with the Companies’ risk than a carrying cost based on the WACC.¹⁶⁹ Even if an equity component were appropriate, the proposed equity return (10.5%) to be built into the carrying charge rate is too high, based on current cost of capital considerations and the DIR’s lowering of business and financial risks.¹⁷⁰

If the Commission approves a DIR, moreover, it must assure that the carrying cost be properly demonstrated and quantified.¹⁷¹ The Companies, however, have not provided evidence to support the proposed carrying cost.¹⁷² Moreover, it is a long-standing Commission policy that adjustments be made to the investment balances on

¹⁶⁶ Stipulation at 8.

¹⁶⁷ IEU-Ohio Ex. 8 at 7.

¹⁶⁸ *Id.*

¹⁶⁹ *Id.* at 7.

¹⁷⁰ *Id.* at 10-11.

¹⁷¹ *Id.* at 7-8.

¹⁷² *Id.* at 8.

which a utility earns a return to reflect accumulated deferred income taxes (“ADIT”) liabilities or assets.¹⁷³ In the case of the DIR, the Stipulation fails to identify if the adjustment has been made to reduce the investment balance by the ADIT liability.¹⁷⁴

Finally, there is not a demonstrated benefit to customers from an authorization of the DIR. As Staff noted,¹⁷⁵ the Companies do not have to make any investment in new distribution plant, yet they still would be authorized to recover revenue up to the caps. This bizarre result, giving the Companies additional revenue with no commitment to improved quality of service or even additional investment, is unlawful and unreasonable.

H. Pool Modification or Termination Rider

The Commission should reject Section IV.5 of the Stipulation regarding the Pool Modification or Termination Rider inasmuch as the rider is not authorized by statute, violates state policy, and contains no mechanism or oversight to control costs proposed to be recovered through the rider. Further, the Companies failed to include the costs of the rider in the ESP versus MRO comparison test.

As previously noted, the Commission may approve riders if they are provided for under Section 4928.143(B)(2), Revised Code. In regard to the Pool Modification or Termination Rider, the Companies have yet to link this element of the Stipulation to one of the enumerated categories under Section 4928.143(B)(2), Revised Code. In fact,

¹⁷³ *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Authority to Establish a Standard Service Offer Pursuant to Section 4928.143, Revised Code, in the Form of an Electric Security Plan*, Case No. 10-388-EL-SSO, Opinion and Order at 14 (August 25, 2010).

¹⁷⁴ IEU-Ohio Ex. 8 at 8.

¹⁷⁵ Tr. Vol. X at 1754-55 (Cross-examination of Robert Fortney).

there is no provision under Section 4928.143(B)(2), Revised Code, that authorizes this proposed rider. Authorization of the rider, therefore, would be unlawful and unreasonable.

Further, the terms of the rider would lead to unreasonable results. The Stipulation provides that if the Companies incur costs in excess of \$50 million associated with Pool termination or modification they can recover the full amount of their costs, inclusive of the \$50 million threshold amount.¹⁷⁶ At this time, however, the Companies have presented no estimate of what the costs associated with Pool termination or modification will be.¹⁷⁷ To the extent that Pool termination or modification will result in OP or CSP incurring costs associated with the loss of revenue from sales to other pool members, this provision in the Stipulation sets up Ohio customers and not the Companies to pick up the tab without any obvious limit.¹⁷⁸

In any case, the Staff concluded that a placeholder rider for Pool termination costs is premature.¹⁷⁹ If for some unexpressed reason this proceeding is an appropriate place to entertain Pool modification or termination costs, the Companies also erred in excluding the Pool Modification or Termination Rider as a cost under the ESP versus MRO test.¹⁸⁰ Although the Stipulation proposes to establish an initial rate of zero for the Pool Modification or Termination Rider, the Companies would not be able

¹⁷⁶ Stipulation at 25. See Tr. Vol. V at 708 (Cross-examination of Philip Nelson).

¹⁷⁷ Tr. Vol. V at 710 (Cross-examination of Philip Nelson).

¹⁷⁸ IEU-Ohio Ex. 9A at 16.

¹⁷⁹ Tr. Vol. X at 1741 (Cross-examination of Robert Fortney).

¹⁸⁰ IEU-Ohio Ex. 9A at 45-46.

to collect these costs under an MRO. Therefore, the potential costs associated with the rider should have been included in the comparison as a cost of the proposed ESP.

I. Phase-In Recovery Rider (“PIRR”)/Securitization

Section 4928.144, Revised Code, requires that any phase-in of a rate be “just and reasonable.” Under a prior Commission order, OP and CSP were authorized to defer collection of rate increases and recover those deferrals through a phase-in mechanism of the amount subsequently authorized by the Commission. The Stipulation proposes to establish this recovery mechanism through the PIRR. The Signatory Parties also “agree to work in good faith to pass suitable and appropriate legislation to address the matter [securitization for the regulatory assets associated with the PIRR] ... and to support subsequent approvals needed or tariffs required by [the Companies].”¹⁸¹

OP claims it will have accumulated a phase-in deferral amount of \$624 million as of December 31, 2011. CSP customers, however, have already paid off their deferred rate increase balance; thus, there is no CSP deferral to phase-in. Despite the fact that there is no deferral balance for CSP customers, the Stipulation proposes to amortize the deferral associated with OP’s ESP on an “AEP Ohio (combined CSP and OPCo) basis,”¹⁸² even though CSP customers received no benefit from the deferral that would be amortized by the PIRR. Because the proposed PIRR requires CSP customers to pay charges to amortize the phase-in deferral that benefitted OP customers, the

¹⁸¹ Stipulation at 25-26.

¹⁸² *Id.* at 26.

proposed PIRR misaligns cost responsibility and benefits, which is inconsistent with regulatory principles.¹⁸³

The Companies, in rebuttal, sought to circumvent the problems presented by the proposal to charge CSP customers for OP deferrals by pointing to the proposed merger and the Commission's decision to assign costs related to the Monongahela Power purchase to CSP customers.¹⁸⁴ Reliance on the merger, however, does not change the fact that CSP customers have already paid the phase-in deferral amount created by CSP's current ESP and the Stipulation is now proposing to saddle CSP customers, after the fact, with responsibility for additional deferrals for which they received no benefit. Reliance on the *Monongahela* decision, likewise, is unwarranted as that decision predated the adoption of SB 221 which provides the statutory structure for the creation of a phase-in as well as the means by which the phase-in deferral is to be amortized, Section 4928.144, Revised Code.¹⁸⁵ The Companies, thus, have presented no valid basis for adopting the Stipulation's proposed PIRR.

Additionally, the design of the PIRR contained in the Stipulation violates Section 4928.20(I), Revised Code, by requiring customers that are part of governmental aggregation programs to pay the PIRR without a determination that they received any benefit from the phase-in. That section requires that any phase-in deferral charge arising from Section 4928.144, Revised Code, and imposed upon customers within a

¹⁸³ IEU-Ohio Ex. 9A at 21-22.

¹⁸⁴ Cos. Ex. 22 at 7.

¹⁸⁵ Tr. Vol. XIII at 2305 (Cross-examination of David Roush); see also *In the Matter of the Transfer of Monongahela Power Company's Certified Territory in Ohio to the Columbus Southern Power Company*, PUCO Case No. 05-765-EL-UNC, Opinion and Order (November 9, 2005) ("*Monongahela*").

community aggregation program be proportionate to the benefits received by those customers. The Stipulation and supporting testimony do not provide any basis for the Commission to make the findings required by Section 4928.20(I), Revised Code.¹⁸⁶ In the case of customers in CSP's service area that are part of a governmental aggregation program, such a finding would be impossible because no CSP customers received any benefit from the rate increase deferred for OP customers.

The PIRR is also unjust and unreasonable because the 5.34% carrying charge proposed to be collected on the unamortized balance is excessive. At issue is the proper rate to be applied to the balance of the deferrals once amortization begins.¹⁸⁷ Newly issued seven-year BBB rated corporate bonds are being issued at an interest rate of 3.75%.¹⁸⁸ Given that the PIRR will be collected over seven years, the same period in which corporate bonds can be currently obtained for 3.75%, there is no valid reason to authorize the significantly higher carrying charge rate proposed in the Stipulation.¹⁸⁹

Furthermore, any carrying charge applicable to the PIRR amortization process must be applied to a balance that has been reduced for ADIT consistent with sound

¹⁸⁶ IEU-Ohio Ex. 9A. at 22.

¹⁸⁷ In rebuttal testimony, Mr. Allen suggested that the Companies could not have secured bonds in 2009 at the rates suggested by Mr. Bowser. Cos. Ex. 20A at 11. Whether that is true is irrelevant. Mr. Allen agreed that the carrying charge is designed to compensate the Companies for the amortization period, 2012 to 2018. Tr. Vol. XII at 2051-52. Thus, the question for the Commission is the appropriate rate now and going forward.

¹⁸⁸ IEU-Ohio Ex. 8 at 15.

¹⁸⁹ *Id.* at 14.

regulatory practices and principles.¹⁹⁰ Under the Stipulation, the “carrying charge will be calculated with no adjustment to the book balance as of year-end 2011.”¹⁹¹ This means that the carrying charge will be calculated on a deferral balance “gross of tax,” while proper ratemaking requires the deferral to be calculated “net of tax.”¹⁹² Deferrals should be and have been calculated “net of tax” because of differences between federal income tax and book accounting treatment. A timing difference reduces the Companies’ federal income tax liability before the Companies recognize the expense and collect it from customers.¹⁹³ As OEG witness Baron stated, “ADIT is effectively an interest-free loan from the government that will be repaid to the government at the time that ratepayers are ultimately charged for the previously deferred amounts.”¹⁹⁴ As a result of this tax benefit, the Companies do not have to fund the entire amount needed to finance the deferrals.¹⁹⁵ The ADIT would amount to approximately 35% of the regulatory asset balance.¹⁹⁶ If the proper adjustments are made for the two items noted above, a lower debt rate and ADIT, customers would see reduced cost of about approximately \$69 million if the phase-in deferral amount is set at approximately \$624

¹⁹⁰ IEU-Ohio Ex. 8 at 14.

¹⁹¹ Stipulation at 26.

¹⁹² IEU-Ohio Ex. 4; see also IEU-Ohio Ex. 8 at 14.

¹⁹³ IEU-Ohio Ex. 8 at 14.

¹⁹⁴ IEU-Ohio Ex. 4.

¹⁹⁵ IEU-Ohio Ex. 8 at 14; IEU-Ohio Ex. 4.

¹⁹⁶ *Id.*

million.¹⁹⁷ Thus, the Stipulation proposes a PIRR that is both unlawful and unreasonable.

The Stipulation also commits the Signatory Parties to support undefined securitization legislation.¹⁹⁸ But the Stipulation and testimony do not explain why new legislation is necessary, what that legislation would look like, why it is tied to shopping caps or the proposed MTR, or the benefits it would provide to customers.¹⁹⁹ As IEU-Ohio witness Bowser testified, the Companies are already using securitization to factor receivables without any additional legislation at an interest rate of .31%.²⁰⁰ In short, there is no basis to tie securitization legislation and approval of unseen and unexplained tariffs, the benefits of which have not been demonstrated, to the substantive provisions regarding deferral amortization and shopping caps in the Stipulation.

J. Timber Road Renewable Energy Purchase Agreement and Shale Gas FAC Review

Section IV.1.j of the Stipulation provides for a one-time up-front prudence review of AEP-Ohio's 20-year contract, a renewable energy purchase agreement ("REPA"), with Paulding Wind Energy LLC ("Paulding") regarding the Timber Road Wind Farm.²⁰¹ Similarly, Section IV.2.a.2 provides for a one-time up-front prudence review of shale gas

¹⁹⁷ Tr. Vol. VIII at 1481 (Direct examination of Joseph Bowser); see also IEU-Ohio Ex. 8 at 15.

¹⁹⁸ Stipulation at 25.

¹⁹⁹ *Id.* at 17-18.

²⁰⁰ IEU-Ohio Ex. 8 at 17.

²⁰¹ Stipulation at 7.

contracts for existing gas units of the Companies.²⁰² Those provisions are in direct conflict with Commission rules and should not be approved.

The approval of these provisions of the Stipulation would violate the express terms of the rule that requires an annual review in which the Companies must demonstrate that the costs are prudently incurred.²⁰³ The only justification for suspending the rule's requirement for annual prudence reviews is a claimed need for certainty of a long-term revenue stream so that investors will bear the up-front costs of the wind farm project (and this testimony was offered with regard to only the Timber Road REPA; nothing was offered regarding shale gas contracts), but the record also demonstrates that the wind farm production on which the REPA was based was completed and operational in the summer of 2011.²⁰⁴ Thus, the need to suspend Commission rules had no bearing on investors' decisions to bear the up-front costs of the wind farm. As the Companies have presented no credible evidence supporting their proposal to suspend the operation of Commission rules regarding either the REPA or prospective shale gas contracts (and regardless of whether the Commission even has the authority to suspend its rules as proposed in the Stipulation), Commission approval of these sections of the Stipulation would be unlawful and unreasonable.

²⁰² Stipulation at 20.

²⁰³ Rule 4901:1-35-09(C), OAC.

²⁰⁴ Tr. Vol. III at 283; Tr. Vol. I at 46.

K. Corporate Separation

The Stipulation proposes that “[a]pproval of [the] Stipulation will serve as the Commission’s approval of full legal corporate separation.”²⁰⁵ Soon after the Stipulation was filed, however, the Companies filed an application to amend the corporate separation plan.²⁰⁶ The attorney examiners correctly denied a motion to consolidate the application to amend the corporate separation plan with the proceedings to review the Stipulation, noting that there “needs to be additional review ... before we actually address” corporate separation.²⁰⁷ Because the Stipulation and supporting testimony do not support the findings required by law to approve corporate separation, this portion of the Stipulation is unlawful and unreasonable.

An application for corporate restructuring is governed by Section 4928.17, Revised Code. That section and the Commission rules implementing that section²⁰⁸ provide a detailed set of requirements that must be satisfied. The Companies, however, have: (1) failed to provide the terms and conditions of any sale or transfer of generating assets; (2) failed to demonstrate the effect any sale or transfer would have on current and future SSO prices; (3) failed to demonstrate how the sale or transfer will affect the public; and (4) failed to state the fair market value of the generating assets it plans to

²⁰⁵ Stipulation at 11.

²⁰⁶ *In the Matter of the Application of Ohio Power Company for Approval of An Amendment to Its Corporate Separation Plan*, Case No. 11-5333-EL-UNC, Application (Sept. 30, 2011).

²⁰⁷ Tr. Vol. V at 640.

²⁰⁸ Ch. 4901:1-37, OAC.

sell or transfer.²⁰⁹ Without this information, it is impossible for the Commission to appreciate the implications of the approval called for by the Stipulation.

Approval of full legal corporate separation as proposed through the Stipulation would also prejudice interested parties' ability to "file specific objections to the plan" as required by Section 4928.17(B), Revised Code.²¹⁰ Section 4928.17(B), Revised Code, directs the Commission to adopt rules which "include an opportunity for any person having a real and substantial interest in the corporate separation plan to file specific objections to the plan and propose specific responses to issues raised in the objections, which objections and responses the commission shall address in its final order."²¹¹ The Commission, by rule, provides that the Commission shall set an application to transfer assets if the application proposes to alter the jurisdiction of the Commission over generation assets.²¹² If the Commission were to approve Sections IV.1.q and IV.1.t of the Stipulation, interested parties currently not involved in the review of the Stipulation and all parties that should have access to a complete application would be denied an opportunity provided for by Ohio law.

Despite the legal requirements that govern corporate separation, the Companies are asking the Commission to approve a separation plan without knowing the details and empower the Companies to fill in the blanks later. This aspect of the Stipulation is unlawful and unreasonable.

²⁰⁹ Rule 4901:1-37-09, OAC.

²¹⁰ Section 4928.17(B), Revised Code.

²¹¹ *Id.*

²¹² Rule 4901:1-37-09(D), OAC.

L. Summary

For the Commission to approve the Stipulation as filed, it would have to ignore that the proposed ESP fails the ESP is less favorable than an MRO, that the proposed rate increases lack justification, that the proposed revenue distribution and rate structure are irrational, that various riders are illegal, poorly structured, or both, that the proposed capacity charges will violate state policy encouraging customer choice and result in unduly discriminatory rates, and that the approval of corporate separation would be premature and in violation of statute. As a legal matter, the Commission does not have the authority to approve the Stipulation. As a policy matter, approval of the Stipulation will have significant negative consequences for the customers of OP and CSP and violate the state's public policy goals in many ways.

VI. THE STIPULATION IS NOT THE PRODUCT OF SERIOUS BARGAINING

The Stipulation should not be approved because it was not the product of serious bargaining among capable, knowledgeable parties. First, there is no demonstration as to how the Stipulation reflects a bargained compromise involving a balancing of interests or how it provides a reasonable and lawful resolution of all issues arising in the proceeding. Many of the Signatory Parties, for example, initially submitted testimony that the ESP Application failed the ESP versus MRO test, but then signed on to a Stipulation which also failed the test.²¹³ The parties do not explain how they were able to reconcile this difference.²¹⁴ Instead, RESA, Paulding Wind Farm, Ohio Environmental Council ("OEC"), Natural Resources Defense Council ("NRDC"), Exelon,

²¹³ IEU-Ohio Ex. 9A at 5.

²¹⁴ *Id.*

EnerNOC, Environmental Law & Policy Center (“ELPC”), Duke Energy Retail Sales (“DERS”), Association of Independent Colleges and Universities (“AICUO”), and AEP Retail each admitted that they did not undertake an independent analysis of whether the proposed ESP is more favorable than an MRO.²¹⁵ During cross-examination, OEG witness Baron admitted that he did not independently verify that the ESP is quantitatively more favorable than an MRO.²¹⁶ Ohio Manufacturers’ Association Energy Group (“OMAEG”), the Ohio Hospital Association (“OHA”), Hilliard, and Grove City pointed to the testimony of Staff witness Fortney and Companies’ witnesses Thomas, Allen, and Hamrock to satisfy the Stipulation’s claim regarding the ESP versus MRO.²¹⁷ Given that the testimony they relied upon was filed after the Stipulation was signed, those parties could not have had personal knowledge when they signed the Stipulation. Even more troubling, the persons and testimony to which they deferred ultimately agreed that the ESP failed the statutory test.

Second, the parties also defined differently provisions of the Stipulation.²¹⁸ An example illustrative of the lack of coherence among the Signatory Parties’ views is their understanding of a key provision of the Stipulation relating to the expected outcome of the “glide path” to an auction-based SSO: the Signatory Parties do not have a common

²¹⁵ *Id.* at 6.

²¹⁶ Tr. Vol. III at 224. OEG witness Baron also admitted that he previously testified that the proportion of the legacy ESP included in an MRO would be different than the proportion used by Companies’ witness Thomas in her ESP versus MRO test. IEU-Ohio Ex. 2; Tr. Vol. III at 253 (Cross-examination of Stephen Baron). During cross-examination, Peggy Claytor admitted she did not perform a quantitative analysis to determine that the ESP is more favorable than an MRO. Tr. Vol. V at 642 (Cross-examination of Peggy Claytor).

²¹⁷ IEU-Ohio Ex. 9A at 6-7.

²¹⁸ *Id.* at 5-6.

understanding on whether the Companies are committing to setting the default rates after the 2015-16 delivery year through a CBP. Most of the Signatory Parties except for Exelon and the Companies²¹⁹ stated that they do not know whether the Companies' next ESP will contain a CBP.²²⁰ The Companies and Exelon both admitted in discovery that Section IV.8 of the Stipulation does not require a CBP in the next ESP.²²¹ Thus, it is unclear whether the parties have an understanding of what is being accomplished through the Stipulation, and more importantly what is being left undone.

Similarly, there is disagreement regarding the Stipulation's provision proposing the Pool Modification or Termination Rider that would authorize the Companies to file an application to recover costs resulting from Pool termination if those costs are in excess of \$50 million. According to RESA witness Ringenbach, the Companies may file an application to seek only the balance of costs that exceed \$50 million.²²² The Companies' witness, however, claims that if the costs of Pool termination exceed \$50 million, the Companies may file an application to recover the entire cost of Pool termination including the first \$50 million.²²³ To make matters worse, some parties, such as Grove City's witness Honsey, did not weigh in one way or the other because they did not know what the Pool Modification or Termination Rider was.²²⁴ Another

²¹⁹ FES Ex. 17(b).

²²⁰ IEU-Ohio Ex. 9A at 7.

²²¹ *Id.* at 8.

²²² Tr. Vol. IV at 554 (Cross-examination of Teresa Ringenbach).

²²³ Tr. Vol. V at 708 (Cross-examination of Philip Nelson).

²²⁴ Tr. Vol. IV at 492-494 (Cross-examination of Phil Honsey). AICUO witness Todd Jones also admitted that he did not know anything about the Pool Modification or Termination Rider. Tr. Vol. IX at 1639.

Signatory Party witness, Stephen Baron, even admitted that he believed the Pool Modification or Termination Rider was illegal.²²⁵

Third, the Signatory Parties also committed to certain key provisions of the Stipulation without any specific knowledge to understand the value of their alleged “bargain.” For example, NRDC, OEC, ELPC, AEP Retail, Paulding Wind Farm, AICUO, DERS, Hilliard, Grove City,²²⁶ Kroger, OMAEG, OHA, RESA, EnerNOC, Exelon, Constellation, and PJM Power Providers Group (“P3”) each admitted that when they signed the Stipulation, they did not know that the RPM-priced capacity set-aside had been fully awarded for any customer class.²²⁷

Fourth, several knowledgeable parties were excluded from negotiations leading up to the execution of the Stipulation.²²⁸ Other parties were narrowly focused and did not consider the overall balance struck by the terms of the Stipulation as a package.²²⁹

In short, the Signatory Parties did not have a common understanding of the implications of the Stipulation or claimed reliance on testimony that did not exist and which would ultimately contradict the basis for their signing the Stipulation. They lacked a common understanding of key provisions of the Stipulation. Many supporting the Stipulation were narrowly focused and offered no support for its outcomes. Taken

²²⁵ Tr. Vol. III at 244 (Cross-examination of Stephen Baron).

²²⁶ Grove City witness Honsey admitted that he never reviewed Appendix C and that he does not know what RPM means. Tr. Vol. IV at 493-494 (Cross-examination of Phil Honsey).

²²⁷ IEU-Ohio Ex. 14.

²²⁸ *Id.* at 3; FES Ex. 1 at 9 and 57-59. The exclusion of parties from negotiations raises a concern that the settlement process was tainted and unreasonable. See *Time Warner AxS v. Pub. Util. Comm.*, 75 Ohio St.3d 229, 233 (1996).

²²⁹ *Id.* at 8.

together, neither the Stipulation nor the supporting testimony demonstrates that the Stipulation is the product of knowledgeable and capable parties that set about to produce a reasonable compromise of contested issues based on the facts and the law.

VII. MODIFICATION OF THE STIPULATION

Because the Stipulation fails to satisfy any of the standards for approval, the Commission must reject the proposed ESP and other provisions of the Stipulation. The Stipulation effects unlawful rate increases while denying customer choice during a period when competitive suppliers are offering better and more predictable prices. It illegally authorizes placeholder riders and discriminatory charges. It is filled with empty commitments based on an assumption that the Companies are entitled to additional time to transition to an open marketplace.

Rejecting the Stipulation for the reasons set forth herein will also put the Commission on firmer legal ground than is possible otherwise.

If the Commission chooses to modify the Stipulation, however, it must make some significant adjustments to bring the Stipulation into compliance with the law governing the approval of an ESP and the policies and practices of the Commission.

Initially, the Commission must perform a reconciliation of the revenue foundation of the proposed ESP with the Supreme Court's decision and the Commission's recent order regarding the Companies' current ESP. This reconciliation must be done for each company separately.²³⁰ The arbitrary rate increases should be eliminated.²³¹ Current

²³⁰ *Id.*

²³¹ *Id.* at 56.

rate schedules should be maintained; any changes should be accomplished by applying a uniform percentage to current rates and charges to maintain the current rate relationship.²³² There would be no need for the LFP or MTR. The DIR should be rejected, and the level and structure of distribution rates should be addressed in the pending rate cases.²³³ The remaining placeholder riders should be eliminated or made bypassable if not eliminated.²³⁴

Further, the Commission should protect and promote customer choice. To that end, the Commission should reject the provisions of the Stipulation that create the limitations on shopping and the arbitrary \$255 per megawatt-day capacity charge. The linkage between shopping and the passage of securitization should be eliminated.²³⁵

Additionally, the Commission should address several other matters in an orderly way not contemplated by the Stipulation. For example, the Commission should delay any recovery of the phase-in deferral for OP until the remand and pending FAC audit cases are completed, and all deferral balances should be adjusted to reflect the effect of ADIT. Any carrying charge on the amortization should be reduced to a reasonable debt interest rate. The linkage between the securitization and amortization should be

²³² *Id.* at 55. The interruptible credit should be no less than the current level or be increased to the amount in the proposed ESP so as to encourage customer-sited demand response initiatives. *Id.*

²³³ *Id.* at 56.

²³⁴ *Id.* at 57.

²³⁵ *Id.* at 56.

broken, and the Commission should not lock itself into a particular approach to establishing the next SSO.²³⁶

If the Commission does modify the Stipulation, all of the modifications discussed above are necessary. Without each one, the resulting ESP and related matters will result in unlawful injury to consumers and unreasonable rates.

VIII. CONCLUSION

In order to approve the Stipulation, the Commission must find that it is the product of serious bargaining among capable, knowledgeable parties, that the settlement as a package benefits ratepayers and the public interest, and that the settlement does not violate any important regulatory principles or practices. On the record presented to the Commission in these cases, the Commission cannot make the necessary findings to approve the Stipulation as filed.

The Companies have made clear that their goal is to raise rates and cut off choice. The Stipulation proposes to accomplish both results. If the Stipulation's terms are authorized, customers of CSP and OP will be trapped in out-of-market ESP rates when lower prices are available from CRES suppliers including the CRES supplier affiliated with the Companies. When market prices are expected to be high, the default service rate will be based on a CBP. Thus, customers would be saddled with higher rates with no place to turn throughout the term of the proposed ESP. That result is not supported by the law or policies of this state and should not and cannot be approved by the Commission. Even if the Commission does not reject the Stipulation, it must

²³⁶ *Id.* at 56-57.

substantially revise its terms. Anything short of outright rejection or substantial modification will leave customers represented by IEU-Ohio and the various other customer groups, already rocked by the effects of a severe and prolonged recession, captive to the Companies' above-market prices.

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I hereby certify that a copy of the foregoing *Initial Brief of Industrial Energy Users-Ohio* was served upon the following parties of record this 10th day of November 2011, *via* electronic transmission, hand-delivery or first class U.S. mail, postage prepaid.

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