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BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

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

MEMORANDUM CONTRA RETAIL ENERGY SUPPLY ASSOCIATION'S MARCH 14, 2012, PETITION FOR REHEARING

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On behalf of Ohio Power Company

MEMORANDUM CONTRA
RETAIL ENERGY SUPPLY ASSOCIATION'S
MARCH 14, 2012 PETITION FOR REHEARING

Background

On September 7, 2011, AEP Ohio, Staff, and numerous other parties filed a Stipulation and Recommendation (Stipulation) in order to resolve the issues raised in ten major proceedings involving Ohio Power Company (OPCo, the Company, or AEP Ohio), including, among other cases, an electric security plan (ESP) proceeding (Case Nos. 11-346-EL-SSO and 11-348-EL-SSO) and the instant proceeding involving appropriate charges for capacity that CRES Providers purchase from AEP Ohio.

On December 14, 2011, the Commission issued an Opinion and Order in the cases addressed by the proposed Stipulation that modified in part and adopted the Stipulation, including its provisions regarding capacity pricing.

On January 23, 2012, the Commission clarified in several respects the capacity pricing provisions that would apply during the term of the ESP approved by the December 14, 2011 Opinion and Order. As part of that January 23 Compliance Entry, the Commission clarified the following about its modification regarding the Stipulation's customer class re-allocation of RPM-priced capacity set-aside:

> For further clarification purposes, the Commission notes that this modification to the Stipulation goes back to the initial allocation among the customer classes based on the September 7, 2011, data, *regardless of whether any customer class is now oversubscribed.*

(Compliance Entry, at 3-4, emphasis added). Thus, the Commission clarified on January 23, 2012 that only the first 21% of shoppers in each customer class would receive the RPM capacity

price – regardless of whether the customer class was already oversubscribed. This is a clear and direct statement by the Commission that load (above the 21% level) furnished to CRES providers associated with customers that already had received RPM-priced capacity under the Stipulation would be bumped back to the second tier pricing of $255/MW-Day. If RESA disagreed with that result, it should have filed an application for rehearing in response to the January 23 Entry. It did not, and the capacity pricing required by the January 23 Entry has remained in effect continuously since then.

Subsequently, on February 23, 2012, the Commission issued an Entry on Rehearing rejecting the September 7, 2011 Stipulation and Recommendation. The Entry on Rehearing provided the following directives, after quoting R.C. 4928.143(C)(2)(b) regarding the requirement to return to the prior SSO rate plan:

> Therefore, we direct AEP-Ohio to file, no later than February 28, 2012, new proposed tariffs to continue the provisions, terms, and conditions of its previous electric security plan, including but not limited to the base generation rates as approved in ESP I, along with the current uncapped fuel costs and the environmental investment carry cost rider set at the 2011 level, as well as modifications to those rates for credits for amounts fully refunded to customers, such as the significantly excessive earnings test (SEET) credit, and an appropriate application of capacity charges under the approved state compensation mechanism established in the Capacity Charge Case.

(Entry on Rehearing at 12.)

On February 27, 2012, AEP Ohio filed a Motion for Relief and Request for Expedited Ruling (Motion for Relief) in the instant case. In its motion, AEP Ohio urged the Commission to consider expeditiously the implementation of a cost-based capacity rate, at least for a transition period during which it would remain a Fixed Resource Requirement (FRR) entity, in lieu of requiring the exclusive use of Reliability Pricing Model (RPM) auction pricing, and requested that the Commission issue a decision on the merits within 90 days. In addition, the Company

requested that a reasonable interim cost-based capacity rate be established during the pendency of the instant proceeding. AEP Ohio estimated that, if RPM auction pricing were relied upon exclusively to price its capacity, it would experience a massive erosion in revenues. Specifically, the Company projected that, under a capacity pricing regime composed solely of RPM-based pricing, its earnings for 2012 and 2013 would decrease by 27 percent and 67 percent, respectively, resulting in a return on equity of 7.6 percent and 2.4 percent, respectively as well as possible downward adjustments to the Company's credit ratings, which would clearly be an unjust and unreasonable result.[1]

Accordingly, in its February 27 Motion for Relief AEP Ohio proposed using, on an interim basis, the same two-tiered capacity pricing contemplated by the Stipulation, as modified and adopted by the revised Detailed Implementation Plan (DIP) that it submitted on December 29, 2011, or, alternatively, as yet further modified by the Commission's January 23, 2012 Entry. (With regard to the alternative capacity pricing based on the January 23 Entry, OPCo requested that, in the event that alternative were adopted, mercantile load should be excepted from the load eligible for RPM-priced capacity.)

On March 7, 2012, the Commission issued its Entry in the instant proceeding granting AEP Ohio's Motion for Relief. The Commission found support in the record for the conclusion that reverting from the capacity pricing structure established by the January 23 Entry to a state

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[1] On February 27, 2012, Fitch Ratings revised its rating outlook for OPCo from Stable to Negative, as a result of the potential impacts on OPCo of the recent adverse regulatory decisions and the uncertainty of future regulatory decisions. *See* http://www.marketwatch.com/story/fitch-affirms-ratings-on-aep-and-subs-ohio-power-outlook-revised-to-negative-2012-02-27. In the press release on the rating action, Fitch indicated, "the Negative Outlook on OPCo reflects the challenging operating environment in Ohio. The most troubling concern in Ohio is the Public Utility Commission of Ohio's (PUCO) decision last week to revoke the stipulation agreement on OPCo's Electric Security Plan (ESP) that it had approved just two months earlier." *Id.* Moody's and S&P have issued similar reports. *See* Moody's, "Ohio's Utility Commission Rescinds Ohio Power's Transition to Market-Based Rates, a Credit Negative for AEP" (Mar. 5, 2012); http://www.reuters.com/article/2012/02/27/idUSWNA105620120227.

compensation mechanism based exclusively on RPM auction pricing could risk an unjust and unreasonable result. Consequently, the Commission's March 7 Entry confirmed that, for the relatively short interim period during which the Commission considers what is a just and reasonable capacity pricing structure for the longer term, AEP Ohio should continue to charge CRES providers for capacity in accordance with the January 23 Entry (including, despite AEP Ohio's request, allowing mercantile load to be eligible for RPM-priced capacity through aggregation programs). In other words, the Commission concluded that for the interim period, capacity will be priced on a status quo basis, using the same regime that the January 23 Entry previously established.

RESA's Petition for Rehearing

On March 14, 2012, the Retail Energy Supply Association (RESA) filed a Petition for Rehearing of the March 7, 2012 Entry. RESA requests the Commission grant rehearing for the purpose of clarifying that its March 7, 2012 Entry did not authorize AEP Ohio to "revoke" RPM pricing to any customer who received RPM pricing under the December 14, 2011 Opinion and Order. (RESA Petition for Rehearing at 1.) RESA contends that "it would be unjust and unreasonable to charge customers who were shopping and receiving RPM [Tier One] capacity pricing prior to the now rejected Stipulation", and now require them to pay the higher Tier Two price ($255/MW-Day) for capacity. (*Id.* at 1-2.) Finally, RESA contends that "it is unjust and unreasonable to decrease the amount of RPM pricing to the commercial class from the level authorized in the Opinion and Order of December 14, 2011, [just] because the Commission authorized expanding RPM pricing for governmental aggregation." (*Id.* at 2.)

ARGUMENT

RESA's Petition for Rehearing should be denied. First, the petition really is an untimely application for rehearing of the January 23 Entry. The March 7 Entry does not change the availability of Tier One (RPM auction-priced) capacity but perpetuates the status quo created by the January 23 Compliance Entry. It maintains the status quo for Tier One (RPM) and Tier Two ($255/MW-Day) pricing that the January 23 Entry established. Respectfully, to the extent RESA had concerns about the impact of the January 23 Entry on capacity pricing, it should have raised them in a timely manner in a rehearing request of that Entry.

Second, RESA's arguments ignore the fact that the February 23, 2012 Entry on Rehearing rejected both the September 7, 2011 Stipulation and the December 14, 2011 Opinion and Order. The Commission did not overturn the Opinion and Order and the Stipulation in part, retaining parts of them that are beneficial to RESA and only rejecting provisions that benefitted or disadvantaged other parties. Rather, the Opinion and Order and Stipulation were overturned in their entireties. Consequently, rights that the Stipulation and the December 14 Opinion and Order provided to CRES providers to purchase capacity at Tier One pricing were either modified by the January 23 Entry or extinguished by the February 23 Entry on Rehearing.

Third, neither the January 23 Entry (nor the December 14 Opinion and Order or the September 7 Stipulation) established prices that *retail customers* pay for capacity. Rather, AEP Ohio furnishes capacity to CRES Providers and charges them for it. The prices that CRES providers charge their retail customers for service are based upon a host of factors, only one of which is the cost of capacity. Indeed, the primary factor is the cost of energy, which has declined dramatically since the Stipulation was submitted on September 7 and the Opinion and Order was issued on December 14. In sum, the amount of head room available to CRES

providers within which they can make competitive offers to retail customers varies up and down over time, and there simply is no basis for believing that CRES providers will be unable to compete for retail customers while paying the Tier II capacity price during the relatively short-term period when the interim capacity pricing structure of the January 23 Entry is in effect.

1. RESA's Petition is an untimely application for rehearing of the January 23, 2012 Entry.

The Commission's January 23, 2012 Compliance Entry, at 3-4, determined that:

> [In] the Opinion and Order, we explicitly modified the Stipulation to ensure "that RPM-priced capacity allocation determined for each customer class is only available for customers in the particular customer class, no RPM-priced capacity can be allocated to a customer in another customer class," (opinion and Order at 55). Nowhere in the Opinion and Order is this modification limited to unused capacity allotments as of January 2012. For further clarification purposes, the Commission notes that this modification to the Stipulation goes back to the initial allocation among the customer classes based on the September 7, 2011, data, *regardless of whether any customer class is now oversubscribed.* (Emphasis added.)

Accordingly, the Commission's January 23 Compliance Entry revised the allocation of RPM-priced capacity so that each customer class would receive a 21% allocation of RPM-priced capacity, and confirmed that no RPM-priced capacity allocated to one customer class, *i.e.*, the residential or industrial customer classes, can be allocated to a customer in another class, *i.e.*, the commercial class. The Commission's January 23 Entry further clarified that this modification to the Stipulation's approach (which had allowed the shifting of under-utilized RPM capacity from the residential or industrial class to the commercial class) "goes back to the initial allocation among customer classes based on the September 7, 2011, data." This directive was explicitly punctuated by the statement that the RPM set-aside would go back to 21% regardless of whether any customer class was oversubscribed. Consequently, the January 23 Compliance Entry limited the commercial class's entitlement to RPM capacity in 2012 under the 21% provision, to 21%

and directed that the oversubscribed customers above 21% be put back to the second tier of pricing at $255/MW-Day. The reallocation to and grandfathering of commercial customers of RPM capacity in excess of the 21% level allowed by the Stipulation was eliminated. However, that Entry also simultaneously and significantly expanded access to RPM-priced capacity by adding a separate and additional allocation of such capacity for aggregation customers (including commercial and industrial customers in the mercantile category).

While the February 23, 2012 Entry on Rehearing rejected the Stipulation and reversed the December 14, 2011 Opinion and Order, the January 23 Compliance Entry's directives regarding the availability and allocation of Tier One (RPM) pricing and Tier Two ($255/MW-Day) pricing will remain in effect on an interim basis. The March 7, 2012 Entry did not revise the capacity pricing regime that the January 23 Compliance Entry established. The March 7 Entry only confirmed that the January 23 Entry regime would be used in order to maintain the status quo with regard to capacity pricing until the Commission issues a decision in this proceeding (which it has committed to do on an expedited basis). RESA's present complaint relates directly to the Commission's January 23 Compliance Entry and not to a new matter decided as part of the March 7 Entry.

Consequently, the existing capacity pricing regime was established by the January 23 Compliance Entry. RESA never raised any of the objections to the January 23 Entry that it now seeks to advance in response to the March 7 Entry. RESA should have raised its objections by seeking rehearing of the January 23 Compliance Entry. RESA's effort to raise its objections to the capacity pricing structure implemented by the January 23 Compliance Entry is now too late. The deadline for seeking rehearing of that Entry expired on February 23, 2012, 30 days after it

was issued. Consequently, RESA's Petition for Rehearing is untimely, and should be denied on that basis.

2. RESA's arguments ignore the fact that the February 23, 2012 Entry on Rehearing rejected both the September 7, 2011 Stipulation and the December 14, 2011 Opinion and Order.

RESA's request, at page 1 of its Petition for Rehearing, that the Commission grant rehearing for the purpose of clarifying that "its March 7, 2012, Entry did not intend or authorize AEP Ohio to revoke RPM pricing to any customer who received RPM pricing under the Opinion and Order of December 14, 2011," is misdirected. First, the loads of customers for which CRES providers might have been able to obtain RPM pricing prior to the January 23 Compliance Entry, pursuant to the Stipulation and the December 14 Opinion and Order, which were in excess of the 21% level, became ineligible for RPM priced capacity as a result of the January 23 Compliance Entry, not due to the March 7 Entry. In addition, the February 23 Entry on Rehearing rejected the Stipulation and reversed the December 14 Opinion and Order. As a result, benefits that CRES providers received pursuant to the specific provisions of the Stipulation and Opinion and Order were eliminated, just as provisions beneficial to AEP Ohio were eliminated, by the February 23 Entry on Rehearing. RESA's argument that it is entitled to receive benefits based on the Stipulation or Opinion and Order ignores the fact that they have been rejected and is meritless.

Nor does RESA have any equitable basis for claiming that CRES providers should receive benefits that the Stipulation and the Opinion and Order provided. First, CRES providers' customers will not necessarily be affected by the January 23 Entry. To the extent that the January 23 Entry affected the availability of RPM pricing for commercial customer loads that were shopping as of, and had entered into agreements with CRES providers prior to, September

7, 2011, and those loads were above the 21% level, the customers associated with those loads will continue to obtain the benefits of the shopping arrangements they made with their CRES providers in accordance with the terms and conditions of those agreements. The CRES providers' costs of serving those customers might change during the term of the agreements, but CRES providers are not required to pass through to customers either cost increases or decreases. For example, wholesale energy costs, which are a major component of CRES providers' costs of serving their retail customers, have declined substantially in recent months, materially increasing CRES providers' margins and offsetting any impacts from increases in other wholesale cost components.

Secondly, CRES providers are not treated in an unfair manner either. When the CRES providers entered into their arrangements with customers prior to September 7, 2011, they knew (or should have known) that the costs of the various wholesale components that, in total, comprise retail electric service can change. CRES providers had no entitlement or guarantee to particular pricing for their wholesale components or that the pricing for such components that they obtain from AEP Ohio or other suppliers would remain fixed for any particular time period. Specifically, they had no reasonable basis for assuming that the price for AEP Ohio capacity that they would purchase to serve the commercial customers' loads, including the loads in excess of the 21% level, would remain available at the RPM price forever.

It is worth reiterating that the difficulty in predicting, and thus relying upon, constant pricing for wholesale components of retail electric service does not necessarily equate to a disadvantage for CRES providers. For example, as noted above, wholesale energy prices, a much larger component of the retail electric service than the cost of capacity, have declined significantly since September 7, 2011, providing additional significant headroom and potential

profits for CRES providers in connection with their retail electric service offerings. Notably, RESA has not contended that it is unprofitable to continue serving customers whose loads are in excess of the 21% level using Tier Two ($255/MW-Day) capacity pricing, let alone that it is unable to continue serving those customers. CRES providers are not offering to provide their customers with rebates when energy prices decrease, but want to maintain a fixed profit margin at AEP Ohio's expense. The inequity of RESA's heads, CRES providers win, and tails, AEP Ohio loses position is clear.

It is also worth keeping in mind that, contrary to the implication of RESA's arguments, customers of utility services, whether they are wholesale or retail customers, do not have an entitlement to continue receiving any particular rate for their service going forward into the future. While rates may not be changed retrospectively, they can and do change prospectively. Notably in that regard, in the instant case, there has been no retroactive change to any prices that RESA's members pay for capacity. Rather, changes to capacity prices available to serve load in excess of the 21% level from Tier One to Tier Two prices have occurred only prospectively as a result, first, of the January 23 Compliance Entry and, second, as maintained by the March 7 Entry.

3. Maintaining the capacity structure established by the January 23 Compliance Entry preserves the status quo.

RESA argues, at 2-5, that in order to preserve the status quo commercial customers who were shopping prior to the Stipulation and being charged RPM capacity should continue to receive Tier One pricing. That is simply incorrect, as explained above. The status quo has been maintained by retaining the capacity pricing structure that the January 23 Compliance Entry established.

4. The January 23 Compliance Entry, which the March 7 Entry confirms remains in effect, requires that each customer class must receive an allocation of RPM capacity pricing for 21% of its load, and does not permit the reallocation of capacity from one customer class to another class.

RESA also attempts to bypass the January 23 Compliance Entry by rendering the 21% limitation on (non-aggregation) load eligible for Tier One (RPM) capacity pricing meaningless, converting it into a minimum rather than a maximum. It does so, at page 5 of its Petition for Rehearing, by misinterpreting Paragraph 26 of the March 7 Entry. Paragraph 26 provides, in pertinent part, as follows:

> We implement the two-tier capacity pricing mechanism proposed by AEP-Ohio in its motion for relief, subject to the clarifications contained in our January 23, 2012, entry, including the clarification including mercantile customers as governmental aggregation customers eligible to receive RPM-priced capacity. Under the two-tier capacity pricing mechanism, the first 21 percent of each customer class shall be entitled to tier-one pricing.

RESA states, at page 5, that Paragraph 26 "specifically states that the first 21% of each class shall receive Tier One pricing." That is accurate. RESA next states that "[Paragraph 26] does not state that 'only' 21% of each class 'can' receive Tier One pricing." *Id.* With all due respect, that is misleading, because it portrays the 21% level as a minimum, but not a maximum.

Similarly, RESA's citation to the Stipulation, Section 1(d) of Appendix C (the Detailed Implementation Plan (DIP)), at page 6, to support its position that commercial customer loads in excess of 21% should continue to get RPM-priced capacity is unavailing. It is inappropriate to cite to the Stipulation in support of its position because, once again, the Stipulation was eliminated by the February 23 Entry on Rehearing. The Stipulation's DIP and its grandfathering provision are not in effect any more. Neither RESA nor any other party, including AEP Ohio, can rely upon provisions of the Stipulation at this point.

At page 6, RESA does attempt to rely upon Paragraph 18 of the January 23 Compliance Entry to support its position, but the reference upon which RESA relies does not refer to, let alone support, RESA's objective. The portion of Paragraph 18 that RESA quotes at page 6 refers to aggregation loads, which the January 23 Entry treated entirely separately from the non-aggregation loads, grandfathered by the defunct Stipulation and Opinion and Order, that are the subject of RESA's Petition for Rehearing.

CONCLUSION

For the reasons provided above, RESA's Petition for Rehearing should be denied.

Respectfully submitted,

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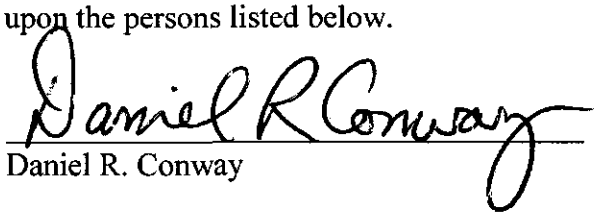
On behalf of Ohio Power Company

CERTIFICATE OF SERVICE

The undersigned hereby certifies that a true and accurate copy of the foregoing Memorandum Contra Retail Energy Supply Association's Petition for Rehearing was served this 23rd day of March, 2012 by electronic mail, upon the persons listed below.



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