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

INDUSTRIAL ENERGY USERS-OHIO'S REPLY BRIEF

Samuel C. Randazzo, Esq.
Frank P. Darr
Joseph E. Oliker
Matthew R. Pritchard
McNees Wallace & Nurick LLC
21 East State Street, Suite 1700
Columbus, OH 43215-4228
Telephone: 614-469-8000
Telecopier: 614-469-4653
sam@mwncmh.com
fdarr@mwncmh.com
joliker@mwncmh.com
mpritchard@mwncmh.com

Attorneys for Industrial Energy Users-Ohio

May 30, 2012

TABLE OF CONTENTS

I. INTRODUCTION 1

II. POSITION OF THE PARTIES 4

III. ARGUMENT 10

A. AEP-Ohio's Claims Regarding the Meaning of Schedule 8.1, Section D.8 of the RAA, are Contrary to the Plain Language of the RAA. 10

B. AEP-Ohio's Proposed Pricing Method Is Without Foundation and Does Not Identify the Cost of Satisfying the FRR Entity's Capacity Obligation. 18

C. AEP-Ohio's Claim that it was Not Allowed to Move to Market-Based Rates is Baseless; AEP-Ohio Charged Market-Based Rates Under its RSP, Under its Agreement to Serve Former Monongahela Power Company Customers, and Under its Agreement to Serve Ormet. 25

D. Contrary to RESA's Claim, the Commission's General Supervisory Authority Does Not Provide the Commission with Unlimited Powers to Approve Rates. 30

E. RESA's Claim that Section 4928.143(B)(2)(d), Revised Code, Gives the Commission Authority to Approve a CRES Capacity Pricing Method is Without Merit. 32

F. AEP-Ohio's Claims About the Effect of RPM-Based Pricing on the Financial Condition of its Generation Business Are Irrelevant. 33

IV. CONCLUSION 34

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I. INTRODUCTION

On May 23, 2012, the Industrial Energy Users-Ohio ("IEU-Ohio") and other parties submitted their briefs. In addition to IEU-Ohio's Initial Brief, initial briefs were also submitted by the following parties (in alphabetical order):

- Buckeye Association of School Administrators, Ohio Association of School Business Officials, Ohio School Board Association and Ohio Schools Council (collectively "Schools");
- Dominion Retail, Inc. ("Dominion");
- Duke Energy Commercial Asset Management and Duke Energy Retail Sales (collectively "Duke");
- Exelon Generating Company, LLC, Exelon Energy Company, Inc., Constellation NewEnergy, Inc. and Constellation Energy Commodities Group, Inc. (collectively "Exelon");
- FirstEnergy Solutions Corp. ("FES");
- Interstate Gas Supply, Inc. ("IGS");
- NFIB/Ohio ("NFIB");
- Office of the Ohio Consumers' Counsel ("OCC");
- Ohio Energy Group ("OEG");
- Ohio Power Company ("AEP-Ohio");
- Retail Electric Supply Association, Direct Energy Business, LLC and Direct Energy Services, LLC (collectively "RESA");
- Staff of the Public Utilities Commission of Ohio ("Staff");
- The Kroger Company ("Kroger"); and
- The Ohio Manufacturers' Association and the Ohio Hospital Association ("OMA/OHA").

On the main question of whether AEP-Ohio's proposal to change the method used to establish a capacity price applicable to Competitive Retail Electric Service ("CRES") providers from 2007 through 2011 and thereby substantially increase such price, the briefs show that the representatives of residential consumers, commercial consumers, industrial consumers, schools, local government, the Public Utilities Commission of Ohio's ("Commission") Staff and CRES providers agree: AEP-Ohio's proposal is unjust, unreasonable and unlawful.

On the same question, AEP-Ohio's Initial Brief shows that AEP-Ohio has completely unhinged itself from the law and facts. AEP-Ohio's Initial Brief shows that it continues to reinvent history, pretends that it is still a vertically integrated utility in defiance of the corporate separation that took place in 2000, broadly disregards the law, defies the evidence and otherwise makes stuff up. The only thing that is persuasively shown by AEP-Ohio's Initial Brief is that AEP-Ohio has still not found a credible legal theory or a legitimate reason for the Commission to interfere, on AEP-Ohio's behalf, with the same market response to AEP-Ohio's excessive generation supply prices that is working for the benefit of consumers in the areas of Ohio outside AEP-Ohio's distribution service territory. There is no moral, legal or evidentiary basis upon which the Commission may permit AEP-Ohio to continue to use the shopping-blocking and arbitrary two-tiered capacity pricing scheme that is presently in place or to authorize AEP-Ohio to bill and collect the more absurd pricing method advanced by AEP-Ohio in this proceeding.

To escape reality and avoid or delay the natural consequences of above-market default generation supply prices, AEP-Ohio has created a mess and dumped it in the

Commission's lap. The mess includes a dizzying and reality-defying "cost-based" maze designed by AEP-Ohio to transform AEP-Ohio's distribution service area into a zone where opportunistic monopoly pricing stiff-arms consumers during the three-year period when consumers are most likely to be able to reduce their electric bills by shopping. Before this customer-friendly three-year period, AEP-Ohio, like all other Ohio electric utilities, used the capacity pricing method it seeks, in this proceeding, to temporarily change. In effect, AEP-Ohio asserts that continued use of market-based capacity pricing is only inappropriate when it is most certain to be useful to consumers. The more cases AEP-Ohio can initiate and string out and the longer the Commission permits AEP-Ohio to deviate from the method previously approved by the Commission, the more time AEP-Ohio can run off the clock that identifies the period within which consumers are most certain to gain the largest advantage by shopping.

The perils of so-called cost-based formulas are exactly why, in 1999, Ohio turned to competition in the electric sector as a preferred tool for serving the public interest in reliable service and reasonable prices. Now, in 2012, AEP-Ohio is asking the Commission to find that the customer choice train never left the station or that the Commission should help AEP-Ohio make sure that the train does not run on time.

The so-called cost-based ratemaking methodology which AEP-Ohio asks the Commission to approve [so that AEP-Ohio can temporarily suspend the use of PJM Interconnection, LLC's ("PJM") Reliability Pricing Model ("RPM") – generally referred to as "RPM-Based Pricing" – during the period when it would lower electric bills] puts the public interest in the hands of a would-be monopoly that has heretofore deceived the Commission and most customers about the purpose and effects of its proposals. The

damage done to the reputation of the Commission following the Commission's reliance on AEP-Ohio to provide accurate information on the impact of the Stipulation and Recommendation ("Stipulation") submitted on September 7, 2011 in this proceeding is the type of lesson that caused Ohio to reject utility-massaged cost-based regulation in favor of the discipline of independently administered market-based approaches. IEU-Ohio urges the Commission to not let AEP-Ohio fool the Commission again.

For the Commission's use and consideration, IEU-Ohio's reply to the initial briefs follows. IEU-Ohio has focused its Reply Brief on the more fundamental contested legal and factual issues before the Commission in this proceeding. Any failure by IEU-Ohio to specifically address an issue or argument raised in the initial brief of another party should not be construed as agreement with such arguments.

II. POSITION OF THE PARTIES

The disputed issues in this proceeding are rather few. No party disputes that historically and prior to the adoption of the Stipulation in this proceeding, capacity available to a CRES provider serving retail customers in AEP-Ohio's distribution service area was priced based on the results of periodic capacity auctions conducted by PJM as part of its RPM which is contained in Attachment DD to PJM's tariff (beginning at page 2291)[1] and which is subject to the regulatory jurisdiction of the Federal Energy Regulatory Commission ("FERC"). This method of capacity pricing is known as RPM-Based Pricing.

[1] FES Ex. 110C. Attachment DD is contained in FES Ex. 110C; however, FES Ex. 110C is not a complete copy of the PJM Open Access Transmission Tariff. The Commission took administrative notice of the entire PJM Open Access Transmission Tariff. Tr. Vol. II at 446.

The uncontested evidence (with details contained in IEU-Ohio witness Murray's confidential Exhibit KMM-5) shows that AEP-Ohio or its affiliates have sold capacity into the PJM capacity market as a willing seller and obtained market-based compensation for such capacity.

All the briefs acknowledge that AEP-Ohio's so-called "embedded cost" pricing method would increase the capacity revenue that AEP-Ohio: (1) collects under the current "temporary" two-tiered scheme; (2) collected previously when RPM-Based Pricing was used beginning in 2007 and through 2011; and, (3) would collect in the future as compared to the known results of the RPM-Based Pricing method. In other words, there is agreement that AEP-Ohio has proposed an increase in rates.

No party claims that AEP-Ohio has satisfied the procedural or substantive requirements that must be satisfied before the Commission can authorize an increase in revenue through its traditional or cost-based ratemaking authority. No party has alleged that such traditional ratemaking authority applies to establish the price of capacity available to a CRES provider serving customers in AEP-Ohio's distribution service territory.

No party claims that AEP-Ohio has satisfied the criteria that the Commission has long applied to determine when, how and to what extent utility rates may be increased to avoid alleged financial harm. IEU-Ohio discussed these criteria at pages 37-39 and 44-45 of its Initial Brief.

All the parties agree that the capacity available to CRES providers serving customers in AEP-Ohio's distribution service area is a generation-related service.

No party claims that the provision of capacity to a CRES provider is a retail transaction.

The briefs acknowledge that AEP-Ohio is contesting the Commission's subject matter jurisdiction over CRES provider capacity pricing. And, IEU-Ohio is also contesting the Commission's authority to consider and act upon AEP-Ohio's CRES provider capacity pricing proposal on procedural and substantive grounds associated with Ohio's ratemaking requirements.

While AEP-Ohio attempts to hide from its commitment to not impose a generation-related lost revenue charge on shopping customers,[2] no party denies that AEP-Ohio made this commitment as part of the implementation process associated with Amended Substitute Senate Bill 3 ("SB 3"). No party denies that this commitment was subsequently incorporated into AEP-Ohio's [then Ohio Power Company ("OP") and Columbus Southern Power Company ("CSP")] rate stabilization plan ("RSP") that was approved by the Commission and in place from 2006 through the effective date of its first electric security plan ("ESP").[3]

No party claims that the opportunity for an electric distribution utility ("EDU") to seek and obtain transition revenue extended beyond the period provided by the electric transition plan ("ETP") process.

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[2] In the Federal Power Act ("FPA") Section 205 filing by American Electric Power Service Corporation ("AEPSC") on behalf of Indiana Michigan Power Company ("I&M"), AEPSC acknowledged that its proposed cost-based capacity price for competitive suppliers would be flowed through to shopping customers. *PJM Interconnection L.L.C.*, FERC Docket No. ER11-1173, AEPSC Transmittal Letter at 6 (Feb. 29, 2012) ("the "capacity charges ultimately will be recovered from retail customers.").

[3] *In the Matter of the Application of Columbus Southern Power Company and 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. 29, 2005).

No party asserts that Amended Substitute Senate Bill 221 ("SB 221") created a new opportunity to seek and obtain "transition revenue" or otherwise obtain compensation for any above-market generation-related asset value.

No party, except AEP-Ohio, opposes RPM-Based Pricing and AEP-Ohio voted for RPM-Based Pricing before it voted against it. And, AEP-Ohio is only proposing to place RPM-Based Pricing in storage until 2015 when it projects wholesale capacity prices will rise again. In effect, AEP-Ohio is only seeking to lock out RPM-Based Pricing when it is most clear that its "just and reasonable" capacity prices would help consumers reduce their electric bills. Thus, all the parties acknowledge, either explicitly or implicitly, that AEP-Ohio's on-again, off-again relationship with RPM-Based Pricing is opportunistically designed to provide AEP-Ohio with revenue based on the higher of RPM-Based Pricing or whatever other method AEP-Ohio is given the opportunity to invent.

No party claims that the default generation supply prices in AEP-Ohio's standard service offer ("SSO") are cost-based prices. Nonetheless, and based on what appears to be a collateral attack on prior Commission and Ohio Supreme Court holdings, AEP-Ohio's Initial Brief argues (and wrongly so) that AEP-Ohio was precluded in the past from going to market-based pricing. In effect, AEP-Ohio is claiming that its rewritten version of history requires the Commission to yield to AEP-Ohio's demand that the Commission authorize AEP-Ohio to uniquely block customers from getting to market in its distribution service area until AEP-Ohio is ready and willing to let it.

No party demonstrated that AEP-Ohio's owned and controlled generating assets are the Capacity Resources required by the PJM Reliability Assurance Agreement

("RAA") or that AEP-Ohio is, in accordance with the RAA, a Fixed Resource Requirement Entity ("FRR Entity"). Additionally, no party demonstrated that AEP-Ohio's owned and controlled generation assets are the source of any capacity made available to CRES providers serving customers within AEP-Ohio's distribution service territory. AEP-Ohio's pivotal witness, Dr. Pearce, just assumed, wrongly and with no foundation, that AEP-Ohio's owned and controlled generating assets are the source of any capacity made available to CRES providers for purposes of his proposed embedded cost-based pricing formula. Other AEP-Ohio witnesses and the witnesses of every other party who opined on this subject demonstrated that this assumption is irreconcilably in conflict with reality and confirmed that the Fixed Reliability Resource Alternative ("FRR Alternative") does not dedicate particular generating resources or Capacity Resources to load within a particular utility's service area. Thus, even if the Commission had authority to authorize AEP-Ohio to use a so-called cost-based method to set the CRES provider capacity price, AEP-Ohio's proposal fails on the applied side of its theory for want of AEP-Ohio's identification of the Capacity Resources that have been supplied to PJM in conjunction with the FRR Alternative.

No party claims that the RAA is subject to the Commission's jurisdiction or that the Commission has the authority to adjudicate questions regarding the rights and obligations under the RAA. No party claims that the pro-competitive purpose of the RAA is not properly set forth in Article 2 of the RAA or that the law of Delaware is not the governing law for purposes of the RAA.

No party identifies any portion of the RAA that calls for or otherwise promotes the use of embedded cost-based ratemaking. Indeed, the RAA (FES Ex. 110A) does not contain the words "embedded cost."

No party claims that the American Electric Power ("AEP") System Interconnection Agreement (often referred to as the AEP Pool Agreement) is subject to the Commission's jurisdiction or that the Commission has the authority to adjudicate questions regarding the rights and obligations under the AEP Pool Agreement.

The record shows beyond doubt that AEP-Ohio used RPM-Based Pricing to establish capacity prices for CRES providers while the current RAA and AEP Pool Agreement were in place and is still using RPM-Based Pricing for the first shopping tier of the temporary capacity pricing scheme that AEP-Ohio urged the Commission to approve when the same two-tiered scheme was struck down as part of the Stipulation. The record shows that affiliates of AEP-Ohio are using RPM-Based Pricing in their retail tariffs. AEP-Ohio's past and current conduct, as documented by the record evidence, shows the RAA and the AEP Pool Agreement are compatible with the use of RPM-Based Pricing. Indeed, the RAA specifically adopts RPM-Based Pricing as the means by which capacity compensation shall be established.

No party claims that AEP-Ohio did not become subject to Ohio's corporate separation requirements in 2000. No party claims that AEP-Ohio's status as an EDU entitles it to obtain relief from the Commission to uniquely advantage its generation business financial performance.

No party claims that AEP-Ohio, the EDU, competes to provide competitive retail electric services to customers located within its distribution service area.

No party questioned IEU-Ohio witness Murray regarding the information disclosure recommendations made at pages 33 to 34 of his prefiled testimony. Such recommendations were also not challenged by any party's brief. These recommendations are designed to bring some much needed transparency to AEP-Ohio's use of any form of CRES provider capacity pricing and to make sure that AEP-Ohio is not putting its thumb on the scales.

III. ARGUMENT

A. AEP-Ohio's Claims Regarding the Meaning of Schedule 8.1, Section D.8 of the RAA, are Contrary to the Plain Language of the RAA.

At page 13 of its Initial Brief, AEP-Ohio identifies the legal theory upon which it is claiming a unilateral right to establish compensation for CRES capacity that is cost-based. AEP-Ohio states that Schedule 8.1, Section D.8 of the RAA is the source of this right.

The RAA is an agreement or contract among Parties that was approved by FERC with the support of AEP-Ohio and its affiliates. The RAA was initially executed as of June 1, 2007 and the current parties to the RAA are set forth in Schedule 17. The "Whereas" provisions as well as the substantive content of the RAA make it clear that it is a mutual assistance agreement as explained by IEU-Ohio witness Murray.[4]

PJM has also described the RAA as a mutual assistance agreement:

> The RAA, with its roots in PJM's prior existence as a power pool, is an agreement among load serving entities to share a common capacity obligation across a broad region, and through that sharing to reduce the capacity burden that each would face on its own.[5]

[4] FES Ex. 110A at 4, 21; Tr. Vol. VI. at 1346-1348.

[5] IEU-Ohio Ex. 110 at 9.

Additionally, as IEU-Ohio has previously noted, Article 2 of the RAA expresses the region-wide scope and pro-competitive purpose of the RAA (emphasis added):

> This Agreement is intended to ensure that adequate Capacity Resources, including planned and Existing Generation Capacity Resources, planned and existing Demand Resources, Energy Efficiency Resources, and ILR will be planned and made available to provide reliable service to loads **within the PJM Region**, to assist other Parties during Emergencies and to coordinate planning of such resources consistent with the Reliability Principles and Standards. **Further, it is the intention and objective of the Parties to implement this Agreement in a manner consistent with the development of a robust competitive marketplace.** To accomplish these objectives, this Agreement is among all of the Load Serving Entities within the PJM Region. Unless this Agreement is terminated as provided in Section 3.3, every entity which is or will become a Load Serving Entity within the PJM Region is to become and remain a Party to this Agreement or to an agreement (such as a requirements supply agreement) with a Party pursuant to which that Party has agreed to act as the agent for the Load Serving Entity for purposes of satisfying the obligations under this Agreement related to the load within the PJM Region of that Load Serving Entity. Nothing herein is intended to abridge, alter or otherwise affect the emergency powers the Office of the Interconnection may exercise under the Operating Agreement and PJM Tariff.[6]

The RAA is governed by Delaware law and that means that if the Commission accepts AEP-Ohio's invitation to take up AEP-Ohio's claim regarding the meaning of the RAA, it will have to do so by applying Delaware law.[7] Relative to this legal reality, AEP-

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[6] FES Ex. 110A at 21.

[7] AEP-Ohio has not made any claims related to the meaning of Delaware law. In *Matria Healthcare, Inc. v. Coral SR LLC*, 2007 WL 763303 at *1, 6 (Del. Ch., March 1, 2007), the Delaware Chancery Court addressed fundamental contract interpretation principles under Delaware law.

> In construing contracts, the function of the Court is to ascertain the shared intentions of the contracting parties when they entered into their agreement. The first level of analysis is deceptively simple: give the words chosen by the parties their ordinary meaning. Disputes over a contract negotiated by sophisticated parties typically fall into three broad categories. First, the parties did not anticipate and provide for future events. Thus, the contract fails to address (or to address fully) the responsibilities of the parties in a particular factual setting. Second, the parties (or their lawyers) understand that there are drafting imperfections, perhaps because the parties cannot devise a mutually acceptable resolution to certain issues. The parties do not want what (at that time) are viewed as minor impediments to derail the transaction. They hope that the identified risks will not materialize and trust that, if the unlikely events occur, some judge will fill in the gaps in a

Ohio has been completely inattentive. AEP-Ohio's inattention to the requirements of the letter of the RAA may be related to the fact that the knowledge of AEP-Ohio's witness who addressed the RAA (Mr. Horton) was incomplete.[8]

The RAA is a multi-party agreement and any attempt to adjudicate the rights of any party to the agreement may affect the rights of other parties to the agreement.[9] Article 6 of the RAA states:

> Except as otherwise provided herein, this Agreement shall be managed and administered by the Parties, Members, and State Consumer Advocates through the Members Committee and the Markets and Reliability Committee as a Standing Committee thereof, except as delegated to the Office of the Interconnection and except that only the PJM Board shall have the authority to approve and authorize the filing of amendments to this Agreement with the FERC.[10]

> way that substantially preserves the benefits of the bargain for each side. Finally, there are disputes like the one now pending. The words, when fairly read and given their ordinary meaning, lead to a result that the Court cannot believe is what reasonable parties would have intended. In a sense, one party's argument boils down to a plea of: "We couldn't have been that obtuse (or worse)." The result reached here is, in large part, unpalatable; it is the product, however, of words chosen by sophisticated parties who drafted a complex and comprehensive agreement. More importantly, it is not for some judge to substitute his subjective view of what makes sense for the terms accepted by the parties.
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> * * *
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> When interpreting a contract, the Court's function is to "attempt to fulfill, to the extent possible, the reasonable shared expectations of the parties at the time they contracted." The Court does this by initially looking to the contract's express terms. If the terms are clear on their face and reasonably susceptible to only one meaning, then the Court gives those terms the meaning that would be ascribed to them by a reasonable third party. If, however, a contract's language is ambiguous, then the Court will look beyond the "four corners" of the agreement to extrinsic evidence. A contract is not ambiguous merely because the parties disagree as to its proper construction. Instead, ambiguity exists when the terms of a contract are reasonably susceptible to different interpretations or have two or more different meanings. Also, when possible, the Court should attempt to give effect to each term of the agreement and to avoid rendering a provision redundant or illusory. (internal citations omitted).

[8] Tr. Vol. II at 468-469.

[9] Ohio R. Civ. P. 19.

[10] FES Ex. 110A at 30.

In spite of all of this, AEP-Ohio claims "[t]he plain language of Schedule 8.1, Section D.8 of the RAA establishes AEP-Ohio's right to elect to charge a cost-based rate to CRES providers."[11] AEP-Ohio's claim regarding the meaning of this portion of the RAA is without merit. Schedule 8.1, Section D.8 of the RAA states:

> In a state regulatory jurisdiction that has implemented retail choice, the FRR Entity must include in its FRR Capacity Plan all load, including expected load growth, in the FRR Service Area, notwithstanding the loss of any such load to or among alternative retail LSEs. In the case of load reflected in the FRR Capacity Plan that switches to an alternative retail LSE, where the state regulatory jurisdiction requires switching customers or the LSE to compensate the FRR Entity for its FRR capacity obligations, such state compensation mechanism will prevail. In the absence of a state compensation mechanism, the applicable alternative retail LSE shall compensate the FRR Entity at the capacity price in the unconstrained portions of the PJM Region, as determined in accordance with Attachment DD to the PJM Tariff, provided that the FRR Entity may, at any time, make a filing with FERC under Sections 205 of the Federal Power Act proposing to change the basis for compensation to a method based on the FRR Entity's cost or such other basis shown to be just and reasonable, and a retail LSE may at any time exercise its rights under Section 206 of the FPA.[12]

AEP-Ohio specifically highlights a portion of the above language in support of its claimed meaning: "**provided that the FRR Entity may, *at any time*, make a filing with FERC under Sections 205 of the Federal Power Act proposing to change the basis for compensation to a method based on the FRR Entity's cost**."[13]

Like most contracts having regulatory significance, the RAA contains a definition section where "Agreement," "Capacity Resources," "Fixed Resource Requirement Alternative or FRR Alternative," "FRR Capacity Plan," "FRR Entity," "FRR Service Area," "IOU," "Load Serving Entity or LSE," "Party," "PJM Region," "Planning Period," "Self-

[11] AEP-Ohio Initial Brief at 13.

[12] FES Ex. 110A at 111.

[13] *Id*. (emphasis added); *see* AEP-Ohio Initial Brief at 14.

Supply,"[14] "State Regulatory Change" and other terms having significance for purposes of the RAA are defined.

Assuming for purposes of argument that the Commission could make determinations regarding the rights and obligations of parties to the RAA, the plain meaning of the above language makes it applicable, if at all, only to an FRR Entity and then only to the FRR Entity's Capacity Plan.

Is AEP-Ohio an FRR Entity?

No.

As the evidence in this proceeding demonstrates, and as admitted by AEP-Ohio, AEP-Ohio is not an FRR Entity. On cross-examination, Mr. Horton acknowledged that no evaluation of FRR status was conducted to determine if it was the best option for AEP-Ohio.[15] Rather, AEPSC is the FRR Entity as agent for the aggregated load of the combined AEP operating companies (including AEP-Ohio) known as AEP East.[16]

Has AEP-Ohio identified the FRR Capacity Plan to which the above-quoted plain language refers?

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[14] The RAA definition of Self-Supply incorporates the definition of Self-Supply that appears in Attachment DD (Section 2.65, page 2305) to PJM's FERC-approved tariff (emphasis added):

> "Self-Supply" shall mean Capacity Resources secured by a Load-Serving Entity, **by ownership or contract**, outside a Reliability Pricing Model Auction, and used to meet obligations under this Attachment or the Reliability Assurance Agreement through submission in a Base Residual Auction or an Incremental Auction of a Sell Offer indicating such Market Seller's intent that such Capacity Resource be Self-Supply. **Self-Supply may be either committed regardless of clearing price or submitted as a Sell Offer with a price bid. A Load Serving Entity's Sell Offer with a price bid for an owned or contracted Capacity Resource shall not be deemed "Self-Supply," unless it is designated as Self-Supply and used by the LSE to meet obligations under this Attachment or the Reliability Assurance Agreement.**

FES Ex. 110C at 2305.

[15] Tr. Vol. II at 493-494.

[16] *Id*. at 475-476; *see also* Tr. Vol. II at 436-437; Tr. Vol. XI at 2533-2534.

No.

Section 1.29 of the RAA defines "FRR Capacity Plan" as follows:

> FRR Capacity Plan shall mean a long-term plan for the commitment of Capacity Resources to satisfy the capacity obligations of a Party that has elected the FRR Alternative, as more fully set forth in Schedule 8.1 to this Agreement.[17]

Has AEP-Ohio identified the FRR Service Area that must be identified according to the above-quoted language?

No.

Section 1.31 of the RAA defines "FRR Service Area" as follows:

> FRR Service Area shall mean (a) the service territory of an IOU as recognized by state law, rule or order; (b) the service area of a Public Power Entity or Electric Cooperative as recognized by franchise or other state law, rule, or order; or (c) a separately identifiable geographic area that is: (i) bounded by wholesale metering, or similar appropriate multi-site aggregate metering, that is visible to, and regularly reported to, the Office of the Interconnection, or that is visible to, and regularly reported to an Electric Distributor and such Electric Distributor agrees to aggregate the load data from such meters for such FRR Service Area and regularly report such aggregated information, by FRR Service Area, to the Office of the Interconnection; and (ii) for which the FRR Entity has or assumes the obligation to provide capacity for all load (including load growth) within such area. In the event that the service obligations of an Electric Cooperative or Public Power Entity are not defined by geographic boundaries but by physical connections to a defined set of customers, the FRR Service Area in such circumstances shall be defined as all customers physically connected to transmission or distribution facilities of such Electric Cooperative or Public Power Entity within an area bounded by appropriate wholesale aggregate metering as described above.[18]

And on this subject, AEP-Ohio's witnesses agreed that PJM does not look to AEP-Ohio for purposes of the FRR election but to AEPSC as agent for the aggregated group of

[17] FES Ex. 110A at 10.

[18] *Id*. at 10-11.

the AEP East operating companies including AEP-Ohio.[19] So whatever the FRR Service Area is, it is clear from the record evidence that the FRR Service Area is not coextensive with AEP-Ohio's distribution service territory.

Has AEP-Ohio identified the FRR capacity obligation that is referenced in the above-quoted language?

No.

Does the plain meaning of the above-quoted language require any lawful state compensation mechanism to be cost-based?

No.

The word cost is not used in conjunction with the "state compensation mechanism" (regardless of whether defined as "embedded cost" or defined as "avoided cost," which would be more in keeping with the content of the RAA and other governing PJM documents).

Can a contract approved by FERC delegate authority to a state regulatory authority such as the Commission?[20]

No.

As explained in its answer to AEPSC's Section 206 Complaint, PJM correctly stated that any authority of the Commission to adopt a state compensation mechanism stems from Ohio law. At page 8 of its answer, PJM stated:

> Notably, although this provision [Section D.8 of Schedule 8.1] is more broadly worded than AEP would like, the RAA does not, indeed cannot, enlarge or contract a state commission's jurisdiction. While AEP contends that the Ohio Commission is improperly regulating wholesale transactions by setting a rate for AEP capacity in connection with retail load-switching,

[19] Tr. Vol. XI at 2533-2534.

[20] IEU-Ohio Ex. 110 at 8.

whether a state has exceeded its jurisdiction is not a matter that can be decided by reference to the RAA.[21]

Does the above-quoted provision from the RAA provide AEP-Ohio with the unilateral right to compensation for capacity that is based on AEP-Ohio's embedded cost?

No.

The above-quoted language permits an FRR Entity to seek a change in the method of compensation to a method that is based "… on the FRR Entity's cost or such other basis shown to be just and reasonable."[22]

If there is no Ohio state compensation mechanism (as AEPSC has repeatedly claimed at FERC), is AEP-Ohio entitled to impose an embedded cost-based capacity price on CRES providers?

No.

If there is no state compensation mechanism, RPM-Based Pricing controls unless or until FERC authorizes some other means of compensation.

The plain language of the RAA destroys the foundation of AEP-Ohio's claim that "… Schedule 8.1, Section D.8 of the RAA establishes AEP Ohio's right to elect to charge a cost-based rate to CRES providers."[23] Since AEP-Ohio has advanced no other legal theory to support its claimed unilateral right to use a so-called embedded cost method to set the CRES capacity price, the Commission's inquiry must end with a rejection of AEP-Ohio's claim. Even if the RAA is wrongly assumed to give AEP-Ohio the opportunity to prosecute such a claim, AEP-Ohio has failed to fill in the RAA blanks

[21] *Id.*

[22] FES Ex. 110A at 111.

[23] AEP-Ohio Initial Brief at 15.

with the information that the RAA requires to evaluate an FRR Entity's proposal to change the method of compensation for the FRR Entity's capacity obligation.

B. AEP-Ohio's Proposed Pricing Method Is Without Foundation and Does Not Identify the Cost of Satisfying the FRR Entity's Capacity Obligation.

AEP-Ohio argues that the formula rate recommended by AEP-Ohio witness Dr. Pearce is appropriate "because [AEP-Ohio] is self-supplying its own generation resources to satisfy these load obligations, the cost to provide this capacity is the *actual embedded capacity cost* of CSP's and OPCO's generation."[24] But Dr. Pearce made clear at page 5 of his direct testimony that he relied upon AEP-Ohio witnesses Munczinski and Horton for his statement that AEP-Ohio elected to utilize the FRR option as a predicate for his formula rate proposal. And the record evidence – including the admissions by Mr. Horton and Mr. Nelson – shows that: (1) AEP-Ohio did not make an FRR election for its distribution service area;[25] (2) no FRR election is associated uniquely with AEP-Ohio's distribution service area;[26] and, (3) AEP-Ohio's owned and controlled generating assets are not the source of capacity available to a CRES provider serving retail customers in AEP-Ohio's distribution service territory.[27]

Thus, Dr. Pearce's formula rate math has no relationship to reality even if: (1) AEP-Ohio had demonstrated that a change from RPM-Based Pricing is warranted based on the facts and law; and (2) The Commission had authority to adopt a cost-based pricing method for a competitive generation service.

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[24] *Id*. at 36 (emphasis in original).

[25] Tr. Vol. II at 429, 475; Tr. Vol. XI at 2530-2534.

[26] *Id*.

[27] *Id*. at 2530-2531, 2533; *see also* Tr. Vol. XI at 2543-2547.

As already discussed, the RAA itself dispels the notion that capacity anywhere in PJM, regardless of FRR or RPM status, is dedicated to specific customers or load. The RAA is a mutual assistance agreement through which Capacity Resources are shared on a region-wide basis within PJM. Schedule 8.1.A dealing with the FRR Alternative makes this clear as well (emphasis added):

> The Fixed Resource Requirement ("FRR") Alternative provides an alternative means, under the terms and conditions of this Schedule, for an eligible Load-Serving Entity to satisfy its obligation hereunder to commit Unforced Capacity **to ensure reliable service to loads in the PJM Region**.[28]

Schedule 8.1.B.2 of the RAA does permit a Party to elect the FRR Alternative for a portion of its load within the PJM Region but a partial FRR Alternative election triggers specific requirements:

> A Party eligible under B.1 above may select the FRR Alternative only as to all of its load in the PJM Region; provided however, that a Party may select the FRR Alternative for only part of its load in the PJM Region if (a) the Party elects the FRR Alternative for all load (including all expected load growth) in one or more FRR Service Areas; (b) the Party complies with the rules and procedures of the Office of the Interconnection and all relevant Electric Distributors related to the metering and reporting of load data and settlement of accounts for separate FRR Service Areas; and (c) the Party separately allocates its Capacity Resources to and among FRR Service Areas in accordance with rules specified in the PJM Manuals.[29]

Section 1.67 of the RAA defines PJM Region as follows:

> PJM Region shall have the same meaning as provided in the Operating Agreement.[30]

Section 1.35A of the PJM Operating Agreement[31] defines PJM Region as follows (emphasis added):

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[28] FES Ex. 110A at 106 (emphasis added).

[29] *Id*. at 107.

[30] *Id*. at 15.

> "PJM Region" shall mean **the aggregate of** the MAAC Control Zone, the PJM West Region, and VACAR Control Zone.

AEP-Ohio has not claimed that a partial FRR Alternative election was made. AEP-Ohio did not offer any evidence showing that the FRR Alternative was uniquely elected for the AEP-Ohio distribution service area.[32]

The fact that PJM treats Capacity Resources as a PJM Region resource was also acknowledged by several AEP-Ohio witnesses. During his cross-examination, Mr. Horton agreed that PJM has a call on AEP-Ohio's owned and controlled generating assets and will dispatch them as necessary to serve load anywhere in PJM's footprint:

> Q. I'm talking about reliability and who has a call on those generating assets to maintain reliability. Am I correct, sir, that PJM can direct AEP to run all of its generating assets in order to solve reliability issues outside AEP's service area?
>
> A. They can request AEP do that, go to max -- maximum generation capacity.
>
> Q. And that has happened; is that correct?
>
> A. Yes.
>
> Q. And AEP has followed PJM's instructions in those circumstances, correct?
>
> A. To my knowledge we have done everything possible to meet PJM's direction.[33]

On a day-to-day basis, the output of all the generating assets of the AEP East operating companies (including AEP-Ohio) are bid into PJM's market by AEPSC with an

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[31] PJM Operating Agreement at 22. The PJM Operating Agreement is available *via* the internet at: http://www.pjm.com/documents/~/media/documents/agreements/oa.ashx.

[32] Tr. Vol. II at 476.

[33] *Id*. at 484-485.

offer price.[34] On a system-wide basis, PJM then determines which resources are actually dispatched to serve load in the PJM Region.[35]

On any given day, AEP-Ohio's actual load requirements are not required to be satisfied from AEP-Ohio's owned and controlled generating assets.[36] The operation of AEP-Ohio's "deregulated"[37] generating assets cannot be separated from the operation of the combined generation fleet of the AEP East operating companies.[38] On an after-the-fact basis, allocations are performed to attribute generation output to off-system sales.[39] It is impossible to simulate a dispatch of the AEP-Ohio owned or controlled generating assets without performing a dispatch for the entire AEP system.[40]

AEP-Ohio witness Nelson, as well as other AEP-Ohio and intervenor witnesses, testified that the demand response capability of AEP-Ohio's retail customers can be used as Capacity Resources to satisfy the capacity obligation of the FRR Entity.[41] Again, AEP-Ohio did not introduce its FRR Capacity Plan so the exact resources relied upon are not known. So, Dr. Pearce's exclusive reliance on costs he attributed to AEP-Ohio's generating plants is not consistent with reality or the definition of Capacity Resources in the RAA. Even if Dr. Pearce would have offered a formula rate proposal that looked to the entire fleet of the AEP East operating companies' generating assets, it would still be out of touch with reality because PJM relies upon Capacity Resources for

[34] Tr. Vol. XI at 2544-2545.

[35] *Id*.

[36] *Id*. at 2546-2547.

[37] *Id*. at 2536-2537.

[38] *Id*. at 2545-2547.

[39] *Id*. at 2547-2550.

[40] *Id*. at 2545-2547.

[41] *See e.g.*, Tr. Vol. XI at 2531.

the entire PJM Region and Capacity Resources includes both demand and supply side Capacity Resources, not just generating plants.

As already discussed, the RAA calls for an FRR Entity to submit an FRR Capacity Plan. The RAA defines the FRR Capacity Plan as follows:

> FRR Capacity Plan shall mean a long-term plan for the commitment of Capacity Resources to satisfy the capacity obligations of a Party that has elected the FRR Alternative, as more fully set forth in Schedule 8.1 to this Agreement.[42]

Assuming for a moment that AEP-Ohio was actually engaged in the kind of "Self-Supply" of Capacity Resources as is permitted under the RAA, Schedule 7 of the RAA would apply. Schedule 7 of the RAA states as follows (emphasis added):

SCHEDULE 7

PLANS TO MEET OBLIGATIONS

A. Each Party that elects to meet its estimated obligations for a Delivery Year by Self-Supply of Capacity Resources shall notify the Office of the Interconnection via the Internet site designated by the Office of the Interconnection, prior to the start of the Base Residual Auction for such Delivery Year.

B. A Party that Self-Supplies Capacity Resources to satisfy its obligations for a Delivery Year **must submit a Sell Offer as to such resource in the Base Residual Auction for such Delivery Year, in accordance with Attachment DD to the PJM Tariff**.

C. If, at any time after the close of the Third Incremental Auction for a Delivery Year, including at any time during such Delivery Year, a Capacity Resource that a Party has committed as a Self-Supplied Capacity Resource becomes physically incapable of delivering capacity or reducing load, the Party may submit a replacement Capacity Resource to the Office of the Interconnection. Such replacement Capacity Resource (1) may not be previously committed for such Delivery Year, (2) shall be capable of providing the same quantity of megawatts of capacity or load reduction as the originally committed Capacity Resource, and (3) shall meet the

[42] FES Ex. 110A at 10.

> same locational requirements, if applicable, as the originally committed resource. In accordance with Attachment DD to the PJM Tariff, the Office of the Interconnection shall determine the acceptability of the replacement Capacity Resource.[43]

Accordingly, satisfaction of the Capacity Resource obligation established by the RAA through Self-Supply calls for the submission of a sell offer in the Base Residual Auction ("BRA"). In other words, the Self-Supply option is only available to LSE's participating in the RPM BRA, and as AEP-Ohio has repeatedly stated, its legal theory relates only to the FRR Alternative. Thus, the Self-Supply RPM-market option defined in the RAA is mutually exclusive from the Capacity Resources that are designated as part of the FRR Entity's FRR Capacity Plan. AEP-Ohio cannot be an FRR Entity and "Self-Supply" Capacity Resources.

Thus, Dr. Pearce's threshold assumptions – that AEP-Ohio is an FRR Entity and that AEP-Ohio's owned and controlled generating assets are the source of capacity provided to a CRES provider serving retail customers in AEP-Ohio's distribution service territory – are wrong. Because these threshold assumptions are wrong, the mathematical computations embedded in Dr. Pearce's proposed formula rate therefore cannot identify any type of cost of capacity provided to a CRES provider serving retail customers in AEP-Ohio's distribution service territory. Because of the fundamental errors made by Dr. Pearce, the Staff's recommended energy credit adjustment to Dr. Pearce's computation of a per megawatt-day ("MW-day") price is a victim of the defects in Dr. Pearce's assumptions and his assumption-driven math.

Since Mr. Kollen's alternative recommendation also assumes that AEP-Ohio's generating assets are being used to provide capacity to a CRES provider serving retail

[43] *Id.* at 101 (emphasis added).

customers in AEP-Ohio's distribution service territory, his alternative recommendation is also disconnected from reality.

Had AEP-Ohio actually been Self-Supplying Capacity Resources or had it actually been a stand-alone FRR Entity, it would have been a simple matter for AEP-Ohio to have identified the FRR Capacity Plan or the Self-Supply resources that it is relying on to meet the RAA obligations. AEP-Ohio did not do so. Instead, it resorted to false assumptions and then embedded the false assumptions in the math associated with a proposed mathematical formula that pulls garbage in and pushes garbage out.

Even if the Commission had authority to permit AEP-Ohio to change from RPM-Based Pricing to a cost-based method for establishing the price for capacity available to a CRES provider serving retail customers in AEP-Ohio's distribution service territory, and even if AEP-Ohio had demonstrated that its proposed temporary deviation from RPM-Based Pricing is warranted during the period when such deviation would block consumers from securing lower electric bills, the so-called embedded cost-based formula rate proposed by AEP-Ohio is based on bankrupt assumptions and numerical inputs that are wrong.

As already mentioned, the defects in Dr. Pearce's proposal are also embedded in the starting point for the Staff's adjustments to Dr. Pearce's results and in OEG witness Kollen's alternative equity return guarantee mechanism which relies on AEP-Ohio's FERC Form 1 data. FES' alternate approach is similarly flawed in that it is based on the assumption that generation assets owned by AEP-Ohio supply capacity to CRES providers. It is important to note, however, that Staff, OEG, and FES all assert that RPM-Based Pricing is the appropriate capacity pricing method and defects in their

alternatives have no impact on their primary recommendation that the Commission continue the use of RPM-Based Pricing.

Thus, no party has presented a reliable cost-based method for establishing a just and reasonable price for capacity available to a CRES provider serving retail customers in AEP-Ohio's distribution service territory.

C. AEP-Ohio's Claim that it was Not Allowed to Move to Market-Based Rates is Baseless; AEP-Ohio Charged Market-Based Rates Under its RSP, Under its Agreement to Serve Former Monongahela Power Company Customers, and Under its Agreement to Serve Ormet.

In its Initial Brief, AEP-Ohio repeats claims that it has made in Commission proceedings and elsewhere to suggest that AEP-Ohio was not fairly treated in the past and this past unfair treatment legitimizes its campaign to secure an unfair advantage for AEP-Ohio's generation business function. But, AEP-Ohio's recounting of history is wrong.

The Commission did not prevent AEP-Ohio from charging market rates following the end of AEP-Ohio's market development period ("MDP"). Under SB 3, there were two mandatory pricing options for default generation supply once the MDP period ended. The first required that:

> [a]fter its market development period, an electric distribution utility in this state shall provide consumers, on a comparable and nondiscriminatory basis within its certified territory, a market-based standard service offer of all competitive retail electric services necessary to maintain essential electric service to consumers, including a firm supply of electric generation service.[44]

[44] *Ohio Consumers' Counsel v. Pub. Util. Comm.*, 109 Ohio St.3d 328, 2006-Ohio-2110 at ¶ 15 (*quoting* former Section 4928.14(A), Revised Code (replaced by SB 221)).

The Commission specifically held that generation pricing under this provision, former Section 4928.14(A), Revised Code, as applied to AEP-Ohio was market-based.[45] The Commission also held that pricing under this Section 4928.14(A), Revised Code, for other EDUs was market-based and in compliance with the law.[46] The Ohio Supreme Court upheld the Commission's determination that rates approved under former Section 4928.14(A), Revised Code, were in fact market-based.[47] AEP-Ohio's RSP contained this first option and, thus, as required by SB 3 and determined by the Commission, AEP-Ohio's RSP rates were market-based.

The second post-MDP default generation supply pricing mechanism called for by SB 3 and, more specifically, former Section 4928.14(B), Revised Code, provided that:

> [a]fter that market development period, each electric distribution utility also shall offer customers within its certified territory an option to purchase competitive retail electric service the price of which is determined through a competitive bidding process. … The commission may determine at any time that a competitive bidding process is not required, if other means to accomplish generally the same option for customers is readily available in

[45] "[W]e conclude that the generation rates that we approve in this RSP today will constitute an appropriate market-based standard service offer, as required by Section 4928.14(A), Revised Code." *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of a Post-Market Development Period Rate Stabilization Plan*, Case No. 04-169-EL-UNC, Opinion and Order at 14 (Jan. 26, 2005).

[46] *In the Matter of the Continuation of the Rate Freeze and Extension of the Market Development Period for The Dayton Power and Light Company*, Case Nos. 02-2779-EL-ATA, *et al.*, Opinion and Order at 26-27 (Sept. 2, 2003); *Ohio Consumers' Counsel v. Pub. Util. Comm.*, 111 Ohio St.3d 300, 2006-Ohio-5789 at ¶ 42.

[47] *Ohio Consumers' Counsel v. Pub. Util. Comm.*, 111 Ohio St.3d 300, 2006-Ohio-5789 at ¶ 44. Additionally, in the Commission's Order on Remand in Duke Energy Ohio, Inc.'s RSP, the Commission further expanded on what it meant when it held rates under Section 4928.14(A), Revised Code, were market-based: "a market-based standard service offer price is not the same as a deregulated price. … Thus, while a standard service offer price need not reflect the sum of specific cost components, the result must produce reasonably priced retail electric service, avoid anticompetitive subsidies flowing from noncompetitive to competitive services, be consistent with protecting consumers from market deficiencies and market power, and meet other statutory requirements." *In the Matter of the Application of The Cincinnati Gas & Electric Company to Modify its Nonresidential Generation Rates to Provide for Market-Based Standard Service Offer Pricing and to Establish an Alternative Competitive-Bid Service Rate Option Subsequent to the Market Development Period*, Case Nos. 03-93-EL-ATA, *et al.*, Order on Remand at 37 (Oct. 24, 2007).

> the market and a reasonable means for customer participation is developed.[48]

When AEP-Ohio (then CSP and OP) filed its proposed RSP, it requested that the Commission waive the CBP option.[49] Thus, it was AEP-Ohio that initially sought to avoid making the CBP option available to consumers as required by SB 3.

The Commission approved AEP-Ohio's proposed RSP, without the CBP option.[50] OCC appealed the Commission's approval of AEP-Ohio's request to omit the CBP option to the Ohio Supreme Court, which vacated and remanded the Commission's exclusion of the CBP option.[51]

On remand, the Commission directed AEP-Ohio to file an application to implement the CBP required by Section 4928.14(B), Revised Code. In response, AEP-Ohio proposed two CBP options, one available to all customers and one for customers who wanted to purchase "green energy."[52] AEP-Ohio's proposal made no mention of any need to terminate the AEP Pool Agreement prior to making the CBP option available. AEP-Ohio eventually settled the remand case by dropping the portion of its proposal that would have made the CBP option available to all customers.[53]

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[48] *Ohio Consumers' Counsel v. Pub. Util. Comm.*, 109 Ohio St.3d 328, 2006-Ohio-2110 at ¶ 15 (*quoting* former Section 4928.14(B), Revised Code (replaced by SB 221)).

[49] *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of a Post-Market Development Period Rate Stabilization Plan*, Case No. 04-169-EL-UNC, Opinion and Order at 11 (Jan. 26, 2005).

[50] *Id.* at 14.

[51] *Ohio Consumers' Counsel v. Pub. Util. Comm.*, 109 Ohio St.3d 511, 2006-Ohio-3054 (*citing Ohio Consumers' Counsel v. Pub. Util. Comm.*, 109 Ohio St.3d 328, 2006-Ohio-2110, 847 N.E.2d 1184).

[52] *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of Their Plan to Provide Additional Options for Customer Participation in the Electric Market*, Case No. 06-1153-EL-UNC, Application (Sept. 22, 2006).

[53] *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of Their Plan to Provide Additional Options for Customer Participation in the Electric Market*, Case No. 06-1153-EL-UNC, Order on Remand (May 2, 2007).

Although AEP-Ohio claims otherwise, AEP-Ohio's RSP permitted AEP-Ohio to establish market-based rates for default generation supply under former Section 4928.14(A), Revised Code, and as AEP-Ohio proposed. Also, it was AEP-Ohio, not the Commission or any other party, that proposed to avoid offering the CBP option.

Beyond the market-based rates that AEP-Ohio began charging for its post-MDP default generation supply as a result of its RSP, AEP-Ohio sought and obtained authority to base portions of its default generation supply costs on competitive solicitations and to recover this market-based cost from retail customers.

After acquiring the Monongahela Power Company's ("MP") Ohio service territory, AEP-Ohio proposed and the Commission authorized AEP-Ohio to conduct a Request for Proposals ("RFP") for the generation supply that AEP-Ohio said it needed to meet the default supply needs of the former MP customers.[54] The Commission then authorized AEP-Ohio to collect the market-based generation supply costs.[55] Thus, when AEP-Ohio requested, in the case of the former MP customers, the Commission authorized AEP-Ohio to recover default generation supply costs based on market prices.

Finally, when AEP-Ohio's service territory was modified in 2005 to include Ormet Primary Aluminum Corporation and Ormet Aluminum Mill Products Corp. ("Ormet"), AEP-Ohio was again granted market-based compensation for the default generation supply costs associated with Ormet's load.[56] In December 2006, AEP-Ohio filed an

[54] *In the Matter of the Transfer of Monongahela Power Company's Certified Territory in Ohio to the Columbus Southern Power Company*, Case No. 05-765-EL-UNC, Opinion and Order at 14-17 (Nov. 9, 2005).

[55] *Id.* at 15-18.

[56] *In the Matter of the Complaint of Ormet Primary Aluminum Corporation and Ormet Aluminum Mill Products Corporation*, Case No. 05-1057-EL-CSS, Supplemental Opinion and Order at 5 (Nov. 8, 2006).

application to set the 2007 market price for the default generation supply for Ormet, indicating a market price of $47.69/MWh,[57] which the PUCO approved on June 27, 2007.[58] Then, in December 2007, AEP-Ohio filed a second application the set the market price for the Ormet default generation supply, indicating the market had increased to $53.03/MWh. In this second application, AEP-Ohio used RPM-Based Pricing to establish the capacity portion of the default generation supply price since the RAA had gone into effect in June 2007.[59] The capacity price included in this second filing by AEP-Ohio was $40.69/MW-day;[60] a capacity price which is not dramatically different than the RPM-Based Price that was scheduled to become effective on June 1, 2012. The Commission again approved AEP-Ohio's application to establish a market-based default generation supply cost for Ormet, which was based in part on RPM-Based Pricing.

AEP-Ohio's post-MDP proposals and pleadings, the Commission's orders and related Ohio Supreme Court decisions show that the statements that are made at page 106 through 111 of AEP-Ohio's Initial Brief are wrong.

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[57] *Columbus Southern Power Company's and Ohio Power Company's Application to Set the 2007 Generation Market Price for Ormet's Hannibal Facilities*, Case No. 06-1504-EL-UNC, Columbus Southern Power Company's and Ohio Power Company's Ormet-Related 2007 Generation Market Price Submission at 1 (Dec. 26, 2006).

[58] *Columbus Southern Power Company's and Ohio Power Company's Application to Set the 2007 Generation Market Price for Ormet's Hannibal Facilities*, Case No. 06-1504-EL-UNC, Finding and Order at 2-3 (June 27, 2007).

[59] *Columbus Southern Power Company's and Ohio Power Company's Application to Set the 2008 Generation Market Price for Ormet's Hannibal Facilities*, PUCO Case No. 07-1317-EL-UNC, Columbus Southern Power Company's and Ohio Power Company's Ormet-Related 2008 Generation Market Price Submission at 1 (Dec, 27, 2007). The PUCO approved the 2008 market price on December 10, 2008.

[60] *Id*., Attachment E.

The Commission did not "deliberate[ly] … move AEP Ohio slowly into competition;"[61] the Commission moved largely at the pace proposed by AEP-Ohio and in ways that allowed AEP-Ohio to generate significantly excessive earnings for its service area while its affiliates were obtaining market share in other service areas based on RPM-Based Pricing.

AEP-Ohio's assertion that "the Commission found a competitive bidding process would not be effective"[62] is also misleading. AEP-Ohio itself chose not to include a CBP as part of its RSP. When given a second chance on remand to include a CBP for all of its SSO customers, AEP-Ohio again presented the Commission with a stipulation without this option, which the Commission approved at AEP-Ohio's request.[63]

D. Contrary to RESA's Claim, the Commission's General Supervisory Authority Does Not Provide the Commission with Unlimited Powers to Approve Rates.

As identified in IEU-Ohio's Initial Brief, the Commission's supervisory powers are generally unavailable for ratemaking purposes.[64] The Ohio Supreme Court has held that the Commission cannot use its general supervisory powers to bypass the ratemaking process that the General Assembly has developed and which is contained elsewhere in Title 49 of the Revised Code. In reviewing whether the seemingly broad grant of authority contained in Section 4901.02 Revised Code, provided the

[61] AEP-Ohio Initial Brief at 107.

[62] *Id.* at 108.

[63] *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of Their Plan to Provide Additional Options for Customer Participation in the Electric Market*, Case No. 06-1153-EL-UNC, Order on Remand (May 2, 2007).

[64] *Utility Serv. Partners, Inc. v. Pub. Util. Comm.*,124 Ohio St.3d 284, 2009-Ohio-6764 at ¶ 12; *Cincinnati N.O. & T.P. Ry. Co. v. Public Utilities Commission*, 31 Ohio St.2d 81, 86 ("The Public Utilities Commission has plenary power under R.C. 4905.04 to promulgate and enforce orders relating to the protection, welfare and safety of railroad employees.").

Commission with independent authority to establish rates outside the Commission's traditional ratemaking process, the Court held:

> [t]he comprehensive ratemaking formula provided by the General Assembly is meant to protect and balance the interests of the public utilities and their ratepayers alike. *Dayton Power & Light Co. v. Pub. Util. Comm., supra,* 4 Ohio St.3d 91, 4 OBR 341, 447 N.E.2d 733. We cannot conclude that it was the General Assembly's intent under the above enabling statute, R.C. 4901.02(A), to permit the PUCO to disregard *that very formula* in instances in which it simply did not agree with the result Cf. *Consumers' Counsel, supra,* 67 Ohio St.2d at 165, 21 O.O.3d at 104, 423 N.E.2d at 828 ("the General Assembly undoubtedly did not intend to build into its recently revised [1976] ratemaking formula a means by which the PUCO may effortlessly abrogate that very formula").[65]

Although, in this instance RESA suggests that the Commission has authority under Sections 4905.04,[66] 4905.05, and 4909.06,[67] Revised Code, instead of the Section analyzed by the Court above, the same principles apply.

The General Assembly has established specific statutory requirements that the Commission must follow to authorize rates and charges for competitive and non-competitive retail electric services. These specific requirements may not be bypassed based on the Court's decision in the *Columbus Southern Power Company* case quoted above. Thus, RESA's argument that the Commission's general investigatory powers

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[65] *Columbus S. Power Co. v. Pub. Util. Comm.,* 67 Ohio St.3d 535, 620 N.E.2d 835, 840 (1993).

[66] "The public utilities commission is hereby vested with the power and jurisdiction to supervise and regulate public utilities and railroads, to require all public utilities to furnish their products and render all services exacted by the commission or by law … ." Section 4905.04, Revised Code.

[67] "The public utilities commission has general supervision over all public utilities within its jurisdiction as defined in section 4905.05 of the Revised Code, and may examine such public utilities and keep informed as to their general condition, capitalization, and franchises, and as to the manner in which their properties are leased, operated, managed, and conducted with respect to the adequacy or accommodation afforded by their service, the safety and security of the public and their employees, and their compliance with all laws, orders of the commission, franchises, and charter requirements. … The commission, through the public utilities commissioners or inspectors or employees of the commission authorized by it, may enter in or upon, for purposes of inspection, any property, equipment, building, plant, factory, office, apparatus, machinery, device, and lines of any public utility. The power to inspect includes the power to prescribe any rule or order that the commission finds necessary for protection of the public safety." Section 4905.06, Revised Code.

under Sections 4905.04, 4905.05, and 4909.06, Revised Code, give it authority to approve a pricing method for capacity made available to a CRES provider serving retail customers in AEP-Ohio's distribution service area is without merit.

E. RESA's Claim that Section 4928.143(B)(2)(d), Revised Code, Gives the Commission Authority to Approve a CRES Capacity Pricing Method is Without Merit.

RESA boldly claims[68] that AEP-Ohio's CRES capacity charge is for a service identified in Section 4928.141, Revised Code, and that the Commission may authorize a charge for such service under Section 4928.143(B)(2)(d), Revised Code (the ESP Statute). RESA's argument ignores the plain meaning of the law.

Section 4928.141, Revised Code, deals with SSO pricing for services provided to ultimate consumers, not the provision of capacity to CRES suppliers pursuant to the RAA, a FERC-approved agreement. This proceeding is not an SSO proceeding and no evidence has been presented to meet the statutory criteria that must be satisfied before the Commission can approve, modify and approve, or reject an SSO.

Second, AEP-Ohio's proposed capacity pricing method is not within the list of terms that can be approved under Section 4928.143, Revised Code. That Section authorizes items that may be included under an SSO in the form of an ESP. Establishment of a capacity pricing method for CRES providers is not on the list of items that may be included in an ESP. If CRES capacity pricing was on the list in some fashion, the Commission still could not approve the ESP unless it determined that the ESP is better, in the aggregate, for consumers. Because AEP-Ohio's proposed capacity pricing method produces a wholesale price which is billed by PJM to CRES

[68] RESA's Initial Brief at 9.

providers who serve shopping customers in AEP-Ohio's distribution service area, it is not an essential service related to serving an SSO customer.

Moreover, Section 4928.141, Revised Code, prohibits an EDU from including in its SSO transition costs.[69] Thus, even if this case could be construed as an ESP proceeding, AEP-Ohio's capacity pricing method could not be approved because it would provide AEP-Ohio with another opportunity to collect transition revenue.

For these reasons, RESA's assertion that the Commission can consider and approve AEP-Ohio's proposed capacity pricing method in this proceeding under Section 4928.143(B)(2)(d), Revised Code is incorrect.

F. AEP-Ohio's Claims About the Effect of RPM-Based Pricing on the Financial Condition of its Generation Business Are Irrelevant.

Throughout this process, AEP-Ohio has repeatedly claimed that continued use of the RPM-Based Pricing method it previously supported will negatively affect the financial condition of its generation business which was supposed to be on its own in the competitive market by the end of 2010. The Commission has previously held that the financial results of generation-related pricing are irrelevant.

In OP's and CSP's RSP, automatic annual generation-related increases of 3% (CSP) and 7% (OP) were proposed for three years. The automatic increases were opposed by several parties.[70] These parties argued that the Commission should reject the proposed annual automatic generation-related increases because the EDUs were already earning healthy returns on common equity and the increases would simply

[69] As explained in IEU-Ohio's Initial Brief at 47-50, AEP-Ohio's proposed charge would be a transition charge.

[70] *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of a Post-Market Development Period Rate Stabilization Plan*, Case No. 04-169-EL-UNC, Opinion and Order at 15, 18 (Jan. 26, 2005).

increase those returns. In response, the Commission rejected the intervenors' objections, stating that market prices and not earnings determine the prices for generation-related services.

> [w]ith the expiration of the MDP, generation rates are subject to the market (not the Commission's traditional cost-of-service rate regulation) … Section 4928.05(A)(1), Revised Code. *We make this observation to point out that, under the statutory scheme, company earnings levels would not come into play for establishing generation rates - market tolerances would otherwise dictate, just as AEP argued (AEP Reply Br. 26-27)*. We are strongly committed to encouraging the competitive market in AEP's service territories as it is the policy of this state, per Section 4928.02, Revised Code. Given that commitment, we do not feel that the earnings levels evidence or cost-based analyses and arguments presented by [the intervenors] justify rejection of this provision.[71]

As the above quote documents, AEP-Ohio has previously and successfully urged the Commission to ignore the financial effects of changes in generation-related prices. In this proceeding, AEP-Ohio has reversed course and is now claiming that the Commission should displace the RPM-Based Pricing method with a method that is largely driven by AEP-Ohio's desire to maintain earnings for its generation business.

Based on Commission precedent, the potential effects of RPM-Based Pricing on the financial condition of AEP-Ohio's generation business is irrelevant.

IV. CONCLUSION

For the reasons discussed herein, IEU-Ohio again urges the Commission to dismiss AEP-Ohio's proposal to change the method of compensation for capacity made available to a CRES provider serving customers in AEP-Ohio's distribution service territory. Even assuming that the Commission has the authority to consider and approve AEP-Ohio's proposal in this proceeding, AEP-Ohio's claim that it has the

[71] *Id*. at 18 (emphasis added).

unilateral right to establish a formula rate tied to FERC Form 1 data pursuant to Schedule 8.1, Section D.8 of the RAA, is meritless.

Additionally, as discussed above and in IEU-Ohio's Initial Brief, the Commission must direct AEP-Ohio to provide details to customers and CRES providers showing how the peak load contribution ("PLC") factor it is assigning to customers corresponds with the customers' PLC value recognized by PJM. Requiring AEP-Ohio to provide this information creates a transparent process; however, without such information there is no way to ensure that capacity compensation is being properly applied to shopping and non-shopping customers. The need for this detail exists regardless of the method by which a CRES capacity price is established.

Respectfully submitted,

/s/ Matthew R. Pritchard

Samuel C. Randazzo (Counsel of Record)
Frank P. Darr
Joseph E. Oliker
Matthew R. Pritchard
MCNEES WALLACE & NURICK LLC
21 East State Street, 17TH Floor
Columbus, OH 43215
sam@mwnmch.com
fdarr@mwncmh.com
joliker@mwncmh.com
mpritchard@mwncmh.com

Attorneys for Industrial Energy Users-Ohio

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing *Industrial Energy Users-Ohio's Reply Brief* was served upon the following parties of record this 30th day of May 2012, *via* electronic transmission, hand-delivery or first class U.S. mail, postage prepaid.

/s/ Matthew R. Pritchard
Matthew R. Pritchard

Steven T. Nourse
Matthew J. Satterwhite
Yazen Alami
American Electric Power Service Corporation
1 Riverside Plaza, 29th Floor
Columbus, OH 43215
stnourse@aep.com
mjsatterwhite@aep.com
yalami@aep.com

Daniel R. Conway
Christen M. Moore
Porter Wright Morris & Arthur
Huntington Center
41 S. High Street
Columbus, OH 43215
dconway@porterwright.com
cmoore@porterwright.com

Derek Shaffer
Quinn Emanuel Urquhart & Sullivan, LLP
1299 Pennsylvania Avenue, NW, Suite 825
Washington, DC 20004
derekshaffer@quinnemanuel.com

COUNSEL FOR COLUMBUS SOUTHERN POWER COMPANY AND OHIO POWER COMPANY

David F. Boehm, Esq.
Michael L. Kurtz, Esq.
Boehm, Kurtz & Lowry
36 East Seventh Street, Suite 1510
Cincinnati, OH 45202
dboehm@BKLlawfirm.com
mkurtz@BKLlawfirm.com

COUNSEL FOR THE OHIO ENERGY GROUP

Kyle L. Kern, Counsel of Record
Melissa R. Yost
Assistant Consumers' Counsel
Office of the Ohio Consumers' Counsel
10 West Broad Street, Suite 1800
Columbus, OH 43215-3485
kern@occ.state.oh.us
yost@occ.state.oh.us

COUNSEL FOR THE OFFICE OF THE OHIO CONSUMERS' COUNSEL

Lisa McAlister
Thomas J. O'Brien
Bricker & Eckler LLP
100 South Third Street
Columbus, OH 43215
lmcalister@bricker.com
tobrien@bricker.com

COUNSEL FOR THE OHIO MANUFACTURERS' ASSOCIATION

Richard L. Sites
General Counsel & Senior Director of Health Policy
Ohio Hospital Association
155 E. Broad Street, 15th Floor
Columbus, OH 43215-3620
ricks@ohanet.org

Thomas J. O'Brien
Bricker & Eckler LLP
100 South Third Street
Columbus, OH 43215
tobrien@bricker.com

COUNSEL FOR OHIO HOSPITAL ASSOCIATION

M. Howard Petricoff
Stephen M. Howard
Lija Kaleps-Clark
Vorys, Sater, Seymour and Pease LLP
52 East Gay Street
PO Box 1008
Columbus OH 43216-1008
mhpetricoff@vorys.com
smhoward@vorys.com
lkalepsclark@vorys.com

COUNSEL FOR DIRECT ENERGY SERVICES, LLC AND DIRECT ENERGY BUSINESS, LLC AND CONSTELLATION NEWENERGY, INC. AND CONSTELLATION ENERGY COMMODITIES GROUP, INC., RETAIL ENERGY SUPPLY ASSOCIATION

Mark A. Hayden
FirstEnergy Service Company
76 South Main Street
Akron, OH 44308
haydenm@firstenergycorp.com

John N. Estes III
Paul F. Wight
Skadden, Arps, Slate, Meagher
& Flom LLP
1440 New York Avenue, N.W.
Washington, DC 20005
john.estes@skadden.com
paul.wight@skadden.com

James F. Lang
Laura C. McBride
N. Trevor Alexander
Calfee, Halter & Griswold LLP
1400 KeyBank Center
800 Superior Ave.
Cleveland, OH 44114
jlang@calfee.com
lmcbride@calfee.com
talexander@calfee.com

David A. Kutick
Jones Day
North Point
901 Lakeside Avenue
Cleveland, OH 44114
dakutik@jonesday.com

Allison E. Haedt
Jones Day
P.O. Box 165017
Columbus, OH 43216-5017
aehaedt@jonesday.com

COUNSEL FOR FIRSTENERGY SOLUTIONS CORP.

Dorothy Kim Corbett
Associate General Counsel
Duke Energy Business Services LLC
139 East Fourth Street
Cincinnati, OH 45202
Dorothy.Corbett@duke-energy.com

Jeanne W. Kingery
Associate General Counsel
155 East Broad Street, 21st Floor
Columbus, OH 43215
Jeanne.Kingery@duke-energy.com

COUNSEL FOR DUKE ENERGY RETAIL SALES, LLC

David M. Stahl
Eimer Stahl LLP
224 S. Michigan Avenue, Suite 1100
Chicago, IL 60604
dstahl@eimerstahl.com

Sandy I-ru Grace
Assistant General Counsel
Exelon Business Services Company
101 Constitution Avenue N.W.
Suite 400 East
Washington, DC 20001
sandy.grace@exeloncorp.com

COUNSEL FOR EXELON GENERATION COMPANY, LLC

Mark A. Whitt
Melissa L. Thompson
Andrew J. Campbell
Whitt Sturtevant LLP
PNC Plaza, Suite 2020
155 East Broad Street
Columbus, OH 43215
whitt@whitt-sturtevant.com
thompson@whitt-sturtevant.com
Campbell@whitt-sturtevant.com

Vincent Parisi
Matthew White
Interstate Gas Supply, Inc.
6100 Emerald Parkway
Dublin, OH 43016
vparisi@igsenergy.com
mswhite@igsenergy.com

COUNSEL FOR INTERSTATE GAS SUPPLY, INC.

Dane Stinson
Bailey Cavalieri LLC
10 West Broad Street, Suite 2100
Columbus, OH 43215
dane.stinson@baileycavalieri.com

COUNSEL FOR THE OHIO ASSOCIATION OF SCHOOL BUSINESS OFFICIALS, THE OHIO SCHOOL BOARDS ASSOCIATION, THE OHIO SCHOOLS COUNCIL AND THE BUCKEYE ASSOCIATION OF SCHOOL ADMINISTRATORS

Chad A. Endsley
Chief Legal Counsel
Ohio Farm Bureau Federation
280 North High Street, P.O. Box 182383
Columbus, OH 43218-2383
cendsley@ofbf.org

COUNSEL FOR THE OHIO FARM BUREAU FEDERATION

Mark S. Yurick
Zachary D. Kravitz
Taft Stettinius & Hollister LLP
65 East State Street, Suite 1000
Columbus, OH 43215
myurick@taftlaw.com
zkravitz@taftlaw.com

COUNSEL FOR THE KROGER CO.

Jeanne W. Kingery
Associate General Counsel
Amy B. Spiller
Deputy General Counsel
139 E. Fourth Street, 1303-Main
P.O. Box 961
Cincinnati, OH 45201-0960
Jeanne.Kingery@duke-energy.com
Amy.Spiller@duke-energy.com

COUNSEL FOR DUKE ENERGY COMMERCIAL ASSET MANAGEMENT, INC.

Barth E. Royer
Bell & Royer Co., LPA
33 South Grant Avenue
Columbus, OH 43215-3927
BarthRoyer@aol.com

Gary A. Jeffries
Assistant General Counsel
Dominion Resources Services, Inc.
501 Martindale Street, Suite 400
Pittsburgh, PA 15212-5817
Gary.A.Jeffries@dom.com

COUNSEL FOR DOMINION RETAIL, INC.

Roger P. Sugarman
Kegler, Brown, Hill & Ritter
65 East State Street, Suite 1800
Columbus, OH 43215
rsugarman@keglerbrown.com

COUNSEL FOR THE NATIONAL FEDERATION OF INDEPENDENT BUSINESS

C. Todd Jones
Gregory H. Dunn
Christopher L. Miller
Asim Z. Haque
Ice Miller LLP
250 West Street
Columbus, OH 43215
Gregory.dunn@icemiller.com
christopher.miller@icemiller.com
asim.haque@icemiller.com

COUNSEL FOR THE ASSOCIATION OF INDEPENDENT COLLEGES AND UNIVERSITIES OF OHIO AND THE CITY OF GROVE CITY, OHIO

David C. Rinebolt
Colleen L. Mooney
Ohio Partners for Affordable Energy
231 West Lima Street
PO Box 1793
Findlay, OH 45839-1793
drinebolt@ohiopartners.org
cmooney2@columbus.rr.com

COUNSEL FOR OHIO PARTNERS FOR AFFORDABLE ENERGY

Steven Beeler
Werner Margard
John Jones
Public Utilities Section
Ohio Attorney General's Office
180 East Broad Street, 6th Floor
Columbus, OH 43215
werner.margard@puc.state.oh.us
steven.beeler@puc.state.oh.us
john.jones@puc.state.oh.us

COUNSEL FOR THE STAFF OF THE PUBLIC UTILITIES COMMISSION OF OHIO

Greta See
Sarah Parrot
Attorney Examiners
Public Utilities Commission of Ohio
180 East Broad Street, 12th Floor
Columbus, OH 43215
Greta.See@puc.state.oh.us
Sarah.Parrot@puc.state.oh.us

ATTORNEY EXAMINERS

This foregoing document was electronically filed with the Public Utilities

Commission of Ohio Docketing Information System on

5/30/2012 3:13:15 PM

in

Case No(s). 10-2929-EL-UNC

Summary: Reply Brief of Industrial Energy Users-Ohio electronically filed by Mr. Matthew R. Pritchard on behalf of Industrial Energy Users-Ohio