

**BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO**

In the Matter of the Commission Review of)
The Capacity Charges of Ohio Power) Case No. 10-2929-EL-UNC
Company and Columbus Southern Power)
Company.)

**THE OHIO MANUFACTURERS' ASSOCIATION'S MEMORANDUM CONTRA OHIO
POWER COMPANY'S APPLICATION FOR REHEARING**

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**On behalf of The Ohio Manufacturers'
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I. INTRODUCTION

The Ohio Manufacturers' Association ("OMA"), pursuant to Rule 4901-1-12, Ohio Administrative Code ("O.A.C."), respectfully submits its Memorandum Contra Ohio Power Company's (formerly Ohio Power Company and Columbus Southern Power Company, collectively, "AEP-Ohio") Application for Rehearing filed July 20, 2012 ("Application for Rehearing").

The purpose of this case is to determine the proper price that AEP-Ohio should be permitted, for a limited time period, to charge competitive retail electric service ("CRES") providers for use of AEP-Ohio's capacity resources prior to AEP-Ohio's transition to full competition and corporate separation on June 1, 2015. At that time, the PJM reliability pricing model ("RPM") auction price will determine the capacity price for all customers in AEP-Ohio's service territory.

On July 2, 2012, the Public Utilities Commission of Ohio ("Commission") issued an Opinion and Order on the merits holding that the state compensation mechanism should be cost-based, thereby entitling AEP-Ohio to recover \$188.88 per megawatt-day ("MW-D"), which the Commission determined to be AEP-Ohio's fully embedded cost of capacity ("July 2 Order"). However, the Commission also found that AEP-Ohio is permitted to collect from CRES providers the PJM RPM price, which is lower than \$189/MW-D in each of the years at issue. July 2 Order at 23. However, the

Commission authorized AEP-Ohio to defer recovery of the difference between the \$189/MW-D and the PJM RPM price, plus carrying costs, for future recovery. *Id.* at 23-24.

On July 20, 2012, AEP-Ohio filed an Application for Rehearing claiming that the Commission's July 2 Order was unreasonable and unlawful in numerous aspects. AEP-Ohio Application for Rehearing at 5. Specifically, AEP-Ohio argues that the Commission's adoption of Staff's energy credit with adjustments was unreasonable; that it was unreasonable for the Commission to adopt a cost-based compensation mechanism but to permit AEP-Ohio to collect the PJM RPM price from CRES providers; and, the Commission's failure to address AEP-Ohio's January 7, 2011 application for rehearing was unreasonable.

While the OMA disagrees with many of AEP-Ohio's arguments, unfortunately, the OMA agrees that the Commission's July 2 Order disregards the harm to customers. *Id.* at 61. Accordingly, the OMA will file its own application for rehearing on the July 2 Order. In the meantime, the OMA respectfully requests that the Commission deny AEP-Ohio's application for rehearing and find that permitting AEP-Ohio to collect the PJM RPM price from CRES providers is not confiscatory. Further, the OMA's failure to address every argument presented by AEP-Ohio should not be considered agreement with those arguments.

II. ARGUMENT

Section 4905.22, Revised Code, requires all charges made or demanded for any service rendered, or to be rendered, to be just, reasonable, and not more than the charges allowed by law or by order of the Commission. Accordingly, the state

compensation mechanism that AEP-Ohio may charge CRES providers for capacity must be just and reasonable. AEP-Ohio's claim that the state compensation mechanism is unconstitutionally confiscatory is inaccurate. Further, all shopping customers should receive RPM auction prices for the purpose of establishing consistent, nondiscriminatory pricing, which is contrary to AEP-Ohio's position of requesting to charge customers that switched a capacity price of \$255/MW-D. The arguments in AEP-Ohio's Application for Rehearing seek to unjustly deny customers access to market rates for capacity simply because market prices are low, therefore, these arguments should be rejected.

A. The Commission's authorization to collect the PJM RPM price from CRES providers is neither confiscatory nor an unconstitutional taking.

In its Application for Rehearing, AEP-Ohio claims that the Commission's July 2 Order adopting a cost-based state compensation mechanism but allowing AEP-Ohio to collect only the PJM RPM price, while deferring recovery of the difference for future recovery, is confiscatory, unjust, unreasonable, and results in an unconstitutional taking of property without just compensation. AEP-Ohio Application for Rehearing at 44. The Commission's authorization to collect the PJM RPM price from CRES providers is neither confiscatory nor an unconstitutional taking. The PJM RPM price is the amount AEP-Ohio should be permitted to recover from CRES providers for the interim period until RPM sets the price for capacity for all of AEP-Ohio's customers.

The question of whether the state compensation mechanism is confiscatory depends on whether the rate is just and reasonable. As the OMA noted in the OMA's

and the Ohio Hospital Association's Joint Post Hearing Brief ("Post Hearing Brief"), the issue of confiscation has been thoroughly addressed under Ohio law.

In *Dayton Power & Light Co. v. Pub. Utilities Commission of Ohio et al.*, the Ohio Supreme Court defined the requirements of a confiscation claim to include:

The first is that * * * he who would upset the rate order * * * carries the heavy burden of making a convincing showing that it is invalid because it is unjust and unreasonable in its consequences. The second precept is that a challenged rate order must be viewed in its entirety to determine whether the rates set pursuant to the order fall within "the broad zone of reasonableness."

Dayton Power & Light Co. v. Pub. Utilities Commission of Ohio et al., 4 Ohio St. 3d 91 at 97 (April 13, 1983).

Additionally, in *Fed. Power Comm. v. Hope Natural Gas Co.*, 320 U.S. 591(1944), that "It is not the theory but the impact of the rate order which counts. If the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry is at an end." *Id.*; see also, *Duquesne Light Co. v. Barasch*, 488 U.S. 299 (1989). Thus, a determination of whether a rate is just and reasonable is not dependent on the financial consequences to a utility that is authorized to charge a specific rate. The *Hope* decision requires balancing investor and consumer interests. Rates that balance these interests are not confiscatory as long as they fall within the broad zone of reasonableness established in *Dayton*.

AEP-Ohio attempts to distinguish this case from *Dayton* and *Ohio Edison Co. v. Pub. Util. Comm.*, 63 Ohio St.3d 555 (1992). AEP-Ohio argues that this case differs from *Dayton* because the utility in the *DP&L* case failed to present witnesses on the confiscation issue, while AEP-Ohio presented evidence and argued on brief that the Staff's energy credit, adopted by the Commission with modifications that resulted in a

higher total capacity rate than the PJM RPM auction price, would result in AEP-Ohio receiving less compensation for its generating capacity than it desires. Application for Rehearing at 48-49. AEP-Ohio argues that its case is distinguishable from the *Ohio Edison* case because the utility failed to prove the unreasonableness of the Commission's determinations but AEP-Ohio believes that the Commission has made fundamental errors that are different than those at issue in the *Ohio Edison* case. While the issues in the cases are different and AEP-Ohio presented witnesses and evidence on the potential impact of various outcomes, the bases for proving confiscation are the same and the *Dayton* and *Ohio Edison* cases are controlling. AEP-Ohio has not demonstrated that the Commission's findings are confiscatory.

Specifically, in addressing the EDU's contention, the *Dayton* Court provided that, absent explicit statutory authorization, "the Commission may not benefit the investors by guaranteeing the full return of their capital at the expense of the ratepayers." *Id* at 102. The Commission has also provided that simply because an EDU will not receive as much revenue as preferred does not mean confiscation exists.¹ Similar to *Dayton*, AEP-Ohio seeks specific, guaranteed rates of return on equity ("ROE"). Although AEP-Ohio provided some evidentiary support, AEP-Ohio's preferred ROE is based upon unsubstantiated estimates of customer shopping, not any actual harm. Tr. Vol. III at 570. In fact, as AEP-Ohio's reported earnings demonstrate, AEP has not suffered the serious financial impact predicted by AEP-Ohio. AEP's earnings from utility operations, in total, were \$15 – 23 million higher for the second quarter of 2012 compared to the

¹ See generally *In the Matter of the Continuation of the Rate, Freeze and Extension of the Market, Development period for the Monongahela Power Company*, PUCO Case No. 04-880, Opinion and Order (December 8, 2004).

second quarter of 2011 and the year to date statistics results are similar.² While AEP-Ohio's second quarter earnings decreased from the 2011 second quarter earnings, AEP-Ohio has provided no record evidence that demonstrates the Commission's decision is confiscatory.

Even if the Commission or the Ohio Supreme Court finds that the Commission made some errors in computing the energy credit, as AEP-Ohio asserts, AEP-Ohio has not demonstrated that either \$189/MW-D or the then-current PJM RPM auction price for capacity fall outside of the broad zone of reasonableness. In fact, AEP-Ohio has acknowledged that the Federal Energy Regulatory Commission ("FERC") has determined that RPM pricing is just and reasonable. Tr. Vol. V at 857.

Thus, regardless of whether AEP-Ohio is ultimately permitted to recover from CRES providers a price for its capacity of anywhere between \$189/MW-D and the PJM RPM auction price, AEP-Ohio has not demonstrated that there is any confiscation.

AEP-Ohio also argues that the Commission's decision resulted in a partial taking without just compensation. AEP-Ohio Application for Rehearing at 2. AEP-Ohio describes the standard set forth in *Penn Central Transp. Co. v. New York City*:

Where a regulation deprives property of less than 100 percent of its economically viable use, a court must consider: (1) the economic impact of the regulation on the claimant, (2) the extent to which the regulation has interfered with distinct investment-backed expectations, and (3) the character of the governmental action. AEP-Ohio Application for Rehearing at 51, citing *Penn Central Transp. Co. v. New York City*, 438

² See, *American Electric Power 2Q12 Earnings Release Presentation*, July 20, 2012, at 13-14, available at: <http://www.aep.com/newsroom/resources/earnings/2012-07/2Q12EarningsReleasePresentation.pdf>.

U.S. 104, 124 (1978). Even by *Penn Central* standard, there is no unconstitutional taking in this case.

First, as noted above, AEP has not suffered an economic impact resulting from this decision. AEP's earnings are higher than the previous year's second quarter. Second, the July 2 Order has not interfered with distinct investment-backed expectations. Contrary to AEP-Ohio's argument, its shareholder (AEP) was aware that AEP-Ohio had previously collected the PJM RPM auction price from CRES providers for shopping customers. Additionally, AEP was cognizant of the fact that when Am. Sub. Senate Bill 3 was signed into law, at some point in the future, generation services would be competitively priced. The fact that this transition would occur is no surprise to AEP-Ohio or its shareholder, AEP. Finally, as the Commission noted, the character of the Commission's action was to determine the fully embedded cost of AEP-Ohio's capacity and to set a state compensation mechanism that furthers the State policy set forth in Section 4928.02, Revised Code. The state compensation mechanism is not for some strictly governmental purpose. Thus, like the *Penn Central* case, AEP-Ohio's submission that it may establish a "taking" simply by showing that it has been denied the ability to exploit an interest that it heretofore (unwisely, at best) believed was available, is quite simply untenable.

The Commission should reject AEP-Ohio's confiscation and takings claims.

B. All shopping customers should be eligible to receive the PJM RPM price for capacity.

AEP-Ohio claims that it was unreasonable and unlawful, as well as unnecessary for the Commission to extend RPM pricing to customers that already switched based on a capacity price to CRES providers of \$255/MW-day. AEP-Ohio Application for

Rehearing at 61-62. AEP-Ohio argues that customers did not have a reasonable expectation of RPM prices for capacity. *Id.* at 62. AEP-Ohio's theory is that, as CRES providers made offers and customers switched at a capacity charge of \$255/MW-D, customers had and have no reasonable expectation to receive PJM's RPM auction price for capacity. Therefore, CRES providers serving those customers should be charged \$255/MW-D for capacity to serve the customers. *Id.* at 61. This argument is simply incorrect.

The State policy requires the Commission to ensure the availability to consumers of adequate, reliable, safe, efficient, *nondiscriminatory*, and reasonably priced retail electric service. Section 4928.02, Revised Code. Charging all CRES providers the PJM RPM auction price is nondiscriminatory and advances state policy, rather than AEP-Ohio's proposed alternative of discriminating based upon timing.

Moreover, customers, regardless of when they shopped, had and have a reasonable expectation of PJM RPM priced capacity. This reasonable expectation is a result of the fact that RPM was the default rate at which CRES providers were required to compensate AEP-Ohio for capacity.³ The Commission made clear in its December 8, 2010 Entry that it expressly adopted as the state mechanism for AEP-Ohio the then-current capacity charges established by the three-year capacity auction conducted by PJM during the pendency of its review. Entry at 2 (December 8, 2010). There have only been two temporary periods since PJM's capacity market began in 2007 that the AEP-Ohio price of capacity for shopping customers was not the PJM RPM auction price. First, there was a short window when the Commission

³ See, PJM Open Access Transmission Tariff, Attachment D, Schedule 8.1 ("Fixed Resource Requirement Alternative").

adopted the ESP Stipulation on December 14, 2011, that implemented the two-tiered capacity pricing scheme. Second, the Commission granted relief at AEP-Ohio's request from the PJM RPM auction price and maintained the two-tiered pricing scheme until a decision on the merits was issued. Entry at 16-17 (March 7, 2012). If the Commission did not resolve the tiered-pricing issue by July 2, 2012, the default capacity price would have reverted back to the PJM RPM auction price. *Id.* During these brief periods when the PJM RPM auction price was not in place, this case was pending with the ultimate outcome unknown. However, since PJM RPM was the default, it was reasonable for customers to expect that their capacity may be priced based upon the PJM RPM auction price once the Commission ultimately resolved the case. In fact, notwithstanding the deferral authorized by the Commission, the Commission has ultimately authorized AEP-Ohio to recover only the PJM RPM auction price from CRES providers from all shopping customers. Accordingly, the OMAEG respectfully requests that the Commission deny AEP-Ohio's request to limit the application of the PJM RPM auction price to only certain shopping customers.

III. CONCLUSION

For the foregoing reasons, the OMA respectfully requests that the Commission find that permitting AEP-Ohio to recover the PJM RPM auction price of capacity for all shopping customers from CRES providers is just and reasonable and not confiscatory or an unconstitutional taking and deny AEP-Ohio's Application for Rehearing.

Respectfully submitted,



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**On behalf of The Ohio Manufacturers'
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CERTIFICATE OF SERVICE

The undersigned hereby certifies that a copy of the foregoing Memorandum Contra of The Ohio Manufacturers' Association was served upon the parties of record listed below this 30th day of July 2012 *via* email transmission or first class mail.



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This foregoing document was electronically filed with the Public Utilities

Commission of Ohio Docketing Information System on

7/30/2012 4:49:08 PM

in

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

Summary: Memorandum The Ohio Manufacturers' Association's Memorandum Contra Ohio Power Company's Application for Rehearing electronically filed by Ms. Andrea P Govan on behalf of Ohio Manufacturers' Association and McAlister, Lisa G. Mrs. and Siwo, J. Thomas Mr.