

**BEFORE  
THE PUBLIC UTILITIES COMMISSION OF OHIO**

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

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**THE JOINT APPLICATION FOR REHEARING OF  
THE OHIO MANUFACTURERS' ASSOCIATION AND  
THE OHIO HOSPITAL ASSOCIATION**

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**On behalf of The Ohio Manufacturers' Association**

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**On behalf of The Ohio Hospital Association**

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Pursuant to Section Ohio Revised Code Section ("R.C.") 4903.10 and Ohio Administrative ("OAC") Rule 4901-1-35, The Ohio Manufacturers' Association ("OMA") and The Ohio Hospital Association ("OHA" collectively "OMA/OHA") respectfully submit this Application for Rehearing of the July 2, 2012 Opinion and Order ("July 2 Order") issued by the Public Utilities Commission of Ohio ("Commission") adopting the state compensation mechanism for AEP-Ohio's recovery of capacity costs from Competitive Retail Electric Service ("CRES") providers serving shopping customers. The Commission's authorization for AEP-Ohio to defer for future recovery the difference between \$189/MW-D and the then-current PJM reliability pricing model ("RPM") auction price is unlawful and unreasonable and substantially harms Ohio manufacturers, hospitals and other customers. Additionally, the Commission's finding that an 11.15% return on equity was appropriate was unjust and unreasonable.

The OMA/OHA respectfully request that the Commission grant this Application for Rehearing and reverse its July 2 Order to the extent it authorizes AEP-Ohio to defer for future recovery the difference between its fully embedded capacity costs and the PJM RPM auction prices for the reasons set forth in the attached Memorandum in Support.

Respectfully submitted,



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**MEMORANDUM IN SUPPORT**

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**I. INTRODUCTION**

On July 2, 2012, the Commission issued an Order on the merits of AEP-Ohio's request to charge CRES providers its fully embedded capacity costs and set a state compensation mechanism that will remain in place until June 1, 2015. The Commission held that the state compensation mechanism should be cost-based and, thus, AEP-Ohio is entitled to recover its costs of capacity, which the Commission held are \$188.88/MW-D. July 2 Order at 22. However, in order to stabilize the market and encourage shopping, the Commission held that AEP-Ohio is permitted to recover from CRES providers only the PJM RPM price, which is currently about \$20/MW-D. *Id.* at 23. The Commission authorized AEP-Ohio to defer the difference between \$188.88/MW-D and the prevailing PJM RPM prices for future recovery plus carrying costs. *Id.* at 23. The Commission stated that this total deferred amount is dependent on the number of customers who shop, or switch to a CRES provider, and will be addressed in AEP-Ohio's electric security plan ("ESP") case.<sup>1</sup>

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<sup>1</sup> *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Authority to Establish a Standard Service Offer Pursuant to § 4928.143, Ohio Rev. Code, in the Form of an Electric Security Plan*, Case No. 11-346-EL-SSO, et al. ("ESP Case").

In reaching its decision, it appears that the Commission attempted to strike a middle ground between the positions of AEP-Ohio and its customers and competitive suppliers. While the July 2 Order may be good for CRES providers (as they have sufficient headroom to compete for customers with PJM RPM capacity pricing), and good for AEP-Ohio (as they will ultimately be recovering their fully embedded costs of capacity), it is bad for customers who will be bearing the brunt of unreasonable, unlawful, and above-market capacity costs, plus interest, for some unknown period. Accordingly, for the reasons set forth below, OMA/OHA urge the Commission to reverse its finding that AEP-Ohio is entitled to defer and recover the difference between its fully embedded capacity costs and the PJM RPM price from Ohio customers.

**II. THE COMMISSION'S DECISION TO AUTHORIZE AEP-OHIO TO DEFER THE DIFFERENCE BETWEEN \$189/MW-D AND THE PREVAILING PJM RPM PRICES FOR FUTURE RECOVERY, PLUS CARRYING COSTS, IS UNREASONABLE AND UNLAWFUL AND WILL HARM CUSTOMERS.**

**A. The Commission exceeded its jurisdiction by authorizing deferrals for future recovery of wholesale costs from retail customers.**

The Commission held that capacity service is a wholesale service – not retail.

Specifically, the Commission stated:

The electric service in question (i.e., capacity service) is provided by AEP-Ohio for CRES providers, with CRES providers compensating the Company in return for its FRR capacity obligations. Such capacity service is not provided directly by AEP-Ohio to retail customers. (AEP-Ohio Ex. 101 at 11; Tr. I at 63.) Although the capacity service benefits shopping customers in due course, they are initially one step removed from the transaction, which is more appropriately characterized as an intrastate wholesale matter between AEP-Ohio and each CRES provider operating in the Company's service territory.... We agree that the provision of capacity for CRES providers by AEP-Ohio, pursuant to the Company's FRR capacity obligations, is not a retail electric service as defined by Ohio law. July 2 Order at 12.

The Commission relied on its general supervisory authority and ratemaking authority in R.C. 4905.04 through 4905.05, and Chapter 4909, to determine that the Commission has jurisdiction to establish a state compensation mechanism and that it should be cost-based. The Commission noted that those chapters require that the Commission use traditional rate base/rate of return regulation to approve rates that are based on cost, with the ultimate objective of approving a charge that is just and reasonable consistent with R.C. 4905.22. July 2 Order at 22.

As the Ohio Energy Group (“OEG”) pointed out in its application for rehearing, the Commission has neither general ratemaking authority nor any specific statutory authority that applies here to order deferrals of costs that the utility is authorized to recover. OEG Application for Rehearing at 3 (citing *Columbus S. Power Co. v. Public Utils. Comm’n* (1993) 67 Ohio St. 3d 535, 620 N.E.2d 835, 1993 Ohio LEXIS 2265). Accordingly, the authorization to defer the amount between \$189/MW-D and the PJM RPM price was unlawful.

Additionally, as the OEG also noted, as the Commission held that capacity is a wholesale service, retail customers may not be lawfully required to pay the wholesale costs owed by CRES providers to AEP-Ohio. *Id.*

The OMA/OHA also agrees that, from a logical standpoint, deferrals do not make sense in this instance. Deferring the difference between AEP-Ohio’s costs and the low PJM RPM auction price will require customers to repay the deferral plus interest at a time when the PJM RPM auction price for capacity will be increasing from the historically low PJM RPM capacity prices that are currently in effect. Thus, rather than smoothing out or phasing in an increase, the deferral produces a “double whammy” for

customers and the competitive market going forward. Additionally, depending on when the deferral repayment begins, the deferral repayment could take place after AEP-Ohio is no longer an FRR entity.

Although, OMA/OHA agree with many of the well-made points in the OEG's application for rehearing, OMA/OHA strongly disagree with the OEG's conclusion that the "proper solution is to charge CRES providers the full wholesale cost-based capacity rate \$188.88/MW-day as AEP-Ohio incurs those costs during the Fixed Resource Requirement ("FRR") period." *Id.* at 4. The lawful solution, as the Commission does not have authority to authorize the deferral and cannot require retail customers to pay wholesale charges directly to AEP-Ohio, is for the Commission to revoke the deferral authority.

**B. The deferral amount of over \$725 million, before carrying costs, will substantially harm customers and is unreasonable.**

As the Commission noted, pursuant to R.C. 4905.22 all charges for service shall be just and reasonable and not more than allowed by law or by order of the Commission. July 2 Order at 22. In this case, the amount that the Commission authorized AEP-Ohio to defer for future recovery is so large that it will substantially harm customers and renders the rates for capacity unjust and unreasonable.

While the OMA Energy Group demonstrated how it derived the deferral amount based upon record evidence in the ESP Case, this case provides record evidence combined with shopping assumptions that produces the same estimate. Specifically, the amount that the Commission authorized for deferral and future recovery is the difference between \$188.88/MW-D and the PJM RPM prices for the period, which are: \$20.01/MW-D in the planning year ("PY") 2012; \$33.71/MW-D in PY 2013; and,

\$153.89/MW-D in PY 2014. July 2 Order at 10. The resulting amounts to be deferred are thus \$168.87/MW-D, \$155.17/MW-D and \$34.99/MW-D, respectively.

To convert the deferral amounts into a per megawatt-hour (“MWh”) rate, the capacity price is divided by the product of 24 (24 hours in a day) and an estimate of AEP-Ohio’s load factor. The load factor can be derived on a customer class basis by reverse calculating information contained in AEP-Ohio witness Allen’s workpaper in IEU Ex. 111. Specifically, Mr. Allen identifies a \$356/MW-D capacity rate and includes the \$/MWh charge for each customer class for the PJM planning year 2102/13. *Id.* Thus, to determine the load factor by customer class, the capacity price would be divided by the product of the \$/MWh charge and 24. For example, for the industrial class, the calculation would be:  $\$355.72 / (17.29 \times 24) = 86\%$  load factor.

Next, AEP-Ohio’s earnings estimates are based upon shopping assumptions of 65 percent of residential customers, 80 percent of commercial customers, and 90 percent of industrial customers switching by the end of 2012. AEP-Ohio Ex. 104 at 4-5. The table below demonstrates how the total deferral amount was derived. AEP-Ohio’s total load minus the shopping estimates provides an estimate of the shopping load. The rate multiplied by the load provides the revenue amount, before adding carrying costs, that AEP-Ohio would collect for the Commission-authorized deferral.



	Customer Class	Rate per MWh	Shopping Load per GWh	Revenue
Year 1	Res	14.0725	8,018	\$112,833,305
	Com	10.825	10,406	\$112,644,950
	Ind	8.181686	11,820	\$96,707,529
Year 2	Res	12.433494	9,418	\$117,098,643
	Com	9.5079657	11,444	\$108,809,159
	Ind	6.8057018	13,570	\$92,353,373
Year 3	Res	2.8586601	11,460	\$32,760,245
	Com	2.2089646	12,643	\$27,927,940
	Ind	1.5676523	15,948	\$25,000,919
				<b>\$726,136,063</b>

The results of the calculations demonstrate that if AEP-Ohio's shopping estimates come to fruition, there will be **over \$725 million in the deferral bucket before any carrying costs are added on top.** This amount would not even be an issue in any other regulated Ohio electric distribution utility service territory.

Obviously, having to repay a \$726 million deferral plus interest, particularly at a time when market prices will be higher than now, results in significant negative customer impacts. *See, for example,* OMA Exs. 101-105. In order for the rates to be just and reasonable, the Commission must balance both investor and consumer interests, and the fact of the matter is that consumer interests have, once again, been lost in the equation. The Commission should reverse its July 2, 2012 Order and revoke the authority to defer and recover the difference between \$188.88/MW-D and the PJM RPM auction prices.

### **III. THE COMMISSION'S HOLDING THAT THE RETURN ON EQUITY TARGET SHOULD BE 11.15% IS UNJUST AND UNREASONABLE.**

AEP-Ohio used formula rates that came out of a settlement from a different jurisdiction as the starting point for its calculation of capacity costs. Although the settlement included language that it should not be used to establish any principles or precedent as to the appropriate rate formulas to be used in any proceeding,<sup>2</sup> the Commission held that it was an appropriate starting point. July 2 Order at 33. The Commission then found that Staff's methodology for determining AEP-Ohio's capacity costs was appropriate. From the starting point of the AEP-Ohio affiliate settlement agreement, Staff used a traditional ratemaking process of making adjustments to AEP-Ohio's proposed capacity pricing mechanism and included an offset for energy sales. The Commission rejected several of Staff's adjustments to arrive at the final cost of \$188.88/MW-Day for AEP-Ohio's capacity.

One of the Staff adjustments rejected by the Commission was a lower return on equity ("ROE") than proposed by AEP-Ohio. Staff recommended a ROE of 10 percent for Columbus Southern Power and 10.3 percent for Ohio Power based upon the ROE's that were agreed upon in AEP-Ohio's base distribution rate case settlement and approved by the Commission.<sup>3</sup> AEP-Ohio recommended between a 10.5 percent and an 11.15 percent ROE. The 11.15 percent ROE was based upon an *increase* to the ROE of 11.10 percent in the AEP-Ohio affiliate settlement that should not be used as precedent. AEP-Ohio Ex. 102 at 11. It was also the ROE amount that AEP-Ohio *proposed* in AEP-Ohio's last base distribution rate case. Of course, that ROE was not

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<sup>2</sup> Tr. Vol. II at 250-251.

<sup>3</sup> Staff Ex. 103 at 12.

negotiated, agreed upon or approved by the Commission. Nonetheless, the Commission held that Staff's recommended ROE should be rejected as "Staff's recommended return on equity was solely based on the negotiated return on equity in the Company's distribution rate case (Staff Ex. 103 at 12-13), which has no precedential effect pursuant to the express terms of the stipulation adopted by the Commission in that case." July 2 Order at 34.

In the event that the Commission does not simply revoke the deferral authority as recommended above, OMA/OHA respectfully requests that, at a very minimum, the Commission find that Staff's recommended return on is reasonable and appropriate and reduce the cost of AEP-Ohio's capacity by \$10.09/MW-D. The Commission's reliance on a settlement from another jurisdiction that contains the same express language that it should not have any precedential effect as the settlement that was actually negotiated by many of the same parties to this case (including AEP-Ohio) and which was adopted by this Commission is unjust and unreasonable. Further, relying on an AEP-Ohio *proposed* (but not adopted) ROE is equally unjust and unreasonable. Accordingly, the Commission should reverse its decision to increase the ROE from Staff's proposed level to 11.15 percent.

#### **IV. CONCLUSION**

For the reasons set forth herein, the OMA/OHA respectfully request that the Commission grant rehearing and revoke the deferral authority granted to AEP-Ohio. In the event that the Commission does not revoke the deferral authority, at the very minimum, the Commission should find that Staff's proposed ROE was appropriate in determining AEP-Ohio's cost of capacity.

Respectfully submitted,



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**On behalf of The Ohio Hospital Association**

## 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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Summary: Application for Rehearing electronically filed by Teresa Orahood on behalf of Ohio Manufacturers' Association and Ohio Hospital Association