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Via E-File

September 7, 2012

Public Utilities Commission of Ohio
PUCO Docketing
180 E. Broad Street, 10th Floor
Columbus, Ohio 43215

In re: 11-346-EL-SSO, 11-348-EL-SSO
11-349-EL-AAM, 11-350-EL-AAM

Dear Sir/Madam:

Please find attached the APPLICATION FOR REHEARING OF THE OHIO ENERGY GROUP for filing in the above-referenced matters.

Copies have been served on all parties on the attached certificate of service. Please place this document of file.

Respectfully yours,

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Encl.
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ALJ Jonathan Tauber, Esq. (via electronic mail)
Chairman Todd A. Snitchler (via overnight mail)
Commissioner Cheryl Roberto (via overnight mail)
Commissioner Steven D. Lesser (via overnight mail)
Commissioner Andre T. Porter (via overnight mail)
Commissioner Lynn Slaby (via overnight mail)
Eric Weldele, PUCO Chief of Staff (via overnight mail)
Certificate of Service

THE
PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Authority to Establish a Standard Service Offer Pursuant to §4928.143, Ohio Rev. Code, in the Form of an Electric Security Plan	:	**Case No. 11-346-EL-SSO**
	:	**Case No. 11-348-EL-SSO**
In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of Certain Accounting Authority	:	**Case No. 11-349-EL-AAM**
	:	**Case No. 11-350-EL-AAM**

APPLICATION FOR REHEARING OF THE OHIO ENERGY GROUP

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TABLE OF CONTENTS

BEFORE THE
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APPLICATION FOR REHEARING OF THE OHIO ENERGY GROUP

Pursuant to R.C. 4903.10 and Ohio Adm. Code 4901-1-35, the Ohio Energy Group ("OEG") submits this Application for Rehearing of the August 8, 2012 Opinion and Order ("Order") of the Public Utilities Commission of Ohio ("Commission"). OEG submits that the Order is unreasonable and unlawful because:

1. It Was Unreasonable To Characterize The 12% Earnings Cap As A Significantly Excessive Earnings Test ("SEET") Threshold Rather Than As An Electric Security Plan ("ESP") Provision Providing Rate Stability And Certainty Pursuant To R.C. 4928.143(B)(2)(d). By Characterizing The 12% Earnings Cap As An ESP Provision, The Commission Can Achieve The Same Result And Avoid Legal Issues Related To Whether The Proper Procedures For Establishing A Formal SEET Threshold Were Followed.

2. The Commission Erred By Using An Improper Competitive Retail Electric Service ("CRES") Capacity Pricing Assumption When Calculating The Level Of The Retail Stability Rider ("RSR"). The Commission Used Current Adjusted RPM Capacity Prices To Determine CRES Revenues For Purposes Of The RSR Calculation, But Should Have Used The Entire $188.88/MW-Day Capacity Price To Calculate The RSR.

3. If The $188.88/MW-Day Capacity Price Is Not Used In The RSR Calculation, Then The Amount Of The Capacity Deferral ($188.88/MW-Day Less RPM) Should Be Included For Purposes Of Enforcing The 12% Earnings Cap. Counting The Deferral Is Consistent With Commission Precedent And In Conformity With How Ohio Power's SEC 10-K And FERC Form 1 Financial Statements Will Be Filed. Ignoring The Deferred Revenue Could Result In Ohio Power Earning Above 12%.

4. The Commission Should Clarify That Separate Energy-Only Auctions Will Be Held For Each AEP-Ohio Rate Zone In Order To Maintain Consistency With The Manner In Which The Fuel Adjustment Clause And Phase-In Recovery Rider Rates Will Be Recovered. Separate Energy-Only Auctions For Each Rate Zone Are Required Because The "Price To Beat" Is Significantly Higher In The Columbus Southern Power Rate Zone Than In The Ohio Power Rate Zone.

5. The Commission Should Leave Open The Possibility Of Blending The Phase-In Recovery Rider Rates After The ESP Expires Because The Energy And Capacity Rates For Both Rate Zones Will Be Determined On A Combined Basis At That Time.

6. The Order Violates the PJM Reliability Assurance Agreement (RAA). The PJM RAA Requires That The State Compensation Mechanism Be Recovered From Either CRES Providers Or Shopping Customers. The PJM RAA Is Central To The Commission's Jurisdiction, And It Does Not Allow For Non-Shopping Retail Customers To Be Charged For The Wholesale Capacity Costs Incurred by CRES Providers to Serve Switched Load.

7. The Commission Has No Authority Under State Law To Allow Any Of The Deferred Wholesale Capacity Costs Which CRES Providers Owe To AEP-Ohio To Be Recovered From Retail Customers (Either Shopping Or Non-Shopping) Through The RSR. Such Costs Are Outside The Scope Of The ESP And Therefore Cannot Be Approved Under R.C. 4928.13 Or Deferred Under R.C. 4928.144.

A memorandum in support of this Application for Rehearing is attached.

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MEMORANDUM IN SUPPORT

1. **It Was Unreasonable To Characterize The 12% Earnings Cap As A Significantly Excessive Earnings Test ("SEET") Threshold Rather Than As An Electric Security Plan ("ESP") Provision Providing Rate Stability And Certainty Pursuant To R.C. 4928.143(B)(2)(d). By Characterizing The 12% Earnings Cap As An ESP Provision, The Commission Can Achieve The Same Result And Avoid Legal Issues Related To Whether The Proper Procedures For Establishing A Formal SEET Threshold Were Followed.**

To ensure that AEP-Ohio does not reap disproportionate benefits as a result of the RSR and/or other components of the ESP, the Commission established for the three year term of this ESP a return on equity SEET threshold for AEP-Ohio of 12%.[1] But the establishment of a three year 12% SEET threshold in this proceeding may give rise to concerns about whether the Commission properly followed the procedure required under R.C. 4928.143(F) for each annual SEET review. For example, some may argue that the Commission must determine the return on equity of a comparable group of companies or undertake other analytical steps each year before establishing a formal SEET threshold. To quell such concerns, the Commission should clarify that the 12% earnings cap was an ESP provision adopted pursuant to R.C. 4928.143(B)(2)(d).

R.C. 4928.143(B)(2)(d) provides that an ESP may include terms, conditions, or charges "...as would have the effect of stabilizing or providing certainty regarding retail electric service." A 12% earnings cap stabilizes retail rates that may otherwise fluctuate too far upward and provides certainty that AEP-Ohio will not substantially overearn as a result of the approved ESP. Hence, the Commission may properly adopt a 12% earnings cap as an ESP provision, while allowing the formal SEET threshold to be adopted independently of the 12% earnings cap. A similar approach was recommended by OEG witness Kollen with regard to the Earnings Stabilization Mechanism proposed in his testimony.[2] The

[1] Order at 37.
[2] Direct Testimony of Lane Kollen (May 4, 2012) at 10:6-11:3; *See also* Direct Testimony of Lane Kollen (April 4, 2012) in the Capacity Case.

Commission should therefore clarify that the 12% earnings cap was adopted as an ESP provision pursuant to R.C. 4928.143(B)(2)(d) rather than as a formal SEET threshold.

2. The Commission Erred By Using An Improper Competitive Retail Electric Service ("CRES") Capacity Pricing Assumption When Calculating The Level Of The Retail Stability Rider ("RSR"). The Commission Used Current Adjusted RPM Capacity Prices To Determine CRES Revenues For Purposes Of The RSR Calculation, But Should Have Used The Entire $188.88/MW-Day Capacity Price To Calculate the RSR.

The Commission erred by using RPM capacity prices to determine the CRES capacity revenues when calculating the level of the Retail Stability Rider ("RSR"). As indicated on page 35 of the Order, the Commission used RPM prices to project that AEP-Ohio would receive CRES capacity revenues of $32 million in 2012/13, $65 million in 2013/14, and $344 million in 2014/15. But the use of RPM significantly understates the compensation that AEP-Ohio will actually receive for its costs of supplying capacity to CRES providers.

Under the state compensation mechanism established in Case No. 10-2929-EL-UNC (the "Capacity Case"), AEP-Ohio will ultimately receive a cost-based rate of $188.88/MW-day as compensation for its Fixed Resource Requirement ("FRR") capacity obligations. Though a portion of the $188.88/MW-day cost-based capacity rate is to be deferred for collection at a later date, AEP-Ohio will book as revenue the entire $188.88/MW-day as capacity service is provided to the CRES providers. The Commission's use of RPM prices to calculate CRES revenues fails to account for this fact, leading to an unreasonable increase in the level of the RSR charge.

The calculation of the RSR by the Commission results in AEP-Ohio being compensated twice for its FRR capacity obligations – once through an increased RSR charge and then again when AEP-Ohio's deferred capacity costs are recovered. Instead of using the RPM capacity prices to calculate CRES capacity revenues for purposes of the RSR, the Commission should use the full $188.88/MW-day cost-based rate that AEP-Ohio will ultimately recover. This approach avoids double compensation to AEP-Ohio and accurately reflects the true economics of the Commission's Orders.

If the Commission does not adopt this recommendation, then at a minimum the Commission should recognize the deferred capacity revenue when enforcing the 12% earnings cap. This is discussed in Section 3 below.

3. If The $188.88/MW-Day Capacity Price Is Not Used In The RSR Calculation, Then The Amount Of The Capacity Deferral ($188.88/MW-Day Less RPM) Should Be Included For Purposes Of Enforcing The 12% Earnings Cap. Counting The Deferral Is Consistent With Commission Precedent And In Conformity With How Ohio Power's SEC 10-K And FERC Form 1 Financial Statements Will Be Filed. Ignoring The Deferred Revenue Could Result In Ohio Power Earning Above 12%.

Even if the Commission does not use the full cost-based rate of $188.88/MW-day to calculate CRES revenues in the RSR calculation, at minimum, the Commission should explicitly confirm that the full cost-based rate of $188.88/MW-day, including the deferred capacity revenues, will be considered for purposes of enforcing the 12% earnings cap. The inclusion of deferred revenues for purposes of enforcing the 12% earnings cap is consistent with Commission precedent.[3] The inclusion of deferred capacity revenue is also consistent with how Ohio Power's earnings will be reported to the SEC on the 10-K and to the FERC on the Form 1. Recognizing the deferred capacity revenue reflects the economic reality that customers will pay the deferred revenue and AEP-Ohio will receive it. Failing to recognize the deferral will improperly push the revenue out to the years after the ESP is over when the 12% earnings cap will not apply. Recognizing the deferral properly protects customers in the event that the ESP is too generous to AEP-Ohio, in accordance with the language and intent of the Order.[4]

When enforcing the 12% earnings cap, the complete regulatory accounting for the capacity deferral and related issues should be: 1) recognize the entire $188.88/MW-day as current earnings (not just the RPM component); 2) recognize the entire $3.50 – $4.00 per MWh RSR as earnings; and 3) the

[3] Opinion & Order, Case No. 10-1261-EL-UNC (Jan. 11, 2011) at 31.
[4] *See* Order at 37 and 70.

$1.00/MWh of the RSR earmarked for deferral repayment should be off-set with an amortization expense of $1.00/MWh.[5]

4. The Commission Should Clarify That Separate Energy-Only Auctions Will Be Held For Each AEP-Ohio Rate Zone In Order To Maintain Consistency With The Manner In Which The Fuel Adjustment Clause And Phase-In Recovery Rider Rates Will Be Recovered. Separate Energy-Only Auctions For Each Rate Zone Are Required Because The "Price To Beat" Is Significantly Higher In The Columbus Southern Power Rate Zone Than In The Ohio Power Rate Zone.

As part of the ESP, the Commission approved the holding of multiple energy-only auctions.[6] The Commission should clarify that these auctions will be held on a separate rate zone basis – one for the Ohio Power Company ("OP") rate zone and one for the Columbus Southern Power Company ("CSP") rate zone.

The Commission decided to maintain separate Fuel Adjustment Clause ("FAC") rates for the OP and CSP rate zones.[7] Because FAC rates will be maintained separately for each rate zone during the ESP, the energy-only auctions approved by the Commission should likewise be held separately for each rate zone. The FAC rate for the OP rate zone is $32.43/MWh. The FAC rate for the CSP rate zone is $38.69/MWh. Hence, CSP's FAC rate is approximately $6/MWh higher than OP's rate.[8] Because the "price to beat" for energy is different in each rate zone, the energy-only auctions should be held separately for each rate zone. Otherwise, the auction may result in unreasonably high energy charges to OP customers.

In addition, the Commission should explicitly state that it will not accept the energy-only auction results if those results lead to rate increases for a particular rate zone. The Commission has the authority to reject auction results. If the Commission exercises this authority, AEP-Ohio will be able to provide

[5] This regulatory accounting assumes no changes to the August 8, 2012 ESP Order. However, as discussed in Section 6, we believe that charging non-shopping customers for the $1/MWh deferral repayment violates the PJM RAA; and as discussed in Section 7, we believe that charging any customer (shopping or non-shopping) for the $1/MWh deferral repayment is not authorized under state law.
[6] Order at 39-40.
[7] Order at 17.
[8] The rates listed are for Subtransmission/Transmission customers.

service to impacted customers as the provider-of-last resort, an obligation for which AEP-Ohio is compensated through SSO rates. Therefore, the Commission should keep in mind that it has the flexibility to reject auction results that are higher than SSO rates for the same service.

Maintaining the flexibility to reject energy-only auctions which would result in rate increases is especially important given the inherent mismatch that will be created. SSO customers pay average embedded cost for capacity through the legacy cost-based rate structure. SSO energy costs are based on OP/CSP's actual costs. Historically, this has meant high capacity costs associated with AEP-Ohio's predominately base load coal generation, but off-set by low coal-based energy prices. An energy-only auction will be based upon locational marginal price (market pricing). The result of the energy-only auction will be that SSO customers will pay the utility's average embedded cost for capacity and marginal or market rates for energy. Marginal energy prices in PJM are now low. But all it would take is an increase in natural gas prices to turn that around. The worst case scenario for SSO customers would be if they are required to pay high average embedded capacity costs based upon base load coal generation and high marginal (market) energy rates. Maintaining the flexibility to reject energy-only auctions results by rate zone which would result in rate increases greatly reduces that risk.

5. The Commission Should Leave Open The Possibility Of Blending The Phase-In Recovery Rider Rates After The ESP Expires Because The Energy And Capacity Rates For Both Rate Zones Will Be Determined On A Combined Basis At That Time.

The Commission determined that the PIRR rates should be maintained separately for the CSP and OP rate zones.[9] Part of the rationale for recovering PIRR costs on a separate rate zone basis is that this approach is consistent with the FAC recovery on a separate rate zone basis. The nonbypassable PIRR runs through December 31, 2018.[10] But the FAC rates expire with AEP-Ohio's ESP on May 31, 2015. At that point, all rates for energy and capacity will be the same for both zones. It may be

[9] Order at 55.
[10] Order at 52.

appropriate to blend the PIRR rates at that time. Therefore, the Commission should state that it is not precluding the possibility of blending the PIRR rates after the ESP expires.

6. The Order Violates the PJM Reliability Assurance Agreement (RAA). The PJM RAA Requires That The State Compensation Mechanism Be Recovered From Either CRES Providers Or Shopping Customers. The PJM RAA Is Central To The Commission's Jurisdiction, And It Does Not Allow For Non-Shopping Retail Customers To Be Charged For The Wholesale Capacity Costs Incurred by CRES Providers to Serve Switched Load.

The Commission ordered that, of the $3.50/MWh and $4/MWh nonbypassable RSR, AEP-Ohio must allocate $1/MWh toward repayment of the capacity costs deferred by the Commission in the Capacity Case.[11] However, the PJM Reliability Assurance Agreement ("RAA") does not provide the Commission authority to impose such a charge on non-shopping retail customers. Therefore, the $1/MWh of the RSR charge that is earmarked to pay AEP-Ohio part of the capacity costs owed to it by CRES providers cannot be assessed to SSO load.

The language of the RAA explicitly limits the parties that can be held responsible for compensating AEP-Ohio under the state compensation mechanism. The RAA contemplates only two categories of entities that could be responsible for compensating AEP-Ohio for its FRR capacity obligations: 1) "switching customers," aka shopping customers; *or* 2) "the LSE," aka CRES providers. Section D.8 of Schedule 8.1 of the RAA provides that *"[i]n 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."*[12] The PJM RAA does not provide the Commission authority to hold *non-shopping retail* customers responsible for compensating AEP-Ohio for its FRR capacity obligations under the state compensation mechanism.

[11] Order at 36.
[12] Emphasis added.

The Commission must abide by the explicit terms of the PJM RAA in setting rates under the state compensation mechanism. OEG urges the Commission not to exceed its authority under the plain language of the PJM RAA by recovering any portion of the state compensation mechanism through a charge to non-shopping retail customers. For to do so would, as the PJM RAA recognizes, improperly charge non-shopping customers for a service they are not using.

The PJM RAA is central to the Commission's jurisdiction to establish a cost-based rate for a competitive retail electric service. The delegation of such authority by PJM and FERC to this Commission will be a critical jurisdictional element on appeal. The PJM RAA is already a critical jurisdictional element in the August 31, 2012 Complaint for Writs of Prohibition and Mandamus filed by IEU at the Supreme Court of Ohio (Case No. 12-1494).

The PJM RAA may be the Commission's ultimate trump card for justifying the establishment of a cost-based rate for a competitive service. Therefore, it is essential that PJM RAA be complied with, including the provision which dictates that the state compensation mechanism must be paid by either the CRES providers or switched load.

7. The Commission Has No Authority Under State Law To Allow Any Of The Deferred Wholesale Capacity Costs Which CRES Providers Owe To AEP-Ohio To Be Recovered From Retail Customers (Either Shopping Or Non-Shopping) Through The RSR. Such Costs Are Outside The Scope Of The ESP And Therefore Cannot Be Approved Under R.C. 4928.13 Or Deferred Under R.C. 4928.144.

The Commission does not have authority under state law to allow AEP-Ohio to recover any of the wholesale costs established under the state compensation mechanism from retail customers (either shopping or non-shopping) through the RSR. Such costs are outside the scope of the ESP and cannot be approved under R.C. 4928.143 or deferred under R.C. 4928.144. Therefore, the $1/MWh of the RSR that is earmarked to pay AEP-Ohio for capacity utilized by CRES providers should be eliminated.

In its Order in the Capacity Case, the Commission took great care to explicitly characterize the state compensation mechanism as a ***wholesale cost-based*** rate not covered by Chapter 4928 of the Revised Code. Throughout the Capacity Case Order, the Commission reinforces this point, stating:

- *"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. Accordingly, we find it unnecessary to determine whether capacity service is considered a competitive or noncompetitive service under Chapter 4928, Revised Code."*[13]
- *"Although Chapter 4928, Revised Code, provides for market-based pricing for retail electric generation service, those provisions do not apply because, as we noted earlier, capacity is a wholesale rather than a retail service."*[14]
- *"We conclude that the state compensation mechanism for AEP-Ohio should be based on the Company's costs."*[15]
- *"Therefore, with the intention of adopting a state compensation mechanism that achieves a reasonable outcome for all stakeholders, the Commission directs that the state compensation mechanism shall be based on the costs incurred by the FRR Entity for its FRR capacity obligations."*[16]
- *"Upon review of the considerable evidence in this proceeding, we find that the record supports compensation of $188.88/MW-day as an appropriate charge to enable AEP-Ohio to recover its capacity costs for its FRR obligations from CRES providers."*[17]
- *"Given that compensation for AEP-Ohio's FRR capacity obligations from CRES providers is wholesale in nature, we find that AEP-Ohio's formula rate template is an appropriate starting point for determination of its capacity costs."*[18]

Because the costs established under the state compensation mechanism are *wholesale* costs not covered by Chapter 4928, those costs are outside of the scope of the ESP and are not properly recoverable from any retail customers through the RSR. The Supreme Court of Ohio has held that an ESP provision is not authorized by statute if it does not fit within one of the categories listed in R.C. 4928.143(B)(2).[19] These categories in the ESP statute are all for costs that consumers may owe the utility for providing retail electric service. The wholesale capacity costs that CRES providers owe the

[13] Capacity Case Order at 13.
[14] Capacity Case Order at 22.
[15] Capacity Case Order at 22.
[16] Capacity Case Order at 23.
[17] Capacity Case Order at 33.
[18] Capacity Case Order at 33.
[19] *In re Columbus Southern Power Co.*, 128 Ohio St.3d 512, 2011-Ohio-1788, ¶32.

utility do not fit into any of those categories. There is no provision of the ESP statute whereby AEP-Ohio's retail customers can be held responsible for wholesale costs that CRES providers owe to AEP-Ohio. Because such costs are not properly recoverable through an ESP, the Commission cannot authorize AEP-Ohio to collect any of the wholesale capacity costs established under the state compensation mechanism from retail customers through the RSR.

Because the wholesale capacity costs which the CRES providers owe AEP-Ohio are not properly recoverable in an ESP, deferred recovery under R.C. 4928.144 is also improper. R.C. 4928.144 provides that the Commission may authorize a phase-in only of a *"rate or price established under Sections 4928.141 to 4928.143 of the Revised Code."* As discussed above, in the Capacity Case the Commission repeatedly stated that the wholesale cost-based state compensation mechanism of $188.88/MW-day was not established under Chapter 4928 of the Revised Code.

The proper solution is to charge CRES providers the full wholesale cost-based capacity rate of $188.88/MW-day. This is what they owe AEP-Ohio and is this is what they should pay. Accordingly, the Commission should modify the portion of the Order allowing AEP-Ohio to recover any of the wholesale capacity costs that CRES providers owe the utility from retail customers through the RSR. Requiring the CRES providers to pay what they owe will:

- Make the Commission's Orders consistent with the PJM RAA, which is the fundamental jurisdictional foundation that allows AEP-Ohio to charge a cost-based rate for a competitive retail electric service;
- Make the Commission's Orders consistent with R.C. 4928.143 and 4928.144, which authorize current or deferred recovery only of certain enumerated costs which do not include wholesale capacity costs owed by CRES providers to the utility;
- Greatly reduce the ratemaking complexity and associated consumer confusion;
- Avoid the accrual of a multi-hundred million deferral balance (plus interest) which will result in consumers paying above market rates once the repayment comes due.

CONCLUSION

WHEREFORE, for the foregoing reasons, the Commission should adopt the Ohio Energy Group's recommendations in this proceeding.

Respectfully Submitted,

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September 7, 2012

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I hereby certify that true copy of the foregoing was served by electronic mail (when available) or ordinary mail, unless otherwise noted, this 7th day of September, 2012 the following:

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Summary: App for Rehearing Ohio Energy Group (OEG) Application for Rehearing electronically filed by Mr. Michael L. Kurtz on behalf of Ohio Energy Group