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BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Ohio Power Company for Approval of an Amendment to Its Corporate Separation Plan	)))))	Case No. 12-1126-EL-UNC

APPLICATION FOR REHEARING AND MEMORANDUM IN SUPPORT OF INDUSTRIAL ENERGY USERS-OHIO

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November 16, 2012

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APPLICATION FOR REHEARING OF INDUSTRIAL ENERGY USERS-OHIO

Pursuant to Section 4903.10, Revised Code, and Rule 4901-1-35, Ohio Administrative Code ("O.A.C."), Industrial Energy Users-Ohio ("IEU-Ohio") respectfully submits this Application for Rehearing of the Finding and Order issued by the Public Utilities Commission of Ohio ("Commission") on October 17, 2012 approving Ohio Power Company's ("OP") (now merged with Columbus Southern Power Company or "CSP") (collectively, "AEP-Ohio") Application for Approval of an Amendment to Its Corporate Separation Plan[1] ("Corporate Separation Application"). The Commission's October 17, 2012 Finding and Order is unlawful and unreasonable in the following respects:

1. **The Finding and Order is unlawful, unreasonable, unjust and not in the public interest because it authorized AEP-Ohio to transfer its generating assets at net book value without netting the above-book market value of AEP-Ohio's generating assets against the non-bypassable transition revenue which the Commission has authorized AEP-Ohio to collect from retail customers. The structure of the asset transfer and price fixing monopoly buy-back transaction approved by the Commission is also**

[1] AEP-Ohio's Application and each previous Commission Entry in this proceeding have referred to this proceeding as "In the Matter of the Application of Ohio Power Company for Approval of Full Corporate Separation and Amendment to Its Corporate Separation Plan." Application (Mar. 30, 2012); Entry (Jul. 24, 2012); Entry (Jul. 9, 2012); Entry (May 29, 2012).

unlawful, unreasonable, unjust and not in the public interest because it is anticompetitive and violates the Valentine Act.[2]

2. **The *Finding and Order* is *unlawful and unreasonable* because *it* authorized AEP-Ohio to pass through non-bypassable transition revenue to AEP Generation Resources thereby providing AEP Generation Resources with an unfair competitive advantage contrary to Ohio's corporate separation requirements, imposing excessive and non-bypassable costs on retail consumers, violating Ohio's requirement that the generation business be fully on its own in the competitive market by December 31, 2010 or sooner and violating Ohio's Valentine Act.**

3. **The Finding and Order is unlawful and unreasonable because it authorized**[3] **AEP-Ohio to enter into an unbid contract with AEP Generation Resources to supply the requirements of the standard service offer load and capacity for shopping transactions at above-market prices. The affiliate contract and the affiliate transfer pricing contained therein are unlawful and unreasonable because they combine to provide AEP Generation Resources an unfair competitive advantage and an undue preference in violation of Section 4928.17(A)(2) and (3), Revised Code, in conflict with the state policy in Section 4928.02, Revised Code, and in conflict with the Valentine Act.**

As discussed in the Memorandum in Support attached hereto, IEU-Ohio respectfully requests that the Commission grant this Application for Rehearing.

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[2] Section 1331.01 (B)(5), Revised Code,[2] makes it clear that the types of agreements that are unlawful and void under the Valentine Act include pool agreements and other contracts "...of any kind by which they bind or have bound themselves not to sell, dispose of, or transport an article or commodity, or an article of trade, use, merchandise, commerce, or consumption below a common standard figure or fixed value, or by which they agree in any manner to keep the price of such article, commodity, or transportation at a fixed or graduated figure, or by which they shall in any manner establish or settle the price of an article, commodity, or transportation between them or themselves and others, so as directly or indirectly to preclude a free and unrestricted competition among themselves, purchasers, or consumers in the sale or transportation of such article or commodity, or by which they agree to pool, combine or directly or indirectly unite any interests which they have connected with the sale or transportation of such article or commodity, that its price might be in any manner affected."

[3] In various applications which AEP-Ohio has filed recently with the Federal Energy Regulatory Commission ("FERC"), AEP-Ohio has attested that the Commission approved the generation supply contract between AEP-Ohio and Genco and has otherwise blessed the entire scope and nature of the transaction which AEP-Ohio has now presented to FERC for approval. *AEP Generation Resources*, FERC Docket No. ER.13-232-000, Cover Letter to the Tariff Filing at 4. (Oct. 31, 2012).

Respectfully submitted,

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MEMORANDUM IN SUPPORT OF INDUSTRIAL ENERGY USERS-OHIO

I. INTRODUCTION

On October 17, 2012, the Commission approved, without a hearing and without requiring AEP-Ohio to provide information required by the Commission's rules,[4] AEP-Ohio's Corporate Separation Application.[5] The Order authorizes AEP-Ohio to proceed with structural separation of AEP-Ohio's generation business long after such separation was required to be completed by Ohio law and on terms that provide AEP-Ohio's affiliate, AEP Generation Resources ("Genco"), with an unreasonable and unlawful advantage in the competitive generation business at the expense of AEP-Ohio's retail customers. More specifically, the Order authorized the transfer of generating assets (and generation contracts or leases) from AEP-Ohio to Genco at the net book value of such assets while providing Genco with above-market compensation for the monopoly service Genco is to exclusively provide to AEP-Ohio subsequent to the asset transfer.

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[4] For example, the Commission permitted AEP-Ohio to avoid filing information on the market value of AEP-Ohio's generating assets. *In the Matter of the Application of Ohio Power Company for Approval of an Amendment to its Corporate Separation Plan*, Case No.12-1126-EL-UNC, Finding and Order at 12 (Oct. 17, 2012) (hereinafter the "Order").

[5] *Id.*

The direct economic prejudice of the unbid monopoly and price fixing supply contract between AEP-Ohio and Genco lands on AEP-Ohio's retail customers through above-market standard service offer ("SSO") generation supply prices and non-bypassable generation-related charges which the Commission has approved elsewhere.[6] The indirect prejudice extends to the larger generation supply market since the monopoly created by the structure approved by the Commission precludes other suppliers from securing the market share which is exclusively extended to Genco, contrary to the overarching pro-competitive purpose of Chapter 4928, Revised Code, and the policies set forth in Section 4928.02, Revised Code.

Ohio law commands the Commission to reject the creation of a monopoly through affiliate transactions and to reject above-market pricing for generation supply. The Commission's rules require that any transfer of generating assets be just, reasonable, and in the public interest. Ohio's corporate separation laws prohibit the anticompetitive subsidies, unfair competitive advantages, and undue preferences approved in the Order. The Valentine Act declares that the agreements sanctioned by the Order are unlawful and void because they work to create a monopoly and to fix prices in excess of the prices established by free commerce.[7] On rehearing, the Commission must rectify these unlawful and unreasonable aspects of the Order.

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[6] *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, Opinion and Order at 33 (Jul. 2, 2012) (hereinafter "Capacity Case" or "Capacity Case Order"); *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 Section 4928.143, Revised Code, in the Form of an Electric Security Plan*, Case Nos. 11-346-EL-SSO, *et al.*, Opinion and Order at 36 (Aug. 8, 2012) (hereinafter "ESP II Order" or "*ESP II Case*").

[7] While the Commission has held that it is not responsible for enforcing the Valentine Act, Capacity Case Order at 9, it is nonetheless obligated to comply with Ohio law. More specifically, the Commission cannot exercise its authority to approve corporate separation applications which contain terms and conditions that violate the Valentine Act. The Commission does not have authority to enforce the Ohio Constitution but it is nonetheless obligated to respect its commands. It is equally true that the Commission may not

II. BACKGROUND

AEP-Ohio filed its Corporate Separation Application on March 30, 2012. The Corporate Separation Application requested authority to transfer generating assets at net book value. As discussed further below, the Corporate Separation Application also requested approval to enter into an unbid generation supply contract with Genco to supply AEP-Ohio's SSO generation requirements after the transfer of generating assets. AEP-Ohio also requested that the Commission authorize AEP-Ohio to remit above-market generation transition revenue collected by AEP-Ohio from retail customers to Genco.

Concurrently with its Corporate Separation Application, AEP-Ohio filed an Application for an electric security plan ("ESP") to establish prices for default generation supply service through May 31, 2015.[8] The ESP Application requested that the Commission authorize AEP-Ohio to establish a non-bypassable retail stability rider ("RSR"). AEP-Ohio claimed that it was entitled to recover $929 million per year in generation-related revenue, and the RSR was proposed to replace generation-related revenue that AEP-Ohio claimed it would not be able to collect as customers switched to generation suppliers offering lower prices.[9] AEP-Ohio claimed the financial integrity of its competitive generation business would be at risk during the ESP period if the Commission did not approve the RSR to protect its generation business from the discipline of the competitive market.[10]

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approve corporate separation applications that violate the state policy set forth in Section 4928.02, Revised Code.

[8] ESP II *Order* at 6.

[9] *Id.* at 27-30.

[10] *Id.*

Over the objections of Industrial Energy Users-Ohio ("IEU-Ohio") and other parties, the Commission authorized AEP-Ohio to collect $508 million through the non-bypassable RSR during the ESP period to protect AEP-Ohio's generation business from competition.[11] While the Commission denied that the RSR provided illegal transition revenue to AEP-Ohio,[12] it is undisputed that the RSR provides AEP-Ohio with above-market generation revenue through non-bypassable charges that insulate AEP-Ohio's generation business from the discipline of the competitive market.

In a separate proceeding, and after asserting that the Commission lacked jurisdiction over generation capacity service provided to competitive retail electric service ("CRES") providers, AEP-Ohio requested Commission approval of a substantial increase in the compensation AEP-Ohio collects for providing such service to CRES providers serving shopping customers in AEP-Ohio's distribution service area. Previously, AEP-Ohio' s compensation for such service was tied to the capacity pricing and valuation methodology established by the PJM Interconnection LLC's ("PJM") Reliability Pricing Model ("RPM"), which relies upon an auction to value and price generation capacity service.[13] Again, AEP-Ohio claimed that, unless the Commission

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[11] ESP II Order at 36.

[12] The Commission stated:

> [W]e reject the claim that the RSR allows for the collection of inappropriate transition revenues or stranded costs that should have been collected prior to December 2010 pursuant to Senate Bill 3, as AEP-Ohio does not argue its ETP did not provide sufficient revenues, and, in light of events that occurred after the ETP proceedings, including AEP-Ohio's status as an FRR entity, AEP-Ohio is able to recover its actual costs of capacity, pursuant to our decision in the *Capacity Case*. Therefore, anything over RPM auction capacity prices cannot be labeled as transition costs or stranded costs.

ESP II Order at 32.

[13] Capacity Case, Opinion and Order at 4. The results of RPM are generally referred to herein as RPM-Based Pricing or the RPM Price.

increased the compensation for generation capacity service well above the RPM Price (the market price for capacity[14]), AEP-Ohio's competitive generation business would be subjected to financial losses as customers switched to CRES providers offering lower prices.[15]

Over the objections of IEU-Ohio and other parties, the Commission invented and applied a cost-based ratemaking methodology on its way to authorizing AEP-Ohio to substantially increase the compensation AEP-Ohio can now collect for the provision of generation capacity service.[16] The cost-based ratemaking methodology invented and applied by the Commission relied in part on the net book value of AEP-Ohio's owned and controlled generating assets.[17] Although the Commission determined that AEP-Ohio's embedded "cost" of capacity was $188.88 per megawatt day ("MW/day"),[18]

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[14] The Commission implicitly recognized that the RPM price is a market-based price, stating:

> All of the intervenors and Staff, on the other hand, recommend that market-based RPM capacity pricing should be approved as the state compensation mechanism for AEP-Ohio. As discussed above, there is a general consensus among these parties that RPM-based capacity pricing is just and reasonable, easily implemented and understood, and consistent with state policy.
>
> .... 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. The Commission's obligation under traditional rate regulation is to ensure that the jurisdictional facilities receive reasonable compensation for the services that they render. We conclude that the state compensation mechanism for AEP-Ohio should be based on the Company's costs.

Capacity Case Order at 22 (Jul. 2, 2012). The Commission also recognized that RPM price for capacity is established by the market, stating: "We note that the state compensation mechanism, once effective, shall remain in effect until AEP-Ohio's transition to full participation in the RPM market is complete...." *Id.* at 24. *See also Capacity Case*, Concurring Opinion of Commissioners Porter and Slaby at 1.

[15] *Id.* at 10-11, 15.

[16] *Id.* at 22.

[17] AEP-Ohio used the generation book value information contained in its FERC Form 1. *Capacity Case*, Opinion and Order at 33.

[18] *Id.* at 33.

the Commission directed AEP-Ohio to continue to charge CRES providers the RPM Price (approximately $20 per MW/day for 2012/2013) and defer the difference between the RPM price and the $188.88 MW/day price, with carrying charges, for future collection.[19]

Part of the capacity compensation increase deferral is being recovered through the non-bypassable RSR. The ESP II Order authorized AEP-Ohio to dedicate $1.00 of the per megawatt hour revenue collected through the RSR to the amortization of the capacity compensation increase deferral.[20] According to the Commission, the balance of such deferral will be recovered through a non-bypassable charge from shopping and non-shopping customers over a three year period, beginning in 2015.[21]

As a result of the Commission's decisions in the *Capacity Case* and the *ESP II Case*, AEP-Ohio is authorized to collect from shopping and non-shopping retail customers several hundred million dollars ($508 million from the RSR alone) in above-market compensation for generation supply service. This above-market compensation for generation supply service is otherwise known as "transition revenue" under Sections 4928.38 and 4928.39, Revised Code.[22] And, Section 4928.39, Revised Code, contains

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[19] *Capacity Case*, Opinion and Order at 23-24. The ESP Order authorized AEP-Ohio to collect the capacity deferral over three years, beginning in 2015.

[20] ESP II Order at 36.

[21] *Id.*

[22] In 2000, the Commission addressed and resolved AEP-Ohio's transition revenue claim by adopting a settlement. *In the Matter of the Applications of Columbus Southern Power Company and Ohio Power Company for Approval of Their Electric Transition Plans and for Receipt of Transition Revenues*, Case Nos. 99-1729-EL-ETP, *et al.*, Opinion and Order (Sep. 28, 2000). The Commission-approved settlement contained a commitment by AEP-Ohio that it would not collect transition revenue from shopping customers. The Commission's decisions in the *Capacity Case* and the *ESP II Case* ignore the prior resolution of AEP-Ohio's transition revenue claim and AEP-Ohio's commitment to not collect transition revenue from shopping customers. Section 4928.38, Revised Code, precludes the Commission form authorizing the collection of transition revenue beyond December 31, 2010 but the Commission has refused to respect this legislative command. Section 4928.38, Revised Code, also states that an EDU's

specific criteria that must be applied by the Commission to determine the amount of any transition revenue that the Commission may authorize an electric distribution utility ("EDU") such as AEP-Ohio to collect. These criteria are as follows:

(A) The costs were prudently incurred.
(B) The costs are legitimate, net, verifiable, and directly assignable or allocable to retail electric generation service provided to electric consumers in this state.
(C) The costs are unrecoverable in a competitive market.
(D) The utility would otherwise be entitled an opportunity to recover the costs.[23]

The statutory criteria which the Commission is obligated to follow for the purpose of addressing a transition revenue claim include a netting requirement. This netting requirement works to make sure that the amount of any transition revenue allowed by the Commission must net the above-book market value of assets against the assets with a market value below book value.

The concept of netting as it relates to the determination of allowable transition revenue has more than academic significance based upon the facts available to the Commission and the circumstances in this case. More specifically, the facts available to the Commission include an AEP-Ohio analysis[24] that shows that the future cash flow

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competitive generation business is to be fully on its own in a competitive market on or before December 31, 2010. Again, the Commission ignored this legislative command. *Capacity Case*, Entry on Rehearing at 19-20, 56-57 (Oct. 17, 2012). IEU-Ohio's assertions regarding the Commission's obligation to net the above-book market value of generating assets for purposes of determining the amount of transition revenue eligible for recovery are advanced herein because the Commission has thus far ignored the law of Ohio that forbids the Commission from authorizing transition revenue for collection post 2010. If the Commission has any authority to authorize AEP-Ohio to collect transition revenue post 2010, the Commission must do so, if it does so at all, based on the transition revenue criteria and process specified by Ohio law.

[23] Section 4928.39, Revised Code.

[24] *ESP II Case*, IEU-Ohio Ex. 121; *ESP II Case*, OCC Ex. 104. The Impairment Test Memo states that the need for the analysis occurred because there was a "triggering" regulatory event: the United States Environmental Protection Agency's ("EPA") Cross-State Air Pollution Rule ("CSAPR") OCC Ex. 104 at 1. The analysis reduced projected cash flow by $100 million per year for 2012-2014 to account for the effects of the rule. *Id.* at 4. On August 21, 2012, however, the United States Court of Appeals for the

from the pool of generating assets that include AEP-Ohio's assets is some $22 billion dollars more than the cash flow required to support the current book value of these generating assets.[25] The analysis assumes that the compensation for generation capacity service is based on the RPM Price (not the much higher $188.88 MW/day price approved by the Commission).[26] In other words, there is good reason to believe that the market value of these generating assets is greater than the net book value. Had the Commission not waived the requirement that AEP-Ohio provide information on the market value of its generating assets, AEP-Ohio would have had to present more detailed and specific information on the market value of its generating assets to secure the relief requested in its corporate separation application.

As explained above, the Commission's Order authorized AEP-Ohio to transfer its generating assets to Genco at net book value. The Commission's Order allows AEP-Ohio to transfer the above-book market value of the generating assets to Genco while concurrently permitting AEP-Ohio to collect generation-related transition revenue. In addition to authorizing AEP-Ohio to transfer the generating assets to Genco at net book value, the Commission's Order authorized AEP-Ohio to pass through to Genco the non-bypassable generation-related transition revenue which the Commission authorized AEP-Ohio to collect from retail customers in Ohio.

Finally, rather than procuring the SSO supply through a competitive bid after corporate separation, the Commission's Order authorized AEP-Ohio to enter into an

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District of Columbia Circuit vacated CSAPR. *EME Homer City Generation v. EPA*, Case No. 11-1302, 2012 WL 3570721 (D.C. Cir. Aug. 21, 2012).

[25] *ESP II Case*, OCC Ex. 104.

[26] *ESP II Case*, OCC Ex. 104; *ESP II Case*, IEU-Ohio Ex. 120; *ESP II Case*, IEU-Ohio Ex. 117; *see also ESP II Case*, IEU-Ohio Ex. 121 (containing confidential cash flow projections specific to AEP-Ohio's generating assets).

unbid contract with Genco to supply AEP-Ohio's SSO requirements. The price at which Genco will supply the SSO requirements will be above-market throughout the term of AEP-Ohio's ESP.[27]

III. ARGUMENT

1. The Finding and Order is unlawful, unreasonable, unjust and not in the public interest because it authorized AEP-Ohio to transfer its generating assets at net book value without netting the above-book market value of AEP-Ohio's generating assets against the non-bypassable transition revenue which the Commission has authorized AEP-Ohio to collect from retail customers. The structure of the asset transfer and price fixing monopoly buy-back transaction approved by the Commission is also unlawful, unreasonable, unjust and not in the public interest because it is anticompetitive and violates the Valentine Act.

Section 4928.17(E), Revised Code, requires an EDU to obtain Commission approval to sell or transfer its generating assets.[28] The Commission can approve a generating asset transfer only if it is just, reasonable, and in the public interest.[29] The Order's authorization to transfer AEP-Ohio's generating assets at net book value fails to satisfy these requirements.

As stated above, the Order effectively authorizes Genco to collect revenue from retail customers through the unbid contract, authorizes Genco to uniquely benefit from

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[27] AEP-Ohio did not solicit competitive bids to determine if a non-affiliate would supply the SSO requirements at a reduced price. ESP II Order at 60. Moreover, "Constellation and Exelon witness Fein testified that Exelon made an offer of energy and capacity and an offer for capacity only to serve AEP-Ohio's SSO load June 1, 2014 through May 31, 2016, at a cost lower than the Company is proposing as a part of this modified ESP." *Id.*

[28] Prior to Amended Substitute Senate Bill 221, EDUs were not required to obtain Commission approval to sell or transfer generating assets. The addition of this requirement and the purpose of the Commission's rules (4901:1-37-02, O.A.C.) dictate that generating assets transfers must be evaluated under the same considerations as corporate separation plan amendments and to ensure compliance with state policy.

[29] Rule 4901:1-37-09, O.A.C.

AEP-Ohio's collection of transition revenue from retail customers, and gifts generating assets to Genco that, according to AEP-Ohio's analysis, appear to have a market value in excess of the net book value transfer price. In light of these circumstances which reflect the combined effects of the Commission's decisions, it was not and is not just, reasonable, or in the public interest for the Commission to authorize AEP-Ohio to transfer its generating assets (and generation supply contracts or leases) to Genco at net book value.

Section 4928.39, Revised Code, requires that transition revenue be "net", meaning that transition costs must be netted against transition benefits including the ability of the utility to capture the above-book market value of its generating assets through the competitive market. Although the Commission has rejected the claim that the RSR and capacity compensation increase deferral mechanism provide AEP-Ohio with transition revenue well beyond the period allowed by Ohio law, it is nonetheless clear that the RSR and capacity compensation increase deferral mechanism provide AEP-Ohio (and ultimately Genco) with above-market compensation for generation-related service which AEP-Ohio asserts it will not be able to collect if customers are permitted to switch to suppliers offering lower and market-based generation supply prices.

The RSR and the capacity compensation increase deferral mechanism illegally provide AEP-Ohio with the equivalent of transition revenue.[30] Once the Commission has, rightly or wrongly, authorized AEP-Ohio to collect transition revenue or equivalent revenue, it must apply the netting principle in Section 4928.39, Revised Code. By

[30] Section 4928.38, Revised Code precludes the Commission from authorizing "...the receipt of transition revenues ***or any equivalent revenues*** ... except as expressly authorized in sections 4928.31 to 4928.40 of the Revised Code." (emphasis added)

allowing AEP-Ohio to transfer generating assets to Genco at net book value, the Commission is effectively evading its responsibility to apply this netting principle. The effective evasion of this netting principle makes the Order unjust, unreasonable, and not in the public interest. To remedy this unlawful and unreasonable condition, the Commission must, on rehearing, reduce the transition or equivalent transition revenue which the Commission has authorized AEP-Ohio to collect from shopping and non-shopping customers by the above-book market value of the assets which AEP-Ohio has been authorized to transfer to Genco.

The Commission's reasoning for authorizing AEP-Ohio to transfer its generating assets at net book value is simply wrong, and it cannot support a determination that the transfer is just, reasonable, and in the public interest:

> Because OP seeks only to transfer its generating assets to an affiliate within the same parent corporation, in compliance with the mandate of Section 4928.17, Revised Code, we agree that it is appropriate for OP to transfer the assets at net book value and note that this approach is consistent with our recent decision in the Duke case, 11-3549, and the Commission's decision in the Company's prior corporate separation case in Case No. 11-5333-EL-UNC, although the request was subsequently withdrawn.[31]

A result that is just, reasonable and in the public interest cannot be obtained in circumstances where the Commission has limited its analysis because the transfer of generating assets is between affiliates. What is just, reasonable and in the public interest does not depend on which entity is receiving AEP-Ohio's generating assets. It depends on the terms and conditions of such transfer and the effect that the transfer has on AEP-Ohio's customers. Regardless of the ultimate destination of the generating assets, one thing remains: retail customers will be required to foot the bill for above-

[31] Finding and Order at 22.

market generation revenue, while AEP-Ohio will be permitted to transfer to its affiliate non-bypassable transition revenue as well as the above-book market value of the generating assets. The combined effect of the Commission's actions in this proceeding with actions by the Commission in the *Capacity Case* and in the *ESP II Case* render the Commission's decision in this proceeding unjust, unreasonable, and not in the public interest.

The Commission's reliance on its decision involving Duke Energy Ohio, Inc. ("Duke") is also inappropriate. The Duke proceeding was resolved as part of a global settlement that recommended, as part of a larger package, that Duke be authorized to transfer its generating assets at net book value.[32] The Duke settlement also called for RPM-Based Pricing. The Duke settlement also specifically states that it cannot be relied upon as precedent in any proceeding.[33] Regardless, the facts and circumstances of AEP-Ohio's proposed generating asset transfer are completely different, and the circumstances identified above dictate that the Order's approval of AEP-Ohio's generating asset transfer is not just, reasonable, and in the public interest. In this case, the Commission's Order is unlawful and unreasonable.

The Commission on rehearing must direct AEP-Ohio to net the above-book market value of its generating assets against the RSR revenue and capacity compensation increase deferral. Otherwise, the Order authorizing the asset transfer is unjust, unreasonable, and not in the public interest.

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[32] The settlement specifically states that neither the settlement nor any Commission Order adopting it may be relied upon as precedent in any other proceeding. *In the Matter of the Application of Duke Energy Ohio for Authority to Establish a Standard Service Offer Pursuant to Section 4928.143, Revised Code, in the Form of an Electric Security Plan Accounting Modifications and Tariffs for Generation Service*, Case Nos. 11-3549-EL-SSO, *et al.*, Stipulation and Recommendation at 25 (Oct. 24, 2011).

[33] *Id.* at 2.

The asset transfer and price fixing monopoly buy-back transaction as a whole also fails to satisfy the standard that the transfer be just, reasonable, and in the public interest.[34] This standard must be applied in the context of the purpose of the Commission's rules on corporate separation and asset transfers. And Rule 4901:1-37-02, O.A.C., states (emphasis added):

> (A) The purpose of this chapter[35] is to require all of the state's electric utilities to meet the same standards so a competitive advantage is not gained solely because of corporate affiliation.
>
> (B) **This chapter is intended to create competitive equality, prevent unfair competitive advantage, prohibit the abuse of market power and effectuate the policy of the state of Ohio embodied in section 4928.02 of the Revised Code.**

Section 4928.06, Revised Code, moreover, states that "[b]eginning on the starting date of competitive retail electric service, the public utilities commission shall ensure that the policy specified in section 4928.02 of the Revised Code is effectuated." Section 4928.02, Revised Code, states that the Commission must avoid anticompetitive subsidies:

> Ensure effective competition in the provision of retail electric service by avoiding anticompetitive subsidies flowing from a noncompetitive retail electric service to a competitive retail electric service or to a product or service other than retail electric service, and vice versa, including by prohibiting the recovery of any generation-related costs through distribution or transmission rates.

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[34] 4901:1-37-09, O.A.C.

[35] Under Rule 4901:1-37-03, O.A.C.:

> (A) The provisions of this chapter shall be applicable in accordance with sections 4928.17 and 4928.18 of the Revised Code and apply to:
>
> (1) The activities of the electric utility and its transactions or other arrangements with its affiliates.
>
> (2) Any shared services of the electric utilities with any affiliates.
>
> (3) The sale or transfer of generating assets.

And, Section 4928.02(C) and (E), Revised Code, require the Commission to promote customer choice.

Because of Ohio's declaration in Section 4928.03, Revised Code, that generation service is a competitive service and the pro "customer choice" policies in Section 4928.02, Revised Code, Ohio's laws directed at anticompetitive conduct must be considered by the Commission for purposes of determining whether AEP-Ohio's proposed transfer of generating assets and corporate separation application are just, reasonable, and in the public interest. In consideration of these criteria, the structure of the transaction between AEP-Ohio and Genco — a transaction designed to fix prices in excess of the prices established by free commerce, subsidize Genco, and promote the establishment of a monopoly — is unjust, unreasonable, and not in the public interest.

Case law further reinforces the principle that competitive considerations, including compliance with antitrust statutes, should be considered in determining whether an activity or transaction is in the public interest. In *Northern Natural Gas Company v. Federal Power Commission*, the Court determined that "competitive considerations are an important element of the 'public interest.'"[36] In *Federal Maritime Commission v. Aktiebolaget Svenska Amerika Linien*, the Supreme Court upheld the Federal Maritime Commission's application of an antitrust test to a public interest standard even though an antitrust test was not specifically required:

> Insofar as this holding rests on the absence of an explicit antitrust test among the "four ways set out in the section, 'we think the Court of Appeals was excessively formalistic in its approach to the Commission's findings.

[36] *Northern Natural Gas Company v. Federal Power Commission*, 399 F.2d 953, 960-961 (1968) (Ct. App., D.C. Cir.) ("because competitive considerations are an important element of the "public interest," we believe that in a case such as this the Commission was obliged to make findings related to the pertinent antitrust policies, draw conclusions from the findings, and weigh these conclusions along with other important public interest considerations.")

> By its very nature an illegal restraint of trade is in some ways 'contrary to the public interest,' and the Commission's antitrust standard, involving an assessment of the necessity for this restraint in terms of legitimate commercial objectives, simply gives understandable content to the broad statutory concept of 'the public interest.'"[37]

Because the contract with Genco and pass through of transition revenue is designed to fix prices in excess of the prices established by free commerce and promote the establishment of a monopoly, the transaction violates Ohio's antitrust law, the Valentine Act, and is against the public interest.

Ohio's Valentine Act[38] (Chapter 1331, Revised Code), like the federal Sherman Act uses the language of the late nineteenth century when it speaks of "trusts" and declares them to be unlawful and against public policy. Section 1331.01, Revised Code, defines a trust as "a combination of capital, skills or acts by two or more persons..." for any of six enumerated anticompetitive purposes.

The circumstances surrounding the passage of the Valentine Act in 1898, however, make it clear that this broad language was intended to encompass a much wider array of anticompetitive combinations [everything from a powerful single firm wielding its power to control production or prices (*i.e.*, a combination of the "capital" of shareholders), to collusive agreements among multiple firms in the market (*i.e.*, a combination of "acts" by conspiring firms)].

The Valentine Act's prohibition of "trusts" was not a new concept under Ohio law. Rather, it was a codification of well-established common law principles, consistent with

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[37] *Federal Maritime Commission v. Aktiebolaget Svenska Amerika Linien*, 390 U.S. 238, 244 (1968).

[38] Much of the discussion below regarding the Valentine Act and the nature and scope of Ohio's prohibitions on anticompetitive behavior is taken from the Brief submitted by the Ohio Attorney General on March 23, 2012 in *Google, Inc. vs. myTriggers.com, Inc.*, Case No. 11AP-1003, Court of Appeals, Tenth Appellate District, On Appeal from the Franklin County Common Pleas Court.

those embodied in the Sherman Act passed at the federal level eight years earlier.[39] At the heart of those common law principles is the idea that monopolies — concentrations of power in a single entity — are antithetical to the public interest and should be prohibited. *See Central Ohio Salt Co. v Guthrie,* 35 Ohio St. 666, 672 (1880) (public policy "unquestionably" favors competition and opposes monopolies); *Crawford & Murray v. Hugh B. Wick* 18 Ohio St. 190, 126 (1868) (voiding a bond that restrains trade because it "tends to a [monopoly] and is against the public good").[40] Indeed the statutory chapter created by the Valentine Act is titled "Monopolies", leaving no doubt as to the intended reach of the legislation.

There is no more clear indication that the Ohio common law which formed the foundation of the Valentine Act prohibited anticompetitive practices than the Ohio Supreme Court's decision in *State v. Standard Oil Co.*, handed down six years prior to the enactment of the Valentine Act and two years after the enactment of the Sherman Act. Attorney General David K. Watson brought suit against The Standard Oil Company, ("Standard Oil"), alleging that the company was an unlawful trust — a single firm comprised of interests that controlled the price of oil to the detriment of the public.[41] The Attorney General prevailed. The Court found *Standard Oil* to be a combination "whereby many separate interests being united under one management, form a virtual

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[39] *See United States Telephone Co. v Central Union Telephone Co.* 202 F2nd 66, 70 (6th Cir. 1913) (common law principles regarding restriction of competition are codified for Ohio in the Valentine Act and for the United States in the Sherman Act).

[40] *See Central Ohio Salt Co. v Guthrie*, 35 Ohio St. 666, 672 (1880) (public policy "unquestionably" favors competition and opposes monopolies); *Crawford & Murray v Hugh B. Wick* 18 Ohio St. 190, 126 (1868) (voiding a bond that restrains trade because it "tends to a [monopoly] and is against the public good").

[41] *State v. Standard Oil Co.*, 49 Ohio St. 137 (1892). (hereinafter cited as "*Standard Oil*")

monopoly through the power acquired of so controlling the production and price of petroleum and its products, as to destroy competition."[42]

The passage of the Valentine Act in 1898 codified the common law that unreasonable concentrations of power are unlawful and injurious to the public interest. Demonstrating the importance of these policies, the General Assembly provided for both criminal and civil enforcement.

In 1905, the Ohio Supreme Court considered the appeal of Perley W. Gage from his criminal conviction under Ohio's new antitrust law for participating in The Delaware Coal Exchange, "an association of persons organized for the purpose of preventing competition in the sale, and to maintain a uniform and graduated figure for the sale of coal . . . ."[43] In affirming a Valentine Act conviction, the Court pointed out that the acts of this single entity violated Ohio's antitrust law saying: "The Delaware Coal Exchange, as its purpose is defined in the indictment, is a trust within both the third and fourth subdivision of the first section of the act and that section defines the combinations which the act prohibits."[44]

In *Gage*, the Ohio Supreme Court recognized that Ohio's new Valentine Act, like the common law on which it was based, proscribed combinations such as those the Court in *Standard Oil* described as "many separate interests being united under one management."[45]

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[42] *Id* at 186.

[43] *State of Ohio v. Gage*, 72 Ohio St. 210 (1905). (hereinafter cited as "*Gage*").

[44] *Id* at 229.

[45] *Standard Oil* at 183

As the evidence in this proceeding, the *Capacity Case* and in the *ESP II Case* shows, AEP-Ohio itself consists of separate distribution, transmission, generation, regulated and unregulated lines of business having different interests that operate under one management. It is clear, from the Commission's decisions and the totality of the relief which the Commission has provided to AEP-Ohio and its affiliates works to restrain commerce that would otherwise occur. The Commission and AEP-Ohio prefer to describe this restraint of commerce as a "transition to competition" but it is a restraint nonetheless. AEP-Ohio has pursued this goal both through the combination of various interests that are subject to common management and through agreements (including the agreement with Genco that was before the Commission in this proceeding) with the support and active approval of the Commission.

Section 1331.01 (B)(5), Revised Code,[46] makes it clear that the types of agreements that are unlawful and void under the Valentine Act include pool agreements and other contracts:

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[46] Section 1331.04, Revised Code, states:

> A violation of sections 1331.01 to 1331.14, inclusive, of the Revised Code, is a conspiracy against trade. No person shall engage in such conspiracy or take part therein, or aid or advise in its commission, or, as principal, manager, director, agent, servant, or employer, or in any other capacity, knowingly carry out any of the stipulations, purposes, prices, or rates, or furnish any information to assist in carrying out such purposes, or orders thereunder, or in pursuance thereof, or in any manner violate said sections. Each day's violation of this section is a separate offense.

Section 1331.06, Revised Code, states:

> A contract or agreement in violation of sections 1331.01 to 1331.04, inclusive, of the Revised Code, is void.

Section 1331.08, Revised Code, states:

> In addition to the civil and criminal penalties provided in sections 1331.01 to 1331.14 of the Revised Code, the person injured in the person's business or property by another person by reason of anything forbidden or declared to be unlawful in those sections, may sue therefor in any court having jurisdiction and venue thereof, without respect to the

> [O]f any kind by which they bind or have bound themselves not to sell, dispose of or transport an article or commodity, or an article of trade, use, merchandise, commerce, or consumption below a common standard figure or fixed value, or by which they agree in any manner to keep the price of such article, commodity, or transportation at a fixed or graduated figure, or by which they shall in any manner establish the price of any article, commodity, or transportation between them or themselves and others, so as directly or indirectly to preclude a free and unrestricted competition among themselves, purchasers, or consumers in the sale or transportation of such article or commodity, or by which they agree to pool, combine or directly or indirectly unite any interests which they have connected with the same or transportation of such article or commodity, that its price might be affected.

Since the Corporate Separation Application, as approved by the Commission, provides AEP-Ohio and its affiliates with the ability and opportunity to establish the price of one or more electric services "between them or themselves and others, so as directly or indirectly to preclude a free and unrestricted competition among themselves, purchasers, or consumers in the sale or transportation of . . ."[47] electricity, the Corporate Separation Application and the Commission's Order approving the Application are, by the force of the Valentine Act, unjust, unreasonable and contrary to the public interest.

> amount in controversy, and recover treble the damages sustained by the person and the person's costs of suit. When it appears to the court, before which a proceeding under those sections is pending, that the ends of justice require other parties to be brought before the court, the court may cause them to be made parties defendant and summoned, whether or not they reside in the county where the action is pending.

Section 1331.99, Revised Code, states:

> (A) Whoever violates section 1331.02 or 1331.05 of the Revised Code is guilty of a felony of the fifth degree.
>
> (B) Whoever violates section 1331.04 or division (L) of section 1331.16 of the Revised Code is guilty of a misdemeanor of the first degree.
>
> (C) Whoever violates section 1331.15 of the Revised Code is guilty of a misdemeanor of the second degree.

[47] 1331.01(B)(5), Revised Code.

2. **The Finding and Order is unlawful and unreasonable because it authorized AEP-Ohio to pass through non-bypassable transition revenue to AEP Generation Resources thereby providing AEP Generation Resources with an unfair competitive advantage contrary to Ohio's corporate separation requirements, imposing excessive and non-bypassable costs on retail consumers, violating Ohio's requirement that the generation business be fully on its own in the competitive market by December 31, 2010 or sooner and violating Ohio's Valentine Act.**

The Commission's Order authorized AEP-Ohio to pass through to Genco the non-bypassable RSR transition revenue and the capacity compensation deferral.[48] Although the Commission refrained from determining whether the revenue pass through violated federal standards pertaining to affiliate transactions,[49] such pass through also violates Ohio law.

Ohio law favors competition and prohibits anticompetitive practices. Section 4928.17(A)(2), Revised Code, requires an EDU's corporate separation plan to satisfy "the public interest in preventing unfair competitive advantage and preventing the abuse of market power" (emphasis added). Additionally, Section 4928.17(A), Revised Code, requires a corporate separation plan to comply with Section 4928.02, Revised Code, which requires the plan to "[e]nsure effective competition in the provision of retail electric service by avoiding anticompetitive subsidies flowing from a noncompetitive retail electric service to a competitive retail electric service or to a product or service other than retail electric service, and vice versa, including by prohibiting the recovery of any generation-related costs through distribution or transmission rates." Consistent with this pro-competitive theme, Section 4928.38 and 4928.40, Revised Code, requires a utility's generation business to be on its own in the competitive market and cease

[48] Order at 19, 25.

[49] Order at 19.

recovery of transition revenue no later than December 31, 2010. Likewise, the Valentine Act declares that the agreements that work to create a monopoly and to fix prices in excess of the prices established by free commerce are void. The pass through of above-market non-bypassable transition revenue from AEP-Ohio to Genco insulates Genco from competition and violates each of these prohibitions.

The Commission previously correctly determined that non-bypassable recovery of generation-related costs is equivalent to an illegal subsidy, stating "[a]pproval of such a charge would effectively allow the Company to recover competitive, generation-related costs through its noncompetitive, distribution rates, in contravention of the statute."[50] The pass through of generation-related non-bypassable revenue from AEP-Ohio subsidizes Genco because it provides Genco with a non-bypassable above-market revenue stream that it would not be able to collect from customers for generation service if such customers were permitted to select their generation service provider at market prices.

The subsidy authorized in this proceeding is even more anticompetitive than the Sporn plant closure costs rejected above. Genco will supply the SSO requirements but it will also compete with other CRES providers. The Commission Order, however, authorized Genco to receive a non-bypassable generation-related revenue stream from AEP-Ohio. There is no evidence to suggest that any other CRES provider is bankrolled by such a non-bypassable revenue stream. Because collection of the capacity deferral

[50] *In the Matter of the Application of Ohio Power Company for Approval of the Shutdown of Unit 5 of the Philip Sporn Generating Station and to Establish a Plant Shutdown Rider,* Case No. 10-1454-EL-RDR, Finding and Order at 16-17 (Jan. 11, 2012) (hereinafter "Sporn Decision").

will occur from 2015 to 2018,[51] the market-distorting effects of the capacity deferral subsidy will resonate for years to come.

The pass through also violates the requirement that Genco be "on its own in the competitive market." Clearly, Genco will not be on its own in the competitive market because the Commission has required AEP-Ohio's retail customers to guarantee that Genco has a non-bypassable revenue stream that would not be available in the absence of the Order. Rather than respecting the December 31, 2010 transition revenue cut-off date included in Ohio law, the Commission has extended the date upon which Genco will be on its own in the competitive market until 2018.

Finally, the pass through of transition revenue from AEP-Ohio to Genco also violates the Valentine Act.[52] The Valentine Act renders void any contract that works to create a monopoly and to fix prices in excess of the prices established by free commerce. The pass through of non-bypassable revenue approved in the Order requires retail customers to pay above-market prices for generation service in violation of the Valentine Act.

Even if the Commission determines that it cannot enforce the Valentine Act, the Commission cannot issue an Order that violates Ohio law or is contrary to the public interest. As identified above in Assignment of Error 1, Courts have determined that antitrust principles should be considered to evaluate the public interest.[53] And Section

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[51] ESP II Order at 36.

[52] IEU-Ohio incorporates its discussion of the Valentine Act in Assignment of Error 1 by reference.

[53] *Federal Maritime Commission v. Aktiebolaget Svenska Amerika Linien*, 390 U.S. 238, 244 (1968); *Northern Natural Gas Company v. Federal Power Commission*, 399 F.2d 953, 960-961 (1968) (Ct. App., D.C. Cir.)

4928.17(A)(2), Revised Code, requires the corporate separation plan to satisfy the "public interest in preventing unfair competitive advantage and preventing the abuse of market power." Thus, the Valentine Act is relevant to the Commission's analysis of the pass through of transition revenue to Genco authorized in the Order.

The Commission can, in part, remedy the anticompetitive effects of its Order by netting against the previously authorized transition revenue the above-book market value of AEP-Ohio's generating assets.

3. The Finding and Order is unlawful and unreasonable because it authorized AEP-Ohio to enter into an unbid contract with AEP Generation Resources to supply the requirements of the standard service offer load and capacity for shopping transactions at above-market prices. The affiliate contract and the affiliate transfer pricing contained therein are unlawful and unreasonable because they combine to provide AEP Generation Resources an unfair competitive advantage and an undue preference in violation of Section 4928.17(A)(2) and (3), Revised Code, in conflict with the state policy in Section 4928.02, Revised Code and in conflict with the Valentine Act.

The Order approved an above-market contract between AEP-Ohio and Genco through which Genco will supply AEP-Ohio's SSO generation requirements and capacity requirements. Genco was not chosen as a result of a competitive bid, and, in fact, AEP-Ohio turned down an offer from Exelon Corporation to supply AEP-Ohio's capacity and SSO generation requirements at a reduced price.[54] Although the Commission did not determine, one way or the other, whether AEP-Ohio's preferential contract with Genco violated federal standards pertaining to affiliate transactions,[55] the contract also violates Ohio law.

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[54] ESP II Order at 60.

[55] Order at 19.

Section 4928.17(A)(2), Revised Code, requires an EDU's corporate separation plan to satisfy "the public interest in preventing unfair competitive advantage and preventing the abuse of market power." And Section 4928.17(A)(3), Revised Code, requires AEP-Ohio's corporate separation plan to be "sufficient to ensure that the utility will not extend any undue preference or advantage to any affiliate . . . ." Likewise, Section 4928.02, Revised Code, contains pro-competitive policies that favor "customer choice" and reasonably priced electricity. And the Valentine Act renders void contracts that work to create a monopoly and to fix prices in excess of the level established by free commerce.[56]

The unbid contract between AEP-Ohio and Genco allows Genco to supply the SSO generation requirements at above-market rates and to recover above-market capacity compensation.[57] These above-market revenue streams are against the public interest because they provide Genco with an unfair competitive advantage relative to other CRES providers that must compete in AEP-Ohio's service territory.

The contract also violates Ohio law because it provides Genco an undue preference. Rather than accepting offers to provide capacity and energy at a lower price, or even soliciting bids to determine whether such offers exist, AEP-Ohio entered into a contract with its affiliate to ensure that retail customers continue to pay above-market rates.

The contract also works against the pro-competitive goals contained in Section 4928.02, Revised Code, because it perpetuates AEP-Ohio's above-market prices rather

[56] IEU-Ohio incorporates its previous discussion of the Valentine Act by reference.

[57] ESP II Order at 60.

than soliciting competitive bids to determine if another generation provider will supply the SSO requirements and capacity at a lower price.

The above-market contract also violates the Valentine Act because it provides Genco with a monopoly over the right to provide capacity and energy to AEP-Ohio retail customers at a price in excess of the level that would be produced by free commerce.[58] Courts have determined that antitrust principles should be considered in determining whether anticompetitive arrangements are in the public interest.[59] Section 4928.17(A)(2), Revised Code, also requires AEP-Ohio's corporate separation plan to satisfy the public interest in preventing an unfair competitive advantage. Because the contract violates the Valentine Act, even if the Commission cannot enforce the Valentine Act, the contract must be rejected because it is against the public interest. The Commission, on rehearing, should direct AEP-Ohio to supply the SSO generation requirements as well as capacity for shopping customers through a competitive bidding process.

IV. CONCLUSION

For the reasons stated herein, the Commission should grant IEU-Ohio's Application for Rehearing.

Respectfully submitted,

Samuel C. Randazzo (Counsel of Record)

[58] IEU-Ohio incorporates its prior arguments in Assignments of Error 1 and 2 by reference.

[59] *Federal Maritime Commission v. Aktiebolaget Svenska Amerika Linien*, 390 U.S. 238, 244 (1968); *Northern Natural Gas Company v. Federal Power Commission*, 399 F.2d 953, 960-961 (1968) (Ct. App., D.C. Cir.)

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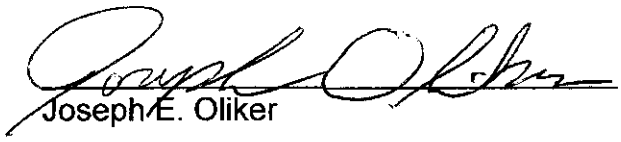
Certificate of Service

I hereby certify that a copy of the foregoing *Application for Rehearing and Memorandum in Support of Industrial Energy Users-Ohio,* was served upon the following parties of record this 16th day of November 2012, *via* electronic transmission, hand-delivery or first class U.S. mail, postage prepaid.



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