

**BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO**

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

**OHIO POWER COMPANY'S MEMORANDUM CONTRA
INTERVENORS' APPLICATIONS FOR REHEARING**

INTRODUCTION

On November 16, 2012, the Office of the Ohio Consumers' Counsel (OCC) and Industrial Energy Users-Ohio (IEU) filed applications for rehearing contending that the Commission's October 17, 2012 Finding and Order is unlawful and unreasonable. Ohio Power Company (AEP Ohio) hereby files its memorandum contra.

ARGUMENT

I. The Commission's decision allowing the Company to transfer its generation assets at net book value to an affiliate within the same parent corporation, in compliance with the mandate of Section 4928.17, is lawful and reasonable.

Both OCC and IEU contend that rehearing is necessary because the Commission erred in finding that the transfer of generating assets should be at net book value, instead of market value. This central point is the basis for all of OCC's and most of IEU's grounds for rehearing.

A. The Commission lawfully waived its administrative rule.

OCC asserts that the finding itself is not based on specific findings of facts and is not supported by the record in violation of R.C. 4903.09. According to OCC, the Commission's decision lacks proper record support because the Commission did not require the Company to submit a market evaluation of its generation assets. (OCC AFR at 3-4). Without this

information, OCC contends it is impossible for the Ohio Supreme Court to determine if the Finding and Order is reasonable and lawful and the "lack of a record stymies a complaining party's effort in demonstrating prejudice, a necessary element for the Ohio Supreme Court to reverse the Commission." (*Id.*)

OCC appears to be arguing that the Commission can never waive one of its administrative rules because doing so will inhibit a losing party's appeal. Taking OCC's view, all evidence must be placed in the record – even information which the Commission determines appropriate to waive – so any losing party can make a record for appeal. Such an approach makes no sense and would deprive the Commission of the ability to grant waivers (which was created at the same time the rule was created) and would effectively deny the waiver for the utility. OCC's approach is not how the Commission administers its proceedings, nor is it consistent with the Commission's rules.

The market valuation concept at issue is reflected in Ohio Admin. Code (AOC) Rule 4901:1-37-09(C)(4). It is a administrative rule adopted by the Commission that has no statutory basis and has never been enforced against any electric utility in implementing corporate separation. Under OAC Rule 4901:1-37-02(C), the Commission may waive any requirement of Chapter 37 for good cause shown. The Company made a request to waive the rule in its Application, which the Commission granted based on good cause shown.

The Commission's decision to waive the rule and, ultimately, to permit AEP Ohio to transfer its generation assets at new book value is lawful and reasonable because the Company seeks to transfer its generating assets to an affiliate within the same parent corporation, in compliance with the mandate of R.C. 4928.17. The Company is not, for example, transferring these assets as a result of some optional for-profit spin off to a third party. Indeed, under SB 3,

all of the generation assets at issue were subjected to market, and EDUs were given a temporary opportunity to recover stranded generation investments during a transition period. EDUs can no longer recover stranded generation investments, and transferring the generation assets based on an arbitrary determination of their current fair market value rather than net book value would be inappropriate.

The Commission recently determined, based on information similar to what the Company provided in its Application, that it was in the public interest to waive Rule 4901:1-37-09(C)(4) and allow Duke Energy Ohio to transfer its generation assets at net book value.¹ If that treatment was in the public interest for Duke Energy Ohio, it is also in the public interest to grant AEP Ohio's similar request. Further, as a result of that recent decision, there was good cause to apply the same rule to similar facts in a consistent manner so as not to create an unfair and unlevel playing field for competition.

R.C. 4928.17 – the controlling statute regarding corporate separation matters – requires the Commission to ensure that an approved corporate separation plan does not extend an undue advantage or preference in the provision of competitive electric services. *See* R.C.

4928.17(A)(3). Granting Duke Energy Ohio's affiliate full and final approval for generation divestiture up front and waiving the filing and process rules, while simultaneously deferring approval of AEP Ohio's transfer of assets to AEP Genco and possibly subjecting it to market valuation studies and protracted litigation, serves to provide Duke Energy Ohio with an undue preference and advantage in violation of this statute. The better approach is to grant AEP Ohio

¹ *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 No. 11-3549-EL-SSO, Opinion and Order (November 22, 2011), and Entry on Rehearing (January 18, 2012).

the same relief afforded to Duke Ohio, which is exactly what the Commission did at page 22 in its Finding and Order.

An inconsistent application of the corporate separation statutory provisions and rules would be anticompetitive and would provide one entity a competitive advantage in violation of R.C. 4928.02. If Duke Energy Ohio is able to transfer its generation assets at net book value and AEP Ohio is subject to greater scrutiny and a different valuation methodology, then Duke Energy Ohio would be receiving an unfair benefit from the truncated process, which would allow Duke Energy Ohio to avoid the costs associated with complying with O.A.C. 4901:1-37-09(C)(4), and potentially transfer its assets at a different valuation level. Nowhere is the direct difference more obvious than in the case of the jointly owned utility assets. If Duke Energy Ohio were able to transfer those assets at net book value to its competitive generation affiliate but AEP Ohio was required to transfer its assets to AEP Genco at a potentially greater cost, over a greater period of time, and in some cases to even transfer the same assets under a different methodology, then Duke's competitive generation company would be receiving a competitive advantage over the AEP Genco.

In sum, OCC's argument that granting the waiver affects a losing party's ability to make a record for appeal ignores the law. The Company is required by law to transfer its generation assets. It filed its Application to implement its corporate separation under R.C. 4928.17. If the General Assembly wanted to require by law that as part of this process the Company must provide a market evaluation of its generation assets, it could have done so. It did not, and there is no such requirement in the law. The only requirement is by Commission rule, which the Commission may – and did – waive. The Commission found good cause to waive its

administrative rule and its decision to permit the transfer at net book value is lawful, reasonable, and is consistent with its precedent.

B. There is no undue preference.

Unlike the potential undue preference or advantage described above that would only be triggered if the Commission had denied the market valuation waiver, OCC argues that “[u]se of net book value instead of market value is likely to result in compensation that is too low, which would provide the Company’s affiliate with an unfair competitive advantage and result in anticompetitive subsidies flowing from the Company to its affiliate.” (OCC AFR at 8). On rehearing, OCC asks that the Commission allow the record to be developed that includes the market value of the transferred assets so that parties can “put forth arguments about how the premium associated with the market value of the assets over their net book value should be allocated.” (*Id.*)

As explained above and as understood by the Commission, a showing of market value is not a statutory requirement, and the Commission can waive an administrative rule when good cause is demonstrated. OCC recycles the same arguments it advanced in opposition to the waiver request, which the Commission already considered and rejected. These arguments completely ignore the Commission's treatment of other electric utilities (FirstEnergy utilities and Duke Energy Ohio) in the past and the fact that the Commission has never applied this administrative rule requirement on any electric utility. OCC's undue preference allegations, additionally, are based solely on pure speculation that the market value of the assets exceeds the book value. This point is not only devoid of any record support, but it is also contrary to OCC’s position in the Capacity Charge case that AEP Ohio’s cost-based rate was substantially “above market.” (OCC Initial Post Hearing Brief in Case No. 10-2929-EL-UNC at pp. 2, 9.)

OCC's suggested remedy to debate how alleged premiums associated with the market value can be "allocated" is based on a fundamental misunderstanding of what customers receive when they pay for electric service. Customers pay for electric service and are not investors in utility plant in service, whether it is poles and wire or a power plant. (*In the Matter of the Regulation of the Electric Fuel Component Contained within the Rate Schedules of Columbus Southern Power Company and Related Matters*, Case No. 88-102-EL-EFC, Opinion and Order (October 28, 1988) at pp. 14-16, and Entry on Rehearing (December 20, 1988) at p. 8.) Under SB 3, all of these generation assets were subjected to market and EDUs, therefore, were given a temporary opportunity to recover stranded generation investments during a transition period. The General Assembly simultaneously required generation divestiture and did not provide for any gain, whether real or artificial, to be flowed back to ratepayers. OCC's arguments to the contrary (OCC AFR at 10-11) are without merit and do not form a valid basis for rehearing.

Generation divestiture from the EDU to an affiliate does not create any premium or gain for AEP – it is simply transferring assets from one affiliate to another within the same holding company – as required by Ohio law. OCC's (and IEU's, see IEU AFR at 12-14) windfall argument is based on a speculative presumption of high market value for the generation assets and incorrectly assumes that ratepayers have an ownership interest in such assets. Requiring AEP Ohio to recognize a gain or loss on the transfer would, in reality, cause an arbitrary financial impact on the Company that would not be shared with ratepayers whether a gain or loss. In addition to being unprecedented and unfair, as the Company noted in its Reply Comments, such an approach would create a "poison pill" in connection with the Modified ESP. It is unacceptable to AEP Ohio to leave the corporate separation issue open and subject AEP Ohio to a potential arbitrary gain or loss at a later date; it is crucial that corporate separation be

resolved and that the assets be transferred at net book value. The Commission's decision appropriately understood that AEP Ohio cannot move forward under the Modified ESP without these issues resolved on that basis.

C. The good cause standard for waiver is satisfied based on the Commission's finding that it was reasonable.

OCC asserts that rehearing should be granted because the Commission applied the wrong standard (reasonable v. good cause) when it granted the Company's waiver. (OCC AFR at 8-9.) As a result, OCC contends, a record of the market value of the assets was not created and it was prejudiced. This is a non-substantive objection, which does not merit rehearing. The Commission has made clear the basis of its decision to grant the waiver; OCC merely disagrees with it for the same reasons it opposed the initial waiver request. If the Commission deems necessary, it can clarify this finding on rehearing. The result, however, will remain the same in that the reasons supporting the Commission's approval of the waiver have not changed.

D. Netting regulatory asset charges against a fictitious market premium is misplaced and without merit.

OCC argues that it was unreasonable for the Commission not to give value to customers for the stranded generation costs that they previously paid through the regulatory asset charges collected from them under Commission-approved regulatory transition charges in Case No. 99-1729-EL-ETP, *et. al.* (OCC AFR at 10.) OCC maintains that in connection with evaluating whether the transfer at net book value was in the public interest, the Commission should have evaluated the fair market value of the assets and netted a portion of the alleged market premium against what customers have paid in regulatory transition charges. (*Id.*)

IEU advances a similar argument. IEU argues that the recovery by the Company of any above-market generation revenue for capacity (and any retail stability rider (RSR) revenues

authorized by the Commission) would be contrary to the netting principles of 4928.39 (regarding total allowable transition costs under SB 3) if at the same time the Company conveys the above-book value of its generating assets to its affiliate. (IEU AFR at 14.) The appropriate remedy in IEU's view is to reduce the RSR, which IEU contends is an equivalent of transition revenues, by the above market values of the assets. (*Id.*) To support its claim that netting is necessary, IEU contends that the Company's internal analysis shows that future cash flows from generation services are in excess of book value. (*Id.* at 10.)

As discussed in detail above, the Commission lawfully waived its rule that required AEP Ohio to state the fair market value of the assets. Consequently, OCC's and IEU's arguments that the Commission should have evaluated the fair market value of the assets and netted a portion of the alleged market premium against what customers have paid in regulatory transition charges or a reduction in the RSR is misplaced. No fair market evaluation is necessary, which is consistent with the Commission's application of this rule to other electric companies. Further, as explained above, the law is clear that a customer pays for the electric service they receive and is not owners of an electric utility. Thus, intervenors' contention that rehearing is warranted because the Commission failed to net a portion of an alleged market premium against what customers have paid in regulatory transition charges or will pay via the RSR is likewise misplaced and without merit. In terms of IEU's use of R.C. 4928.39 in support of netting the imaginary market premium, the Commission has consistently held in both the ESP II and Capacity Charge cases that the RSR is not a "transition charge," thus, R.C. 4928.39 is not at issue.

It is important to keep in mind that the sole reason why this affiliate asset transfer is occurring is to comply with R.C. 4928.17. There is no "market premium" caused by this internal transfer in which to net against. IEU incorrectly relies on an accounting analysis performed in

late 2011 by AEP in conjunction with the (now-rejected) 11-346 Stipulation, in an attempt to support its speculation that the market value of the generation assets is greater than the book value. The internal AEP accounting memorandum performed a long-term analysis of the entire AEP-East generation fleet to determine whether the total expected revenue stream for the life of the assets exceeds their book value. The accounting memorandum makes clear that the impairment analysis of the generation fleet was done through a 30-year long-term view and from the aggregated perspective of AEP East (versus a short-term view of RPM pricing just for the AEP Ohio's fleet.) (OCC Ex. 104 in ESP II Case.) In other words, the memorandum merely concludes that the combination of revenue streams from all of the AEP East regulated rates over 30 years exceeded the net book value of the plants. For purposes of this accounting impairment query, the generation plants outside of Ohio were presumed to be cost-based regulated for the entire life of the facility. Mathematically, the net present value of the future payment stream for individual generation assets (or groups of assets) within Ohio could be zero and the impairment test would still pass based on the lifetime revenue analysis for AEP East collectively. In reality, the accounting analysis was done for a completely unrelated purpose and it does not support the OCC/IEU notion that market value of the generating assets should be explored or required as part of corporate separation.

Once again, neither OCC nor IEU have raised a new argument worthy of rehearing. The Commission should reject these netting arguments as it has considered and rejected them before.

E. Permitting AEP Ohio to transfer its generation assets at net book value is consistent with prior Commission decisions.

OCC asserts that the Commission unreasonably extricated a distinct provision of the Duke Stipulation package (net book asset transfer) and used it on a stand-alone-basis as binding precedent to approve AEP Ohio's request for similar treatment, which will, according to OCC,

chill the stipulation process in future proceedings. (OCC AFR at 12-14.) IEU makes a similar argument at p. 15 of its memorandum in support.

This allegation is based on a mischaracterization of the Commission's reference to its prior decision. The Commission is not using the terms of the Duke Stipulation as binding precedent that it or any signatory party must adhere to. Rather, it is noting that waiver of O.A.C. 4901:1-37-09(C)(4) and its decision to allow AEP Ohio to transfer its generation assets at net book value is consistent with its decisions in the Duke case and the Company's prior corporate separation case. OCC and IEU mischaracterize the Commission's decision and advocate that the Commission pretend that the Duke Stipulation does not exist. The Commission should again reject this argument as it wisely did before, as it is appropriate for a regulator to illustrate that it is engaging in evenhanded regulation consistent with its prior decisions.

F. The Commission lacks jurisdiction over Valentine Act.

IEU contends that approving the transfer at net book value, among other elements of the Application, resulted in a violation of the Valentine Act, which it alleges must be considered in connection with the Commission's evaluation of the public interest when it considers the Company's Application. (IEU AFR at 17-22.) IEU also alleges that the pass through of above-market non-bypassable transition revenue from AEP Ohio to AEP Genco insulates AEP Genco from competition and violates the Valentine Act. (*Id.* at 24.)

This is not the first time that IEU has tried to evoke the Valentine Act. In the Capacity Charge case, IEU made a similar plea to no avail. As the Commission well understands, the General Assembly has expressly endowed Ohio's *common pleas courts* with jurisdiction over Valentine Act claims. R.C. 1331.11 ("Courts of common pleas are invested with jurisdiction to restrain and enjoin violators of sections 1331.01 to 1331.14 of the Revised Code.") The Power

Siting Board recently rejected an objection to a Stipulation that had been lodged pursuant to the Valentine Act, acknowledging the common pleas courts' jurisdiction over such matters and noting "[n]or has the General Assembly vested the Board with the task of regulating competition among power plant developers." *In the Matter of the Application of Black Fork Wind Energy, L.L.C. for a Certificate to Site a Wind-Powered Electric Generating Facility in Crawford and Richland Counties, Ohio*, Ohio Power Siting Board No. 10-2865-EL-BGN, Entry on Rehearing (March 26, 2012), at ¶¶ 93-94. The Commission cannot either directly or indirectly, in the context of its public interest analysis of the Company's Application, evaluate alleged violations of the Valentine Act for which it lacks jurisdiction to consider.

Both OCC's and IEU's grounds for rehearing are based on the same arguments each advanced when they opposed the Company's waiver request, which the Commission has already considered and rejected. Their objections do not present a valid basis for rehearing, as the Commission's decision to waive its administrative rule and permit the Company to transfer its generation assets at net book value is lawful and reasonable. As the Company explained in its Application, Initial Comments, and Reply Comments, the position that a market valuation is needed rests on false assumptions that have no basis in Ohio law. Section 4928.17, Revised Code, requires corporate separation but does not indicate any need for a market valuation and, contrary to the intervenors' assertion, contains no indication that any gain (whether artificial or real) should be captured, "allocated," or netted in any fashion. In sum, the Commission's decision to waive its administrative rule and permit the Company to transfer its generation assets at net book value is lawful and reasonable, and the intervenors' related grounds for rehearing should be denied.

II. IEU's objections regarding RSR or SSO revenues paid to AEP Ohio for generation-based services that will be passed on to AEP Genco are not appropriate grounds for rehearing in this docket.

IEU argues that the Finding and Order is unlawful and unreasonable because it authorized AEP Ohio to pass through RSR revenue to AEP Genco thereby providing AEP Genco with an unfair competitive advantage contrary to Ohio's corporate separation requirements, imposing a non-bypassable cost on retail consumers, and violating the Valentine Act. (IEU AFR at 23.) IEU also alleges as a separate ground for rehearing that the Finding and Order is unlawful and unreasonable because it authorized AEP Ohio to enter into an unbid contract with AEP Genco to supply SSO load and capacity at above market prices. (*Id.* at 26.) According to IEU, the contract and related pricing are unlawful and unreasonable because they provide AEP Genco with an undue preference in conflict with R.C. 4928.17, R.C. 4928.02, and the Valentine Act.

The October 17, 2012 Finding and Order in this docket did not authorize the alleged unlawful acts for which IEU seeks rehearing. As the Commission noted at paragraph 38 of its Finding and Order, the issues above were considered and addressed by the Commission in the modified ESP II Order issued August 8, 2012. Indeed, these issues make up IEU's sixth ground for rehearing in its September 7, 2012 application for rehearing in the ESP II docket. (See pages 62-65 of IEU's AFR in Docket No. 11-346-EL-SSO, et. al.) Accordingly, IEU's second and third grounds for rehearing should be rejected because the Commission did not address them in this docket, and they are already teed up for consideration in the ESP II docket.

CONCLUSION

For all the foregoing reasons, OCC's and IEU's objections do not establish a valid basis for rehearing. The Commission should deny rehearing accordingly.

Respectfully submitted,

/s/Steven T. Nourse

Steven T. Nourse

Mathew J. Satterwhite

American Electric Power Service Corporation

1 Riverside Plaza, 29th Floor

Columbus, Ohio 43215

Telephone: (614) 716-1606

Fax: (614) 716-2950

Email: stnourse@aep.com

mjsatterwhite@aep.com

CERTIFICATE OF SERVICE

The undersigned hereby certifies that a true and accurate copy of the foregoing document was served this 26th day of November, 2012 by electronic mail, upon the persons listed below.

/s/ Steven T. Nourse

Steven T. Nourse

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

James F. Lang
Laura C. McBride
N. Trevor Alexander
Calfee, Halter & Griswold, LLP
1400 Key Bank Center
800 Superior Avenue
Cleveland, Ohio 44114
jlang@calfee.com,
lmcbride@calfee.com,

M. Howard Petricoff
Lija Kaleps-Clark
Vorys, Sater, Seymour and Pease LLP
52 East Gay Street
P.O. Box 1008
Columbus, Ohio 43216-1008
mhpeticoff@vorys.com
lkalepsclark@vorys.com

Rocco D'Ascenzo
Elizabeth Watts
Duke Energy Ohio, Inc.
139 E. Fourth Street
1303-Main
Cincinnati, Ohio 45202
Elizabeth.watts@duke-energy.com
Rocco.d'ascenzo@duke-energy.com

Joseph E. Oliker
McNees Wallace & Nurick, LLC
21 East State Street, 17th Floor
Columbus, Ohio 43215
joliker@mwncmh.com,

Robert A. McMahon
Eberly McMahon LLC
2321 Kemper Lane, Suite 100
Cincinnati, OH 45206
BMcMahon@emh-law.com

Mark A. Hayden
FirstEnergy Service Company
76 South Main Street
Akron, Ohio 4430
haydenm@firstenergycorp.com

Thomas O'Brien
Bricker & Eckler LLP
100 South Third Street
Columbus, Ohio 43215-4291
tobrien@bricker.com

Matthew W. Warnock
Bricker & Eckler LLP
100 South Third Street
Columbus, Ohio 43215-4291
mwarnock@bricker.com

David A. Kutik
Allison E. Haedt
Jones Day
901 Lakeside Avenue
Cleveland, OH 44114
dakutik@jonesday.com
aehaedt@jonesday.com

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

Michael L. Kurtz
Kurt J. Boehm
Jody M. Kyler
Boehm, Kurtz & Lowry
36 East Seventh Street, Suite 1510
Cincinnati, Ohio 45202
dboehm@bkllawfirm.com
mkurtz@bkllawfirm.com

William Wright
Werner Margard
Thomas Lindgren
Stephen A. Reilly
Assistant Attorneys' General
Public Utilities Section
180 East Broad Street, 6th Floor
Columbus, Ohio 43215
Werner.Margard@puc.state.oh.us
William.Wright@puc.state.oh.us
Thomas.Lindgren@puc.state.oh.us

Maureen R. Grady
Assistant Consumers' Counsel
Office of the Ohio Consumers' Counsel
10 West Broad Street, Ste. 1800
Columbus, Ohio 43215-3485
grady@occ.state.oh.us

Joseph M. Clark
6641 North High Street, Suite 200
Worthington, Ohio 43085
joseph.clark@directenergy.com,

Kurt P Helfrich
Ann B. Zallocco
Thompson Hine, LLP
41 South High Street, Ste. 1700
Columbus, Ohio 43215
Kurt.Helfrich@ThompsonHine.com
Ann.Zallocco@ThompsonHine.com

William Wright
Werner Margard
Thomas Lindgren
Stephen A. Reilly
Assistant Attorneys' General
Public Utilities Section
180 East Broad Street, 6th Floor
Columbus, Ohio 43215
Werner.Margard@puc.state.oh.us
William.Wright@puc.state.oh.us
Thomas.Lindgren@puc.state.oh.us

Stephen Bennett
General Generation Company, LLC
300 Exelon Way
Kennett Square, PA 19348
Stephen.bennett@exeloncorp.com

Richard L. Sites
Ohio Hospital Association
155 East Broad Street, 15th Floor
Columbus, OH 43215-3620
ricks@ohanet.org

David M. Stahl
Eimer Stahl Klevorn & Solberg LLP
224 S. Michigan Avenue, Suite 1100
Chicago, IL 60694
dstahl@eimerstahl.com

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

COLUMBUS/1653831v.1

This foregoing document was electronically filed with the Public Utilities

Commission of Ohio Docketing Information System on

11/26/2012 4:23:21 PM

in

Case No(s). 12-1126-EL-UNC

Summary: Memorandum Contra Intervenors' Applications for Rehearing electronically filed by Mr. Steven T Nourse on behalf of Ohio Power Company