BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Ohio Power Company to Establish a Competitive Bidding Process for Procurement of Energy to Support its Standard Service Offer	)))))	Case No. 12-3254-EL-UNC

INITIAL BRIEF OF INDUSTRIAL ENERGY USERS-OHIO

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The Public Utilities Commission of Ohio ("Commission") found that conducting energy-only auctions as part of Ohio Power Company's ("AEP-Ohio") electric security plan ("ESP") would provide an "invaluable benefit" to customers as AEP-Ohio transitions to market.[1] The Commission held that "[t]he entire crux of the Opinion and Order was the value in providing customers with the opportunity to take advantage of market-based prices" and "that it is important for customers to be able to benefit from market-based prices while they are low …."[2] The evidence in this proceeding, however, demonstrates that AEP-Ohio's proposed structure for the energy-only auctions would further increase customers' bills, above and beyond the rate increases the Commission authorized in its Opinion and Order in AEP-Ohio's most recent ESP proceeding, the

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[1] *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 11, 39-40 (Aug. 8, 2012) (hereinafter "*ESP II Case*" or "ESP II Order", as appropriate); *ESP II Case*, Entry on Rehearing at 34-39 (Jan. 30, 2013).

[2] *Id.* at 35-36 (Jan. 30, 2013).

ESP II Case. In the 12 months since the Commission issued the ESP II Order, rates have gone up for non-shopping customers by 20%.[3]

To prevent further increases above the substantial rate increase approved by the Commission in the ESP II Order, the Industrial Energy Users-Ohio ("IEU-Ohio") proposes a reserve price for the energy-only auctions. The Office of the Ohio Consumers' Counsel ("OCC") and the Ohio Energy Group ("OEG"), also representing the interests of customers, support a reserve price as well.

The competitive retail electric service ("CRES") providers active in this case, FirstEnergy Solutions Corp. ("FES"), Constellation New Energy, Inc. ("Constellation"), and Exelon Generation Company LLC ("Exelon"), have also made proposals to mitigate the rate increases that will likely occur from the energy-only auctions. FES recommends that the Commission reduce base generation rates to reflect a price of capacity of $188.88/megawatt-day ("MW-day"), instead of the $355/MW-day currently embedded in base generation rates.[4] Constellation and Exelon jointly propose reducing the portion of AEP-Ohio's compensation for generation capacity service that the Commission held AEP-Ohio could defer in Case No. 10-2929-EL-UNC (the "*Capacity Case*") by an amount commensurate with any rate increase that occurs through the energy-only auctions.[5]

Even AEP-Ohio has recognized the need to mitigate the rate increases that will occur if its proposed auction structure is approved. AEP-Ohio proposes to include the expected rate increase from the energy-only auctions in the calculation of the 12%

[3] IEU-Ohio Exs. 3-7; *infra*, at 6.

[4] FES Ex. 7 at 8-9.

[5] Exelon Ex. 1 at 21-25.

individual bill increase cap that the Commission authorized in the ESP II Order.[6] However, AEP-Ohio's proposal does not limit the magnitude of the rate increase that will occur if its proposed auction structure is approved; rather, it will have the opposite effect as the rate increase will be deferred ***with interest***.[7]

As discussed in more detail below, the Commission should adopt IEU-Ohio's proposal to include a reserve price in the energy-only auctions and should reject AEP-Ohio's request to continue double-recovery of the fixed costs in the current fuel adjustment clause ("FAC") through a new rider.

I. BACKGROUND

This proceeding is an outgrowth of the Commission's approval of AEP-Ohio's most recent ESP. In its ESP application, AEP-Ohio proposed to conduct a competitive bidding process ("CBP") energy-only slice of the system auction.[8] AEP-Ohio proposed to conduct an energy-only slice of the system auction for five percent of its standard service offer ("SSO") load within six months of a final Commission order in Case No. 12-1126-EL-UNC (the "*Corporate Separation Case*"), followed by an energy-only auction for 100% of its SSO load for delivery beginning January 1, 2015.[9] AEP-Ohio's ESP application did not provide any substantive details regarding how the CBP would

[6] AEP-Ohio Ex. 2 at 11.

[7] *ESP II Case*, Entry on Rehearing at 40 (Jan. 30, 2013) ("we authorize the deferral of any expenses associated with the rate cap pursuant to Section 4928.144, Revised Code, *inclusive of carrying charges,* ....") (emphasis added).

[8] IEU-Ohio Ex. 8 at 3.

[9] *Id.* at 3-4.

be conducted or how the results of the CBP process would be translated into retail rates paid by SSO customers.[10]

In the ESP II Order, the Commission modified AEP-Ohio's CBP proposal and directed AEP-Ohio to increase the percentage of SSO to be served by generation acquired through the initial energy-only auction from 5% to 10%.[11] Further, the Commission ordered AEP-Ohio to conduct an energy-only auction for delivery commencing on June 1, 2014, for 60% of its SSO load, and conduct an energy-only auction for delivery commencing on January 1, 2015 for 100% of AEP-Ohio's SSO load.[12] Over the objection of some parties, the Commission stated that nothing precluded AEP-Ohio or its affiliates from bidding in the energy-only auctions.[13] The Commission also directed AEP-Ohio to develop its CBP in consultation with interested parties and submit an application to establish its CBP.[14]

On December 21, 2012, AEP-Ohio filed its application in this proceeding to establish a CBP. Notably, AEP-Ohio's application contained a request to unbundle the fuel adjustment clause ("FAC") into fixed and variable components. AEP-Ohio claims that it is proper to unbundle the FAC because the energy-only auctions should only be blended with what AEP-Ohio claims are variable costs in the FAC.[15] Directionally,

[10] *Id.* at 4.

[11] ESP II Order at 39-40.

[12] *Id.*

[13] *Id.* at 40.

[14] *Id.*

[15] AEP-Ohio Ex. 2 at 7-9.

AEP-Ohio's request to unbundle the FAC rate will increase the likelihood that the proposed CBP will increase SSO rates.[16]

AEP-Ohio's application did not propose a reserve price for the energy-only auctions. As the testimony of IEU-Ohio witness Mr. Murray and OCC/OEG witness Mr. Kollen demonstrate, without a reserve price, the energy-only auctions are likely to increase rates for SSO customers.[17] Mr. Murray testified that if an auction were held now, an energy-only auction without a reserve price would produce a rate that was greater than AEP-Ohio's current FAC.[18] Mr. Kollen testified that without a reserve price in the energy-only auctions, customers' rates would increase by an additional $211 million over the term of the ESP.[19]

II. <u>ARGUMENT</u>

A. Consistent with the Commission's findings in the *ESP II Case*, the Commission should impose an auction reserve price to protect customers from unreasonable results

Although some parties urge the Commission to move forward blindly with the energy-only auctions without regard to the expected impacts on customers' bills, IEU-Ohio urges the Commission to address the likely rate increases that will result from the energy-only CBP auctions and AEP-Ohio's proposed auction structure. In the *ESP II Case* the Commission found that the energy-only auctions would be an "invaluable benefit" to customers and found that customers should have access to the current low

[16] IEU-Ohio Ex. 8 at 6.

[17] IEU-Ohio Ex. 8 at 9; OCC/OEG Joint Ex. 1 at 3-5.

[18] IEU-Ohio Ex. 8 at 9-10.

[19] OCC/OEG Joint Ex. 1 at 4. As Mr. Kollen identified in his testimony and on cross-examination, the $211 million harm to customers includes an annualized value for 2013 and will likely decrease as time passes. *Id.* at 4, n.1. However, the magnitude of the potential harm to customers is real and should not be taken lightly.

market prices. AEP-Ohio's proposed structure for the energy-only auctions will, however, not provide customers with any benefit. Specifically, the record in this case demonstrates that customers will see rate increases from the energy-only auction. Accordingly, IEU-Ohio recommends that the Commission set a reserve price on the energy-only auctions equal to AEP-Ohio's expected FAC, with separate reserve prices for the Columbus Southern Power Company ("CSP") and Ohio Power Company ("OP") rate zones.

i. IEU-Ohio's proposed reserve price will prevent the energy-only auctions from further increasing SSO rates above the 20% increase that SSO customers have experienced over the past year

As the record shows, since the Commission approved AEP-Ohio's current ESP in August 2012, SSO customers' rates have gone up by approximately 20%. A typical industrial customer taking service under the GS-4 tariff in the CSP rate zone has seen a 20.86% increase between August 2012 and June 2013; a GS-4 customer in the OP rate zone saw a 22.32% increase over the same timeframe.[20] Additionally, on June 16, 2013, AEP-Ohio filed an application to update its transmission rates for non-shopping customers ("TCRR Application"), seeking an average increase in transmission rates of 33%; however, AEP-Ohio's TCRR application seeks an increase in GS-4 transmission rates of 42.06%.[21] AEP-Ohio agrees that the effect of the CBP may result in higher SSO rates. It recently stated in comments filed with the Commission that it "recognizes

[20] IEU-Ohio Exs. 3-6 (the increase was based on a typical bill for a CSP and OP GS-4 customer with 20,000 kW demand and usage of 13 million kWh); Tr. Vol. I at 160-172.

[21] IEU-Ohio Ex. 7 at 4, Schedule B-2. IEU-Ohio and OCC have filed comments regarding AEP-Ohio's TCRR Application challenging the magnitude of the transmission rate increase that AEP-Ohio seeks.

that the clearing prices for the energy auctions may come in higher than the Company's internal variable energy costs."[22]

IEU-Ohio's proposal to include a reserve price for the energy-only auctions will help ensure prices do not rise further for SSO customers as a result of the energy-only auctions. Under AEP-Ohio's proposal, the energy secured through the CBP will be treated as a purchased power cost and blended with the Auction Phase-In Rider (the variable cost portion of the current FAC) to produce the energy rates charged to SSO customers.[23] Based upon this methodology, unless the CBP is conducted with a reserve price (equal to the forecasted FAC rates expected to be in effect during the delivery period for the energy secured through the CBP), it is likely that the CBP auction will clear at a price that is higher than the forecasted variable FAC rates.[24] Mathematically, the only way that the energy-only auctions will not result in an overall rate increase to SSO customers is if the cleared bid price is lower than AEP-Ohio's forecasted FAC rates, *i.e.* the auctions clear lower than the reserve price.[25]

ii. IEU-Ohio's proposed reserve price that is distinct to the CSP and OP rate zones is consistent with the ESP II Order

The reserve price for the energy-only auctions should be established on a separate rate zone basis to recognize that AEP-Ohio has two separate FAC rates; one rate for the CSP rate zone, and one rate for the OP rate zone.[26] In the ESP II Order, the Commission ordered AEP-Ohio to maintain separate rate zones for AEP-Ohio's

[22] *In the Matter of the Commission's Review of Customer Rate Impacts from Ohio Power Company's Transition to Market Based Rates*, Case No. 13-1530-EL-UNC, AEP-Ohio Comments at 6 (Aug. 12, 2013).

[23] IEU-Ohio Ex. 8 at 9.

[24] *Id.*

[25] *Id.*

[26] *Id.* at 8.

FAC rates.[27] Accordingly, because AEP-Ohio is required to maintain separate FAC rate zones, it is appropriate to establish separate reserve prices.

iii. IEU-Ohio's proposed reserve price is consistent with the Commission's expectation that the energy-only auctions would be an "invaluable benefit" to customers

Requiring a reserve price for the energy-only auctions would also help to align the auction results with the Commission's expectation that these auctions would provide an "invaluable benefit" to customers.[28] In fact, the Commission found that AEP-Ohio's ESP included non-quantifiable benefits in the form of a faster transition to market than a market rate offer ("MRO"), which included the energy-only auctions, offset at least $386 million in known costs of the ESP.[29] With regard to the energy-only auctions, the Commission identified its expectations that the energy-only auctions would offset the rate increases associated with the Generation Resource Rider ("GRR") and Retail Stability Rider ("RSR") and several of AEP-Ohio's distribution riders approved in the ESP.

> We acknowledge that there may be costs associated with distribution related riders and the gridSmart and ESRR that currently are not readily quantifiable, we believe any of these costs are significantly outweighed by the non-quantifiable benefits this modified ESP leads to [*sic*]. ... Further,

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[27] ESP II Order at 17.

[28] ESP II Order at 11, 39-40; *ESP II Case*, Entry on Rehearing at 34-39 (Jan. 30, 2013).

[29] *ESP II Case*, Entry on Rehearing at 75-76 (Jan. 30, 2013). In the *ESP II Case,* IEU-Ohio agreed with the Commission that AEP-Ohio's ESP, as approved by the Commission, was less favorable than an MRO; however, the Commission's $386 million figure grossly understates how less favorable AEP-Ohio's ESP, as approved, truly is. *ESP II Case*, IEU-Ohio's Application for Rehearing at 17 (Sept. 7, 2012). Additionally, the notion that there is a benefit from the claim that AEP-Ohio is transitioning to market faster than the MRO option is fundamentally at odds with Ohio law, which required AEP-Ohio to transition to market by the end of the market development period ("MDP"), which could end no later than December 31, 2005, and that following the MDP AEP-Ohio's generation was fully on its own in the competitive market. Section 4928.38. Revised Code. IEU-Ohio has addressed this topic in its application for rehearing. *See, e.g., ESP II Case*, IEU-Ohio's Application for Rehearing at 2 (Sept. 7, 2012) ("The ESP II Order subordinates the interests of customers to provide AEP-Ohio's competitive generation business with more time to transition to a competitive electric market even though Ohio law states that the time for such a transition ended long ago.").

> these costs will be mitigated by the increase in auction percentages, including the slice-by-slice auction, as we modified to ten percent each year, which will offset some of these costs in the statutory test and moderate the impact of the modified ESP. Further, the acceleration to 60 percent of AEP-Ohio's energy only auction by June 1, 2014, not only enables customers to take advantage of market based prices, but also creates a qualitative benefit which, while not yet quantifiable, may well exceed the costs associated with the GRR and RSR.[30]

Certainly energy-only auctions that increase SSO customers' rates further are not a benefit for customers, in any stretch of the imagination.

In sum, the Commission should require a reserve price set at AEP-Ohio's expected FAC rate, specific to the CSP and OP rate zones, to prevent the energy-only auctions from further increasing non-shopping customers' rates in excess of the 20% increase seen over the last year.

B. AEP-Ohio's request to bifurcate its FAC into fixed cost and variable cost components is unlawful and unreasonable because AEP-Ohio is currently double-recovering the fixed cost portion of AEP-Ohio's FAC, and AEP-Ohio's proposal would allow AEP-Ohio to continue its double-recovery

The Commission should deny AEP-Ohio's request to split the FAC into fixed and variable components and only blend the variable portion of the FAC with the energy-only auction results because AEP-Ohio is already recouping these costs through its compensation for generation capacity service, *i.e.* the fixed costs are included in the $188.88/MW-day compensation.

The fixed costs that AEP-Ohio requests to include in its proposed Fixed Cost Rider relate to purchased power costs from Ohio Valley Electric Corporation ("OVEC") and Lawrenceburg.[31] The OVEC and Lawrenceburg costs are recorded in Account

[30] ESP II Order at 75-76.

[31] Tr. Vol. I at 98.

555.[32] Currently, the costs in Account 555 are recovered through the FAC.[33] However, the fixed costs in Account 555 were included in the calculation that produced the Commission-approved generation capacity service compensation of $188.88/MW-day.[34] Specifically in the *Capacity Case*, AEP-Ohio witness Dr. Pearce included the fixed costs from Account 555 in his formulaic methodology that produced a price of capacity of $355/MW-day.[35] The Commission accepted the $355/MW-day price as a starting point and then made several adjustments recommended by Staff to produce a price of capacity of $188/MW-day.[36] Thus, AEP-Ohio's proposal simply amounts to a request that it be allowed to continue double-recovering the costs associated with the Lawrenceburg and OVEC power purchases, a result that is clearly unlawful and unreasonable.

Additionally, in AEP-Ohio's pending FAC audit proceedings, the Commission should direct the auditor to investigate whether AEP-Ohio is in fact recovering fixed costs through the FAC that are reflected in the $188.88/MW-day price for capacity authorized by the Commission and, if so, the Commission should use any double-recovered amounts as a credit against AEP-Ohio's regulatory asset balances otherwise eligible for amortization or in the alternative as a credit against future FAC rates.[37] This

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[32] *Id.* at 99.

[33] *Id.* at 98-99.

[34] *Id.* at 99-101.

[35] *Id.*

[36] As IEU-Ohio argued in the *Capacity Case*, the Commission invented its own cost-based ratemaking methodology, found nowhere in Ohio law, when it concluded AEP-Ohio's cost of capacity was $188.88/MW-day.

[37] *In the Matter of the Fuel Adjustment Clauses for Columbus Southern Power Company and Ohio Power Company*, Case Nos. 09-872-EL-FAC, *et al.,* Opinion and Order at 13 (Jan. 23, 2012).

would be consistent with the Commission's orders in Case Nos. 09-872-EL-FAC, *et al.*[38] Finally, it is important to note that AEP-Ohio's base generation rates are over-compensating AEP-Ohio for generation capacity service and adjustments are necessary to ensure that customers are not forced to over-compensate AEP-Ohio.[39]

III. CONCLUSION

For the reasons specified herein, the Commission should adopt a reserve price for both the OP and CSP rate zones and should reject AEP-Ohio's request to continue collecting the fixed costs in the FAC without blending these costs with the results of the energy-only auctions. Additionally, the Commission should investigate whether AEP-Ohio is in fact recovering fixed costs through the FAC that are reflected in the $188.88/MW-day price for capacity authorized by the Commission, and any double-recovered amounts should be credited against AEP-Ohio's regulatory asset balances otherwise eligible for amortization or in the alternative credited against future FAC rates.

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[38] *Id.*

[39] Tr. Vol. I at 242 (AEP-Ohio's base generation rates provide AEP-Ohio with compensation for generation capacity service in the range of $340/MW-day to $355/MW-day, far in excess of the $188.88/MW-day price approved by the Commission); *ESP II Case*, IEU-Ohio's Application for Rehearing at 67-69 (Sept. 7, 2012).

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing *Initial Brief of Industrial Energy Users-Ohio* was served upon the following parties of record this 16th day of August 2013 *via* hand-delivery, electronic transmission, or first class mail, U.S. postage prepaid.

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