

BEFORE

THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Ohio )  
Power Company for Administration of )  
the Significantly Excessive Earnings ) Case No. 14-875-EL-UNC  
Test Under R.C. 4928.143(F) and Ohio )  
Adm.Code 4901:1-35-10. )

OPINION AND ORDER

The Commission having considered the application, the evidence, the applicable law, and the Stipulation and Recommendation, and being otherwise fully advised, hereby issues its Opinion and Order.

APPEARANCES:

Steven T. Nourse, American Electric Power Service Corporation, 1 Riverside Plaza, Columbus, Ohio 43215-2373, on behalf of Ohio Power Company.

Mike DeWine, Ohio Attorney General, by Thomas W. McNamee, Assistant Attorney General, 180 East Broad Street, 6th Floor, Columbus, Ohio 43215-3793, on behalf of the Staff of the Public Utilities Commission of Ohio.

OPINION:

I. History of the proceedings

Pursuant to R.C. 4928.141 electric utilities are required to provide consumers with a standard service offer, consisting of either a market-rate offer (MRO) or an electric security plan (ESP). R.C. 4928.142(D)(4), 4928.143(E), and 4928.143(F) direct the Commission to evaluate the earnings of each electric utility's approved ESP or MRO to determine whether the plan or offer produces significantly excessive earnings for the electric utility.

On May 15, 2014, Ohio Power Company (AEP Ohio or Company) filed its application and supporting testimony for the administration of the significantly excessive earnings test (SEET) for 2013 revenues, as required by R.C. 4928.143(F) and Ohio Adm.Code 4901:1-35-10. By entry issued August 13, 2014, the procedural schedule was established for this case. No motions to intervene were filed in this matter. Staff testimony was timely filed on October 9, 2014. On October 10, 2014, AEP Ohio and Staff filed a Stipulation and Recommendation (Stipulation) to resolve all the issues raised in this case. The hearing was held, as scheduled, on November 5, 2014.

At the hearing, the following exhibits were offered and admitted into the record of evidence: the testimony of AEP Ohio witnesses William A. Allen (Co. Ex. 1) and Thomas E. Mitchell (Co. Ex. 2), the Stipulation (Joint Ex. 1), and the testimony of Staff witness Joseph P. Buckley (Staff Ex. 1 and 1A).

## II. Applicable law

AEP Ohio's current ESP, as adopted and modified by the Commission became effective September 2012, and is scheduled to continue until June 2015. *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 No. 11-346-EL-SSO et al. (ESP 2 Case), Opinion and Order (Aug. 8, 2012), Entries on Rehearing (Jan. 30, 2013, Mar. 27, 2013). R.C. 4928.143(F) sets forth the statutory requirements of the SEET for an ESP with a term of three years. R.C. 4928.143 provides, in relevant part:

- (F) With regard to the provisions that are included in an electric security plan under this section, the commission shall consider, following the end of each annual period of the plan, if any such adjustments resulted in excessive earnings as measured by whether the earned return on common equity of the electric distribution utility is significantly in excess of the return on common equity that was earned during the same period by publicly traded companies, including utilities, that face comparable business and financial risk, with such adjustments for capital structure as may be appropriate. Consideration also shall be given to the capital requirements of future committed investments in this state. The burden of proof for demonstrating that significantly excessive earnings did not occur shall be on the electric distribution utility. If the commission finds that such adjustments, in the aggregate, did result in significantly excessive earnings, it shall require the electric distribution utility to return to consumers the amount of the excess by prospective adjustments; provided that, upon making such prospective adjustments, the electric distribution utility shall have the right to terminate the plan and immediately file an application pursuant to section 4928.142 of the Revised Code. Upon termination of a plan under this division, rates shall be set on the same basis as specified in division (C)(2)(b) of this section, and phase-in of any amounts that occurred prior to that termination and the recovery of those amounts as contemplated under that electric security

plan. In making its determination of significantly excessive earnings under this division, the commission shall not consider, directly or indirectly, the revenue, expenses, or earnings of any affiliate or parent company.

Further, Ohio Adm.Code 4901:1-35-03(C)(10)(a) provides:

For the annual review pursuant to division (F) of section 4928.143 of the Revised Code, the electric utility shall provide testimony and analysis demonstrating the return on equity that was earned during the year and the returns on equity earned during the same period by publicly traded companies that face comparable business and financial risks as the electric utility. In addition, the electric utility shall provide the following information:

- (i) The federal energy regulatory commission form 1 (FERC form 1) in its entirety for the annual period under review. The electric utility may seek protection of any confidential or proprietary data if necessary. If the FERC form 1 is not available, the electric utility shall provide balance sheet and income statement information of at least the level of detail as required by FERC form 1.
- (ii) The latest securities and exchange commission form 10-K in its entirety. The electric utility may seek protection of any confidential or proprietary data if necessary.
- (iii) Capital budget requirements for future committed investments in Ohio for each annual period remaining in the ESP.

The Commission also provided guidance on the interpretation and application of R.C. 4928.142(D)(4), 4928.143(E), and 4928.143(F) to electric utilities in *In the Matter of the Investigation into the Development of the Significantly Excessive Earnings Test Pursuant to Amended Substitute Senate Bill 221 for Electric Utilities*, Case No. 09-786-EL-UNC (*Generic SEET Case*), Finding and Order (June 30, 2010), Entry on Rehearing (Aug. 25, 2010).

### III. Application of SEET

To determine whether an electric utility has significantly excessive earnings, under R.C. 4928.143(F), the Commission must compare the earned return on common equity

(ROE) of the electric utility to the earned ROE of a group of publicly traded companies, including utilities that face comparable business and financial risk. Although both AEP Ohio and Staff utilizing the Utilities Select Sector SPDR as the comparable group of publicly traded companies to develop the SEET ROE, the parties ultimately calculate different SEET threshold ROE.

A. AEP Ohio's analysis

In its application and supporting testimony, AEP Ohio submits that the Company's earned per books ROE for 2013 was 8.95 percent. AEP Ohio adjusted earnings to eliminate off-system sales margins, special accounting items and for corporate separation. AEP Ohio witness Mitchell submits that the special accounting items relate to impairment of certain AEP Ohio generating units and certain restructuring charges. No adjustments were made to remove extraordinary items, minority interest or non-recurring items for 2013, as the witness testified there were no such items recorded. The 2013 after tax amounts for each specific item have been added back to net earnings available for common shareholders and common shareholder equity. AEP Ohio also adjusted earnings to eliminate off-system sales margins. Accordingly, AEP Ohio calculates an adjusted ROE of 11.28 percent for 2013. (Co. Ex. 2 at 4-9, Ex. TEM-1.)

Relying on the Company's interpretation of the Commission's Opinion and Order and Commission-approved settlements in the Company's prior SEET proceedings, AEP Ohio concludes that the mean ROE for the comparable risk group companies for 2013, according to the Utilities Select Sector SPDR is 9.09 percent with a standard deviation of 3.22 percent. Multiplying the standard deviation of AEP Ohio's comparable group of companies by 1.64 yields an adder of 5.29 percent. Thus, AEP Ohio's SEET analysis yields a threshold ROE, the point at which earnings should be considered significantly excessive for 2013, of 14.38 percent ( $9.09 + 5.29$ ) for AEP Ohio. (Co. Ex. 1 at 4-5.)

B. Staff's analysis

After reviewing AEP Ohio's application, testimony, and supporting information, Staff witness Buckley accepted AEP Ohio's determination of its per books ROE of 8.95 percent, and the calculation of the Company's ROE, including the adjustments, to produce an adjusted ROE of 11.28 percent for 2013. However, Staff also utilizing the SPDR Select Sector Fund-Utility as the comparable group of companies, calculates the threshold ROE of the comparable group of companies differently than AEP Ohio. From the 30 companies, including AEP Corporation, in the Utilities Select Sector SPDR, Staff determined the ROE for the group of companies by totaling the net income earned by the select sector fund companies, dividing the total net income earned by the total common equity of the companies to establish the average ROE. Utilizing the companies in the select sector fund, Staff calculates the average ROE for the group of companies for 2013 to be 9.04 percent

with a standard deviation of 3.17 percent. Staff's SEET process uses 1.64 standard deviations above the mean, which Staff asserts equates to a confidence level of 95 percent. Staff's SEET analysis results in an adder of 5.20 percent ( $3.17 \text{ percent} \times 1.64 = 5.1988$ ).<sup>1</sup> For 2013, Staff's SEET calculation yields a threshold ROE of 14.24 percent (9.04 percent + 5.20 percent). (Staff Ex. 1 at 3-5; Staff Ex. 1A.)

C. Summary of the 2013 SEET Stipulation

On October 10, 2014, AEP Ohio and Staff (Signatory Parties) filed a Stipulation to resolve all the issues presented in this case. The Signatory Parties agree that based on a review of the 2013 FERC Form 1 for AEP Ohio, after adjustments for off-system sales and special accounting items, AEP Ohio's earned ROE was 11.28 percent. The Signatory Parties aver that the method for determining AEP Ohio's earned ROE for 2013 earnings is consistent with the methodology utilized by the Commission in the Company's SEET proceedings for 2010 and 2011 earnings. See *In the Matter of the Application of Ohio Power Company for Administration of the Significantly Excessive Earnings Test under Section 4928.143(F), Revised Code, and Rule 4901:1-35-10, Ohio Administrative Code*, Case No. 11-4571-EL-UNC, et al. (2010 SEET Case), Opinion and Order (Oct. 23, 2013), Entry on Rehearing (Dec. 18, 2013); *In the Matter of the Application of Ohio Power Company and Columbus Southern Power Company for Administration of the Significantly Excessive Earnings Test under R.C. 4928.143(F) and Ohio Adm.Code 4901:1-35-10*, Case Nos. 13-2249-EL-SSO and 13-2250-EL-SSO (2011 SEET Case), Opinion and Order (Mar. 26, 2014). (Joint Ex. 1 at 4-5.)

Further, the Signatory Parties agree that Staff's testimony supports a finding that the mean ROE earned by publicly traded companies, including utilities, that face comparable business and financial risks as AEP Ohio for 2013 is 9.04 percent and AEP Ohio's testimony supports a finding that the comparable risk group's mean earned ROE is 9.09 percent. On that basis, the Signatory Parties recommend that the Commission find the comparable risk group's earned ROE for 2013 is within the range of 9.04 percent to 9.09 percent. (Joint Ex. 1 at 5.)

The Signatory Parties also agree that, consistent with the process adopted by the Commission in the 2010 SEET Case, an adder be applied to the baseline mean earned ROE of 1.64 standard deviations resulting in an adder of 5.29 percent. The Signatory Parties aver that with the adder, using the Company's calculation results in a SEET threshold of 14.38 percent and using Staff's calculation results in an adder of 5.20 percent for a SEET threshold of 14.24 percent. (Joint Ex. 1 at 5.)

The Signatory Parties stipulate that in the *ESP 2 Case*, the Commission established a SEET threshold of 12.0 percent. *ESP 2 Case*, Opinion and Order (Aug. 8, 2012) at 37.

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<sup>1</sup> Staff's adder has been rounded up from 5.1988 to 5.20.

Accordingly, the Signatory Parties conclude that regardless of which SEET threshold used, AEP Ohio's adjusted earned ROE does not indicate significantly excessive earnings for 2013 and the Company did not have significantly excessive earnings for 2013 pursuant to R.C. 4928.143(F). (Joint Ex. 1 at 5.)

### CONCLUSION:

Ohio Adm.Code 4901-1-30 authorizes parties to Commission proceedings to enter into stipulations. Although not binding on the Commission, the terms of such an agreement are accorded substantial weight. See, *Consumers' Counsel v. Pub. Util. Comm.*, 64 Ohio St.3d 123, 125 (1992), citing *Akron v. Pub. Util. Comm.*, 55 Ohio St.2d 155 (1978). This concept is particularly valid where the stipulation is unopposed by any party and resolves all of the issues presented in the proceeding in which it is offered.

The standard of review for considering the reasonableness of a stipulation has been discussed in a number of prior Commission proceedings. See, e.g., *Cincinnati Gas & Electric Co.*, Case No. 91-410-EL-AIR (April 14, 1994); *Western Reserve Telephone Co.*, Case No. 93-230-TP-ALT (March 30, 1994); *Ohio Edison Co.*, Case No. 91-698-EL-FOR et al. (December 30, 1993); *Cleveland Electric Illum. Co.*, Case No. 88-170-EL-AIR (January 30, 1989); *Restatement of Accounts and Records (Zimmer Plant)*, Case No. 84-1187-EL-UNC (November 26, 1985). The ultimate issue for the Commission's consideration is whether the agreement, which embodies considerable time and effort by the signatory parties, is reasonable and should be adopted. In considering the reasonableness of a stipulation, the Commission has used the following criteria:

- (1) Is the settlement a product of serious bargaining among capable, knowledgeable parties?
- (2) Does the settlement, as a package, benefit ratepayers and the public interest?
- (3) Does the settlement package violate any important regulatory principle or practice?

The Ohio Supreme Court has endorsed the Commission's analysis using these criteria to resolve issues in a manner economical to ratepayers and public utilities. *Indus. Energy Consumers of Ohio Power Co. v. Pub. Util. Comm.*, 68 Ohio St.3d 547 (1994) (citing *Consumers' Counsel*, supra, at 126). The court stated in that case that the Commission may place substantial weight on the terms of a stipulation, even though the stipulation does not bind the Commission.

In this case, the Signatory Parties submit that the Stipulation violates no regulatory principle or precedent, and is the product of serious arm's length bargaining among

knowledgeable and capable parties in an open and cooperative process. Further, the Signatory Parties state that the Stipulation represents a comprehensive compromise of issues raised by parties representing diverse interests and the Stipulation presents a fair and reasonable result that, as a package, benefits ratepayers and is in the public interest. (Joint Ex. 1 at 2.)

William A. Allen, managing director of regulatory case management for American Electric Power Service Corporation, testified in support of the Stipulation. The witness stated that he was familiar with the three-part test used by the Commission to evaluate stipulations and that the Stipulation filed in this case meets those criteria. AEP Ohio witness Allen testified that based on the independent analysis of the Company and Staff, as reflected in the testimony, each party determined AEP Ohio's earnings were not excessive pursuant to R.C. 4928.143(F). Witness Allen also stated the Stipulation was the product of serious bargaining between AEP Ohio and Staff whom are capable and knowledgeable parties. According to witness Allen, the Stipulation, as a whole, benefits ratepayers and the public interest in that the Stipulation complies with Commission regulations and the underlying law. Finally, AEP Ohio witness Allen testified the Stipulation is consistent with the Commission's decisions in AEP Ohio's prior SEET proceedings and did not violate any important regulatory principle or practice. For these reasons, witness Allen recommended that the Commission adopt the Stipulation. (Tr. at 9-10.)

The Commission finds, based on our review of the three-pronged test, the first criterion, that the process involved serious bargaining by knowledgeable, capable parties, is met. The Stipulation filed in this case appears to be the product of serious bargaining among capable, knowledgeable parties familiar with regulatory proceedings, particularly the SEET analysis. Counsel for the Signatory Parties and the witnesses have been involved in numerous cases before the Commission, including several SEET proceedings. Further, the Commission concludes that the Stipulation meets the second criterion. As a package, the Stipulation advances the public interest by resolving all the issues raised in this matter consistent with R.C. 4928.143(F), the *Generic SEET Case*, and the methodology implemented by the Commission in the Company's prior SEET proceedings, the *2010 SEET Case* and *2011 SEET Case*, without extensive litigation. *Generic SEET Case*, Finding and Order (June 30, 2010), Entry on Rehearing (Aug. 25, 2010); *2010 SEET*, Opinion and Order (Oct. 23, 2013) at 10-29; *2011 SEET Case*, Opinion and Order (Mar. 26, 2014); *In the Matter of the Application of Ohio Power Company for Administration of the Significantly Excessive Earnings Test under R.C. 4928.143(F) and Ohio Adm.Code 4901:1-35-10*, Case No. 13-2251-EL-SSO (*2012 SEET Case*), Opinion and Order (May 28, 2014). Finally, the Commission finds that the Stipulation meets the third criterion because it does not violate any important regulatory principle or practice. *Consumers' Counsel*, supra, at 126. Accordingly, we find that the Stipulation filed by the Signatory Parties on October 10, 2014, is reasonable and should be adopted.

FINDINGS OF FACT AND CONCLUSIONS OF LAW:

- (1) AEP Ohio is a public utility as defined in R.C. 4905.02, and, as such, is subject to the jurisdiction of this Commission.
- (2) On May 15, 2014, AEP Ohio filed its application for administration of the SEET in accordance with R.C. 4928.143(F) and Ohio Adm.Code 4901:1-35-10.
- (3) On October 10, 2014, the Signatory Parties filed a Stipulation to resolve all the issues raised in this proceeding.
- (4) The hearing was held on November 5, 2014.
- (5) In the Stipulation, the Signatory Parties agree that AEP Ohio did not have significantly excessive earnings for 2013 pursuant to R.C. 4928.143(F).
- (6) The Commission finds that the Stipulation is supported by the record and is reasonable. On that basis, the Commission finds that the Stipulation should be adopted in its entirety.

ORDER:

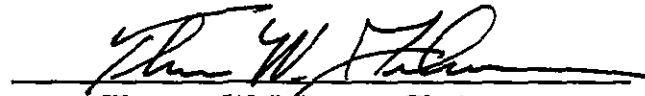
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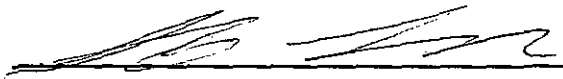
ORDERED, That the Stipulation filed by the Signatory Parties in this matter be adopted in its entirety. It is, further,



ORDERED, That a copy of this Opinion and Order be served upon all person of record.

THE PUBLIC UTILITIES COMMISSION OF OHIO

  
Thomas W. Johnson, Chairman

  
Steven D. Lesser

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Lynn Slaby

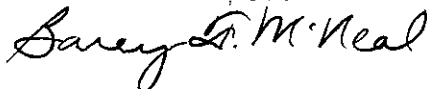
  
M. Beth Trombold

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Entered in the Journal

~~DEC 03 2014~~



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Barcy F. McNeal  
Secretary