BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Ohio Power Company for Administration of the Significantly Excessive Earnings Test for 2016 Under Section 4928.143(F), Revised Code, and Rule 4901:1-35-10, Ohio Administrative Code.	))))))	Case No. 17-1230-EL-UNC

REPLY BRIEF
BY
THE OFFICE OF THE OHIO CONSUMERS' COUNSEL

BRUCE WESTON (0016973)
OHIO CONSUMERS' COUNSEL

William J. Michael, (0070921)
Counsel of Record
Christopher Healey (0086027)
Bryce McKenney (0088203)
Assistant Consumers' Counsel

Office of the Ohio Consumers' Counsel
65 East State Street, 7th Floor
Columbus, Ohio 43215
Telephone: [Michael] (614) 466-1291
Telephone: [Healey] (614) 466-9571
Telephone: [McKenney] (614) 466-9585
william.michael@occ.ohio.gov
christopher.healey@occ.ohio.gov
bryce.mckenney@occ.ohio.gov
(All willing to accept service by e-mail)

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TABLE OF CONTENTS

PAGE

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I. INTRODUCTION

The Settlement between the PUCO Staff and the utility in this proceeding allows the utility, Ohio Power Company ("AEP Ohio"), to keep $53 million in significantly excessive profits that should be returned to consumers. That unfair, one-sided Settlement harms customers and should be rejected.

The evidence shows that the Settlement fails the PUCO's three-prong test for evaluating whether a settlement is reasonable and should be approved. Any bargaining that occurred in this case was not serious, as required, but in the words of the PUCO Staff, "trivial."[1] Customers do not benefit from the Settlement because it allows AEP Ohio to keep $53 million in excessive earnings that, by law, should be returned to customers. And it violates regulatory principles and practices by allowing AEP Ohio to take some of its earnings and exclude them from the significantly excessive earnings test ("SEET") review altogether.

[1] Post-Hearing Brief Submitted on Behalf of the Staff of the Public Utilities Commission of Ohio at 6 (May 1, 2018) (the "PUCO Staff Initial Brief").

The PUCO should reject the Settlement. Instead the PUCO should adopt the Office of the Ohio Consumers' Counsel's ("OCC") recommendation for a $53 million refund to customers of the significantly excessive profits the utility earned during 2016 under the PUCO approved electric security plan.

II. RECOMMENDATIONS

A. The settling parties have not met their burden of proving that the Settlement is the product of serious bargaining.

1. The PUCO's three-prong test requires not just bargaining, but *serious* bargaining.

The first prong of the PUCO's three-prong test requires the signatory parties to demonstrate that the Settlement is the product of serious bargaining among capable, knowledgeable parties. AEP Ohio did not seriously bargain with the parties in this case.

In its initial brief, AEP Ohio admitted that serious bargaining did not occur. It stated that because of the "straightforward issues" in this case, "there was *no need to compromise* on the outcome-determinative question or provide some level of refund as advocated by OCC."[2] If there was no need to compromise, then AEP Ohio and the PUCO Staff could not have engaged in serious bargaining.

The PUCO Staff similarly admitted that serious bargaining did not occur in this case: "Because the Staff's analysis and the company's analysis agreed on the result, reaching an agreement between the two ***was trivial***."[3] If the PUCO Staff's negotiations with AEP Ohio were trivial, then they could not have also been serious—"trivial" being the opposite of "serious."

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[2] Initial Post-Hearing Brief of Ohio Power Company in Support of the Stipulation and Recommendation at 5 (May 1, 2018) (the "AEP Initial Brief").

[3] PUCO Staff Initial Brief at 7 (emphasis added); *see also id.* at 6 (describing the settlement negotiations as "quite simple").

The PUCO's three-part test requires not just bargaining, but serious bargaining. If the word "serious" is to have any meaning, there must be a difference between mere bargaining and serious bargaining. In this case, AEP Ohio acknowledged that there was no need for it to compromise with the PUCO Staff. The PUCO Staff likewise admitted that its negotiations were trivial. Serious bargaining did not occur, and the Settlement therefore fails the first prong of the settlement test.

2. The settling parties' interpretation renders the first part of the PUCO's three-part test meaningless.

AEP Ohio cites just a single piece of evidence of serious bargaining: "the three parties to the case – the Company, Staff and OCC – discussed and considered various options for resolving the issue presented."[4] The PUCO Staff also provides very little evidence demonstrating serious bargaining, stating only that "[d]iscussions were also held between the company and the Consumers' Counsel."[5] Indeed, the PUCO Staff argues that the first part of the test can be reduced to the following: "All that is required is that discussions were had...."[6]

When establishing the three-part test for evaluating settlements, the PUCO could have written the first prong like this: "Did the parties have discussions regarding the settlement?" But it didn't. Instead, it ruled that "serious bargaining" must occur. According to AEP Ohio and the PUCO Staff, as long as a party receives a single phone call regarding a settlement, the first prong is met. This cannot be what the PUCO intended when it required settlements to be the product of serious bargaining.

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[4] AEP Initial Brief at 4.

[5] Staff Initial Brief at 6.

[6] *Id.* at 7.

The record demonstrates that there was very little bargaining in this case, if any at all. The minimal bargaining that took place cannot be considered serious. The Settlement fails the first prong of the PUCO's three-prong test for settlements.

B. The settling parties have not demonstrated that the Settlement contains any benefit to customers.

1. AEP Ohio misstates the second prong of the three-prong test to the detriment of consumers.

There is no dispute that the second prong of the PUCO's three-part test requires the PUCO to consider whether the Settlement, as a package, benefits customers (ratepayers) and the public interest.[7] Yet AEP Ohio attempts to rewrite this part of the test to exclude customers from the equation. According to AEP, "all that is required under the second prong of the settlement test is a just and reasonable result that serves the public interest."[8] AEP has not demonstrated that the public interest has been served by allowing it to keep $53 million of its customers' money.

This is simply not what the second part of the three-part test requires. It requires the PUCO to determine whether a settlement benefits customers *and* the public interest. If "customers" and the "public interest" were synonymous, then the PUCO's test would not mention both of them independently and require a settlement to benefit both. The PUCO should not find that a settlement meets the second prong of its three-prong test based solely on purported unsupported benefits to the public interest. Although the interests of customers and the public interest may at times be aligned in some regards, they are not one and the same. The PUCO must find that the Settlement benefits the public interest

[7] AEP Initial Brief at 3.

[8] *Id.* at 6.

and customers for the second prong of the test to be met. And because there are no benefits to customers, the Settlement fails.

2. The Settlement did not resolve this case in a timely manner.

AEP Ohio identified only a single purported benefit to customers: that the Settlement allowed the case to be resolved in a timely manner.[9] But as OCC explained in its initial brief, the Settlement delayed the case by two months.[10] Contrary to assertions otherwise, the Settlement did not allow the case to be resolved in a timely manner. Having eliminated AEP Ohio's sole purported customer benefit, there is one conclusion: there are no benefits to customers under the Settlement and the public interest has not benefited by allowing AEP Ohio to retain significantly excessive profits owed to its customers.[11]

3. The PUCO Staff did not identify any benefits to customers under the Settlement.

The PUCO Staff addressed the second part of the three-part test for settlements in a single paragraph that does not use the words "customer" or "ratepayer" once. Instead, the PUCO Staff summarily concluded only that the Settlement "benefits the public."[12] According to the PUCO Staff, the Settlement benefits the public because it "avoids the need for disagreements" and "recommends the correct outcome of the case."[13] Of course

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[9] *Id.*

[10] Initial Brief by the Office of the Ohio Consumers' Counsel at 10-11 (May 1, 2018) (the "OCC Initial Brief").

[11] AEP claims that in the absence of the Settlement, the PUCO Staff, "there would have been additional data requests issued by Staff; additional testimony filed, additional cross examination conducted, and additional briefing by Staff on each area of disagreement." *See* AEP Initial Brief at 9. There is no record evidence of any of this, and the PUCO should give these conjectures no weight.

[12] PUCO Staff Initial Brief at 7.

[13] *Id.*

the Settlement avoids the need for disagreements between the settling parties—that's what a settlement is. And of course the parties to the Settlement believe that they are recommending the "correct outcome." Otherwise, they wouldn't recommend it. The fact that the PUCO Staff believes that the Settlement leads to the "correct outcome" does not mean that customers benefit from the Settlement.

Regardless, as discussed above, a settlement must benefit both the public interest and customers. So even if the PUCO agrees with the PUCO Staff's claimed benefits to the public (which it should not), the PUCO Staff cites no evidence of any benefit to customers.

4. Applying the SEET alone is not sufficient to benefit customers and the public interest.

AEP Ohio asserts that performing the statutory SEET, by itself, is enough to promote the public interest.[14] The PUCO, however, is required to apply the significantly excessive earnings test whether there is a settlement or not.[15] To the extent customers or the public interest receive any benefit from mere application of the SEET, they would receive that benefit even if there were no settlement in this case. Thus, the Settlement provides no added benefit to customers or the public interest.

5. AEP Ohio's renewable energy projects, smart grid investments, and energy efficiency programs have nothing to do with the Settlement.

AEP Ohio argues that its programs and investments in renewable energy, smart grid, and energy efficiency justify its significantly excessive earnings.[16] But these programs are not part of the Settlement. Nor does the law prohibiting significantly

[14] AEP Initial Brief at 7.

[15] R.C. 4928.143(F).

[16] AEP Initial Brief at 7-8.

excessive earnings contain any exception for utilities that might invest in renewable energy, smart grid, or energy efficiency.[17] Further, AEP Ohio charges customers for these programs and investments. And AEP profits from offering energy efficiency to customers. In fact, AEP Ohio earned over $31 million in profit from its energy efficiency programs in 2016, which contributed to its significantly excessive earnings.[18]

Further, when the PUCO conducts the statutory SEET, it compares AEP Ohio's earnings to those of companies facing comparable business and financial risk. Those comparable companies may provide many of the same programs and investments without exerting monopoly power over their customers. The PUCO should reject AEP Ohio's assertion that its renewable energy projects, energy efficiency programs, and smart grid investments justify charging customers for significantly excessive earnings and profits.

6. The SEET is designed to protect consumers, not the utility's shareholders.

At various points in its initial brief, the PUCO Staff discusses the purported risks to the "investing public" related to the SEET. For example, the PUCO Staff claims that "the existence of the SEET creates a significant element of risk for the investing public."[19] The PUCO Staff asserts that its proposed SEET methodology "minimizes the riskiness of an investment in the EDU."[20] It further states that without comparing AEP Ohio to comparable companies under the SEET, "it would be impossible for a potential investor or Wall Street analyst to understand the scope of the EDU's exposure to the

[17] *Id.*

[18] AEP Ex. 4 at 6 (Allen Direct).

[19] PUCO Staff Initial Brief at 3.

[20] *Id.*

possibility of refund."[21] And ultimately, the PUCO Staff claims that the Settlement "helps to reduce the risk that is inherently created by the SEET itself."[22]

Through these statements, the PUCO Staff suggests that the "investing public" is the same as the "public interest." But the PUCO Staff ignores the fact that there is no "investing public" in AEP Ohio. It is not a publicly-traded company.

The second prong of the PUCO's test requires the PUCO to determine whether the Settlement benefits customers and the public interest. It does not require the PUCO to determine whether the Settlement benefits the utility's shareholders. The PUCO should reject the PUCO Staff's suggestion that the Settlement somehow benefits the public interest because it may reduce the risk that AEP Ohio's shareholders face. This would be a perverse result in a case that is designed to protect consumers, whose interests are very different and often diametrically opposed to the interests of utility shareholders.

C. The Settlement violates Ohio law and thus fails the third prong of the PUCO's test for settlements.

1. AEP Ohio's proposed adjustments to shield its earnings from SEET review are unlawful.

By law, the PUCO is required to compare AEP Ohio's actual 2016 earnings, as measured by return on common equity, to the actual 2016 earnings of publicly-traded companies that face comparable business and financial risk.[23] The law does not contemplate any adjustments to such earnings based on appeals, settlements, or regulatory delay. In fact, the law requires that all ESP earnings must be considered when

[21] *Id.*

[22] *Id.* at 7.

[23] R.C. 4928.143(F).

applying the SEET.[24] Simply put, 2016 earnings are 2016 earnings, regardless of *why* AEP Ohio may have earned them in 2016 as opposed to in another year.

Yet in applying the SEET, AEP Ohio took earnings that it admits were booked in 2016 and shifted them to different years that are no longer under SEET review. According to AEP Ohio, $13.8 million of its 2016 earnings should be excluded because they relate to an accounting liability that AEP Ohio had previously recorded in 2014.[25] But as OCC explained in its initial brief, these earnings were not counted for purposes of AEP Ohio's 2014 SEET, so this adjustment effectively allows them never to be counted in any SEET case.[26]

AEP Ohio similarly excluded $14.7 million in 2016 earnings under its Phase in Recovery Rider for purposes of its 2016 SEET.[27] AEP Ohio's logic is that this money "should have" been earned in previous years.[28] But the SEET law does not say anything about earnings that a utility believes it "should have" earned in a different period. The law requires the PUCO to compare the utility's actual earnings during the period under review to the actual earnings of comparable companies.[29] The PUCO lacks the authority to adopt AEP Ohio's proposal to ignore $14.7 million in actual 2016 earnings simply because AEP Ohio wanted to reflect that it earned that money in prior years.

The PUCO should ensure that all utility earnings are subject to SEET review. By allowing AEP Ohio to shift earnings from the year under review to another year that is no

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[24] *See In re Application of Columbus S. Power Co.*, 134 Ohio St.3d 392 (2012).

[25] AEP Ex. 3 at 10 (Ross Direct).

[26] OCC Initial Brief at 9.

[27] AEP Ex. 3 at 11 (Ross Direct).

[28] AEP Ex. 5 at 6 (Allen Supplemental).

[29] R.C. 4928.143(F).

longer under review, millions of dollars of AEP Ohio's earnings will avoid SEET review altogether. This violates the law and thus violates regulatory principles and policies.

2. The PUCO should give no weight to witness Buckley's results-oriented SEET analysis.

AEP Ohio argues that the Settlement does not violate any regulatory principles or practices because its witness and the PUCO Staff's witness arrived at similar SEET thresholds.[30] This argument fails for at least two reasons.

First, the fact that the PUCO Staff and AEP Ohio may have arrived at similar SEET thresholds is irrelevant because both of their SEET thresholds are unreasonably high, as explained by OCC witness Duann.[31] The fact that two wrong results are similar does not make them right.

Second, PUCO Staff witness Buckley admitted that his proposed 16.08% SEET threshold was a results-oriented, and not a process-oriented, result. In his testimony, he stated that he initially applied his preferred SEET methodology.[32] Using this preferred methodology, he arrived at a SEET threshold of 39.7 percent.[33] Only after seeing the result, and deciding that it seemed unreasonable, did he modify his methodology until he arrived at a result similar to AEP Ohio's.[34] Thus, the fact that AEP Ohio's and the PUCO Staff's end results differ by 1.61% says nothing about whether they are reasonable.

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[30] AEP Initial Brief at 17.

[31] OCC Ex. 3 at 5-6 (Duann Testimony).

[32] PUCO Staff Ex. 1 at 4 (Buckley Direct).

[33] *Id.*

[34] PUCO Staff Ex. 1 at 4-5 (Buckley Direct).

III. CONCLUSION

AEP Ohio used its monopoly power to charge consumers $53 million for earnings that significantly exceeded the earnings of similar utility companies. The statutory earnings test adopted by the Ohio General Assembly and used by the PUCO to protect consumers from being overcharged by monopoly utilities demonstrates that AEP Ohio had significantly excessive earnings. Ohio law requires AEP Ohio to refund that $53 million to its customers.

Respectfully submitted,

BRUCE WESTON (0016973)
OHIO CONSUMERS' COUNSEL

/s/ William J. Michael
William J. Michael, (0070921)
Counsel of Record
Christopher Healey (0086027)
Bryce McKenney (0088203)
Assistant Consumers' Counsel

Office of the Ohio Consumers' Counsel
65 East State Street, 7th Floor
Columbus, Ohio 43215
Telephone: [Michael] (614) 466-1291
Telephone: [Healey] (614) 466-9571
Telephone: [McKenney] (614) 466-9589
william.michael@occ.ohio.gov
christopher.healey@occ.ohio.gov
Bryce.mckenney@occ.ohio.gov
(All will accept service via email)

CERTIFICATE OF SERVICE

I hereby certify that a copy of this Reply Brief was served on the persons stated below via electronic service, this 22nd day of May 2018.

/s/ William J. Michael
William J. Michael
Assistant Consumers' Counsel

SERVICE LIST

stnourse@aep.com
Thomas.mcnamee@ohioattorneygeneral.com

Attorney Examiners:

Sarah.Parrot@puc.state.oh.us
Greta.See@puc.state.oh.us

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