

**BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO**

In the Matter of the Review of the Power)
Purchase Agreement Rider of Ohio) Case No. 18-1004-EL-RDR
Power Company for 2018.)

In the Matter of the Review of the Power)
Purchase Agreement Rider of Ohio) Case No. 18-1759-EL-RDR
Power Company for 2019.)

**REPLY BRIEF
BY
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I. INTRODUCTION

Staff and AEP argue that the Audit Report filed by London Economics International (“LEI”) was independent, responsive to the PUCO’s Request for Proposals, and demonstrated that AEP’s actions were prudent and in the best interest of consumers. The Audit Report was none of these things.

Staff and AEP cannot escape the fact that in 2018 and 2019 consumers paid \$74.5 million in above-market costs for electricity produced by two aging coal plants (OVEC plants), one located outside Ohio. ¹ This came on the heels of consumers paying \$21.7 million and \$39.2 million in above-market charges in 2016 and 2017, respectively.² A key point is that after incurring such high above-market costs in 2016 and 2017, AEP did absolutely nothing to change how the plants were operated or to find an alternative resource to serve as a so-called financial hedge. AEP knew it had consumers as their

¹ Hearing Transcript at Vol. I, p. 9 (Jan. 26, 2022).

² Staff Ex. 1 at 32, Figure 13 and *In the Matter of the Review of the Power Purchase Agreement Rider of Ohio Power Company*, Case No. 18-1003-EL-RDR, Audit Report at 37 (Aug. 8, 2019).

backstop for any losses resulted from running the OVEC plants. Under these circumstances, doing nothing was not prudent or in the best interest of consumers.

A key fact revealed at the hearing is that the Auditor *changed her draft report to remove the sentence*: “Therefore, keeping the plants running *does not seem to be in the best interests* of the ratepayers.”³ The Auditor claimed she exercised her own judgment to remove this sentence because it was “too broad.”⁴ She admitted, however, that this edit was in the “conclusion” section and did not affect her overall opinion contained in the body of the Audit Report.⁵ Based on this explanation by the Auditor, the Audit Report establishes that running the plants is not in the consumers’ best interests irrespective of the exact words in the conclusion section. The PUCO should so find and should disallow the entire \$74.5 million in above-market costs that AEP collected under the PPA Rider.

II. LAW AND ARGUMENT

A. The PUCO should disallow AEP’s \$74.5 million in charges to consumers during the audit period (2018 and 2019).

1. In spite of undue interference from Staff, LEI’s Audit Report did demonstrate running the OVEC plants was not in the best interest of consumers.

Staff’s Initial Brief uses the word “independent” seven times. Apparently, Staff believes the more often you say something, the more convincing it becomes. Staff “vehemently rejects any arguments (or even suggestions) made by any party that Staff specifically directed or forced the removal of any statements or overstepped its role in

³ Direct Testimony of Michael P. Haugh (OCC Ex. 21), filed Dec. 29, 2021, Attachment MPH-3 at 1 (Emphasis added).

⁴ Hearing Transcript at Vol. I, p. 177 (Jan. 26, 2022).

⁵ *Id.*

this proceeding by making “suggestions” regarding the content of the draft Audit Report.⁶ Staff’s explanation in the Initial Brief ignores what really happened.

Specifically, after reviewing the initial draft Audit Report, Staff told the Auditor to use a “milder tone and intensity of language.”⁷ Staff Witness Rodney Windle also asked the Auditor to “balance” her conclusion by listing the other benefits that also led the PUCO to approve the Coal Plant Charge, namely, jobs and fuel diversity.”⁸ The next draft, dated September 9, 2020, incorporated the changes suggested by Mr. Windle including “jobs and fuel diversity” language. The conclusion states: “However, LEI’s analysis shows that the OVEC contract overall is not in the best interest of AEP Ohio ratepayers.”⁹ For reasons never really explained at the hearing, the Auditor sent this draft first to AEP, but not Staff.¹⁰ These are just a few examples of the clear undue interference by the Staff, that aided the utility, on the supposedly independent audit by LEI.

Additionally, Staff gave the Auditor “editorial suggestions” that “milder tone and intensity of language would be recommended.”¹¹ The Staff’s “suggestions” favored AEP to the detriment of consumers. The Staff directed the Auditor to “please take a look and incorporate Staff’s comments as far as possible.”¹² The Auditor testified that Staff asked

⁶ Staff Post-Hearing Brief at 10 (Mar. 18, 2022).

⁷ Direct Testimony of Michael P. Haugh (OCC Ex. 21), filed Dec. 29, 2021, Attachment MPH-3 at 1.

⁸ Hearing Transcript at Vol. VI, p. 1699:4-14 (Feb. 17, 2022).

⁹ *Id.* at Vol. I, p. 175:6 – 177:2 (Jan. 26, 2022).

¹⁰ OCC Ex. 27 at 3 and 16; Hearing Transcript at Vol. VI, p. 177:10-11; Hearing Transcript at Vol. VI, p. 1578:3 – 1579:19 (Feb. 17, 2022).

¹¹ Direct Testimony of Michael P. Haugh (OCC Ex. 21), filed Dec. 29, 2021, Attachment MPH-3 at 1.

¹² *Id.*

her to remove this statement: “And the -- our client, Staff, asked us to edit, take it out, whatever, and all the rest of the audit stands without it.”¹³

In spite of all this undue interference, the LEI Auditor nevertheless concluded that *it was not in the best interest of ratepayers to keep the OVEC plants running* in 2018 and 2019. The exact language may be edited out the final Audit Report, but the findings by the Auditor are quite clear. These findings include:

- “However, LEI’s analysis shows at this time that the OVEC plants cost customers more than the cost of energy and capacity that could be bought on the PJM wholesale market;”¹⁴
- “However, LEI’s analysis showed that some of the time, the PJM energy price did not cover fuel and variable cost”;¹⁵ and
- “LEI recommends that OVEC re-consider its ‘must-run’ offer strategy.”¹⁶

2. AEP’s operation of the OVEC units and management of its output during the 2018-2019 audit period was imprudent.

By using legal terms like *res judicata* and *collateral estoppel*, AEP wants the PUCO to believe OCC (and the other Intervenors) are trying to relitigate the PPA Rider.¹⁷ AEP also claims OCC (and the other Intervenors) use “after-the-fact data and second guess the original decision to approve the ICPA for inclusion on the PPA Rider during the audit period.”¹⁸ AEP even recommends the PUCO “reject OCC’s categorical position

¹³ Hearing Transcript at Vol. I at p. 177:10-12 (Jan. 26, 2022).

¹⁴ Staff Ex. 1 (Audit Report) at 8.

¹⁵ *Id.*

¹⁶ *Id.*

¹⁷ *Id.* at 32 and 33.

¹⁸ *Id.* at 34.

based purely on hindsight that all above-market costs should be disallowed at imprudent.”¹⁹ According to AEP, OCC (and the other Intervenors) have engaged in “Monday Morning Quarterback[ing].”²⁰ AEP is mistaken. OCC is not exploiting hindsight criticism, but instead is focusing on the audit, the purpose of the audit, and what the audit uncovered.

On January 15, 2020, the PUCO directed its Staff to submit a request for proposal for an auditor to conduct a prudency and performance audit of AEP’s Coal Plant Charge for the period January 1, 2018 through December 31, 2019.²¹ The RFP defined the audit’s purpose as being “to establish the prudency of all costs and sales flowing through the PPA Rider and to demonstrate that the Company’s actions were in the best interest of ratepayers.”²²

Merriam-Webster defines the term “audit” as a “methodical examination and review.” As a verb, “audit” is synonymous with check (out), examine, inspect, review, and scrutinize. Prudence is defined as:

Carefulness, precaution, attentiveness, and good judgment as applied to action or conduct That degree of care required by the exigencies or circumstances under which it is to be exercised. This term, in the language of the law, is commonly associated with ‘care’ and ‘diligence’ and contrasted with ‘negligence.’²³

In other words, LEI was asked to review and scrutinize whether AEP was careful and used good judgment when it charged consumers, in 2018 and 2019, \$74.5 million

¹⁹ *Id.* at 35.

²⁰ *Id.* at 7.

²¹ Entry (Jan. 15, 2020).

²² *Id.*; RFP at 4.

²³ Black’s Law Dictionary Online.

more than the market price for the same energy²⁴ or whether these charges and the system used to produce them was in the best interest of consumers. With the instant hearing, OCC (and the other Intervenors) were allowed to challenge LEI's conclusions and AEP's practices in 2018 and 2019. It is not a challenge to the decision to approve the PPA Rider.

AEP tries to shift the Commission's focus by quoting the Supreme Court of Ohio and (former) Commissioner Haque. AEP is correct when it says, "the intended purpose of the rider [is] to provide a financial hedge against fluctuating prices in the wholesale power market in order to stabilize retail-customer rates."²⁵ AEP also is correct when it reminds everyone that (former) Commissioner Haque said the "general consensus that the PPA Riders will result in a charge to customers for at least the first two to three years of the riders."²⁶ These statements, however, do not allow the PUCO to ignore what actually happened in 2018 and 2019, and that these followed two years of substantial above-market costs in 2016 and 2017.

As OCC witness Ms. Glick explained, the costs to operate the OVEC plants were substantially higher than the PJM market prices for the same energy, capacity, and ancillary service during the 2018-2019 audit period.²⁷ No matter how hard it tries, AEP must concede it charged customers \$74.5 million for power from the OVEC plants, rather than purchase cheaper power from the PJM market. While some customer charges may have been expected in these early years of the rider, customers were paying substantially

²⁴ OCC Ex. 14, Direct Testimony of Devi Glick at 26 (Dec. 29, 2021).

²⁵ OCC Initial Brief at p. 40 (Mar. 18, 2022).

²⁶ *Id.* at 41.

²⁷ Direct Testimony of Devi Glick (OCC Ex. 14) at 18 (Dec. 29, 2021).

more under AEP's Coal Plant Charge in twenty-three of the twenty-four months of the audit period.²⁸

Looking at these alarming numbers is not Monday-Morning Quarterbacking. Instead, it is a review of the actual cost and sales flowing through the PPA Rider. AEP wants the PUCO to overlook the undeniable data for this audit period (2018 and 2019) and look to the promise of the 2020 audit period. No reasonable person can conclude AEP's practice in 2018 and 2019 was in the consumer's best interest. AEP only had to look at the poor performance of the OVEC plants in 2016 and 2017 to see that 2018 and 2019 would also cost customers millions of dollars. AEP knew these plants would continue to lose money but didn't care because consumers, not shareholders, were footing the bill. Therefore, the PUCO should disallow the \$74.5 million in above-market charges to consumers in 2018 and 2019.

Then, there is AEP's must-run commitment strategy. OCC witness Mr. Haugh testified what we all know. That is, AEP and OVEC committed the plants on a "must run" basis.²⁹ He also explained good utility practice, where operators perform a daily financial analysis of the projected costs and projected revenues for operating plants before deciding whether to commit the plant as must-run or economic, is the best practice. Why? Because it can avoid a situation like the one created by AEP's imprudence – a plant being operated during months when the plant's revenue did not cover variable operating costs. AEP supports, actually blames, its must-run decision on "OVEC's design and operating characteristics."³⁰ AEP contends that if "OVEC units

²⁸ *Id.*

²⁹ Direct Testimony of Michael P. Haugh (OCC Ex. 21), at 27-32 (Dec. 29, 2021).

³⁰ OCC Initial Brief at 47 (Mar. 18, 2022).

were to cycle on-and-off instead of operating as baseload generators, coal deliveries could pile up, causing an unsafe overabundance of coal.”³¹

AEP even tries to dodge its responsibilities by arguing it could not unilaterally change the must-run commitment.³² These are, and should be viewed by the PUCO as, nothing more than hollow excuses that harmed consumers. AEP witness Mr. Stegall acknowledged AEP performs this daily financial analysis when making commitment decisions for plants that it directly owns.”³³ According to Mr. Stegall, this is good utility practice. However, AEP did not employ this good utility practice here. AEP doesn’t refrain from this practice due to some worry that an overabundance of coal deliveries could occur.

Consequently, the undisputed facts show AEP did not act carefully, diligently, and with good judgment when it committed the OVEC plants as “must run” during the audit period. The PUCO should not support AEP’s “it has to be this way because our plants are old” attitude. This is another example of poor management of the plants because the losses would be passed on to consumers. Therefore, the PUCO should disallow the \$74.5 million in above-market charges to consumers in 2018 and 2019.

The difference between the plants AEP owns (that Mr. Stegall was discussing) and the OVEC plants is competition. The plants AEP owns are operated in the competitive market and AEP’s shareholders bear the risk of operating losses. The OVEC are not operating as competitive generating plants, which unfortunately puts consumers at

³¹ *Id.* at p. 48.

³² *Id.* at p. 49.

³³ Hearing Transcript at Vol. III, p. 782:9 – 783:23 (Jan. 28, 2022). *See also* Direct Testimony of Dr. Jeremy I. Fisher, PhD at 18:3-20 (Dec. 29, 2021).

risk for the operating losses. To allow AEP to charge its consumers the \$74.5 million goes against the PUCO's consumer protection intention when this rider was approved. Notably, then-PUCO Chair Haque wrote in a concurring opinion when the PPA Rider was approved: "This should not be perceived as a blank check, and consumers should not be treated like a trust account."³⁴

AEP also believes the rider "does not require or contemplate (or authorize) active management of the [financial] hedge."³⁵ To support this careless attitude and justify passing along \$74.5 million to consumers in 2018 and 2019, AEP actually states "[n]one of the findings of the PUCO or the Court are contingent upon OVEC costs creating a below-market credit . . . Rather it was always envisioned as a passive hedge that was set up and operated automatically in response to market conditions."³⁶ AEP ignores the fact that the Rider's purpose was to offer consumer protection against price volatility. The Rider was meant to

supplement the benefits derived from the staggering and laddering of the SSO auctions and *protect retail customers from price volatility in the market*. The record reflects that the PPA rider will provide added rate stability during periods of extreme weather, when the rider can be expected to offset severe price spikes. *The different scenarios reflected in AEP Ohio's projection of the PPA rider's impact demonstrate the effect of variation in load due to severe weather or economic factors, including the asymmetric impact that such factors have on electric prices, where increases in load tend to increase prices more so than load reductions decrease prices. If load increases due to weather or economic conditions, shopping and SSO*

³⁴ *In the Matter of the Application Seeking Approval of Ohio Power Company's Proposal to Enter into an Affiliate Purchase Power Agreement*, Case No. 14-1693-EL-RDR, Opinion and Order, Concurring Opinion of Chairman Haque at 5 (Mar. 31, 2016).

³⁵ OCC Initial Brief at 39 (Mar. 18, 2022).

³⁶ *Id.* at 40.

*customers will be exposed to the resulting higher wholesale prices, which the PPA rider will partially offset.*³⁷

The volatility that the rider was supposed to protect never happened, and the rider simply cost consumers substantially. As Ms. Glick testified, actual market prices have been much lower than originally projected.³⁸ AEP's Coal Plant Charge, therefore, has not provided anything close to its projected value, and there is no indication that this trend is likely to change.³⁹ Moreover, there is no indication that AEP's Coal Plant Charge, which cost customers significantly in twenty-three of the twenty-four months, had anything to do with severe weather or economic factors.

When AEP sought approval for the Coal Plant Charge, it projected the Charge would produce a net credit to consumers of about \$110 million over eight years, or an average credit of \$13.75 million per year.⁴⁰ In the words of Commissioner Beth Trombold: "Based on the forecasts submitted by the Company and evidence in the record, it is my clear expectation, just as it is Commissioner Haque's, that the PPA rider approved today will result in a credit (i.e. benefit) to ratepayers over the next eight years."⁴¹

AEP has a duty to act in the consumers' best interest. It did not. This is not a hindsight analysis, as AEP claims. To the contrary, AEP knew the plants lost \$21.7

³⁷ *In the Matter of the Application Seeking Approval of Ohio Power Company's Proposal to Enter into an Affiliate Power Purchase Agreement for Inclusion in the Power Purchase Agreement Rider*, Case No. 14-1693-EL-RDR, Opinion and Order at 83 (Mar. 31, 2016) (emphasis added).

³⁸ Direct Testimony of Devi Glick (OCC Ex. 14) at 37 (Dec. 29, 2021).

³⁹ *Id.*

⁴⁰ *In the Matter of the Application Seeking Approval of Ohio Power Company's Proposal to Enter into an Affiliate Power Purchase Agreement for Inclusion in the Power Purchase Agreement Rider*, Case No. 14-1693-EL-RDR, Fifth Entry on Rehearing at 31 (Apr. 5, 2017).

⁴¹ *In the Matter of the Application Seeking Approval of Ohio Power Company's Proposal to Enter into an Affiliate Purchase Power Agreement*, Case No. 14-1693-EL-RDR, Opinion and Order, Concurring Opinion of Commissioner M. Beth Trombold at 2 (Mar. 31, 2016).

million in 2016 and \$39.2 million in 2017 and should have done something in 2018 and 2019 to limit losses.

Doing nothing to mitigate above-market costs, when consumers sustained four straight years of above-market costs totaling \$135 million, was not prudent. Therefore, the PUCO should act to protect consumers and disallow the entire \$74.5 million in above-market charges to consumers in 2018 and 2019.

III. CONCLUSION

The evidence demonstrates AEP's \$74.5 million in above-market energy charges to consumers through the Coal Plant Charge in 2018 and 2019 were imprudent. The evidence also demonstrates AEP operated the OVEC plants not in the best interest of consumers. And, the PUCO does not have to take OCC's word on that. It can use LEI's initial conclusion – "keeping the [OVEC] plants running does not seem to be in the best interests of the ratepayers."

Respectfully submitted,

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CERTIFICATE OF SERVICE

It is hereby certified that a true copy of the foregoing Reply Brief was served upon the persons listed below by electronic transmission this 8th day of April 2022.

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