ORIGINAL

IN THE SUPREME COURT OF OHIO

Columbus Southern Power Company and Ohio Power Company	:	**Case No. 09-2060**
Appellants,	:	**Appeal from the Public Utilities Commission of Ohio**
v.	:	
The Public Utilities Commission of Ohio,	:	**Public Utilities Commission of Ohio Case No. 09-119-EL-AEC**
Appellee.	:	

APPELLANT BRIEF OF COLUMBUS SOUTHERN POWER COMPANY AND OHIO POWER COMPANY

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INTRODUCTION

Although the facts involved with the case are complex, the outcome of the appeal turns squarely on the law. The approved standard service offer (SSO) rates of Columbus Southern Power Company and Ohio Power Company (collectively, AEP Ohio) include a *non-bypassable* Provider of Last Resort (POLR) charge. The POLR charge was approved to cover two types of risk related to customers shopping for generation service since AEP Ohio stands ready as the default service provider: (1) the risk of allowing a customer to remain with the SSO when market prices are higher than the SSO, and (2) the risk of customers leaving the SSO when market prices are favorable and subsequently returning to the SSO when market prices exceed SSO rates. The Commission provided as part of approving AEP Ohio's SSO that shopping customers would pay the POLR charge when receiving SSO service as well as during the time they are receiving generation service from a competitive supplier, unless a shopping customer promises to pay a market price if that customer subsequently returns to the SSO. Approval of a POLR charges is common to all of the electric utilities in Ohio, consistent with the statutory POLR obligation imposed upon all electric utilities. Yet the decision below exposes AEP Ohio to uncompensated POLR risk based on an unsupportable conclusion that AEP Ohio faced no risk that the involved customer, Ormet Primary Aluminum Company (Ormet), would shop for generation service from another supplier during the term of the contract – even though this very customer has previously left AEP Ohio's service territory and promised not to return, only to come back when market prices rose.

Contemporaneous with finalizing AEP Ohio's ESP through the rehearing process, the Commission was actively considering an application filed by Ormet for approval of a discounted rate for electric service. In deciding that case, the Commission granted a substantial discount to Ormet and approved a ten-year term for the contract. Over AEP Ohio's objection, the Commission approved a controversial provision that rendered AEP Ohio the "exclusive supplier" to Ormet for the entire term of the contract. The Commission found that there was "no risk" that Ormet would shop during the contract term and held that AEP Ohio would not be permitted to recover the otherwise applicable POLR charge in connection with the contract. Thus, even though the Commission had recently approved AEP Ohio's non-bypassable POLR charge, it contemporaneously decided in the case below to order AEP Ohio to enter into a service agreement without fully compensating AEP Ohio the revenue foregone as a result of the discounted economic development rate. In reaching this decision, the Commission concluded that it has full discretion to decide whether to allow recovery of revenue foregone.

The Commission's decision to adopt the exclusive supplier provision conflicts with the central tenets of Ohio electric restructuring laws and should be reversed and remanded. Ten years, the term of the compulsory agreement, is an extended period of time nearly equal to the decade that the State of Ohio has steadfastly maintained customer choice for electricity supply. Serving Ormet's enormous power requirement is equal to supplying power to more than 400,000 households and it is extremely significant and potentially harmful to the enhancement of retail electric competition in Ohio that the Commission inexplicably decided to pull Ormet's load out of the competitive market for such a substantial period of time.

Neither the Commission's conclusion that it can unilaterally order a utility to "agree" to an objectionable service contract, nor the Commission's harmful conclusion that it has plenary discretion to require a utility to absorb the costs associated with any discount it approves, are legally sustainable. There is no basis in the controlling statute, R.C. 4905.31, to support the Commission's interpretation. And it makes little sense to require the utility to involuntarily absorb the costs of an economic development venture, given that the approved discount is not related to avoided costs in providing service and given that the anticipated economic benefits are expected to accrue primarily to Ohio's economy.

This dispute is no academic matter – the Commission's decision directly inflicts up to $11.7 million dollars of harm to AEP Ohio annually, paving the way for an even larger adverse impact based on similar decisions for other large industrial customers in the future. Under the Commission's view that it has unbridled discretion to approve economic development discounts and simultaneously disallow recovery of the associated revenue foregone, there is no limit to the potential financial harm that is yet to befall AEP Ohio and other utilities if the Court does not reverse this decision. Indeed, another case has already been similarly decided by the Commission.[1]

AEP Ohio is committed to economic development and has continuously demonstrated this commitment in the communities it serves. AEP Ohio collaboratively works with existing customers to provide needed electrical infrastructure in an effort to retain existing jobs and investment. For example, in September 2008, AEP (including AEP Ohio) was named in the top 10 list of utilities in economic development by Site Selection magazine, a national publication of corporate real estate strategy and area

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1 *In the Matter of the Application for Establishment of a Reasonable Arrangement Between Eramet Marietta, Inc. and Columbus Southern Power Company*, Case No. 09-516-EL-AEC, October 15, 2009 Opinion and Order, Ap. at 100.

economic development.[2] While AEP Ohio supports economic development in many ways and has consistently worked with the Commission and the State of Ohio to promote economic development opportunities, it must challenge as unreasonable and unlawful the Commission's decision which inflicts financial harm on the serving utility as a method of promoting economic development. When approving economic development arrangements that are perceived to benefit the State of Ohio, the Commission must permit the affected utility recovery of the full discount granted, in accordance with R.C. 4905.31.

STATEMENT OF FACTS AND OF THE CASE

A. Overview of the Legislative Restructuring of the Electric Industry

Am. Sub. S.B. No. 3, 1999 Ohio SB 3, effective October 5, 1999 (SB 3), restructured regulation of electric utilities and introduced retail customer choice for electric generation service, largely deregulating generation service in Ohio. Am. Sub. S.B. No. 221, 2007 Ohio SB 221, effective July 31, 2008 (SB 221), modified the method for setting standard service offer (SSO) rates for electric service and created new requirements for alternative energy, energy efficiency and peak demand reductions. Thus, through the enactment of SB 3 by the General Assembly (and retained by SB 221), customers were given the statutory right to shop for generation service on their own or as part of an aggregated group.

Of equal importance to this case, SB 3 granted customers the right to not shop and avoid market-based rates by taking service under the SSO of their electric distribution

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2 http://www.siteselection.com/portal/

utility (EDU). Ohio Rev. Code Ann. 4928.141 (2010), Ap. at 17.[3] As a related but distinct matter, customers can also return to the EDU's SSO if they shopped for generation service and subsequently decided to return or if their competitive service provider defaulted on its obligation to serve. Ohio Rev. Code Ann. 4928.14 (2010), Ap. at 17. Despite significant changes made to the regulatory framework established by SB 3 back in 1999, the enactment of SB 221 in 2008 retained the same "customer choice" components as the cornerstone of the continuing structure for deregulation of electric service in Ohio.

A corollary to these customer rights is the EDU's obligation to be the Provider of Last Resort (POLR), a requirement imposed on EDUs by multiple statutory provisions. R.C. 4928.141(A) imposes on an EDU the requirement to provide consumers within its certified service territory "a standard service offer of all competitive retail electric services necessary to maintain essential electric service to consumers, including a firm supply of electric generation service." Ohio Rev. Code Ann. 4928.141(A) (2010), Ap. at 17. When coupled with the right to choose a retail generation supplier, availability of the SSO to any customer means that a customer can freely leave the EDU when market price is lower than the stabilized SSO rate and can just as easily return when the market price rises above the SSO rate. Given the volatile nature of market prices for electricity, there exists a potential for "churn" or migration of customers on and off SSO service. Another POLR obligation is based on R.C. 4928.14, which provides that customers of a defaulting competitive provider return to the EDU's SSO until the customers choose an alternative

[3] References to Appellant's Appendix are designated as "Ap."

supplier. Ohio Rev. Code Ann. 4928.14 (2010), Ap. at 16. EDUs must stand ready to serve in these situations and fulfill their statutory POLR obligation.

Another significant amendment within SB 221 that is pertinent to this case involves reasonable arrangements, also known as "special contracts," whereby a customer typically receives service at a discounted rate based on furthering economic development purposes within the State of Ohio or other unique circumstances. R.C. 4905.31 was amended to allow a "mercantile customer"[4] to petition the Commission for approval of a reasonable arrangement with an EDU. Previously (and continuing for non-electric public utilities), only a public utility could petition the Commission for approval of a reasonable arrangement. When creating this novel provision for mercantile customers, the General Assembly simultaneously decided to permit a financial device "to recover costs incurred in conjunction with any economic development and job retention program of the utility within its certified territory, including recovery of revenue foregone as a result of any such program." Ohio Rev. Code Ann. 4905.31(E) (2010), Ap. at 4 (emphasis added).

B. AEP Ohio's Electric Security Plan Cases

Under SB 221, electric utilities can either seek approval of an Electric Security Plan (ESP) or a Market Rate Offer (MRO) to establish an SSO rate plan. Ohio Rev. Code Ann. 4928.141 (2010), Ap. at 17. While an ESP may be considered more of a hybrid pricing plan, combining elements of traditional regulation and market-based deregulation, the MRO is ultimately designed, after a possible transition period, to fully

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[4] A "mercantile customer" as defined in R.C. 4928.01 (A)(19), is a commercial or industrial customer that consumes more than 700,000 kWh of electricity per year, for nonresidential use, or is part of a national account involving multiple facilities in one or more states.

achieve permanent market-based pricing for the utility. In particular, a utility's decision to opt for an MRO is permanent under R.C. 4928.142(F). Ohio Rev. Code Ann. 4928.143 (2010), Ap. at 21. In approving the special arrangement in the decision below, the Commission denied full recovery of revenues foregone as a result of the special arrangement, by excluding recovery of the otherwise applicable POLR charges authorized by the Commission as part of AEP Ohio's ESP. Understanding AEP Ohio's approved POLR charge is central to this case. Columbus Southern Power and Ohio Power filed an ESP proposal on the same date that SB 221 became effective, July 31, 2008.[5] As part of its ESP application, AEP Ohio proposed a non-bypassable POLR rider to collect an annual revenue requirement reflecting the costs of fulfilling the POLR obligation. (*ESP Cases*, Opinion and Order at 38 (internal citations omitted), Ap. at 151.)

In considering the proposal, the Commission recognized that AEP Ohio's proposed POLR charge would cover two distinct risks: "the cost of allowing a customer to remain with the Companies, or to switch to a [competitive] provider and then return to the Companies' SSO after shopping" and noted that AEP Ohio "utilized the Black-Sholes Model to calculate their cost of fulfilling the POLR obligation, comparing customers' rights to 'a series of options on power.'" (*ESP Cases*, Opinion and Order at 38-39, Ap. at 151-152) (internal citations omitted). The Commission also recognized its Staff's position that there are "two risks involved: one risk is the risk of customers returning to the SSO and the other risk is that the customers leave and take service from a

[5] *In the Matter of the Application of Columbus Southern Power Company for Approval of an Electric Security Plan; an Amendment to its Corporate Separation Plan; and the Sale or Transfer of Certain Generating Assets,* Case No. 08-917-EL-SSO, and *In the Matter of the Application of Ohio Power Company for Approval of its Electric Security Plan; and an Amendment to its Corporate Separation Plan,* Case No. 08-918-EL-SSO (collectively, the "*ESP Cases*") (March 18, 2009 Opinion and Order), at 1, Ap. at 114.

[competitive] provider (migration risk). Staff witness Cahaan testified that the risk associated with customers returning to the SSO could be avoided by requiring the customer to return at a market price…" (*ESP Cases*, Opinion and Order at 39, Ap. at 152) (internal citations omitted). As between the two risks, the Commission noted that AEP Ohio's testimony indicated "the migration risk equals approximately 90 percent of the Companies' POLR costs pursuant to the Black-Scholes model." (*Id.*)

The Commission decided to grant and modify AEP Ohio's proposed POLR charge as part of its decision in the *ESP Cases*:

> Therefore, based on the record before us, we conclude that the Companies' proposed ESP should be modified such that the POLR rider will be based on the cost to the Companies to be the POLR and carry the risks associated therewith, including the migration risk. The Commission accepts the Companies' witness' quantification of that risk to equal 90 percent of the estimated POLR costs, and thus, finds that the POLR rider shall be established to collect a POLR revenue requirement of $97.4 million for CSP and $54.8 million for OP.

(*ESP Cases*, Opinion and Order at 40, Ap. at 153) (internal citations omitted). Thus, regarding the migration risk (that customers could migrate, *i.e.*, leave, when market prices drop below the SSO rate during the period of the ESP), the Commission agreed that 90% of the requested POLR revenue requirement proposed should be allowed to compensate AEP Ohio for that risk. Regarding the second risk (a customer shopping and then returning to the SSO rate when the market price goes back up), the Commission permitted shopping customers to bypass the POLR charge if they agree to pay a market price if they end up returning to SSO service later; otherwise, those shopping customers would continue to pay the POLR charge during the time they received generation service from a competitive service provider. (*ESP Cases*, Opinion and Order at 40, Ap. at 153.)

C. The Proceeding Below

On February 17, 2009 Ormet Primary Aluminum Corporation (Ormet) filed an application for approval of a unique arrangement with Columbus Southern Power Company and Ohio Power Company, collectively AEP Ohio.[6] (*In the Matter of the Application of Ormet Primary Aluminum Corporation for Approval of a Unique Arrangement with Ohio Power Company and Columbus Southern Power Company*, Case No. 09-119-EL-AEC ("*Ormet Case*") (July 15, 2009 Opinion and Order), at 1, Ap. at 34.) AEP Ohio did not join Ormet in filing the application, but did move to intervene on February 27, 2009. (*Ormet Case*, February 27, 2009 Motion of AEP Ohio to Intervene, Ap. at 96.) Although AEP Ohio's motion to intervene expressed general support for Ormet's initial proposal in this proceeding, it conditioned the support upon full recovery of revenues foregone as a result of the discount from tariff rates. (*Id.* at 2, Ap. at 97.) Notably, Ormet's application proposed full recovery of revenues foregone as a result of the proposed contract. (*Ormet Case*, Application at 7-8, Supp. at 40-41.)[7]

One of the provisions in the arrangement proposed by Ormet (Article 2.01) was for AEP Ohio to be the exclusive supplier to Ormet during the 10-year term of the arrangement. (*Ormet Case*, Opinion and Order at 13, Ap. at 46; Power Agreement at Article 2.03, Supp. at 11.) AEP Ohio argued against adoption of this provision, as violating the policy of the State of Ohio and the fundamental notion of customer choice

[6] Ormet receives service from the joint service territory of CSP and OP and, under the approved contract, the AEP Ohio tariff rate is defined as the amount Ormet would pay if 50% of its load was billed under CSP tariff rates and 50% under OP tariff rates. (*Ormet Case*, Power Agreement at Article 1.01, Supp. at 6.)

[7] References to Appellant's Supplement are designated as "Supp."

embodied in SB 3 and SB 221. Without addressing AEP Ohio's arguments, the Commission simply held as follows:

> The Commission finds that under the terms of the unique arrangement AEP-Ohio will be the exclusive supplier to Ormet. Therefore, there is no risk that Ormet will shop for competitive generation and then return to AEP-Ohio's POLR service.

(*Ormet Case*, Opinion and Order at 13, Ap. at 46) (internal citations omitted). Accordingly, the Commission went on to require that "AEP-Ohio shall credit any POLR charges paid by Ormet to its economic development rider... ." (*Id.* at 14, Ap. at 47.)

AEP Ohio filed an application for rehearing, requesting that the Commission reconsider its adoption of the compulsory agreement generally and "exclusive supplier" provision specifically – not only to uphold State policy and statutory mandates regarding customer choice but also to preserve the Commission's decision to adopt a non-bypassable POLR charge in the *ESP Cases* and enable AEP Ohio to fully recover "revenues foregone" as a result of the Ormet arrangement. (*Ormet Case*, AEP Ohio Application for Rehearing at 13-14, Ap. at 63-64.) The Commission rejected AEP Ohio's rehearing arguments and found that R.C. 4905.31 enabled it to order AEP Ohio to execute the "agreement." (*Ormet Case*, September 15, 2009 Entry on Rehearing, at 19, Ap. at 95.) With respect to the exclusive supplier provision, the Commission found that the provision "may, or may not, adversely affect competition in this state, but there is no evidence in the record to support that determination." (*Ormet Case*, Entry on Rehearing at 13, Ap. at 89.) Regarding AEP Ohio's challenge to the POLR offset decision, the Commission found that, under R.C. 4905.31, "the recovery of delta revenues is a matter for the Commission's discretion." (*Id.* at 11, Ap. at 87.) AEP Ohio timely filed a Notice of Appeal with this Court.

STANDARD OF REVIEW

This Court has "complete and independent power of review as to all questions of law" in appeals from the commission. *Ohio Edison Co. v. Pub. Util. Comm.* (1997), 78 Ohio St. 3d 466, 469. *See also Ohio Consumers' Counsel v. Pub. Util. Comm.* (2009), 121 Ohio St. 3d 362, 365. Pursuant to R.C. 4903.13, a Commission order will be reversed, vacated, or modified by this court when, upon consideration of the record, the court finds the order to be unlawful or unreasonable. *Ohio Consumers' Counsel v. Pub. Util. Comm.* (2009), 121 Ohio St. 3d 362, 365. *See also Constellation NewEnergy, Inc. v. Pub. Util. Comm.* (2004), 104 Ohio St.3d 530. In order to reverse or modify a Commission decision as to questions of fact, the Court must find that the record does not contain sufficient probative evidence or find that the Commission's decision was manifestly against the weight of the evidence or so clearly unsupported by the record as to show misapprehension, mistake, or willful disregard of duty. *Monongahela Power Co. v. Pub. Util. Comm.* (2004), 104 Ohio St.3d 571 *quoting AT&T Communications of Ohio, Inc. v. Pub. Util. Comm.* (2000), 88 Ohio St. 3d 549, 555. The appellant bears the burden of demonstrating that the Commission's decision is against the manifest weight of the evidence or is clearly unsupported by the record. *Id.* Furthermore, the Court will not reverse a Commission order absent a showing by the appellant that it has been or will be harmed or prejudiced by the order. *Myers v. Pub. Util. Comm.,* (1992), 64 Ohio St.3d 299, 302.

ARGUMENT

<u>PROPOSITION OF LAW NO. I:</u>

The Commission erred as a matter of law in concluding that "the recovery of delta revenues is a matter for the Commission's discretion" under R.C. 4905.31.

The Commission made its position on recovery of delta revenues perfectly clear on rehearing by stating as follows:

> Contrary to AEP Ohio's analysis, the plain language of Section 4905.31, Revised Code, does not require the Commission to approve the full recovery of all delta revenue resulting from the unique arrangement. Section 4905.31, Revised Code, states that a unique arrangement "*may include* a device to recover *costs incurred* in conjunction with any economic development and job retention program . . . including recovery of revenue foregone." The Commission finds that the use by the General Assembly of "may" in this context authorizes, but does not require, the recovery of delta revenues. If the General Assembly had intended to require the recovery of delta revenues, the General Assembly would have used "shall" or "must" rather than "may." * * * Thus, the Commission finds that, according to the plain language of the statute, the recovery of delta revenues is a matter for the Commission's discretion.

(*Ormet Case*, Entry on Rehearing at 10-11 (emphasis original), Ap. at 86-87.) While the Commission's position is clear, it is unreasonable and unlawful.

The Commission's interpretation employs a strained interpretation that reads the phrase "may include" out of context and conflicts with the plain meaning of the complete sentence when read as a whole. Though the Commission has authority to approve or disapprove proposals under R.C. 4905.31, the statute does not permit the Commission to approve a proposed arrangement and simultaneously disallow a portion of the resulting foregone revenue (also known as "delta revenues," referring to the difference between the discounted rate and the otherwise applicable tariff rate). The Commission below did, in fact, approve an arrangement and proceeded to offset AEP Ohio's recovery of delta revenues associated with the compulsory arrangement relative to the otherwise applicable POLR charge that would be paid by Ormet. Not only is the Commission's interpretation flawed based on the plain language of R.C. 4905.31, it also conflicts with the Commission's own rules, AEP Ohio's ESP recently adopted by the Commission and SB 221's new regimen for establishing electricity rates. Having "complete and independent power of review as to all questions of law" in appeals from the commission, the Court should reverse the Commission's flawed interpretation of the controlling statute. *Ohio Edison Co. v. Pub. Util. Comm.* (1997), 78 Ohio St. 3d 466, 469.

A. R.C. 4905.31 does not authorize the Commission to impose an involuntary contract on a utility and then deny full recovery of the resulting revenue foregone under the compulsory arrangement.

R.C. 4905.31 provides, in pertinent part, for Commission approval of financial devices as follows:

> (E) Any other financial device that may be practical or advantageous to the parties interested. In the case of a schedule or arrangement concerning a public utility electric light company, such other financial device may include [1] *a device to recover costs incurred in conjunction with any economic development and job retention program of the utility within its certified territory, including recovery of revenue foregone as a result of any such program*; [2] any development and implementation of peak demand reduction and energy efficiency programs under section 4928.66 of the Revised Code; [3] any acquisition and deployment of advanced metering, including the costs of any meters prematurely retired as a result of the advanced metering implementation; and [4] compliance with any government mandate.

Ohio Rev. Code Ann. 4905.31 (2010), Ap. at 4 (emphasis and bracketed numbering supplied). While the bracketed numbering above was added for convenience in discussing the four listed items, it is evident from the precise language and punctuation used by the General Assembly in this new sentence that it intended to create four new permissible categories of special arrangements involving electric utilities. It is also evident that the General Assembly wanted to specify these categories simultaneously with its creation of the novel opportunity for mercantile customers to petition the Commission.

Understanding that the new sentence creates four categories is necessary to properly interpret the sentence. The Commission's erroneous interpretation glosses over the fact that the new sentence creates four items and interprets the phrase "may include" out of context as if the entire first part of the sentence only applied to the first category. Upon cursory examination, it is evident that the introductory language in the sentence preceding the list applies to all of the four items and the entire sentence must be examined and understood before reaching any conclusions about the General Assembly's use of the phrase "may include" in the introductory part of the sentence.

Under R.C. 1.42, the General Assembly has expressed that, when interpreting any provision in the Revised Code, words and phrases shall be read in context and construed according to the rules of grammar and common usage. Ohio Rev. Code Ann. 1.42 (2010), Ap. at 1. The context and grammatical structure of the sentence used by the General Assembly in R.C. 4905.31(E), including the use of semicolons to separately list the four items, is that a financial device "may include" 1; 2; 3 and 4. Contrary to the Commission's interpretation, the phrase "may include" in the first part of the sentence is in prelude to listing the four permitted items and the phrase does not modify the language internally used to describe any of the individual items 1; 2; 3; and 4.

As a practical matter, any given financial device that is proposed will likely include only one of the four items listed as being permissible (though it could include multiple items and would rarely, if ever, include all four categories of items). The applicant – whether it is a utility or a mercantile customer – gets to choose which type of item(s) to include in its proposal. Hence, the phrase "may include" is plainly designed to permit (but not require) the applicant to include any one or more of the permissible items in its proposal. This case involves the Commission approving a contract under the first option and, as such, it must apply to entirety of the provision.[8]

By contrast to this obvious grammatical structure and context, the Commission's decision misapprehends the phrase "may include" as modifying the far-removed phrase "including recovery of revenue foregone." Thus, the Commission's interpretation improperly joins the distant phrases together to awkwardly interpret that language as saying that a financial device "may include … including recovery of revenue foregone." In addition to the fact that this strained reading makes no grammatical sense, it inappropriately grafts the introductory phrase "may include" onto the internal language describing item one in the list of four items.

The language describing the first item in the list describes "a device to recover costs incurred in conjunction with any economic development and job retention program of the utility within its certified territory, including recovery of revenue foregone as a result of any such program." This description produces a complete thought and needs no further interpretation in order to be clear. The General Assembly provided that a

[8] As referenced above, the applicant in the case below (Ormet) included recovery of revenues foregone as part of its proposal. (*Ormet Case*, Application at 7-8, Supp. at 40-41.)

permissible item to be included in a financial device under R.C. 4905.31 is a device to recover costs of an economic development program, including foregone revenue (delta revenue). There is no "may" in the phrase "including revenue foregone" within the first option in the list of four. The Commission's flawed interpretation emasculates the General Assembly's manifest intention to permit recovery of economic development costs "including revenue foregone."

Not only does the Commission's primary interpretation effectively rewrite the statute, the Commission's secondary argument is equally flawed in stating that the General Assembly would have used "shall" or "must" rather than "may" if it had intended to require recovery of delta revenues. (*Ormet Case*, Entry on Rehearing at 10, Ap. at 86.) If the General Assembly had used the phrase "shall include" instead of "may include" in this instance, then the sentence would have been rendered useless as a list of permissible alternatives. Under the secondary argument used in the Commission's entry on rehearing, the sentence structure would be that a financial device "shall include" 1; 2; 3 and 4. In other words, all of the four categories would have to be included in a financial device in order to be permissible under R.C. 4905.31. That approach makes no sense and further exposes the fallacy of the Commission's interpretation. Thus, the phrase "may include" cannot reasonably be interpreted to limit the recovery of revenue foregone. Accordingly, AEP Ohio submits that, because the General Assembly provided that recovery of economic development costs, including revenue foregone, is permissible without attaching any qualifying or modifying language within that listed item, the Commission's conclusion that is has full discretion to grant or deny recovery of revenue foregone is unlawful and must be reversed.

Further, application of the legislative cannon *expressio unius est exclusio alterius* confirms that the Commission cannot reasonably read this statutory language as creating the authority to offset the recovery of revenues foregone by an actual or perceived avoidance of an expense by the electric utility. AEP Ohio's position that the Commission cannot require a utility to enter into an agreement and then refuse to allow recovery of the resulting foregone revenue is further bolstered by the fact that the General Assembly has expressly provided for comparable offsets elsewhere within SB 221 – when it actually intended to do so. For instance, the General Assembly provided in R.C. 4928.143 (B) (2) (c) that:

> Before the commission authorizes any surcharge pursuant to this division, it may consider, as applicable, the effects of any decommissioning, deratings, and retirements.

Ohio Rev. Code Ann. 4928.143(B)(2)(c) (2010), Ap. at 21.

Another example of an explicit offset provision is found in R.C. 4928.142 (D), also enacted as part of SB 221, where the General Assembly provided that:

> In making any adjustment to the most recent standard service offer price on the basis of costs described in division (D) of this section, the commission *shall include the benefits that may become available to the electric distribution utility* as a result of or in connection with the costs included in the adjustment... The *commission shall not apply its consideration of the return on common equity to reduce any adjustments authorized under this division unless the adjustments will cause the electric distribution utility to earn a return on common equity that is significantly in excess* of the return on common equity that is earned by publicly traded companies, including utilities, that face comparable business and financial risk, with such adjustments for capital structure as may be appropriate.

Ohio Rev. Code Ann. 4928.142(D) (2010), Ap. at 18 (emphasis added).

These provisions demonstrate that in some instances the General Assembly chose to have the Commission offset revenue recovery by cost savings or other considerations such as impact on return on equity. In those instances, the Commission was given explicit authority to make such an offset. The absence of such authorization in R.C. 4905.31(E) is particularly telling in light of the presence of such authorization in other provisions in the same piece of legislation. The legislative canon *expressio unius est exclusio alterius* applies, meaning the inclusion of one thing implies exclusion of the other. *See Crawford-Cole v. Lucas Co. Dept. of Jobs & Family Services,* (2009), 121 Ohio St.3d 560, 566. The inclusion of authority to make a rate offset in certain statutes, but not in the amendment to R.C. 4905.31 – enacted as part of the same legislation – compels a finding that R.C. 4905.31 does not provide the Commission with inherent authority to make a rate offset to the statutorily permitted recovery of revenues foregone.

Finally as to whether the second sentence in R.C. 4905.31(E) should be interpreted to grant the Commission unlimited discretion to disallow recovery of foregone revenues when imposing a compulsory economic development agreement, AEP Ohio submits that such an interpretation would also violate the first sentence in R.C. 4905.31(E). This is true because a reduction in recovery of revenue foregone would necessarily be harmful to the utility's interests, and such an arrangement would not be "advantageous" to both parties to the contract as is required by the first sentence in R.C. 4905.31(E). This deliberate language also confirms AEP Ohio's reading of R.C. 4905.31(E) and undermines the Commission's strained interpretation.

The ultimate problem with the Commission's interpretation is that it leads to the conclusion that the Commission could disallow recovery of all revenues foregone under a contract filed unilaterally by a mercantile customer and imposed on the utility by the Commission. While AEP Ohio realizes that the Commission is permitting recovery of the majority of the revenues foregone relating to the compulsory contract adopted in the case below, the true test of the merits of the Commission's interpretation is whether it stands the test of reasonableness in the context of other possible outcomes. Moreover, the Commission's interpretation could be broadly applied to any customer who agrees not to shop and, case by case, erode AEP Ohio's authorized POLR revenue without offsetting compensation. In any case, requiring a utility to enter into a contract, and then denying recovery of the revenues foregone under that contract cannot be permitted under R.C. 4905.31. While the Commission has substantial discretion under R.C. 4905.31 to adopt or reject a proposal for a reasonable arrangement, it cannot adopt a compulsory agreement and simultaneously deny recovery of revenues foregone. For all of these reasons, the Commission's interpretation of R.C. 4905.31 should be reversed and remanded.

B. The decision below, which denies AEP Ohio recovery of POLR charges that Ormet would pay but for the compulsory agreement, conflicts with the Commission's contemporaneously-adopted Electric Security Plan for AEP Ohio and undermines SB 221's new regimen for establishing electricity rates.

In addition to lacking a basis in R.C. 4905.31, affirming the Commission's interpretation of R.C. 4905.31(E) would also conflict with the ESP rates recently adopted by the Commission for AEP Ohio and undermine other provisions within R.C. Chapter 4928. The Commission in the *ESP Cases* specifically rejected arguments that AEP Ohio's non-bypassable POLR charges can be avoided if a customer agrees not to shop. Moreover, the interpretation adopted by the Commission below also conflicts with SB 221's new pricing regimen for electric service. The Commission's decision forces AEP

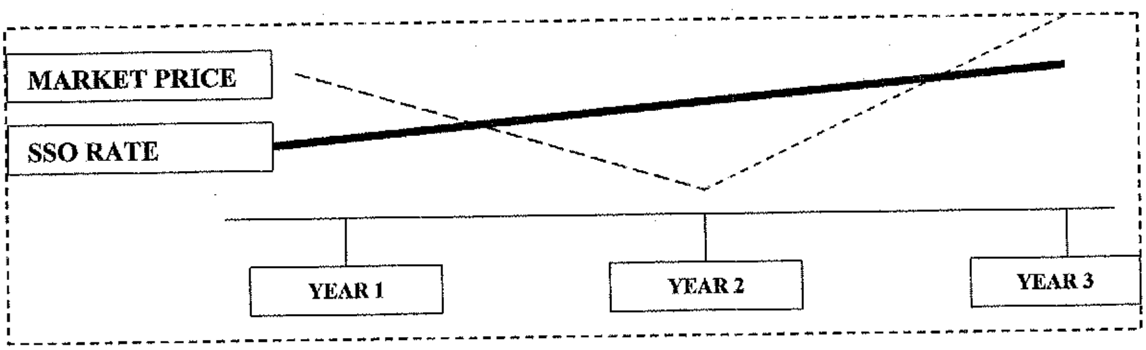
Ohio to forego the approved POLR charge for Ormet even though AEP Ohio's statutory POLR obligations continue.

1. Background regarding AEP Ohio's approved POLR charge

As discussed above, regarding the migration risk (that customers could leave, *i.e.*, migrate, when market prices drop below the SSO rate during the period of the ESP) the Commission acknowledged that risk and agreed that 90% of the requested POLR revenue requirement should be allowed to compensate AEP Ohio for that risk. (*ESP Cases*, Opinion and Order at 39, 40 (internal citations omitted), Ap. at 152-153.) Regarding the second risk (a shopping customer subsequently returning to the SSO rate when the market price goes back up), the Commission separately acknowledged that risk and permitted shopping customers to only bypass the POLR charge if they agree to pay a market price when/if they subsequently return to SSO service; otherwise, shopping customers would continue to pay the POLR charge during the time they received service by a competitive service provider. (*Id.* at 40, Ap. at 153.)

AEP Ohio's approved POLR charge is based on the interrelationship between the cost to the Companies of providing this service and the value to the customers of having the "optionality" provided by SB 221. In financial terms the customers' rights are equivalent to a series of financial options on power. Economically rational customers will exercise their rights to change providers when the economic benefits are apparent. On the other side of the transaction, however, the Companies bear the difference between market and ESP prices as a loss and collecting the approved POLR charge enables AEP Ohio to stand ready to discharge its POLR obligations.

The value of the customers' right to switch under S.B. 221 comes from the *option* customers are given to switch suppliers, while still having the safety net of the ESP rate to come back to, *if* electricity prices move in a way that makes switching back to the Companies an economically attractive choice or if their supplier defaults. The value of that option exists at the beginning of the ESP term, independent of the actual outcomes that eventually materialize in the future. The Companies committed at the outset of the term of their ESP, based on current circumstances and uncertainties, to provide an SSO price for the full three-year term and undertake the attendant POLR risk. The diagram below illustrates this relationship through a hypothetical example:



Under this hypothetical, customers may stay on (or return to) the SSO rate in years 1 and 3, while they would likely shop in the market during year 2. At the outset of AEP Ohio's three-year ESP, nobody (including AEP Ohio) could predict with certainty where the free market price (dotted line) would go during the subsequent three years. There are a myriad of factors that affect the market price of electricity, causing it to be volatile over any given period of time. Yet, AEP Ohio's obligation to support the SSO price during the entire ESP term was firmly established on the first day of the ESP. The migration risk, for which the Commission authorized AEP Ohio's POLR charge, is illustrated in year 2 when customers could leave the SSO to pursue more favorable market prices. The amount collected through the POLR charge allows AEP Ohio to "hedge" against such market changes and ride out those fluctuations.

The POLR risk exists because customers can switch, not based on whether they exercise their right to switch. An option gives one a right to do something, and one pays for the right to do it. The value and legitimacy of the option is not dependent upon whether it is exercised. Like purchasing casualty or fire insurance covering one's home, it is common to pay for insurance coverage and the event being insured against never occurs. Nonetheless, the insurance company stands ready to cover damages arising from a fire or casualty and is obligated to do so. Similarly, because AEP Ohio's POLR obligation is statutory and will not be eliminated during the term of the contract, the approved POLR charge should be collected.

2. **The Commission's decision below conflicts with its contemporaneous decision in the *ESP Cases*, the SSO pricing regimen under SB 221 and the language of the contract approved below.**

By allowing Ormet to effectively bypass AEP Ohio's otherwise applicable non-bypassable POLR charge, the decision below conflicts with the Commission's decision in the *ESP Cases*. On rehearing in the *ESP Cases*, the Commission considered and rejected the following argument made by the Ohio Energy Group (OEG):

> OEG states that the Commission properly found that the POLR rider should be avoidable for those customers who shop and agree to return at a market price; however, OEG believes that the Commission did not go far enough. *OEG requests that the Commission grant rehearing to allow the POLR rider to be avoidable by those customers who agree not to shop during the ESP through a legally binding commitment.*

(*ESP Cases*, July 23, 2009 Entry on Rehearing, at 25, Ap. at 127) (emphasis added). The Commission denied OEG's rehearing and reaffirmed its decision without modification, finding that the parties had not raised any new issues for consideration. (*Id.*, at 26.) More directly stated, the decision below was based on the very same theory the Commission explicitly rejected in the proceeding that approved the POLR charge.

Based on the extensive development of OEG's proposals in the record and the Commission's explicit consideration of those proposals in its orders in the *ESP Cases*, the Commission declined to allow customers to avoid the POLR charge by agreeing that AEP Ohio would be the customer's exclusive provider. On the contrary, after considering these arguments in the *ESP Cases*, the Commission adopted a *non-bypassable* POLR charge reflecting 90 percent of the estimated POLR costs presented by the Companies and found that only customers who actually switch to a competitive supplier – and agreed at the time they decided to shop that, if they returned it would be at a market price – would avoid the POLR charge during the time they are served by a competitive provider. (*ESP Cases*, Opinion and Order at 40, Ap. at 153.) The narrow exception for customers who promise to return at market has no application to this case. In other words, regardless of whether a customer promised not to shop during the ESP term, all customers would pay the POLR charge for the entire time they are served under AEP Ohio's SSO and would avoid POLR charges only during the period served by a competitive provider only if they agreed at the time they decided to shop that they would pay a market price if they return to generation service from AEP Ohio. That basic shopping rule was established as an integral part of AEP Ohio's approved ESP and it was supposed to control such matters during the three-year ESP term. The Commission explicitly wrestled this same issue to the ground in the *ESP Cases* and only allowed the

POLR charge to be bypassed under narrow circumstances – rejecting OEG's broader proposal to avoid POLR charges any time a customer promised not to shop.

The Commission's Entry on Rehearing in the *ESP Cases* stated that "the Commission carefully considered all of the arguments, testimony, and evidence in the proceeding and determined that the Companies should be compensated for the cost of carrying the risk associated with being the POLR provider, including the migration risk." (*ESP Cases*, Entry on Rehearing at 26, Ap. at 218.) The *ESP Cases* rehearing decision was issued on July 23, 2009 – *eight days after* the Commission issued its initial decision in the case below on July 15, 2009. Though the two decisions were issued contemporaneously, the result reached in the decision below squarely conflicts with the Commission's own decision in the *ESP Cases* to reject OEG's proposal to avoid the POLR charge by promising not to shop. The OEG's proposal rejected by the Commission in the *ESP Cases* is not substantively different than the "exclusive supplier" provision adopted by the Commission below.

In the *ESP Cases*, the Commission plainly stated that "[t]he POLR charge was proposed to collect a POLR *revenue requirement* of $108.2 million for CSP and $60.9 million for OP." (*ESP Cases*, Opinion and Order at 38, Ap. at 151) (emphasis added). Similarly, when deciding to grant 90% of the POLR proposed rate, the Commission ordered that "the POLR rider shall be established to collect a POLR *revenue requirement* of $97.4 million for CSP and $54.8 million for OP." (*Id.* at 40, Ap. at 153) (emphasis added). This demonstrates that the Commission's intention in the *ESP Cases* was to increase AEP Ohio's revenue requirements and create firm revenues to support the POLR duty a non-bypassable revenue stream as part of the overall ESP decision – not just create a charge that can simply be avoided by a promise not to shop. It is unreasonable and unlawful for the Commission to contemporaneously issue an order in another case that directly undermines that result.

Under the controlling statute, AEP Ohio's ESP, approved by the Commission, necessarily reflects a *total package* that the Commission held to be more favorable, in the aggregate, than the expected results under an MRO. The orders in the *ESP Cases* were issued pursuant to R.C. 4928.143. As referenced above, an electric utility can establish its SSO rates either by establishing a Market Rate Offer under R.C. 4928.142 or an Electric Security Plan under R.C. 4928.143. Regarding approval of an ESP, the General Assembly provided that the Commission shall approve an ESP if it is more favorable, *in the aggregate*, than the expected results of an MRO for that utility. Ohio Rev. Code Ann. 4928.143(C)(1) (2010), Ap. at 21. In deciding AEP Ohio's *ESP Cases*, the Commission repeatedly found that the ESP (including the non-bypassable POLR charge) met this standard. (*ESP Cases*, Opinion and Order at 72, Ap. at 185; Entry on Rehearing at 51, Ap. at 243.) Contemporaneously modifying that carefully-balanced package of terms and conditions in the case below violates that controlling statutory standard and process for establishing an ESP, especially where the Commission does so in a manner that precludes full recovery of the ESP rates.

The overall package and balancing of interests reached in the *ESP Cases* is undermined by the decision below and, as the Commission extends its precedent to other customers, a much larger group of customers (possibly all mercantile customers) could eventually avoid paying the POLR charge simply by agreeing to make their electric utility their exclusive supplier. Not only would the potential for competition in Ohio become more and more significantly impaired, but such a result would also exponentially undermine the Commission's orders in the *ESP Cases*.

When examined in the larger context of the SSO pricing provisions of SB 221, it becomes even more evident that the decision below to disallow full recovery of revenues foregone as a result of a compulsory economic development contract is unlawful. As discussed above, an electric utility can establish its SSO pricing either through an MRO adopted under R.C. 4928.142 or an ESP adopted under R.C. 4928.143. When the Commission imposes an involuntary economic development contract on a utility without making the utility whole for revenue foregone *vis-à-vis* its approved SSO rates (*i.e.*, full delta revenue recovery), it undermines the approved SSO pricing established under SB 221 – whether that rate plan is an ESP or an MRO.

Consider an example where the MRO utility has achieved fully market-based SSO rates under R.C. 4928.142 and is entitled to collect market rates for electricity from all of its SSO customers. If the customer leaves the SSO, the utility would sell the power in the wholesale market or to another retail customer outside its service territory, collecting a market price for doing so. It would undermine such a market-based pricing regimen for the Commission to force the utility to serve a mercantile customer at a lower price in order to promote the State of Ohio's economic development goals – without making the utility whole by allowing recovery of revenues foregone. By requiring the utility to serve the customer at a price below market, the Commission would directly undermine the statutory pricing scheme. In addition to harming the utility, the Commission would also undermine competition by subsidizing electric service to the customer and distorting the market's price for serving the customer. Though it may be more obvious when considering a similar example involving an MRO utility, the same problem is present for an ESP. Just as the market prices determine an MRO utility's SSO rates, the approved ESP determines AEP Ohio's SSO rates during the term of the rate plan. The Commission's decision to require AEP Ohio to enter into a contract with Ormet without permitting recovery of revenues foregone violates both the statutory SSO scheme generally and AEP Ohio's approved ESP specifically.

Finally in this regard, the decision below even conflicts with the language of the contract ordered to be adopted below. Consistent with R.C. 4905.31(E), Article 1.07 of the involuntary contract filed with, and approved by, the Commission defines "delta revenue" to mean "all revenue which would be recoverable from Ormet under the AEP Ohio Tariff Rate, but for this Power Agreement, foregone by AEP Ohio as a result of the provisions of the Power Agreement, including as a result of an Event of Default by Ormet of this Power Agreement." (*Ormet Case*, Power Agreement at Article 1.07, Supp. at 8.) There is no dispute that AEP Ohio's POLR charge is an otherwise applicable rate for Ormet but for the compulsory contract. Consequently, this crucial fact provides an additional and independent basis for the Court to reverse the Commission's conclusion that AEP Ohio is not entitled to full recovery of delta revenues.

In sum, the applicable law supports recovery of all revenues foregone under the Ormet contract. There is no statutory authority for the Commission to offset these revenues foregone by an amount of expense reductions, whether actual or not. The revenues foregone equal the difference between what Ormet would pay under the Companies' applicable rate schedules and what it would pay under the unique arrangement rate – no more and no less. If the Commission wanted to approve the full discount requested by Ormet based on perceived benefits to the State of Ohio, it simply needed to permit full recovery of revenues foregone to AEP Ohio. Whereas, if the Commission wanted to reduce the impact of the unique arrangement on other ratepayers' bills, the proper course of action would have been to reduce further the amount of the maximum discount to which Ormet would be entitled. Since it approved the discount as being beneficial and ordered AEP Ohio to enter into an arrangement with Ormet, the Commission was required to permit full recovery of revenues foregone.

PROPOSITION OF LAW NO. II:

> **The Commission unlawfully adopted a provision within the involuntary contract requiring that AEP Ohio's largest customer forego its statutory right to shop for competitive generation service for an entire decade, in violation of the well-established policy of the State of Ohio and the fundamental retail shopping provisions of SB 3 and SB 221.**

The Commission below ordered AEP Ohio to be the exclusive supplier to Ormet's enormous electric load for an entire decade. (*Ormet Case*, Opinion and Order at 13, Ap. at 46.) The Commission's approval of an "exclusive supplier" provision is contrary to the most basic and central premise of SB 3 and SB 221: development of competitive electric generation markets for retail customers in Ohio. As discussed below, the effect of the Commission's decision is to pull from the competitive market for a full decade an electric load equivalent to more than 400,000 households. The entire dispute in this case stems from the Commission's adoption of this exclusive supplier provision and the Court should resolve this case by reversing or vacating the unlawful ruling.

SB 3 provided for restructuring Ohio's electric utility industry in order to achieve retail competition with respect to the generation component of electric service. *Indus.*

Energy Users-Ohio v. Pub. Util. Comm. (2008), 117 Ohio St. 3d 486, 487. *See also Ohio Consumers' Counsel v. Pub. Util. Comm.* (2007), 114 Ohio St. 3d 340; *Elyria Foundry Co. v. Pub. Util. Comm.* (2007), 114 Ohio St. 3d 305; *Ohio Consumers' Counsel v. Pub. Util. Comm.* (2006), 111 Ohio St. 3d 300, 301; *Constellation NewEnergy, Inc. v. Pub. Util. Comm.* (2004), 104 Ohio St. 3d 530. This Court has repeatedly recognized that the enactment of SB 3 by the General Assembly signaled customer choice for the State of Ohio and adopted "a comprehensive statutory scheme to facilitate and encourage competition in Ohio's retail electric market." *FirstEnergy Corp. v. Pub. Util. Comm.* (2002), 96 Ohio St.3d 371.

SB 3, together with amendments made in SB 221, set forth the State's continuing policy to ensure diversity of electricity supplies and suppliers,[9] to recognize the continuing emergence of competitive electricity markets through the development and implementation of flexible regulatory treatment,[10] and to ensure effective competition in the provision of retail electric service.[11] Even more explicit than the policy statements in R.C. 4928.02, SB 3 directly establishes a right to shop for generation and other competitive retail electric services:

> *Beginning on the starting date of competitive retail electric service, retail electric generation,* aggregation, power marketing, and power brokerage services supplied to consumers within the certified territory of an electric utility are *competitive retail electric services that the consumers may obtain subject to this chapter from any supplier or suppliers.*

Ohio Rev. Code Ann. 4928.03 (2010), Ap. at 12. This provision was retained through the enactment of SB 221 and, thus, has been in effect for a decade. Rather than defending

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[9] Ohio Rev. Code Ann. 4928.02 (C) (2010), Ap. at 10.
[10] Ohio Rev. Code Ann. 4928.02 (G) (2010), Ap. at 10.
[11] Ohio Rev. Code Ann. 4928.02 (H) (2010), Ap. at 10.

and upholding the right to shop, the Commission's decision below unduly restricts retail competition and locks Ormet's enormous electric load out of the competitive market for a decade.

In addition, the General Assembly enacted R.C. 4928.06 entitled "Commission to ensure competitive retail electric service" – originally as part of SB 3 and retained by SB 221. Ohio Rev. Code Ann. 4928.06 (2010), Ap. at 14. Through the enactment of this provision, the General Assembly directly provided multiple directives to the Commission concerning retail choice and empowered the Commission to address and resolve any decline or loss of effective competition. Among other things, the Commission is to consider specific factors in determining whether effective competition exists:

> (1) The number and size of alternative providers of that service;
>
> (2) The extent to which the service is available from alternative suppliers in the relevant market;
>
> (3) The ability of alternative suppliers to make functionally equivalent or substitute services readily available at competitive prices, terms, and conditions;
>
> (4) Other indicators of market power, which may include market share, growth in market share, ease of entry, and the affiliation of suppliers of services.

Ohio Rev. Code Ann. 4928.06(D) (2010), Ap. at 14. The exclusive supplier provision adopted below cannot survive scrutiny under any serious application of these factors. From the General Assembly's unequivocal policy pronouncements to the structure and fundamental purpose of R.C. Chapter 4928, it is clear that a contract by which AEP Ohio's largest customer pulls its power requirements from the market stifles the development of a competitive retail electric generation market.

Though Ormet is a single customer, the significance of the Commission's error becomes even more evident when one considers the sheer enormity of Ormet's electric load. The involuntary contract ordered by the Commission, through Article 4.01, requires AEP Ohio to supply Ormet with up to 540 megawatts (MWh) of electricity at any given hour or up to 401,760 megawatt hours (MWh) per month (540 MWh x 24 hours x 31 days). (*Ormet Case*, Power Agreement at Article 4.01, Supp. at 13.) According to the Commission's website, a typical Ohio household consumes, on average, approximately 800 kWh per month.[12] Thus, a conservative estimate for each household is to use 1,000 kWh (1 MWh) per month for comparison. This approach means that Ormet's load is roughly equivalent to the load of 401,760 residential homes. According to publicly available data from the U.S. government, this is more than the residential households in Hamilton County (373,000) and nearly the total of Franklin County (471,000) at the time of the 2000 Census.[13] Prohibiting shopping for such an enormous electric load is unquestionably a major constraint on the competitive generation market in Ohio for the next ten years.

After AEP Ohio objected to the exclusive supplier provision below on brief, the Commission simply found without further comment that "under the terms of the unique arrangement, AEP-Ohio will be the exclusive supplier to Ormet." (*Ormet Case*, Opinion and Order at 13 (citations omitted), Ap. at 46.) Even after AEP Ohio pressed the issue on rehearing, the Commission again summarily dismissed the significance of its competitive restriction, saying that "the exclusive supplier provision may, or may not, adversely

[12] http://www.puco.ohio.gov/PUCO/Consumer/Information.cfm?id=8076

[13] http://factfinder.census.gov/servlet/GCTTable?_bm=y&-geo_id=04000US39&-_box_head_nbr=GCT-PH1&-ds_name=DEC_2000_SF1_U&-format=ST-2

affect competition in this state, but there is no evidence in the record to support that *determination*." (*Ormet Case*, Entry on Rehearing at 13, Ap. at 89) (emphasis original). Thus, while the Commission plainly admits that the exclusive supplier provision may end up adversely affecting competition in Ohio (a revealing and significant admission), it simply declined to pursue the matter further simply because AEP Ohio did not hire an independent expert witness and present written testimony on this subject. This reluctant approach to guarding the centerpiece of Ohio electric restructuring laws should not be sanctioned by this Court. AEP Ohio submits that expert testimony is not needed for the Commission to enforce the clear policy articulated by the General Assembly and reflected throughout R.C. Chapter 4928 or for this Court to recognize the dangerous and unprecedented effects of the Commission's decision.

The enforceability of an exclusive supplier provision is also legally suspect, given that it contradicts the public interest, as expressed in Ohio's policy adopted in SB 3 and SB 221. The Commission's adoption of a contractual provision, which is contrary to public policy and casts uncertainty over the enforceability of the contract, surely must be declared unreasonable and unlawful. It is well-established that where there is a strong public policy against a particular practice, a contract or clause inimical to that policy will likely be declared unconscionable and unenforceable unless the policy is clearly outweighed by some legitimate interest in favor of the individual benefited by the contractual provision. 8 Williston on Contracts (4th Ed. 1998) 43, Section 18:7.

This Court has declared contracts unconscionable and void where the contract purports to violate important public policies, including policies articulated by the General Assembly in statutes. *See e.g. Taylor Building Corp. of America v. Benfield* (2008), 117

Ohio St.3d 352. An "exclusive supplier" provision that contradicts the public interest as expressed in Ohio's policy adopted in SB 3 and SB 221 should be considered void as against public policy and unenforceable. There can be no question that the Commission's adoption of this offensive provision has caused substantial harm to AEP Ohio, as required for this Court to reverse. *Cincinnati v. Pub. Util. Comm.* (1949), 151 Ohio St. 353.

Under Article 1.01 of the involuntary contract approved by the Commission, the AEP Ohio tariff rate that would otherwise apply is defined as the amount Ormet would pay if 50% of its load was billed under CSP tariff rates and 50% under OP tariff GS-4 rate schedules. (*Ormet Case*, Power Agreement at Article 1.01, Supp. at 6.) This equates to $0.0024290 per KWh.[14] (*Ormet Case*, Tr. Vol. I, at 51, 52, Supp. at 43-44.) Thus, if Ormet operated at full load in 2010, equal to approximately 400,000,000 KWh per month,[15] the monthly POLR charge paid by Ormet to AEP Ohio in 2010 would be $971,600 (400,000,000 * $0.0024290). Over a full year, the POLR revenues foregone by the involuntary contract would be up to approximately $11.7 million. (12 * $971,600). Even if Ormet consumed only half of its full load, the revenues foregone in 2010 and as ordered by the Commission are not being recovered, would be approximately $5.8 million. The same calculation would apply to 2011 during the ESP.

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[14] CSP's and OP's POLR rates for their respective GS-4 customers for 2010, as filed with the Commission, are 0.32753 cents per KWH and 0.15828 cents per KWh, respectively. (Columbus Southern Power Standard Service Tariff, Original Sheet No. 69-1, http://www.puco.ohio.gov/apps/directorylister/docketingfiles.cfm?path=Electric%5CColumbus%20Southern%20Power%20Company%20%28AEP%29%5C&filearea=2, Ap. at 246); Ohio Power Standard Service Tariff, Original Sheet No. 69-1, http://www.puco.ohio.gov/apps/directorylister/docketingfiles.cfm?path=Electric%5COhio%20Power%20Company%20%28AEP%29%5C&filearea=2, Ap. at 247).
Thus, Ormet would pay the average of CSP's and OP's POLR charge or 0.24290 cents per KWh (0.32753 + 0.15828 / 2) or $0.0024290 per KWh.

[15] See the calculation of Ormet's electric load under the approved contract, supra, at 31.

As demonstrated, the Commission's adoption of the exclusive supplier provision is contrary to the retail choice provisions in SB 3 and SB 221, conflicts with the public policy goals explicitly articulated by the General Assembly, and has significant potential to inhibit retail competition in Ohio. The harmful impact on AEP Ohio of this unlawful provision is presently substantial and potentially far reaching. Consequently, this Court should reverse or vacate the Commission's adoption of the exclusive supplier provision as being unreasonable and unlawful.

PROPOSITION OF LAW NO. III:

> **The Commission's conclusion that there is no risk of Ormet shopping for competitive generation service and subsequently return to SSO service conflicts with controlling statutes and is otherwise against the manifest weight of the record.**

Even if the Court does not determine as a matter of law that the "shopping elimination" provision of the compulsory contract ordered below by the Commission must be considered void and unenforceable as against public policy and violating the basic structure and provisions of SB 221, the Court should reverse the Commission's conclusion that there is no risk that Ormet will shop and subsequently return to SSO service from AEP Ohio. Based on its finding that Ormet's proposed contract would make AEP Ohio Ormet's exclusive supplier for the 10-year term of the contract, the Commission also concluded that "there is no risk Ormet will shop for competitive generation and then return to AEP-Ohio's POLR service." (*Ormet Case*, Opinion and Order at 13, Ap. at 46.) As a related matter, the Court should find to be unreasonable the Commission's revised approach on rehearing of considering only the first three years of the 10-year contract to determine if there is a shopping risk under the contract. The

Commission's conclusions in this regard should be reversed as they conflict with controlling law and are otherwise against the manifest weight of the record. *Monongahela Power Co. v. Pub. Util. Comm.* (2004), 104 Ohio St.3d 571.

As a matter of law, a schedule or reasonable arrangement approved by the Commission pursuant to R.C. 4905.31(E) "shall be under the supervision and regulation of the commission, and is subject to change, alteration or modification by the commission." Ohio Rev. Code Ann. 4905.31(E) (2010), Ap. at 4. This is explicitly provided for in Article 2.03 of the approved contract, which provides that "the Commission may, upon petition or *sua sponte*, require modification of this Power Agreement upon a finding that the rates produced under this Power Agreement are no longer just and reasonable." (*Ormet Case*, Power Agreement at Article 2.03, Supp. at 11.) The Commission's authority over these matters is continuous in nature. Therefore, as circumstances change, the Commission can order a modification of the Ormet contract. For example, less than two weeks after the Commission's Opinion and Order in this case was issued, the future operation of Ormet had been cast in uncertainty. (*Ormet Case*, Entry on Rehearing at 4-5, Ap. at 80-81.) While the Commission concluded that the unexpected development did not turn out to warrant a change or termination of the contract, some other unforeseen future development over the course of the next decade could well cause a modification or termination of the contract. As events continue to unfold it is natural that the Commission would preserve its options regarding the contract terms it previously approved. But the Commission's finding that there is "no risk" of contract termination should be reversed because it ignores the continuing jurisdiction conferred by the General Assembly through this statutory provision.

There are other provisions for early termination of the power agreement. Either party may terminate, with notice, if there is a default by the other party. (*Ormet Case*, Power Agreement at Article 3.01, Supp. at 11.) For example, Ormet could simply decide not to pay its bill and trigger a default. (*Id.* at Article 8.01, Supp. at 21.) Another provision indicates that Ormet may unilaterally simply decide to shut down its facilities and terminate the agreement early even where Ormet subsequently decides to ramp-up its operations again more than 24 months later. (*Id.* at Article 3.02, Supp. at 12.) All of these general provisions approved by the Commission undercut its conclusion that there is no risk that Ormet will shop and subsequently return to SSO service with AEP Ohio.

In addition, the specific modifications made by the Commission to Ormet's proposed contract, requiring employee levels and reductions in accumulated deferrals through payment of above-tariff rates by April 2012, also reflect the termination risk associated with this contract. (*Ormet Case*, Opinion and Order at 11, 15, Ap. at 44, 48.) Ormet could end up shopping for generation service if the contract were terminated on either of those bases. The Commission should have recognized that scenario as presenting POLR risk for AEP Ohio. Failing to do so and finding "no risk" conflicts with R.C. 4905.31(E) and is against the manifest weight of the record.

Moreover, as a matter of undisputed factual history, Ohio Power Company has experienced once before the situation of Ormet shopping for competitive generation service and then returning to AEP Ohio, even after Ormet had promised not to return. That situation was a real example of a customer's desire to switch back and forth as the relationship between market prices and regulated prices fluctuated – not just an example of any customer but one involving the very same customer involved in this case. The

Entry on Rehearing below acknowledged this history in referencing "the repeated transfer" of Ormet's facilities among certified service territories. (*Ormet Case*, Entry on Rehearing at 7, 9, Ap. at 83, 85.) It is undisputed that Ormet has previously obtained special permission to "permanently" leave AEP Ohio's service territory to take advantage of low market prices for electricity[16] only to subsequently seek and obtain permission to return to being served by AEP Ohio when market prices rose.[17] Suffice to say that what was initially thought to be a "no risk" situation of Ormet returning to the AEP Ohio system proved to be something quite different. Based on this experience with the same customer and the Commission's continuing jurisdiction over the compulsory arrangement adopted below, the Court should reverse the Commission's erroneous conclusion that there is "no risk" of Ormet shopping during the 10-year term of the arrangement.

On rehearing, the Commission attempted to circumvent this problem by transparently narrowing the scope of its review to only three years of the 10-year contract. The Commission's attempt to analyze the effects of a 10-year contract by

[16] In 1996, based on Ormet's desire to pursue low prices in the wholesale power market, Ohio Power agreed to allow Ormet to permanently leave Ohio Power's service territory and reallocate the service territory of South Central Power Company, such that Ohio Power no longer had any legal obligation to serve the retail load of Ormet. *In the Matter of the Joint Petition of Ohio Power Company and South Central Power Company for Reallocation of Territory*, Case No. 96-1000-EL-PEB ("*South Central*"), September 19, 1996 Joint Petition, Ap. at 248. The Commission approved this permanent service territory reallocation to be effective January 1, 2000. *South Central*, November 14, 1996 Finding and Order, Ap. at 278.

[17] In 2005, Ormet filed a complaint and motion asking the Commission to transfer Ormet back to Ohio Power's certified service territory – based on rising prices in the electricity market. *Ormet Primary Aluminum Company v. Ohio Power Company and South Central Power Company*, Case No. 05-1057-EL-CSS ("*Ormet CSS*"), November 29, 2005 Motion, Ap. at 286. The Commission ultimately adopted an agreement in 2006 between the parties to allow Ormet to be served by a new combined service territory of Columbus Southern Power and Ohio Power. *Ormet CSS*, November 8, 2006 Supplemental Opinion and Order, Ap. at 306.

looking at only the first three years is flawed. Whether Ormet might shop for generation service during the term of the contract requires an analysis of the full ten years. The Commission's truncated analysis permitted the Commission to disregard the potential of Ormet shopping for generation service during the full term of its contract.

The decision below did not approve a 3-year contract for Ormet; the agreement was approved with a 10-year term. Regardless of the term of AEP Ohio's ESP or whether its next SSO contains an identical POLR charge, the term of the compulsory contract with Ormet is ten years. That is the period of time that is relevant to the inquiry concerning POLR risk when approving a 10-year contract. AEP Ohio will continue to bear the statutory POLR obligation throughout the term of the contract and the potential of Ormet shopping anytime during the 10-year term imposes POLR risks on AEP Ohio – just as it does for all customers that are able to shop.

The Commission's approach of "assuming away" AEP Ohio's POLR charge after three years is purely speculative and without any basis in the record. The Commission apparently realized the weakness of its conclusion but its attempt to unduly narrow the scope of its review of this issue is unreasonable and against the manifest weight of the evidence. Regardless of the fact that it is not presently known whether AEP Ohio will have a similar POLR charge after 2011 (*i.e.*, as part of its next SSO rate plan), the Commission should have simply provided for full recovery of "revenues foregone" without tying its decision to a specific charge that may or may not be in effect for the entire 10-year term of the Ormet contract.

Under that more appropriate "delta revenue" approach, if there ends up being a POLR charge as part of the next SSO, there would be full recovery of delta revenues and, if the next rate does not include a POLR charge, there would still be full recovery of delta revenues – albeit at a lower level because the contract would not result in foregone POLR revenues. The Commission's approach of attempting to sidestep this key question does not change AEP Ohio's ever-present POLR obligation and does not change the legally-required outcome mandated by R.C. 4905.31(E) that AEP Ohio must be permitted to fully recover revenues foregone. AEP Ohio submits that it is patently unreasonable to adopt a ten-year contract and impose an offset to recovery of delta revenues based on a finding of "no risk" that is limited to three years in scope.

Under the Commission's approach of narrowing the inquiry to only the first three years of the 10-year contract, AEP Ohio would need to wait until its next SSO rate plan for 2012 and beyond is established or wait until the remainder of the 10-year contract term transpires to actually determine whether the contract was ever terminated or whether Ormet shopped for generation service. In the future after those contingencies unfold, however, it will be too late for AEP Ohio to legally go back and challenge the decision below. Such a "Catch -22" approach is unreasonable and unlawful.

On rehearing below, the Commission admitted that the contract could be amended or terminated:

> Moreover, the unique arrangement provides that the Commission may modify the unique arrangement only after January 1, 2016, *unless the cumulative net discount under the unique arrangement exceeds 50 percent of the amount that Ormet would have been required to pay under AEP-Ohio's applicable tariff rates*. Although the Commission modified the unique arrangement to provide an additional independent termination provision, this termination provision, by its terms, cannot be effective before April 1, 2012. However, AEP's electric security plan, and its authority to assess POLR charges to its standard service offer customers, expires on December 31, 2011. Therefore, under the terms of the unique arrangement as modified by the Commission, there is no risk that Ormet will shop and return to AEP-Ohio's standard service offer during its

current electric security plan.

(*Ormet Case*, Entry on Rehearing at 8-9, Ap. at 84-85) (internal citations omitted; emphasis added). The Commission's narrowed focus of inquiry appears to be an attempt to circumvent the obvious fact that there are several ways the Ormet contract may be terminated over the extended ten-year term.

As admitted by the Commission in its own description of the above-referenced re-opener clause, the amendments may not be made under that provision "unless the cumulative net discount under the unique arrangement exceeds 50 percent of the amount that Ormet would have been required to pay under AEP-Ohio's applicable tariff rates." Thus, if the cumulative discount does exceed 50 percent, the Commission is able to modify the agreement before 2016 and even before 2012. (*Ormet Case*, Power Agreement at Article 2.03, Supp. at 11.) This provides yet another example of how AEP Ohio faces POLR risk under the contract ordered by the Commission.

Ultimately, Ormet may again find – just like it did only ten years ago – that at some point during the contract term market prices for electricity become cheaper than the prices being paid under the involuntary contract imposed upon AEP Ohio. Consistent with the Commission's prior orders in providing assistance to Ormet under just such circumstances, AEP Ohio believes that the Commission would not hold Ormet to a higher price for electricity than would otherwise be available in the competitive market, especially since doing so would also reduce or eliminate the delta revenues that ultimately are collected from the other ratepayers. Alternatively, there are several plausible scenarios (as outlined above) where the Commission could either determine that Ormet has not fulfilled its obligations under the arrangement and terminate it for that reason or the Commission may exercise its continuing jurisdiction over the contract to amend or terminate it based on circumstances that develop during the long ten-year term of this contract. Whether considered for three years or more appropriately for the full ten-year term of the compulsory contract, the POLR risk to AEP Ohio is real and the Commission erred in concluding that there is "no risk" of Ormet shopping during the next decade.

PROPOSITION OF LAW NO. IV:

> **There can be no "reasonable arrangement" with AEP Ohio under R.C. 4905.31 where the Commission orders an involuntary contract that causes harm to AEP Ohio's financial interests.**

It is beyond dispute that the basic elements of a contract include, among other things, manifestation of mutual assent. *Kostelink v. Helper* (2002), 96 Ohio St. 3d 1, 3. The Commission's interpretation and application of R.C. 4928.31 (E) not only violates this principle, but is contrary to the terms of that statute as amended by SB 221.

Prior to the enactment of SB 221, R.C. 4905.31 allowed a "public utility" to file a schedule or enter into "any reasonable arrangement" with its customers, providing for certain enumerated outcomes, including variable rates and different classifications of service. The statute provided that no "such arrangement" is lawful until it was filed with and approved by the Commission. SB 221 amended R.C. 4905.31 in a number of ways. As relevant to this appeal, it now provides that a mercantile customer of an electric distribution utility is not prohibited "from establishing a reasonable arrangement with that utility..." Ohio Rev. Code Ann. 4905.31(E) (2000), Ap. at 4. Such a reasonable arrangement can be filed with the Commission by the mercantile customer. The

Commission understands this language to permit a mercantile customer, with the Commission's approval, to impose the arrangement *on* the utility, despite the words of the statute which contemplate an arrangement *established with* the utility.

A. The common usage interpretation of the statute, as amended, supports AEP Ohio

These statutory changes, however, do not allow mercantile customers to establish an arrangement without the agreement of the electric distribution utility by unilaterally submitting a proposed arrangement for approval by the Commission. An analysis of the statute as modified shows there can be no arrangement approved by the Commission if the public utility to be bound by the arrangement does not agree to its terms.

As a general rule the words in a statute must be read in accordance with the common usage of the terms.[18] Therefore, the terms "establish" and "arrangement" should be given their ordinary meaning. The term "establish" is not ambiguous; it is commonly used as a synonym for "create, originate or bring into existence."[19] AEP Ohio believes that the term "arrangement" refers to a contract. Understanding "arrangement" to refer to a "contract" is consistent with the common reference of "arrangements" under R.C. 4905.31 as "special contracts."[20]

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[18] R.C. 1.42 provides: "Words and phrases shall be read in context and construed according to the rules of grammar and common usage. Words and phrases that have acquired a technical or particular meaning, whether by legislative definition or otherwise, shall be construed accordingly." Ohio Rev. Code Ann. 1.42 (2010), Ap. at 18. *See also Weiss v. Pub. Util. Comm.*, (2000), 90 Ohio St.3d 15, 17.

[19] Webster's Third New International Dictionary at 778; Black's Law Dictionary (8th ed.) at 568.

[20] *Columbus S. Power Co. v. Pub. Util. Comm*. (1993), 67 Ohio St. 3d 535, 539; 620 N.E. 2d 835, 840; *Canton v. Pub. Util. Comm.* (1980), 63 Ohio St. 2d 76, 77.

To the extent "arrangement" is ambiguous, it may mean either a "*mutual* agreement or understanding" or "a preliminary step or measure."[21] To ascertain which meaning of "arrangement" is intended in this instance, it is necessary to look at the context in which the words appear. The statute states that a "mercantile customer of an electric distribution utility" is not prohibited "from establishing a reasonable arrangement with that utility or another public utility electric light company." Since "establishing" means "creating or bringing into existence," then any ambiguity of "arrangement" suggests that the statute means either that:

> a mercantile customer is not prohibited from creating or bringing into existence a reasonable [*mutual agreement or understanding i.e., a contract*] with its EDU or other public utility electric light company; or
>
> a mercantile customer is not prohibited from creating or bringing into existence a reasonable [*preliminary step or measure*] with its EDU or other public utility.

The former is a fair and reasonable interpretation of the statute; the latter is not.

In common usage one would not speak of creating a preliminary measure with another. "Creating" connotes that the object created has a sense of finality or permanence; it has come into existence. A preliminary step or measure lacks this quality of permanence and instead implies that something more needs to happen before the reasonable arrangement is brought before the Commission for its approval. On the other hand, one would speak of creating a mutual agreement or understanding with another, and in such instances permanence and finality are implied. Thus, a mercantile customer can work with a utility to mutually establish an arrangement but cannot independently do so.

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[21] Webster's, supra, at 120.

It also is significant that the statute provides that the mercantile customer may establish "a reasonable arrangement *with* [its EDU] or another public utility electric light company." The clear indication is that the customer is working cooperatively *with* the utility to jointly establish the arrangement.

B. The context of the statute supports AEP Ohio's position

The paragraph of the statute requiring Commission approval also confirms that the mutual agreement interpretation is the better reading of the statute. It states that "no such . . . arrangement is lawful unless it is filed with and approved by the commission." The statute goes on to provide that the public utility "is required to conform its schedules of rates, tolls, and charges to such arrangement." The statute thus envisions that the arrangement submitted to the Commission is an arrangement already in existence (*i.e.*, established) which becomes lawful and immediately enforceable upon approval. As a matter of common usage and basic contract law, a preliminary step or measure lacks the requisite finality to become a lawful and enforceable arrangement upon approval by the Commission. Indeed it is difficult to imagine how the Commission could "approve" a mere preliminary measure or how a public utility could be "required to conform its schedules of rates, tolls and charges to [a preliminary measure]" that had not evolved into an agreement or understanding.

C. The Commission did not give effect to the entire amendment

Another equally important rule of statutory interpretation applicable here is that all portions of the statute must be given effect.[22] In order to read the SB 221 amendment as authorizing only mutually agreeable arrangements between a utility and one or more customers, there also has to be a reason why the General Assembly would have authorized the mercantile customer, as well as the utility, to establish an arrangement and to submit it to the Commission for approval. Such reasons exist.

Prior to the amendment, the statute authorized a public utility to enter into a special contract only with its own customers. A utility could not enter into a special contract with a party not already a customer nor could a customer enter into a special contract with a different utility operating outside the certified territory. SB 221 fills in this gap for mercantile customers of EDUs, consistent with the overall goal of the act of fostering competition in the electric industry. The new language recognizes that a mercantile customer has the option of establishing a special contract not only with its EDU but also with some other public utility electric light company. This language also suggests mutual agreement – it would be strange for the Commission to force an EDU serving another its territory to enter into an arrangement with a customer in another EDU's service territory.

SB 221 also gives the mercantile customer and its EDU or another public utility electric light company the option of having the customer submit the application for approval of the mutual arrangement. There are obvious reasons for this change too. Two

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[22] R.C. 1.47(B) provides that in enacting statutes, it is presumed that the entire statute is intended to be effective. Ohio Rev. Code Ann. 1.47 (2010), Ap. at 2.

likely reasons for proposing a special contract are to have the arrangement support economic development or to further energy efficiency. In both of these situations, the customer has the key role to play in persuading the Commission that the arrangement furthers the intended purpose. For example, to justify an economic development arrangement, the customer has to provide the documentation to establish, among other things, the number of jobs that will be created, the customer's financial viability and the secondary and tertiary benefits of the project. Ohio Admin. Code 4901:1-38-03(A) (2) (2010), Ap. at 28. In the case of an energy efficiency arrangement, the customer must describe its status in the community and how the arrangement furthers state policy and must submit verifiable information to establish that it meets the criteria for an energy efficiency arrangement. Ohio Admin. Code 4901:1-38-04(A) (1) and (2) (2010), Ap. at 30. The fact that in some instances the customer logically bears the burden of establishing the reasonableness of the arrangement is a good reason for allowing the customer, instead of the public utility, to submit the application for approval.

Another good reason for allowing the customer, in lieu of the public utility, to submit the arrangement to the Commission is that the utility may not want to actively support or bear the burden of persuasion regarding the amount of discount being requested by the mercantile customer, leaving that determination to the Commission. Such was the case in the case below for AEP Ohio with a very aggressive pricing proposal being advanced by Ormet. This consideration is applicable not only in reasonable arrangements for economic development and energy efficiency, but also for unique arrangements under Ohio Admin. Code 4901:1-38-05.

Finally, as noted earlier, R.C. 4905.31 (E) refers to the recovery of costs associated with the "development and implementation of peak demand reduction and energy efficiency programs under section 4928.66 of the Revised Code." Ohio Rev. Code Ann. 4905.31(2010), Ap. at 4. R.C. 4928.66 (2)(d) specifically provides for facilitating efforts by mercantile customers to offer their customer-sited demand-response, energy efficiency, or peak demand reduction capabilities to their EDUs as part of a reasonable arrangement under R.C. 4905.31. Ohio Rev. Code Ann. 4928.66 (2010), Ap. at 26. The amendment to R.C. 4905.31 allowing mercantile customers to file related applications with the Commission is consistent with the General Assembly's apparent desire to "facilitate efforts" by mercantile customers to make such offers to their EDUs. Of course, just because mercantile customers can file such applications with the Commission does not mean that the affected EDU has to accept the offer or must accept the offer if ordered to do so by the Commission. Similarly, the right of mercantile customers to file applications for the other types of reasonable arrangements set out in R.C. 4905.31 does not negate the right of the EDU to refrain from accepting the offer made in the filing.

Thus, R.C. 4905.31, as amended, is properly read, according to common usage, as continuing to allow only arrangements agreed to by the public utility and its customer(s), as opposed to opening the door to unilateral arrangements proposed by the customer and imposed on the public utility. In fact, this is the reading given to the statute by the Commission itself. In its September 17, 2008, Finding and Order adopting Ohio Admin. Code Chapter 4901:1-38, the Commission "determined that it is necessary to approve all reasonable arrangements *entered into between the utility and one or more of its customers.*" (emphasis added).[23]

CONCLUSION

For the foregoing reasons, AEP Ohio respectfully requests that this Court reverse and remand the Commission's decision below.

Respectfully submitted,

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[23] *In the Matter of the Adoption of Rules for Standard Service Offer, Corporate Separation, Reasonable Arrangements, and Transmission Riders for Electric Utilities Pursuant to Sections 4928.14, 4928.17 and 4905.31, Revised Code, as amended by Amended Substitute Senate Bill No. 221*, Case No. 08-777-EL-ORD Finding and Order (Sept. 17, 2008) at 7, Ap. at 323.

PROOF OF SERVICE

I certify that Columbus Southern Power Company's and Ohio Power Company's Merit Brief was served by First-Class U.S. Mail upon counsel for all parties of record identified below this 22nd day of January, 2010.

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