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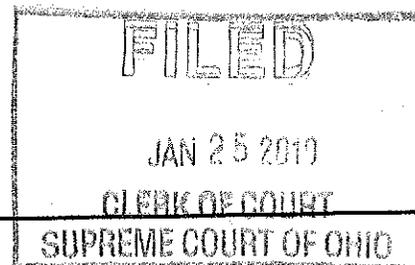
IN THE SUPREME COURT OF OHIO

In the Matter of the Application of)
Columbus Southern Power Company for)
Approval of its Electric Security Plan; an)
Amendment to its Corporate Separation)
Plan; and the Sale or Transfer of Certain)
Generation Assets, 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.)

Supreme Court Case No. 09-2022

Appeal from the Public Utilities)
Commission of Ohio)
Case Nos. 08-917-EL-SSO and)
08-918-EL-SSO)

(The Office of the Ohio Consumers')
Counsel v The Public Utilities Commission)
of Ohio))



**MERIT BRIEF OF
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I. INTRODUCTION

The Columbus Southern Power Company (“CSP”) and Ohio Power Company (“OP”) (collectively “the Companies” or “AEP Ohio”) on July 31, 2008, filed electric security plans (“ESPs”). In March of 2009, the Public Utilities Commission of Ohio (“Commission” or “PUCO”) modified and approved the Companies’ electric security plans. (Appx. 10-86). This appeal focuses on the PUCO’s decision to approve an ESP that charges residential customers for expenses that are unlawful and unreasonable under the provisions of newly enacted S.B. 221 (Appx. 242-301). The appeal also challenges the PUCO’s failure to fulfill its duties under R.C. 4903.09 (Appx. 685) to set forth findings of fact and the reasoning followed in reaching its decision—a decision which resulted in hundreds of millions of dollars in revenues being granted to the Companies.

II. STANDARD OF REVIEW

R.C. 4903.13 (Appx. 686) governs this Court’s review of PUCO Orders. It provides in pertinent part: “A final order made by the public utilities commission shall be reversed, vacated, or modified by the supreme court on appeal, if, upon consideration of the record, such court is of the opinion that such order was unlawful or unreasonable***.” The Court has interpreted this standard as one turning upon whether the issue presents a question of law or a question of fact.

As to questions of fact, the Court has held that it will not reverse the PUCO unless the PUCO’s findings are manifestly against the weight of the evidence or are so clearly unsupported by the record as to show misapprehension, mistake, or willful disregard of duty.¹ This standard should be applied to OCC’s Propositions of Law 4 and 5. Proposition of Law 4 contends that the

¹ *Cleveland Elec. Illuminating Co. v. Pub. Util. Comm.* (1975), 42 Ohio St.2d 403, 330 N.E.2d 1, ¶ 8 of the syllabus, writ of certiorari denied (1975), 423 U.S. 986, 96 S.Ct. 393, 46 L.Ed.302, appeal after remand (1976), 46 Ohio St.2d 105, 75 O.O.2d 172, 346 N.E.2d 778.

PUCO was unreasonable in failing to protect customers from paying unlawful rates during the appeal process. In Proposition of Law 5 OCC is challenging the sufficiency of the evidence the PUCO relied upon to exact \$456 million from customers for provider-of-last-resort (“POLR”) charges.

Questions of law, such as those raised by OCC’s Propositions of Law 1, 2, 3, and 6 are held to a different standard of review. This Court has complete, independent power of review on questions of law.² Accordingly legal issues are subject to a more intensive examination than are factual questions. OCC’s Propositions of Law 1 and 2 challenge the PUCO’s unlawful approval of retroactive rates under S.B. 221. In addressing these errors the Court will need to apply the respective provisions of newly enacted S.B. 221. Propositions of law 3 and 6 contend that the PUCO failed to meet the standards of R.C. 4903.09. These too are questions of law which will demand a de novo review.

With these rules in mind, the Court must consider and resolve the errors alleged by OCC.

III. STATEMENT OF FACTS

On July 31, 2008, CSP and OP filed their electric security plan applications with the PUCO. (R. 1). Under R.C. 4928.143(C)(1) (Appx. 708-709), the order should have been issued by the PUCO in 150 days. It was not.

Evidentiary hearings commenced after testimony was filed (R. 2-16, 100-117,120,122-123, 137-151). Hearings were concluded on December 10, 2008. When it became apparent that the 150-day deadline would not be met, the Companies filed an application to continue their existing rates. The PUCO approved the application. (Appx. 543-546). The Companies were

² *Office of Consumers’ Counsel v. Pub. Util. Comm.* (1979), 58 Ohio St.2d 108, 110, 12 O.O.3d 115, 388 N.E.2d 1370, 1373.

ordered to collect continued rates for January through March 2009, or until the Companies' ESP filing was adjudicated. (Appx. 543-549).

On March 18, 2009, the PUCO issued an Opinion and Order ("ESP Order") that approved but modified the Companies' ESP. (Appx. 10-86). The PUCO approved \$330 million³ in carrying charges for environmental investment made from 2001 through 2008. (Appx. 33-39). The ESP also included a \$456 million⁴ increase for POLR charges. (Appx. 47-49). Total increases, with some exceptions, were "capped" from 2009 through 2011.⁵ If the Companies incur generation fuel expenses above the caps they may defer such expenses and collect these from customers during 2012 through 2018. (Appx. 29-33). Additionally, the ESP Order approved the term of the ESP as beginning January 1, 2009. (Appx. 73). The PUCO ordered revenues collected from customers for the first three months of 2009 to be recognized and offset against revenues collected under the ESP rates. (Appx. 73).

Notwithstanding the significant increases to customers, the PUCO rejected arguments to offset the increases by the Companies' profits from off-system sales⁶—sales made possible from generating units built for and funded by the Companies' customers. (Appx. 25-26). The Companies filed tariffs to implement the Order on March 23, 2009. (R. 215-220). The tariffs were approved. (Appx. 90-94). Customers began to pay the increased ESP rates for electric service beginning with bills rendered under the April 2009 billing cycle.

³ This figure is the total AEP Ohio carrying charges on the environmental investment over the 3-year term of the ESP. On an annual basis \$26 million will be collected from CSP customers and \$84 million will be collected from OP customers. (Appx. 33).

⁴ This figure is the total AEP Ohio POLR charges to be collected over the 3 year term of the ESP. On an annual basis \$97.4 million will be collected from CSP customers and \$54.8 million collected from OP customers. (Appx. 47).

⁵ The Commission ordered a cap for CSP of 7% for 2009, 6% for 2010, and 6% for 2011. For OP, the Commission adopted a cap of 8% for 2009, 7% for 2010, and 8% for 2011. (Appx. 31).

⁶ During the term of the ESP the Companies estimated that the profits from off-system sales for both OP and CSP would be approximately \$791 million. (See Supp. 17).

OCC and others applied for rehearing on April 17, 2009. (Appx. 161-241). On July 23, 2009, OCC's application for rehearing was denied. (Appx. 95-149). On November 4, 2009, the PUCO issued a Second Entry on Rehearing, denying the remaining applications for rehearing. (Appx. 153-160). On November 5, 2009, OCC filed its notice of appeal. (Appx. 1-160). A second appeal was filed by Industrial Energy Users-Ohio on November 17, 2009. (R. 282). On November 30, 2009, OCC filed a motion to suspend and a motion to require past collections to be escrowed. The PUCO and the Companies opposed OCC's motions by filing memoranda contra. The Court has not ruled on OCC's motion. On December 22, 2009, CSP filed an appeal that was docketed as S.Ct. Case No. 09-2298.

IV. ARGUMENT

Proposition of Law 1: The Public Utilities Commission of Ohio is prohibited by R.C. 4928.141(A) from charging anything other than existing rates if no first-authorized standard service offer has been approved by January 1, 2009.

S.B. 221 (Appx. 242-301) established a framework to provide customers with electric generation services. The electric distribution utilities shall provide consumers a standard service offer ("SSO") for generation service beginning January 1, 2009.⁷ Accordingly, electric utilities shall apply to the PUCO to establish the standard service offer.⁸ The PUCO shall issue an order under R.C. 4928.143(C) (Appx. 708-709) not later than 150 days after the application is filed. The PUCO shall, in that order, approve, modify and approve, or disapprove the utility's application.⁹

Yet despite establishing these directives, the Legislature recognized a gap might be created if, on January 1, 2009, there was no first-authorized SSO. The Legislature filled

⁷ R.C. 4928.141(A). (Appx. 703).

⁸ Id.

⁹ R.C. 4928.143. (Appx. 707-710).

that gap by Section 4928.141(A) (Appx. 703): “Notwithstanding the foregoing provision [the provision of generation service to customers through a standard service offer beginning January 1, 2009], the rate plan of an electric distribution utility shall continue for the purpose of the utility’s compliance with this division *until a standard service offer is first authorized* under section 4928.142 or 4928.143 of the Revised Code***.”¹⁰ The “rate plan” that continues is the standard service offer in effect on July 31, 2008, the date the Revised Code was amended by S.B. 221.¹¹

R.C. 4928.141(A) is not ambiguous. It requires a utility’s rate plan to continue if there is no first-authorized SSO. This Court’s duty is to apply that statute when its meaning is unambiguous.¹² An unambiguous statute must be applied in a manner consistent with the plain meaning of the language. The Court (and the PUCO) cannot simply ignore or add words to the statute.¹³ Applying the statute as written leads to a lone inescapable conclusion—the statute requires the rate plan that existed on July 31, 2008 to continue if there is no first-authorized SSO.

A. No first-authorized standard service offer existed on January 1, 2009, and so the PUCO could only permit the Companies’ rate plan to continue.

The Companies filed their application (R. 1-2) on July 31, 2008. Under R.C. 4928.143(C)(1) (Appx. 708-709), the PUCO was to issue an order within 150 days (before January 1, 2009). The Companies anticipated that the PUCO would not meet the deadline, and

¹⁰ R.C. 4928.141(A) (emphasis added). (Appx. 703).

¹¹ R.C. 4928.01(33). (Appx. 693). S.B. 221 became effective on July 31, 2009, ninety days after the law was signed.

¹² *State ex rel. Savarese v. Buckeye Local School Dist. Bd. Of Edn.* (1996), 74 Ohio St.3d 543, 545, 660 N.E.2d 463, 465 (citation omitted).

¹³ *State ex rel. Burrows v. Indus. Comm.* (1997), 78 Ohio St.3d 78, 81, 676 N.E.2d 519, 521, reconsideration granted (1997), 78 Ohio St.3d 1505, 679 N.E.2d 7. See also *Morgan v. Ohio Adult Parole Auth.* (1994), 68 Ohio St.3d 344, 347, 626 N.E.2d 939.

filed a contingency plan to fill the gap. Under Section V.E of their applications the Companies presented a “short-term implementation plan.” (R. 1 at 17-18). In its short-term implementation plan, the Companies proposed that whatever Order the PUCO ultimately issued be made effective beginning with the January 2009 billing cycle.¹⁴ Since the Companies expected that the PUCO’s final Order would result in a rate increase, the Companies proposed a “reconciliation” or “true-up” of the PUCO's Order. (R. 1 at 17-18). The true-up was to be implemented through a rider that would charge customers for any under-collection occurring when the short-term implementation plan was in effect. The rider was to begin after the PUCO approved the ESP order. As the Companies conceived the law, it would not matter when the PUCO issued its ESP order - the Company would be able to recoup first-authorized ESP revenues beginning January 1, 2009.

The first stage of the hearings was devoted to this short-term implementation plan. The PUCO invited testimony from parties. The PUCO Staff’s Witness J. Edward Hess rejected the Companies’ proposal for reconciling short-term rates with the ultimate first-authorized rates. (Supp. 26-28). OCC’s Witness Beth Hixon testified that only the existing rates could be charged starting January 1, 2009, no more, no less. (Supp. 33-37). Ms. Hixon also testified that no reconciliation of rates should be permitted.¹⁵

Parties also tendered briefs on this issue on December 4, 2009. In its Brief, PUCO Staff, consistent with Witness Hess’ testimony, opposed the reconciling of short-term and first-authorized rates: “[T]here is no statutory basis for the Companies’ true-up proposal. The statute requires that the ‘rate plan***shall continue.’ There is no guarantee that the Companies collect as though the ESP had been in effect throughout the year.” (R. 161 at 2).

¹⁴ Id.

¹⁵ Tr. II at 218-219 (Nov. 18, 2008)(R. Dec. 4, 2008).

After briefs on the short-term plan were filed, but before December 31, 2009, the Companies filed yet another application. This time the Companies requested that the PUCO permit them to continue their existing rate plans.¹⁶ On December 19, 2008, the new application was approved.¹⁷ The PUCO concluded that the rates in effect on July 31, 2008 should continue.¹⁸ The PUCO ordered the Companies to continue existing rates until it ruled on the ESP plan or until the last billing cycle of February 2009, whichever occurred first.¹⁹ There was no indication that these authorized rates were to be adjusted or recalculated once an ESP plan was approved. On December 23, 2008, CSP and OP accepted the ruling and filed tariffs to comply.

On February 25, 2009, the PUCO issued, sua sponte, a second continuation order²⁰ that further extended the continued rates until the Companies' March billing cycle.²⁰ Yet again, no provision in this order sanctioned truing up or reconciling rates once an ESP plan was approved. On February 26, 2009, OP and CSP filed tariffs to comply. Accordingly, under these Continuation Orders, from January 1, 2009 through March 31, 2009, customers paid rates under the Companies' continued rate plan, not rates that were first-authorized SSO rates.

¹⁶ *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Authority to Modify the Expiration Dates on Certain Rate Schedules and Riders*, PUCO Case No. 08-1302-EL-ATA, Application (Dec.15, 2008) ("Continuation Application").

¹⁷ *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Authority to Modify the Expiration Dates on Certain Rate Schedules and Riders*, PUCO Case No. 08-1302-EL-ATA, Finding and Order (Dec. 19, 2008) ("Continuation Order I"). (Appx. 543-546).

¹⁸ *Id.* at 3.

¹⁹ *Id.*

²⁰ *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Authority to Modify the Expiration Dates on Certain Rate Schedules and Riders*, PUCO Case No. 08-1302-EL-ATA, Finding and Order (Feb. 25, 2009) ("Continuation Order II"). (Appx. 547-549).

B. The PUCO violated R.C. 4928.141(A) by extending the first-authorized rates back to the first three months of 2009, thus countermanding the continued rates in effect during that time.

In December of 2008, and in February 2009, the PUCO approved continued rates for the Companies. (Appx. 543-549). But the PUCO turned around in its March 18, 2009 ESP Order (Appx.1- 86) and countermanded those earlier approved rates.²¹ The PUCO allowed the first-authorized ESP rates to be applied to customers, effective January 2009, as if the Companies had a first-authorized SSO, and not continued rates.

This feat was accomplished not through obvious means such as rebilling, or back-billing customers, but through a less transparent device. The artifice employed was the term of the ESP—the PUCO decreed that the term should begin January 1, 2009 and continue through December 31, 2011. (Appx.73). The ESP term is the period over which rate increases are collected from customers. Hence with the ESP term set back to January 1, 2009, the PUCO enabled the Companies to collect first-authorized rates from customers for January through March 2009. This was allowed despite the fact that customers had already paid continued rates for that same time, consistent with R.C. 4928.141(A), and with the rulings of the PUCO in their Continuation Orders (Appx. 543-549).²²

In one fell swoop, the lower continued rates, lawfully established, implemented by the Companies, and paid by customers during January through March 2009, were annulled. Rather than charging customers double rates—continued rates and first-authorized rates—the

²¹ The PUCO ruled that the short term implementation plan presented under Section V.E of the Companies' applications was "moot" and thus declined to address any of the issues raised by Appellants. (Appx. 73). The ESP Order though virtually accepted carte blanche the Companies' short term implementation plan. It did so by making the ESP effective January 1, 2009, and collecting increased first-authorized rates for the first three months of 2009 beginning April, 2009.

²² The Companies admit that the impact of the Commission's decision "may effectively be the financial equivalent of having issued a decision before January 1, 2009." See (R. 223 at 4).

PUCO improvised around the law: it ordered the Companies to “offset” and recognize the revenues already collected from customers during the “interim period” (January through March 2009) against the first-authorized rates. (Appx. 73). Thus, the Companies would not need to rebill or backbill customers as the incremental increase could be lumped onto the already burgeoning increases that customers would begin to pay with the April 2009 billing cycle.

The incremental difference between the continued rates and the first-authorized rates, for a mere three-month period, is an astounding \$63 million.²³ The \$63 million represents the revenues that the Companies would have collected from customers had the PUCO first authorized the Companies’ ESP on January 1, 2009. Allowing the Companies to pocket these additional unlawful revenues is exactly what the PUCO Staff and OCC advocated against. But it is what the Companies were hunting for.

The PUCO violated R.C. 4928.141(A). It endorsed replacing continued rates with first-authorized rates, despite the contrary and specific language requiring continued rates when no first-authorized SSO rates existed. The PUCO reached back to those first three months and retracted the continued rates in effect. The Companies were authorized to collect additional revenues during April through December 2009, as if the first-authorized rates had been in effect January 1, 2009. The PUCO blatantly disregarded R.C. 4928.141(A), to the detriment of the Companies’ customers.

This Court has “reiterated, many times, the obvious truth that the commission [PUCO] is solely a creature of the General Assembly and may exercise no jurisdiction beyond that conferred

²³ See (Supp. 51-52), line labeled “Increase due to 12 months Increase in 9 months.” See also Motion to Supplement the Record on Appeal by the Office of the Ohio Consumers’ Counsel, filed on January 25, 2010.

by statute.”²⁴ The PUCO cannot legislate in its own right, and is prohibited from engrafting exceptions to the statutory ratemaking scheme.²⁵ But this is just what the PUCO has done. The PUCO has allowed the Companies to collect increased rates from customers for services provided and billed during the first three months of 2009, creating an exception to the requirement for continued rates under R.C. 4928.141(A).

The PUCO also disregarded the express provisions of R.C. 4928.141(A), and consequently defied the rules of statutory construction in Ohio, including Rule 1.47 (Appx. 682). Under R.C. 1.47, in enacting a statute, it is to be presumed that the entire statute is to be effective. R.C. 4928.141 is rendered superfluous if the PUCO can ignore it by judicial fiat.

The PUCO’s actions contradicted its own Staff, who testified against a true-up for rates. (Supp. 28). The PUCO also failed to heed its own attorneys’ warning that “there is no statutory basis” for a true-up of rates ultimately approved with those already in effect for January through March 2009. (R. 161 at 2). The PUCO’s order is unlawful. It should be reversed.

Proposition of Law 2: The Public Utilities Commission of Ohio is not statutorily authorized, in setting first-authorized rates under R.C. 4928.143, to charge customers for revenues foregone under continued rates.

A. Prospective adjustments to rates which compensate a utility for revenues foregone under prior rates equate to balancing past rates with present rates,

²⁴ *Akron & Barberton Belt Rd. Co. et al. v. Pub. Util. Comm.* (1956), 165 Ohio St. 316, 319, 59 O.O. 410, 135 N.E.2d 400, 402 citing *City of Toledo v. Pub. Util. Comm.* (1939), 135 Ohio St. 57, 13 O.O. 329, 19 N.E.2d 162.

²⁵ The Court has restricted the Commission from legislating and making changes to the statutory scheme in the past. See e.g. *Consumers’ Counsel v. Public Util. Comm.* (1981), 67 Ohio St.2d 153, 164, 21 O. O.3d 96, 423 N.E.2d 820, appeal dismissed (1982), 455 U.S. 914, 102 S.Ct. 1267, 71 L.Ed.2d 455; *Pike Natural Gas Co. v. Pub. Util. Comm.* (1981), 68 Ohio St.2d 181, 22 O.O. 3d 410, 429 N.E.2d 444 (no authority for the PUCO to enact an excise tax adjustment clause); *Montgomery County Bd. of Comm. v. Public Util. Comm.* (1986), 28 Ohio St.3d 171, 503 N.E.2d 167 (no authority for the PUCO to authorize PIPP plan arrearages to be collected through the EFC rate).

which is retroactive ratemaking under *Lucas County Comm'rs. v. Pub. Util. Comm.*²⁶

The Companies have accurately identified their short-term proposal, which the PUCO adopted in principle, as “retroactive.” Senior Vice President, AEP Service Corporation, J. Craig Baker testified: “What we are saying as part of our ESP plan, that if it’s approved, whatever is ultimately approved be retroactive to January 1 and that’s the provision in the ESP.”²⁷

And yet in its Entry on Rehearing the PUCO professes that it did not order unlawful retroactive rates. (Appx. 137-139). Instead, the PUCO theorizes that because the adjustment is allegedly “prospective” it is exculpated from the legal quagmire it has slogged into. The PUCO rationalizes that it did not permit the Companies to go back to January 2009, and re-bill customers at a higher rate for their consumption.²⁸ That, the PUCO admits, would constitute retroactive ratemaking.²⁹

Unfortunately for Ohio consumers the fact that the PUCO chose to prospectively apply first-authorized rates to January through March 2009 billings does not cure the retroactivity. The PUCO reached back to those months and adjusted future rates (rates paid April through December 2009) to compensate for revenues foregone when continued rates were charged. The PUCO’s own words convey the true retroactive nature of the rates: “[A]ny revenues collected from customers during the interim period [January through March 2009] must be recognized and offset by new rates and charges approved by this opinion and order.” (Appx. 73). Offsetting future rates (April through December) with past rates (January through March 2009) is retroactive ratemaking. Contrary to the PUCO’s reasoning, retroactive ratemaking can be found even if there has been no rebilling.

²⁶ *Lucas County Comm'rs. v. Pub. Util. Comm.* (1997), 80 Ohio St. 3d 344, 686 N.E.2d 501.

²⁷ Tr. Vol. 2 at 12. (Supp. 13).

²⁸ (Appx. 137-139).

²⁹ Id.

In fact this Court specifically ruled that using a prospective device to balance past rates with future rates is retroactive ratemaking in *Lucas County Comm'rs. v. Pub. Util. Comm.*³⁰ Lucas County had filed a complaint with the PUCO alleging that, under a weather normalization program, Columbia Gas had collected excessive charges from its customers. Lucas County sought to return the excess either through a rebate or a prospective service credit. The PUCO dismissed the complaint, and Lucas County appealed.³¹ Noting that no mechanism adjusting the weather normalization had been incorporated into the PUCO's initial rate order, this Court concluded that "were the commission to order either a refund or a credit, the commission would be ordering Columbia Gas to balance a past rate with a different future rate, and would be thereby engaging in retroactive ratemaking***."³²

The PUCO, by requiring revenues collected during January through March 2009 be recognized and offset by the new rates, ordered the Companies to balance a past rate with a different future rate. This is retroactive ratemaking just like the retroactive ratemaking that the Court encountered in *Lucas County*. Like *Lucas County* the rates in effect from January through March 2009 were approved by the PUCO with no mechanism reserved for adjusting such rates.

The Court should recognize the substance of the order for what it is—retroactive ratemaking—and not be fooled by surface arguments aimed at disguising the true nature of the PUCO's actions. As noted by this Court, "[t]oo much legal ingenuity is today employed in advising clients how to do a perfectly unlawful thing in a prima facie lawful way, and in advising courts to do a perfectly unconstitutional thing in a prima facie constitutional way. Whether or not such sophistry

³⁰ *Lucas County Comm'rs. v. Pub. Util. Comm.*, 80 Ohio St.3d 344, 349, 686 N.E.2d 501.

³¹ *Id.* at 348.

³² *Id.* at 348-349.

shall succeed depends upon whether the courts shall regard the substance of things, or merely the surface of things.”³³

B. The Public Utilities Commission of Ohio is not statutorily authorized under S.B. 221 to engage in retroactive ratemaking.

The PUCO, in approving the term of the ESP as beginning January 1, 2009, alleges that its ruling is consistent with R.C. 4928.141. (Appx. 703). The PUCO culls from that section the clause that requires an electric utility to provide consumers an SSO beginning on January 1, 2009. (Appx. 73, 137). “Beginning January 1, 2009, an electric distribution utility shall provide consumers, on a comparable basis *** a standard service offer***. Only a standard service offer authorized in accordance with section 4928.142 or 4928.143 of the Revised Code shall serve as the utility’s standard service offer for the purpose of compliance with this section***.” That provision is trumpeted as requiring retroactive ratemaking. The PUCO cites no other authority for its actions.

This solitary argument is flawed for at least two reasons. First, as fully explained in OCC’s Proposition of Law 1, the language immediately following establishes an exception to that provision requiring a standard service offer (via first-authorized rates) on January 1, 2009. That language explains that “notwithstanding the foregoing provision” if there is no standard service offer first authorized under R.C. 4928.142 or 4928.143, then the rate plan of the utility shall continue. By this language, the General Assembly expressly rejected the notion that rates could be established retroactively by a later first-authorized standard service offer. Instead, the continued rates are to be charged.

The PUCO’s theory further implodes because it is incompatible with principles beyond Chapter 49 of the Revised Code that generally inhibit retroactive laws. Specifically, in Ohio

³³ *Columbus v. Pub. Util. Comm.* (1921), 103 Ohio St. 79, 135, 133 N.E. 800.

there are two fundamental sources that check retroactive laws: R.C. 1.48 (Appx. 683) and Article II, Section 28 of the Ohio Constitution.³⁴ (Appx. 711). Under R.C. 1.48, statutes in Ohio are presumed to be prospective, unless expressly made retrospective or retroactive.³⁵ The other source, Article II, Section 28 of the constitution, precludes the General Assembly from passing retroactive laws. Article II is inapplicable only when the General Assembly enacts procedural or remedial legislation.³⁶

In reviewing statutes that are being applied retroactively, the Court has acknowledged it must comply with these sources and has adopted a two part inquiry: Did the General Assembly expressly make the statute retroactive? And, if so, is the statutory restriction substantive or remedial in nature?³⁷ Importantly, the Court has determined that it will not tackle the constitutionality unless it concludes that the General Assembly expressly made the statute retroactive.³⁸ “Upon its face, R.C. 1.48 establishes a threshold analysis which must be utilized prior to inquiry under Section 28, Article II of the Ohio Constitution.”³⁹

The presumption under R.C. 1.48 that statutes are prospective is not easily overcome. This Court has dictated that a statute must “clearly proclaim” its retroactive application.⁴⁰ A

³⁴ “The general assembly shall have no power to pass retroactive laws***.”

³⁵ The terms “retroactive” and “retrospective” are used interchangeably to refer to a law that affects “acts or facts occurring, or rights accruing, before it came into force” *State v. Consilio*, 114 Ohio St.3d 295, 2007-Ohio-4163, 871 N.E.2d 1167, ¶1, fn. 1 (Quoting Black’s Law Dictionary (6th Ed. 1990) 1317).

³⁶ *French v. Dwiggins*, (1984), 9 Ohio St.3d 32, 36, 9 OBR 123, 458 N.E.2d 827, 832 (citation omitted).

³⁷ *Id.*

³⁸ *Van Fossen et al. v. Babcock & Wilcox Co.* (1988), 36 Ohio St.3d 100, 522 N.E.2d 489, syllabus ¶1.

³⁹ *Id.*, citing *Kiser v. Coleman* (1986), 28 Ohio St.3d 259, 262, 28 OBR 337, 339-340, 503 N.E.2d 753, 756; *Wilfong et al. v. Batdorf* (1983), 6 Ohio St.3d 100, 6 OBR 162, 451 N.E.2d 1185; and *French v. Dwiggins* (1984), 9 Ohio St.3d 32, 9 OBR 123, 458 N.E.2d 827.

⁴⁰ *State of Ohio v. Consilio*, 114 Ohio St.3d 295, 2007-Ohio-4163, 871 N.E.2d 1167, ¶1 syllabus.

mere inference of retroactivity is insufficient.⁴¹ Nor is ambiguous language adequate to overcome the presumption. The language must do more than suggest retroactivity.⁴²

There is no strong and unmistakable declaration by the General Assembly that ESP rates can be made retroactive. Although the language establishes a mandate that ESP rates be in effect on January 1, 2009, within the very same breath the General Assembly grants an exception, establishing continued rates if there is a gap in approval.

Even if the clause had not been followed by this gap filler, the language in S.B. 221 falls short. It does not clearly proclaim retroactivity, and under the Court's holdings, the threshold has not been met. Thus, this Court's inquiry is at an end. It need not progress to the constitutional question of whether this provision of S.B. 221 impairs vested substantive rights, and thus violates the Ohio Constitution.

The Ohio General Assembly knows how to legislate to allow rate increases to be collected where a PUCO order is not timely; but it chose not to do so in S.B. 221. For example, in R.C. 4909.42 (Appx. 689A) the General Assembly provided a remedy to utilities where the PUCO has not issued an Order on a rate increase application (under R.C. 4909.18) within 275 days of its filing. Under that statute "the proposed increase shall go into effect***" upon the satisfactory filing of an undertaking by the public utility, after the 275 days has passed. The rates are collected subject to refund when the PUCO issues a final order. There is a similar provision in the same statute that relieves the utility from refunding amounts collected subject to

⁴¹ *State of Ohio v. Consilio*, 114 Ohio St.3d 295, 2007-Ohio-4163, ¶ 15 citing *Kelley v. State* (1916), 94 Ohio St. 331, 338-339, 114 N.E. 255.

⁴² See for example *Van Fossen et al. v. Babcock & Wilcox Co.*, 36 Ohio St.3d 100,103 ("This section applies to and governs any action***pending in any court on the effective date of this section ***notwithstanding any provisions of any prior statute or rule of law of this state."); *State v. Cook* (1998), 83 Ohio St.3d 404, 410,700 N.E.2d 570, 576-577(statute applies to anyone who "was convicted of or pleaded guilty to a sexually oriented offense prior to the effective date of this section, if the person was not sentenced for the offense on or after" that date.)

refund if the PUCO does not render a decision within 545 days after the filing of the application. But in S.B. 221, unlike R.C. 4909.42, the General Assembly enacted no such alternative for the public utility (or the PUCO) to implement a rate increase upon the expiration of the 150-day time period in R.C. 4928.143(C)(1). To the contrary, the General Assembly required existing rates to continue after the expiration of the 150 days.⁴³

The Court should find that the PUCO had no authority under R.C. 4928.141 to alter the first-authorized ESP rates to make them retroactive as if they were approved on January 1, 2009. The authority is illusory. R.C. 4928.141 does not expressly proclaim that the PUCO can enact retroactive rates. Instead, the remaining section of that statute clearly proclaims that continued rates must be charged if there are no approved first-authorized rates. The PUCO should be reversed.

Proposition of Law 3: The Public Utilities Commission acts unreasonably when it fails to provide customers an opportunity or means to be made whole if its rulings on a utility's electric service plan are reversed on appeal.

Appellant OCC attempted to obtain a stay of the ESP rates at numerous times, before both the PUCO and the Court.⁴⁴ As early as March 25, 2009, OCC moved to stay the rates at the PUCO and requested alternatively that the rates be collected subject to refund. (R. 222). That motion was denied by the PUCO five days later. (Appx. 90-94). On April 17, 2009, OCC sought rehearing, among other things, because the PUCO failed to order rates collected subject to refund. (Appx. 197-199). Additionally, OCC argued that the PUCO had not complied with R.C. 4903.09 (Appx. 685) because it did not provide the basis for denying OCC's request to collect

⁴³ R.C. 4928.141(A).

⁴⁴ The possibility of a stay as an effective remedy may be more illusory than real when dealing with consumers' claims, because of the difficulties in posting a bond. See E. Levin, *Illinois Public Utility Law and the Consumer: A Proposal to Redress the Imbalance* (1977), 26 DePaul L. Rev. 259, 268-269.

rates subject to refund. Also on that date, OCC and others filed an original action in prohibition⁴⁵ seeking to halt rates from being retroactively collected from customers. That writ was denied on June 17, 2009, with the Court finding in part, that OCC had an “adequate remedy at law.” OCC filed an appeal from the PUCO’s order on September 10, 2009, which was docketed as S.Ct. Case No. 09-1620. After its appeal was filed, OCC moved to stay the collection of the retroactive portion of the rate increase and alternatively moved to collect the rates subject to refund. That appeal (and the motion to stay) was dismissed by the Court on October 29, 2009. On November 5, 2009, OCC filed the instant appeal, and as part of its appeal claimed that the PUCO erred by failing to provide “an opportunity or means for customers to be made whole in the event that the PUCO rulings in these cases are reversed on appeal.” (Appx. 4). On November 30, 2009, OCC moved to suspend the PUCO’s order implementing the approved ESP rates.⁴⁶

Despite the opportunities to protect customers, the PUCO turned a deaf ear to OCC’s concerns. Moreover, the PUCO avoided explaining why it could not order rates collected subject to refund. OCC is left to surmise why the PUCO denied its motion. This is because the PUCO did not issue any findings of fact or set forth the reasons why the rates could not be collected subject to refund, in either the entry denying the OCC motion (R. 224) or in the Entry on Rehearing (Appx. 135-138, 145-146). Thus, the PUCO violated R.C. 4903.09.⁴⁷ OCC had

⁴⁵ S.Ct. Case No. 09-0710, *State of Ohio, ex rel. Office of the Ohio Consumers’ Counsel et al. v. Alan R. Schriber et al.*, Complaint for Writ of Prohibition (Apr. 17, 2009).

⁴⁶ The Court has not yet ruled on the OCC’s Motion to Suspend.

⁴⁷ R.C. 4903.09 requires the PUCO to set forth “findings of fact and written opinions setting forth the reasons prompting the decisions arrived at, based upon said findings of fact.”

offered precedent to support its motion, referring to the PUCO's order in 1982 pertaining to Zimmer nuclear plant issues.⁴⁸ This precedent was not discussed by the PUCO.

The PUCO's unsubstantiated ruling precluding rates from being collected subject to refund was unreasonable in light of the well known precedent in *Keco*.⁴⁹ *Keco* stands for the proposition that in the post-appeal process, even if the Court overturns the PUCO, consumers are precluded from seeking restitution for that portion of the rate increase found to be excessive. The utility is allowed to keep the proceeds from the unlawful rate increase. Any relief given to the consumer is, under *Keco*, prospective only. Lawful rates to be collected prospectively would be established on remand minus the unlawful elements.

If such a remand were to be ordered, following this Court's decision, it is likely that even relief in the form of prospective adjustments to rates will all but be eliminated. This transpires because the Companies' ESP rates are only in effect for a three-year period,⁵⁰ until December 31, 2011. Prior to that time, it is expected that the Companies will apply for new rates to take effect immediately thereafter. With an order implementing new ESP or MRO rates, it will likely be argued that those new rates would not be affected by the Court's decision here. Thus any consumer victory would be purely academic.

⁴⁸ See *In the Matter of the Application of Columbus & Southern Ohio Electric Company for Authority to Amend and Increase Certain of its Rates and Charges for Electric Service, Amend Certain Terms and Conditions of Service and Revise its Depreciation Accrual Rates and Reserves*, PUCO Case No. 81-1058-EL-AIR, Entry (Nov. 17, 1982) (Appx. 540-542).

⁴⁹ *Keco Indus. Inc. v. Cincinnati & Suburban Bell Tel. Co.* (1957), 166 Ohio St. 254, 2 O.O.2d 85, 141 N.E.2d 465, writ of certiorari denied and appeal dismissed (1957), 355 U.S. 182, 78 S.Ct. 267, 2 L.Ed.2d 187.

⁵⁰ Although the Companies define the term of the ESP as three years, under the modified ESP approved by the PUCO, generation fuel costs incurred above the annual caps on total bill increases will be deferred, with carrying charges, for future collection from customers during 2012 through 2018. OCC opposed the creation of such deferrals and the carrying charges on the basis that if the cost increases to generation fuel charges had been appropriate, as recommended by OCC Witness Smith, (R.113), small increases would have resulted and there would be no need for the deferrals.

Moreover, the PUCO's ruling was unreasonable as well in light of the fact that the only other protection customers have is to seek a stay, a remedy largely unobtainable for them. In the case below, the PUCO denied OCC's motion for a stay. Consumers' options, thus, were narrowed down to arguing for a stay or suspension of rates at the Supreme Court. Not surprisingly, Appellees have insisted that a stay (or suspension) from the Court can only be obtained if bond is posted.⁵¹ As OCC has argued in its unsuccessful attempts to obtain stays, it is not financially capable of posting any bond other than a nominal amount. Thus, a stay as a remedy to be obtained from this Court is truly an illusory remedy at best unless the Court relieves OCC from filing a bond.⁵²

Thus, the PUCO was well aware that without permitting rates to be collected subject to refund, under the limited period rates would be in effect, customers would have virtually no means to obtain relief from rate increases this Court might find unlawful. In light of the illegal retroactive ratemaking that the PUCO undertook, this result is particularly harsh and inequitable. The PUCO left customers unprotected when it could simply have ordered rates collected, subject to refund, with little financial harm to the Companies. The Court should reverse the PUCO.

Proposition of Law 4: Where an opinion and order of the Public Utilities Commission fails to state specific findings of fact, supported by the record, and fails to state the reasons upon which the conclusions in the commission's opinion and order were based, such order fails to comply with the requirements of R.C. 4903.09, and is, therefore, unlawful.

A. Although the Public Utilities Commission may depart from its prior precedent, if it does not show the need to depart is clear and that prior

⁵¹ See e.g. Companies' Memorandum Contra Appellant's Motion to Suspend at 5-7 (Dec. 10, 2009); PUCO Memorandum Contra Appellant's Motion to Suspend at 3-7 (Dec. 8, 2009).

⁵² OCC has argued that in the past the Court and the Commission have both permitted stays to be granted without the posting of a bond. Additionally OCC has argued that under R.C. 2505.12 (Appx. 684), the OCC is a public officer of the state and need not give a supersedeas bond. OCC has argued as well that no bond should be required because R.C. 4903.16 (Appx. 687) is unconstitutional under the separation of powers doctrine.

decisions were in error it fails to comply with the requirements of R.C. 4903.09.⁵³

R.C. 4903.09 requires the PUCO to set forth “findings of fact and written opinions setting forth the reason prompting the decisions arrived at, based upon said findings of fact.” Where the PUCO does not set forth detailed findings, it fails to comply with the requirements of this section and its Order is unlawful.⁵⁴

In particular, where the PUCO issues a decision departing from precedent, it has a heightened responsibility to explain its decision, in order to comply with R.C. 4903.09.⁵⁵ This responsibility is created because this Court values predictability in administrative law. Such predictability is assured when precedent set by an administrative body, such as the PUCO, is followed. Indeed, the Court has noted that prior determinations of the PUCO should not be disregarded and set aside unless the need to change is clear and the prior decisions are in error.⁵⁶

The Court has in fact reversed the PUCO when the PUCO has failed to explain why its earlier orders and rationale should be overruled. For example, in *Office of Consumers' Counsel*

⁵³ See e.g. *Office of Consumers' Counsel v. Pub. Util. Comm.* (1985), 16 Ohio St.3d 21, 16 OBR 371, 475 N.E.2d 786.

⁵⁴ *Ideal Transportation Co. v. Pub. Util. Comm.* (1975), 42 Ohio St.2d 195, 71 O.O.2d 183, 326 N.E.2d 861.

⁵⁵ See for e.g. *Cleveland Electric Illuminating Co. v. Pub. Util. Comm.* (1975), 42 Ohio St.2d 403, 431-432, 71 O.O. 393, 330 N.E.2d 1, writ of certiorari denied (1975), 423 U.S. 986, 96 S.Ct. 393, 46 L.Ed.2d 302, appeal after remand (1976), 46 Ohio St.2d 105, 75 O.O.2d 172, 346 N.E.2d 778 (citing *State ex rel. Automobile Machine Co. v. Brown* (1929), 121 Ohio St. 73,75, 166 N.E. 903—“It has been held in this state that ‘administrative interpretation of a given law, while not conclusive, is, if long continued, to be reckoned with most seriously and is not to be disregarded and set aside unless judicial construction makes it imperative to do so.’” (citation omitted).

⁵⁶ *Cleveland Electric Illuminating Co. v. Pub. Util. Comm.*, 42 Ohio St. 2d at 431-432.

v. Pub. Util. Comm.,⁵⁷ the Court reviewed an appeal in which the PUCO had changed expensing levels for station connections, without explaining why the earlier order and rationale should be overruled. The Court observed that to determine whether the PUCO had abused its discretion, and should be reversed under R.C. 4903.09, it must first understand why the PUCO's prior orders are no longer controlling.⁵⁸

Articulating the reasons for an order without referring to prior orders, "makes ascertaining an abuse of discretion virtually impossible."⁵⁹ A few simple sentences from the PUCO could have sufficed in this regard, the Court held. Because this was not done, the Court reversed the PUCO, finding that "we will not allow the commission to arbitrarily change expensing levels unless the commission explains why its 1981 order and the rationale behind gradual phase-in should be overruled. ***Consumers who rely on commission directives are unable to understand why the basis for the 1981 order, the ostensible protection of consumers for four years with a gradual phase-in of station connections expenses, must now give way to utility convenience rather than need."⁶⁰ Having given the PUCO ample warning in its earlier decisions, the Court reversed the PUCO's order.⁶¹ It is with these principles in mind, that the Court must address errors OCC alleges related to the PUCO's treatment of off-system sales.

⁵⁷ See also *Office of Consumers' Counsel v. Pub. Util. Comm.* (1985), 16 Ohio St. 3d 21, 16 OBR 371, 475 N.E.2d 786. See also *Consumers' Counsel v. Pub. Util. Comm.* (1984), 10 Ohio St.3d 49, 10 OBR 312, 461 N.E.2d 303; *Cincinnati Bell Tel. Co. v. Pub. Util. Comm.* (1984), 12 Ohio St. 3d 280, 287-288, 12 OBR 356, 466 N.E.2d 848, appeal dismissed (1986), 476 U.S. 1166, 106 S.Ct. 2884, 90 L.Ed.2d 972, which addressed the very same issues.

⁵⁸ *Office of Consumers' Counsel v. Pub. Util. Comm.*, 16 Ohio St.3d 23, 475 N.E.2d 788.

⁵⁹ *Id.* at 23.

⁶⁰ *Id.*

⁶¹ *Id.*

B. The Public Utilities Commission of Ohio departed from precedent in failing to credit customers with revenues from off-system sales.

1. Factual Background

Off-system sales are sales by a utility to individuals or entities that are not Ohio retail customers. They have been called “opportunity” sales—sales that are made possible because the generation plant produces more power than is needed for Ohio retail electric customers.⁶² The revenue from such sales is recorded in FERC Account 447—Sales for resale. The margin or profit on these sales is derived by taking the revenue received less the variable cost of making the sale including fuel and purchased power.⁶³ AEP Ohio’s off-system sales come from generation plant that was built for the benefit of Ohio customers. Moreover, AEP Ohio’s jurisdictional customers have funded a return on and a return of such generation assets under traditional pre-S.B. 221 regulation.

Off-system sales profits from AEP Ohio are significant for customers. In 2007, profits from off-system sales were \$146.7 million for OP and \$124 million for CSP for an AEP Ohio total of \$270.7 million. (Appx. 26). During the period of the ESP, the Companies projected profits from off-system sales of \$431 million for OP and \$360 million for CSP, for an AEP Ohio total of \$791 million – more than three-quarters of a billion dollars over three years!⁶⁴ The Companies, however, excluded all of these profits from their rates.

OEG Witness Lane Kollen testified that in each of the jurisdictions where AEP operates, these profits are used to lower rates.⁶⁵ Kollen characterized AEP Ohio’s proposal as discriminatory and concluded that it placed Ohio customers at a disadvantage, compared to

⁶²See for example, Limited Rebuttal Testimony of J. Craig Baker at 8. (R. 147).

⁶³ Id.

⁶⁴ OCC Ex. 6 at 7-8; OCC Ex. 7 (Exhibits for Tr. Vol. V, filed Dec. 8, 2008). (Supp. 14-18).

⁶⁵ Testimony of OEG Witness Kollen at 14 (Supp. 19-22). See also Testimony of Kroger Witness Higgins at 9. (Supp. 24).

customers in other states. OEG argued all revenues from the power plants should be a rate credit.⁶⁶ Similarly, Kroger Witness Higgins presented testimony recommending a credit to customers for profits from off-system sales. A fuel adjustment charge without such a credit is “asymmetrical and fundamentally unreasonable,” he opined.⁶⁷ OCC on brief proposed profits from off-system sales should be used either as an offset to the fuel adjustment clause (“FAC”) component or an adjustment to rates. Either of these treatments is permissible, though not required, under the broad language of R.C. 4928.143(B)(2): “[t]he [ESP] plan may provide for or include without limitation, any of the following***.” (Appx. 707). OCC argued that since the costs of the power plants that are making the sales are in rates, some share of the profits should be ordered. Doing so would also promote the policy of state, under R.C. 4928.02(A) (Appx. 695), to “ensure the availability to consumers of adequate, reliable, safe, efficient, nondiscriminatory, and reasonably priced retail electric service.”

The PUCO, nonetheless, approved a modified ESP plan, and found that the off-system sales profits should be retained by AEP shareholders.⁶⁸ The PUCO merely parroted the argument of the Companies: the law does not require an offset. (Appx. 26). The PUCO admonished that Ohio law governs the Companies’ ESP application; how other jurisdictions handle off-system sales is not persuasive.⁶⁹ The PUCO chastised interveners for arguing to include off-system sales in the significantly excessive earnings test (“SEET”) and also seeking a credit for the same sales—“Intervenors cannot have it both ways: they cannot request that OSS margins be credited against the fuel costs (i.e. offset the expenses); and, at the same time, ask us to count the OSS

⁶⁶ OEG Brief at 10. (R. 180).

⁶⁷ Testimony of Kroger Witness Higgins at 9 (Supp. 24).

⁶⁸ (Appx. 26).

⁶⁹ Id.

margins as earnings for purposes of the significantly excessive earnings test (SEET) calculation.”⁷⁰

On April 17, 2009, OCC applied for rehearing on a number of issues including the PUCO’s unwillingness to credit customers for profits from off-system sales. (Appx. 186-188). There OCC argued that persuasive precedent existed establishing a policy of requiring electric utilities to share profits of off-system sales with customers.⁷¹ If the PUCO was to abandon the precedent, it had to show that its prior decisions were wrong and there is a need to deviate from the precedent, OCC argued.⁷²

In denying OCC’s application for rehearing, the PUCO recited the obvious: the ESP proceeding is not an electric fuel component (“EFC”) proceeding.⁷³ The PUCO further opined that while some aspects of S.B. 221 may be analogous to the EFC mechanism, the statutory provisions regarding the EFC were repealed many years ago. Thus, OCC’s “cited precedent” is “irrelevant to our ruling in this case with respect to OSS,” the PUCO ruled.⁷⁴ Rehearing was denied.

⁷⁰ Id. The Commission also excluded off-system sales from the SEET calculation, making it clear interveners could not have it any way, let alone “both ways.” (See Appx. 78).

⁷¹ OCC cited, as examples of such precedent, *In the Matter of the Application of the Cleveland Electric Illuminating Company for an Increase in Rates*, Case No. 84-188-EL-AIR. (Appx. 314-358). Additionally, OCC cited *In the Matter of the Application of the Cincinnati Gas & Electric Company for an Increase in its Rates for Gas Service to All Jurisdictional Customers*, Case No. 95-656-GA-GCR Entry on Rehearing (Feb. 12, 1997), as a case recognizing that sharing of off-system sales profits is a means to assist in achieving the goal of providing reliable and safe gas service to GCR customers at the lowest reasonable cost. (See Appx. 302-313).

⁷² Id.

⁷³ (Appx. at 98, ¶14).

⁷⁴ Id.

2. The PUCO's policy of crediting customers for profits from off-system sales and non-jurisdictional revenues is well established precedent that should have been followed.

While the PUCO seeks to dismiss the notion that there is any precedent to support crediting customers for profits from off-system sales, this is not true. AEP Ohio Witness Nelson in fact confirmed that the current continued rates for generation (i.e. pre-ESP) contain credits for off-system sales profits.⁷⁵ The current continued rates were set in the Companies' last base rate proceeding, Case No. 91-418-EL-AIR.⁷⁶

Crediting customers for the profits of off-system sales, as was done in CSP's last base rate case, is consistent with well established precedent. Back in 1985, the PUCO first addressed this issue and established the standard that was to be adhered to henceforth. In PUCO Case No. 84-188-EL-AIR,⁷⁷ the PUCO encountered non-jurisdictional interconnection revenues. There, the utility was receiving revenues by acting as a middleman in providing transmission service between other utilities. The utility was also selling generation from its system to other utilities. The PUCO defined the difference between the amount the utility was paid by others and the cost to the utility as "non-jurisdictional interconnection revenue." This revenue had not been included in the utility's EFC or base rates. Finding that the transmission plant had been constructed for the benefit of jurisdictional customers, "fairness would suggest some consideration nevertheless ought to be given to revenues realized by CEI utilizing plant included

⁷⁵ Tr. V at 90-93.

⁷⁶ *In the Matter of the Application of Columbus Southern Power Company for Authority to Amend its Filed Tariffs to Increase the Rates and Charges for Electric Service*, PUCO Case No. 91-418-EL-AIR, Opinion and Order at 82 (May 12, 1992). (Appx. 502).

⁷⁷ *In the Matter of the Application of Cleveland Electric Illuminating Company for Authority to Amend and to Increase Certain of its Filed Schedules Fixing Rates and Charges for Electric Service; In the Matter of the Application of The Cleveland Electric Illuminating company for Authority to Revise its Book Depreciation Accrual Rates for Electric Property and Plant*, PUCO Case No. 84-188-EL-AIR, Opinion and Order at 17-18 (Mar. 7, 1985). (Appx. 330-331).

in jurisdictional rate base.”⁷⁸ The PUCO allowed one half of the revenues to reduce base rates of jurisdictional customers.

Many electric base rate case proceedings followed in the footsteps of this Order. Later that year, in another electric rate proceeding, the PUCO credited customers for revenues from the utility’s off-system sales to AMP-Ohio.⁷⁹ Another case allocated one hundred percent of the net non-jurisdictional interconnection revenue from transmission facilities to customers.⁸⁰ Still another found that Ohio Edison’s “adder revenue”— the mark-up on the utility’s energy costs for sales to other utilities—should be credited to customers in electric base rates.⁸¹

The PUCO did not confine its rulings to electric base rate proceedings either. It began to extend its holdings to gas cost recovery proceedings. For instance, in reviewing amendments to a 1994 stipulated base rate increase,⁸² the PUCO rejected provisions in a follow-up stipulation allowing the utility to retain significant off-system sales profits. It ruled instead that all off-system sales and capacity release revenues generated from capacity secured for customers must

⁷⁸ *Id.* at 18.

⁷⁹ *In the Matter of the Application of Ohio Edison Company to change certain of its Filed Schedules Fixing Rates and Charges for Electric Service*, PUCO Case No. 84-1359-EL-AIR, Entry on Rehearing (Dec. 15, 1985). (Appx. 550-552).

⁸⁰ *In the Matter of the Application of the Cleveland Electric Illuminating Company for Authority to Amend and Increase Certain of its Filed Schedules Fixing Rates and Charges for Electric Service*, PUCO Case No. 85-675-EL-AIR, Opinion and Order at 20 (June 24, 1986). (Appx. 378-379).

⁸¹ *In the Matter of the Application of Ohio Edison Company for Authority to Change Certain of its Filed Schedules Fixing Rates and Charges for Electric Service*, PUCO Case No. 89-1001-EL-AIR, Opinion and Order at 22-23 (Aug. 16, 1990). (Appx. 574-575).

⁸² *Re Columbia Gas of Ohio, Inc.*, PUCO Case Nos. 96-1113-GA-ATA, 98-222-GA-GCR, 03-1459-GA-ATA, Order at 9 (Mar. 11, 2004). (Appx. 626).

be shared, with 80% going to customers. The following year, in a 2005 Opinion and Order,⁸³ the PUCO ordered the utility to credit gas cost recovery (“GCR”) customers for profits from the utility’s activities in accepting, loaning and exchanging gas for third parties. In its ruling the PUCO cited Case No. 84-188-EL-AIR, characterizing it as “instructive.” The PUCO found that it had “long required LDCs [local distribution companies] to credit GCR customers with the revenue from the third party use of GCR financed assets.”⁸⁴ The PUCO also noted that providing such revenue to customers assists in achieving the goal of providing reliable and safe gas service to GCR customers at the lowest reasonable cost.⁸⁵

This precedent should have been followed by the PUCO in setting the ESP rates to be charged to customers. Sharing of the off-system sales profits between the utility and its customers is based upon a fundamental principle of basic fairness—customers of a utility should be entitled to share in the profits that flow from assets they have funded and continue to fund through rates.

S.B. 221 has not altered the fact that customers have funded and continue to fund the generation assets of the Companies which are being utilized to generate significant profits for the

⁸³ *In the Matter of the Regulation of the Purchased Gas Adjustment Clause contained within the Rate Schedules of the East Ohio Gas Company; In the Matter of the Long-Term Forecast Report of the East Ohio Gas Co.*, PUCO Case No. 03-219-GA-GCR, 03-119-GA-FOR, Opinion and Order at 9 (Mar. 2, 2005). (Appx. 663).

⁸⁴ *Id.*, citing for example *In the Matter of the Regulation of the Purchased Gas Adjustment Clause Contained Within the Rate Schedules of Vectren Energy Delivery of Ohio*, PUCO Case No. 00-220-GA-GCR, Opinion and Order at 8-9 (Sept. 25, 2001)(holding that where pipeline capacity was purchased by GCR customers, GCR customers should receive the benefits from use of such capacity). (Appx. 645-646).

⁸⁵ *In the Matter of the Regulation of the Purchased Gas Adjustment Clause Contained within the Rate Schedules of the East Ohio Gas Company; In the Matter of the Long-Term Forecast Report of the East Ohio Gas Co.*, PUCO Case No. 03-219-GA-GCR et al., Opinion and Order at 8-9 (Mar. 2, 2005) (Appx. 629), citing *In the Matter of the Application of the Cincinnati Gas & Electric Company for an Increase in its Rates for Gas Service to All Jurisdictional customers*, PUCO Case No. 95-656-GA-GCR et al., Entry on Rehearing at 7 (Feb. 12, 1997). (Appx. 308).

Companies' shareholders. Nor has S.B. 221 obliterated the basic fairness in allocating profits of customer funded assets between shareholders and customers. Although S.B. 221 does establish a different mechanism for determining rates, that mechanism does not preclude the PUCO from using the profits from off-system sales to ensure reasonably priced retail electric service.⁸⁶ True, S.B. 221 does not require profits from off-system sales to be included in the ESP rates; but neither did the prior ratemaking formula require such, and yet the PUCO required sharing. Nor does S.B. 221 mandate that utilities horde all the profits generated from off-system sales using assets included in rates that customers must pay. Rather, it was the PUCO that in 1985 established a policy that in the interest of fairness it should require a sharing of profits from customer funded assets, ostensibly as a means to achieve reasonable rates.

C. The PUCO failed to explain why it was departing from precedent, abusing its discretion under R.C. 4903.09.

That same precedent should have been applied to ensure reasonably priced electric service to the Companies' customers, consistent with R.C. 4928.02(A). It was not, and the PUCO failed to explain why. The Order should be reversed.

A mere declaration that the precedent is not relevant will not suffice to meet the PUCO's burden. It must, under R.C. 4903.09, set forth "findings of fact and written opinions setting forth the reason prompting the decisions arrived at, based upon said findings of fact." It failed to do so here. The PUCO has thus violated R.C. 4903.09 (Appx. 685) and the Court's holdings in *Cleveland Electric Illuminating Co. v. Pub. Util. Comm.*, supra, and its progeny. The Court should reverse the PUCO and order the PUCO to implement further proceedings to establish

⁸⁶ See R.C. 4928.02(A) "It is the policy of this state to do the following throughout this state: (A)Ensure the availability to consumers of adequate, reliable, safe, efficient, non-discriminatory, and reasonably priced retail electric service***." (Appx. 695).

customers' share of the off-system sales profits. Doing so would assist in achieving the goal of providing reasonably priced electric service under R.C. 4928.02(A). (Appx. 695).

Proposition of Law 5: Where the Commission grants a utility a Provider-Of-Last-Resort charge, contrary to the manifest weight of the evidence and fails to supply supporting rationale for its decision so as to constitute mistake, it violates R.C. 4903.13⁸⁷

A. Background

The Companies' request to collect costs from customers through a provider-of-last-resort charge was premised upon an obligation placed upon electric distribution utilities ("EDUs") to serve. In concept, the POLR charge recognizes that customers are permitted to switch away from the utility and then may later return to the EDUs for electric generation service.⁸⁸ Formerly, when a POLR charge was approved, the Commission based the charge on the financial risk for the EDU pertaining to customers who shop for alternative suppliers and subsequently return to the EDU.

To compensate it for financial risk associated with POLR responsibilities, AEP Ohio sought to collect from customers \$108.2 million annually during the three-year term of CSP's ESP and \$60.9 million annually during the three-year term of OP's ESP.⁸⁹ The total POLR charge that AEP Ohio requested from customers equaled \$508 million over the three-year term of the ESP.⁹⁰ The Companies claimed that the POLR charge was to compensate them for the financial risk that customers will purchase their generation from a competitive retail electric service ("CRES") supplier and later decide to return to the Companies for their generation

⁸⁷ (Appx. 686).

⁸⁸ R.C. 4928.14. "The failure of a supplier to provide retail electric generation service to customers within the certified territory of an electric distribution utility shall result in the supplier's customers, after reasonable notice, defaulting to the utility's standard service offer under sections 4928.141 [4928.14.1], 4928.142 [4928.14.2], and 4928.143 [4928.14.3] of the Revised Code until the customer chooses an alternative supplier."

⁸⁹ (R.9). Baker Testimony, JCB-2.

⁹⁰ Id.

service.⁹¹ The Companies suggested that the PUCO recognizes that a POLR charge is appropriate and therefore should be continued in the ESP.⁹² In its ESP Applications, AEP Ohio estimated the proposed POLR “financial risk” using a method called the Black-Scholes Model (“model”) which was developed for a different purpose altogether, quite unrelated to valuing POLR risk. The model is primarily used to hedge equities.⁹³ It is used by coal traders to value coal options.⁹⁴

The PUCO ultimately granted 90% of the POLR charge revenue that AEP Ohio requested—based on the Companies’ equity hedging model and tied to what the Company and the PUCO newly coined as the “migration risk.”⁹⁵ CSP will collect \$97.4 million annually for its alleged POLR risk; OP will collect \$54.8 million annually for its alleged POLR risk. The POLR charge will be collected from customers through a nonbypassable POLR rider.⁹⁶ These POLR charges reflect an increase of 567 percent over the current POLR charges that customers pay in the case of CSP (from \$14.6 million to \$97.4 million) and a 38 percent increase (from \$39.7 million to \$54.8 million) in the case of OP.⁹⁷ The amount of the POLR charge granted by the Commission is allegedly tied to the risk of customers migrating to a supplier and leaving AEP Ohio’s system when prices are below tariff. The POLR charge approved relates to the “migration risk” only and applies whether or not the customer returns to AEP Ohio.⁹⁸

⁹¹ (R.9). AEP Ohio Ex. 2A at 25-26 (Baker).

⁹² OCC Ex. 11 at 8 (Medine). (Supp. 59).

⁹³ Id.

⁹⁴ Id. at 8, 10. (Supp. 59, 61).

⁹⁵ ESP Order at 40. (Appx. 49).

⁹⁶ ESP Order at 38. (Appx. 47).

⁹⁷ (R.6). Ex. DMR-5.; (R.214). ESP Order at 40. (Appx. 49).

⁹⁸ (R. 194). Tr. XIV at 205-206 (Dec.10, 2008) Mr. Baker had previously described the major part of the POLR risk as the “put” or when customers leave when prices are below tariff rates. Tr. XI at 147 (Dec. 3, 2008)(Baker).

OCC is appealing the PUCO's decision because not only is there a huge increase in the POLR charge but also because the tool used by AEP Ohio is indecipherable, vague, and does not measure POLR risks. Consequently, the model could not identify any specific costs that the Companies are incurring or are expected to incur relating to the POLR obligation.⁹⁹ At the hearing, OCC argued that the evidence did not support any POLR risk to AEP Ohio. OCC does not consider the so-called "migration risk" as part of POLR but rather views POLR as an obligation to serve, which is only impacted if customers who shop return.¹⁰⁰ If the Commission were to allow such a charge, OCC alternatively argued that the POLR charge customers are paying in continued rates is sufficient to cover AEP Ohio's POLR risk.¹⁰¹

B. The Commission's decision to approve most of AEP Ohio's proposed POLR charge based on the use of the Black-Scholes model is against the manifest weight of the evidence and should be reversed.

The scope of the Court's review of the PUCO's decisions is set forth in R.C. 4903.13.¹⁰² Under the "unlawful or unreasonable" standard set forth in R.C. 4903.13, the Court will reverse a decision of the Commission if it is so clearly unsupported by the record and against the manifest weight of the evidence as to constitute mistake.¹⁰³ The PUCO's acceptance of AEP Ohio's model to determine POLR charges was just that - against the manifest weight of the evidence and clearly unsupported by the record in the case. The PUCO should not have accepted the model to

⁹⁹ OCC Ex. 11 at 12 (Medine). (Supp. 63).

¹⁰⁰ Tr. VI 220-221 (Nov. 24, 2008)(Medine). "[A]gain, I don't accept the fact that the obligation to serve is equal to a POLR risk. So the obligation to serve – with obligation to serve comes lots of other advantages to the utility, like the reimbursement of their fuel costs during good times and bad times and a number of other benefits."

¹⁰¹ (R.184 at 33).

¹⁰² R.C. 4903.13. "A final order made by the public utilities commission shall be reversed, vacated, or modified by the supreme court on appeal, if, upon consideration of the record, such court is of the opinion that such order was unlawful or unreasonable. * * *" (Appx. 686).

¹⁰³ *MCI Telecommunications Corp. v. Pub. Util. Comm.* (1987), 32 Ohio St.3d 306, 312, 513 N.E.2d 337 citing *Dayton Power & Light Co. v. Pub. Util. Comm.* (1983), 4 Ohio St.3d 91, 4 OBR 241, 447 N.E. 2d 733, *Columbus v. Pub. Util. Comm.* (1979), 58 Ohio St.2d 103, 12 O.O.3d 112, 388 N.E. 2d 1237.

determine POLR charges given the weight of the evidence produced by the parties against the model, and the lack of evidence supporting any increased POLR risks to the Companies.

Commissioner Roberto recognized these fundamental flaws in the Companies' case in her Concurring Opinion filed in the Commission's Entry on Rehearing. There she declared that the model was an inappropriate tool for determining POLR risk and there was no evidence of an increased risk of migration,¹⁰⁴ necessitating an increase in the POLR charge: "Nor can I find *** that the Black-Scholes Model is an appropriate tool to determine an appropriate POLR charge or that an increased risk of migration exists which requires an incremental increase in POLR***."¹⁰⁵

There is an enormous amount of evidence in the record to support Commissioner Roberto's conclusions. The model is ill-suited for determining AEP Ohio's so-called POLR risk.¹⁰⁶ First, and foremost, the model is not capable of measuring customer shopping behavior or market development progress.¹⁰⁷ And yet customer shopping behavior is what creates the POLR risk that is supposedly measured by the model. Thus, if the model fails accurately measure shopping risk, it cannot be relied upon to calculate the POLR risks the Companies will incur if customers shop.

The use of the model, an untested and unproven tool to calculate a POLR charge, is unprecedented in any regulatory proceedings where POLR revenues have been sought. As Ms. Medine testified, "I am not aware of any utilities that use the Black-Scholes model for this purpose (calculating a POLR charge)."¹⁰⁸ Also, AEP Ohio Witness Baker is not aware of any

¹⁰⁴ Entry on Rehearing, Commissioner Roberto's Concurring Opinion at 2. (Appx. 148-149).

¹⁰⁵ Id.

¹⁰⁶ OCC Ex. 11 at 15-16 (Medine). (Supp. 66-67). See also IEU Application for Rehearing at 16-17. (R. 230).

¹⁰⁷ Tr. XI at 214 (Dec. 3, 2008)(Baker).

¹⁰⁸ OCC Ex. 11 at 17 (Medine). (Supp. 68).

other utilities that use the model for this purpose.¹⁰⁹ A review of the record reflects that AEP Ohio does not even use the model to value its own coal pricing options, because it is not reliable.¹¹⁰ The record also reflects that no party other than AEP Ohio accepted the use of the model or its underlying premises.¹¹¹ Even the PUCO Staff did not understand some of the underlying premises inherent in AEP Ohio's use of the model, especially the inclusion of the risk of customer migration as part of the POLR charge.¹¹²

The model used by the Companies for measuring shopping and the risk created by shopping is not capable of measuring shopping behavior, primarily because it was never designed to do so. AEP Ohio admits as much. The Companies concede that the model fails to account for how long it will take customers to see choice develop in AEP Ohio's service territories—and how quickly customers switch to a CRES provider.¹¹³ Moreover, the POLR charge produced by the model, supposedly to measure the risk of shopping, is the same whether there is 95% shopping or 5% shopping.¹¹⁴ The POLR charge produced under the model is the same regardless of the length of time customers shop. And the POLR charge produced under the model is the same, regardless of the circumstances of the markets or number of customers shopping.

In direct contrast to the overwhelming evidence against the model, is the paucity of evidence supporting AEP's POLR charge. And yet the PUCO accepted that evidence. The Commission, in accepting the POLR charge calculation, closed its eyes to the shortcomings of the model. For instance the Commission relied upon the model despite the subjectivity of the

¹⁰⁹ Id.

¹¹⁰ OCC Ex. 11 at 11 (Medine). (Supp. 68).

¹¹¹ OCC Ex. 11 at 11 (Medine). (Supp. 62).

¹¹² Tr. XII at 256-257 (Dec. 4, 2008)(Cahaan).

¹¹³ Tr. XI at 214 (Dec. 3, 2008)(Baker).

¹¹⁴ Tr. XI at 210 (Dec. 3, 2008)(Baker).

inputs.¹¹⁵ AEP Ohio, at its sole discretion substituted its own unique inputs in lieu of the inputs required by the model.¹¹⁶ It thus was able to manipulate the results to produce what it wanted—a significant increase in POLR revenues.

Moreover, the Commission ignored the overwhelming evidence that was presented by other parties to the proceeding which contradicted the Companies' position and, without explanation, adopted only certain provisions of the model.¹¹⁷ For instance, according to the Companies' own testimony, only when AEP Ohio is subject to both the risks of customers leaving and returning does it incur the POLR risk calculated under the model.¹¹⁸ Yet, the PUCO did not consider the POLR risk to include the risk of customers returning. Nonetheless it approved ninety percent of the POLR charge produced under the model, with no explanation as to how it chose 90%. There is nothing on the record that supports the PUCO's guesstimate that of the POLR charge produced by the model, 90% of it solely relates to the risk of customers leaving. Thus, there is a mismatch between what the model produced and what the Commission was willing to accept and valued as POLR risk.

The Commission's Order also ignored the opposing parties' demonstration that the model did not consider the actual costs of providing POLR. The Commission ignored all but AEP Ohio's contrived model to impose a dramatic increase in POLR charges on AEP Ohio's customers. Similarly, the Commission's Entry on Rehearing accepted the use of AEP Ohio's

¹¹⁵ The Black-Scholes Model, OCC Ex. 11 at 8 (Medine). (Supp. 59).

¹¹⁶ OCC Ex. 11 at 15 (Medine). (Supp. 66).

¹¹⁷ (R.112 at 6-9 (Murray)). See also OCC Ex. 11 at 6-17 (Medine). (Supp. 57-68).

¹¹⁸ AEP Ohio is assuming that the option value it calculates with the Model is equal to the risk to shareholders. AEP Ohio has provided no evidence through shopping studies or the like that this is the case.

version of the model for determining the novel, POLR-related “migration risk” without addressing the merits or efficacy of the model in determining POLR risk and charges.¹¹⁹

The PUCO’s analysis of the evidence presented regarding the POLR charge was limited largely to the following: “However, we agree with the intervenors and Staff that the POLR charge as proposed by the Companies is too high, but we do not agree that there is no risk or a very minimal risk as suggested by some.”¹²⁰ The Commission’s statement is ironic. More importantly it is against the weight of the evidence.

With the exception of AEP Ohio’s proposed POLR charge derived through the use of the flawed model, all of the parties testified that there is minimal or no risk, particularly as associated with shopping. The record reflects that the risk of AEP Ohio’s customers shopping is quite low and there has been “virtually no customer switching in the last eight years.”¹²¹ Staff Witness Cahaan testified that “there are many reasons to think that substantial migration will not quickly occur, even if the market price falls below the SSO price.”¹²²

AEP Ohio’s POLR charge should reflect this minimal risk. But it does not. Its POLR charge will collect \$456 million from customers for what all parties, save AEP Ohio, believe will be minimal risk. This is unreasonable given the state of the record in the proceeding below.

In granting a POLR charge increase based on an inappropriate model, the PUCO ignores the manifest weight of the evidence produced by other parties, including the PUCO Staff¹²³ and makes a decision that amounts to mistake under *Cleveland Electric Illuminating Co.* Because the Commission’s Order contains findings that are manifestly against the weight of the evidence,

¹¹⁹ Entry on Rehearing at 26. (Appx. 120).

¹²⁰ Opinion and Order at 40. (Appx. 49).

¹²¹ (R.9). AEP Ex. 2A at 33 (Baker).

¹²² Staff Ex. 10 at 7 (Cahaan). (Supp. 54).

¹²³ Tr. XII at 254-258 (Dec. 4, 2008)(Cahaan).

the Court should reverse the Order, and set aside the POLR charge.¹²⁴ In the alternative, the Court should permit a POLR charge that is no greater than the POLR charge in current rates as determined in the Companies' Rate Stabilization Plan.¹²⁵

Proposition of Law 6: When the Public Utilities Commission of Ohio allows a utility to collect carrying charges on environmental investments in violation of R.C. 4928.143(B)(2) and R.C. 4928.38, the Commission's order should be reversed.

AEP Ohio's residential customers will have to pay approximately \$330 million in carrying charges on the Companies' environmental investments made from 2001 through 2008, according to the PUCO's Order.¹²⁶ The PUCO allowed these collections from customers which directly contravenes R.C. 4928.143(B)(2) (Appx. 707) and R.C. 4928.38 (Appx. 699). The PUCO action also was retroactive ratemaking, in violation of R.C. 1.48 (Appx. 683) and Article II, Section 28 of the Ohio Constitution (Appx. 711).

This Court uses a de novo standard of review to decide matters of law.¹²⁷ This Court has repeatedly stated that the PUCO is a creature of statute, and as such may not act beyond the authority provided under Ohio statutes.¹²⁸ As discussed below, the Court should reverse the PUCO's unlawful application of Ohio law.

¹²⁴ *Cleveland Electric Illuminating Co.*, 42 Ohio St. 2d 403, syllabus ¶4.

¹²⁵ OCC Application for Rehearing at 33. (Appx. 203).

¹²⁶ The Companies identified \$110 million—\$26 million per year from CSP customers and \$84 million per year from OP customers—in environmental-related carrying charges each year of the three-year ESP. See ESP Order at 24. (Appx. 33).

¹²⁷ *Grafton v. Ohio Edison* (1996), 77 Ohio St.3d 102, 105, 671 N.E.2d 241; *Cleveland Electric Illuminating Co. v. Public Util. Comm.* (1996), 76 Ohio St.3d 521, 523, 668 N.E.2d 889; *Industrial Energy Consumers of Ohio Power Co. v. Public Util. Comm.* (1994), 68 Ohio St.3d 559, 563, 629 N.E.2d 423.

¹²⁸ See, e.g., *Canton Storage and Transfer Co. v. Public Util. Comm.* (1995), 72 Ohio St.3d 1, 647 N.E.2d 136.

A. Carrying charges for environmental investments a utility made from 2001 through 2008 are neither costs incurred nor an expenditure made after January 1, 2009, and thus are not recoverable under R.C. 4928.143(B)(2).

In R.C. 4928.143(B)(2) (Appx. 707), the General Assembly outlined the elements of electric security plans, and specified nine components that may be included in electric security plans. The listed components evince an intent to provide parameters that limit the type of expenses permitted, despite the broad prefatory language of the section. The broad prefatory language serves to convey that there is no limit on the type of ratemaking adjustments so long as such adjustments fall within one of the enumerated components. The PUCO must also provide sufficient factual information so the Court may determine the reasonableness and lawfulness of its decision to include expenses in the ESP plan that fall outside the enumerated components of R.C. 4928.143(B)(2).¹²⁹

In the Order, the PUCO allowed the Companies to collect “the incremental capital carrying costs that will be incurred after January 1, 2009, on past environmental investments (2001-2008) that are not presently reflected in the Companies’ existing rates, as contemplated in AEP Ohio’s RSP Case.”¹³⁰ On rehearing, the Commission stated that those carrying costs “fall within the ESP period and, therefore, may be included in the ESP pursuant to the broad language of Section 4928.143(B)(2), Revised Code, permitting recovery for unenumerated expenses.”¹³¹ The PUCO, however, did not specify, in either the ESP Order or the Entry on Rehearing, which of the enumerated provisions of R.C. 4928.143(B)(2) authorized recovery of the carrying charges for past environmental investment.

¹²⁹ *Tongren v. Pub. Util. Comm.* (1999), 85 Ohio St.3d 87, 88, 706 N.E.2d 1255.

¹³⁰ ESP Order at 28. (Appx. 37).

¹³¹ Entry on Rehearing at 12. (Appx. 106).

The Commission misapplied R.C. 4928.143(B)(2). As a result, the PUCO allowed the Companies are allowed to collect from customers approximately \$330 million in environmental investment carrying charges not permitted under the statute.

R.C. 4928.143(B)(2) specifically mentions only two categories of environmentally related costs that are collectable in an electric security plan. R.C. 4928.143(B)(2)(a) allows “[a]utomatic recovery of any of the following costs of the electric distribution utility, provided the cost is prudently incurred: the cost of fuel used to generate the electricity supplied under the offer; the cost of purchased power supplied under the offer, including the cost of energy and capacity, and including purchased power acquired from an affiliate; the cost of emission allowances; and the cost of federally mandated carbon or energy taxes.” (Appx. 707). Only the latter two costs—emission allowances and federally mandated carbon or energy taxes—are environmentally related. Neither is relevant to the carrying charges for environmental investment from 2001 through 2008. Further, the section requires an after-the-fact determination as to whether the costs were prudently incurred, which the PUCO did not make.

The other environmentally related provision is R.C. 4928.143(B)(2)(b), which allows electric distribution utilities to recover “[a] reasonable allowance for construction work in progress for any of the electric distribution utility’s cost of constructing an electric generating facility or for an environmental expenditure for any electric generating facility of the electric distribution utility, provided the cost is incurred or the expenditure occurs on or after January 1, 2009.” (Appx. 707). In order to be collectable under R.C. 4928.143(B)(2)(b), environmental costs must be incurred on or after January 1, 2009, and environmental expenditures must occur on or after January 1, 2009. The carrying charges for environmental investments made from

2001 through 2009, authorized by the PUCO in the Order below, do not meet either of these statutory criteria.

First, the carrying charges were for environmental expenditures that occurred between 2001 and 2008. The carrying charges were determined in proceedings that took place before January 1, 2009. The Companies thus did not incur the carrying charges after January 1, 2009, as R.C. 4928.143(B)(2)(b) requires. Further, nothing in the record of the proceeding below shows that AEP Ohio ever sought, prior to the ESP proceeding, approval to defer recovery of the carrying charges that were not included in rates.

Second, the carrying charges themselves do not represent expenditures that the Companies may actually make after January 1, 2009. Instead, the carrying charges merely represent the cost to the Companies for the use of the capital for a certain period of time. As the Companies' witness Nelson stated, "The capital carrying cost is determined by applying an annual carrying cost rate, expressed as a percent of the capital expenditure, to the total amount spent on a capital project or projects. The carrying cost rate includes the cost of money (weighted average cost of capital), a depreciation component, an income tax component, property and other taxes component and an administrative and general component. It does not include direct O&M expenses."¹³² The carrying charges are thus nothing more than bookkeeping entries. They neither were incurred nor occurred after January 1, 2009, and as such are not collectable expenditures under R.C. 4928.143(B)(2)(b).

None of the other provisions in R.C. 4928.143(B)(2) apply to the collection of carrying charges for environmental investments made from 2001 through 2008. R.C. 4928.143(B)(2)(c)

¹³² Companies' Ex. 7 at 16 (Nelson). (Supp. 16). The Companies calculated a carrying cost rate of 5.8% for CSP and 16.38% for OP. See Companies' Ex. 1 at Exhibit DMR-2, page 8 (Roush). (Supp. 70).

allows the establishment of a surcharge for the life of an electric generating facility that is “newly used and useful on or after January 1, 2009***.” (Appx. 707). The carrying charges were not the result of an expenditure for such a facility.

R.C. 4928.143(B)(2)(d) provides for “charges relating to limitations on customer shopping for retail electric generation service, bypassability, standby, back-up, or supplemental power service, default service, carrying costs, amortization periods, and accounting or deferrals, including future recovery of such deferrals, as would have the effect of stabilizing or providing certainty regarding retail electric service.” (Appx. 708). The carrying charges allowed in the Order do not have such an effect.

R.C. 4928.143(B)(2)(e) allows for automatic increases or decreases in any component of the standard service offer price. (Appx. 708). This is not pertinent to the carrying charges at issue. R.C. 4928.143(B)(2)(f) allows for the electric distribution utility “to securitize any phase-in, inclusive of carrying charges, of the utility’s standard service offer price***.” (Appx. 708). The environmental carrying charges authorized in the Order are not for that purpose. R.C. 4928.143(B)(2)(g) addresses future costs “relating to transmission, ancillary, congestion, or any related service required for the standard service offer***.” (Appx. 708). The environmental carrying charges authorized in the Order do not qualify under this section.

R.C. 4928.143(B)(2)(h) deals with ratemaking and distribution infrastructure incentives, and R.C. 4928.143(B)(2)(i) concerns provisions regarding the implementation of economic development, job retention, and energy efficiency programs. (Appx. 708). Neither is pertinent to the collection of the environmental carrying charges authorized in the Order.

The record of the proceeding below does not show that the Companies will make any actual expenditure after January 1, 2009 related to carrying charges for the environmental

investments made from 2001 through 2008. The collection of such carrying charges is not authorized under any of the enumerated provisions of R.C. 4928.143(B)(2), and the PUCO has not explained its basis for allowing the Companies to collect these carrying charges. The PUCO thus acted beyond its statutory authority. The Court should reverse the PUCO's decision and prevent the unlawful collection of approximately \$330 million from consumers.

B. R.C. 4928.38 excludes from rates any carrying charges for environmental investments made during the market development period of the Companies' previous rate structure.

In 1999, the General Assembly established the framework for Ohio's investor-owned electric utilities to transition into a competitive marketplace. The electric utilities were allowed to receive transition revenues through, among other things, "a nonbypassable and competitively neutral transition charge *** as such transition charge is determined under section 4928.40 of the Revised Code."¹³³ R.C. 4928.40(A) required the PUCO to establish the transition charge for each customer class with the transition charges being collected during a market development period that "shall end on December 31, 2005, unless otherwise authorized under division (B)(2) of this section." (Appx. 701). AEP Ohio's market development period ended on December 31, 2005.¹³⁴

The Companies' ability to receive transition revenues ceased at the end of the market development period. R.C. 4928.38 provides, in relevant part: "The utility's receipt of transition revenues shall terminate at the end of the market development period. With the termination of that approved revenue source, the utility shall be fully on its own in the competitive market. The commission shall not authorize the receipt of transition revenues or any equivalent revenues by an electric utility except as expressly authorized in sections 4928.31 to 4928.40 of the Revised Code." (Appx. 699). This was reflected in R.C. 4928.141(A): "A standard service offer under

¹³³ R.C. 4928.37(A)(1)(b). (Appx. 697).

¹³⁴ See Companies' Ex. 7 at 9 (Nelson). (Supp. 72).

section 4928.142 or 4928.143 of the Revised Code shall exclude any previously authorized allowances for transition costs, with such exclusion being effective on and after the date that the allowance is scheduled to end under the utility's rate plan." (Appx. 703).

The PUCO's Order below, however, allowed AEP Ohio to continue receiving transition revenues, in the form of carrying charges on environmental investments made during the market development period, in violation of R.C. 4928.38. When S.B. 221 was enacted, this section was not amended or repealed. Thus, R.C. 4928.38 is still in full force and effect and cannot be countermanded by the Commission. The \$330 million in environmental costs are not lawfully recoverable.

The only transition revenues that are allowed to be collected beyond the market development period are regulatory assets.¹³⁵ The carrying charges on environmental investments made from 2001 through 2008, however, were not included as regulatory assets in the case below.¹³⁶

The collection of carrying charges on environmental investments made from 2001 through 2008 is not authorized under R.C. 4928.38. The PUCO thus acted beyond its statutory authority, and the Court should reverse the PUCO's decision.

C. By authorizing the collection of carrying charges on environmental investments made from 2001 through 2008, the Public Utilities Commission of Ohio violated statutory prohibitions against retroactive ratemaking.

In allowing the Companies to collect carrying charges on environmental investments made from 2001 through 2008, the PUCO asserted that "[t]he carrying costs on the environmental investments fall within the ESP period and, therefore, may be included in the ESP pursuant to the broad language of Section 4928.143(B)(2), Revised Code, permitting recovery

¹³⁵ See R.C. 4928.40(A). (Appx. 701).

¹³⁶ See ESP Order at 24-28. (Appx. 33-37).

for unenumerated expenses.”¹³⁷ As discussed in Sections A and B above, nothing in the record of the proceeding below supports that claim. In addition, the Companies never sought PUCO approval to defer collection of the carrying charges that were not included in rates prior to the ESP proceeding. There is a very significant difference between a cost *incurred* during the ESP and the request to recover pre-ESP costs *during* the ESP. If the Commission’s rationale were to prevail here, it would open the floodgates for all electric utilities to come back and ask to collect all sorts of costs that were not contemplated in prior settlements. It would render the terms – with respect to the costs and charges customers would be responsible for – upon which consumer and business parties alike relied on in settling cases null and void and would have a chilling effect on the ability to rely on settlements in good faith.

By including carrying charges on past environmental investments in customers’ rates under the ESP, the PUCO engaged in unauthorized retroactive ratemaking, in violation of R.C. 1.48 (Appx. 683) and Article II, Section 28 of the Ohio Constitution (Appx. 711).¹³⁸ Under R.C. 1.48, statutes in Ohio are presumed to be prospective, unless retroactivity is express, not implied. Article II, Section 28, precludes the General Assembly from passing retroactive laws except for procedural or remedial legislation.

There is no express language in R.C. 4928.143(B)(2) that would give rise to retroactive application. Indeed, the language of the statute is quite the opposite. Two sections specifically reference the costs and expenditures that occur after January 1, 2009.¹³⁹ Another refers to recovery of costs incurred “on or after that date pursuant to the standard service offer.”¹⁴⁰

¹³⁷ Entry on Rehearing at 12. (Appx. 106).

¹³⁸ For a full discussion of the law regarding retroactive ratemaking, see Section B under Proposition of Law 2.

¹³⁹ R.C. 4928.143(B)(2)(b); R.C. 4928.143(B)(2)(c). (Appx. 707).

¹⁴⁰ R.C. 4928.143(B)(2)(g). (Appx. 708).

Although it is unclear what date is referenced, the standard service offer was to begin on January 1, 2009 under R.C. 4928.141(A) (Appx. 703). Thus, the only clear expression of applicability for R.C. 4928.143(B)(2) is prospective.

Further, there is nothing remedial about R.C. 4928.143(B)(2). Nothing in the statute overturns the requirement that a standard service offer under R.C. 4928.142 or 4928.143 “shall exclude any previously authorized allowances for transition costs, with such exclusion being effective on and after the date that the allowance is scheduled to end under the utility’s rate plan.”¹⁴¹

The Court should find that the PUCO engaged in unauthorized retroactive ratemaking by including in the Companies’ service offer carrying charges for environmental expenditures made from 2001 through 2008. The PUCO’s decision should be reversed.

V. RELIEF REQUESTED

In each of the propositions of law, OCC is seeking to reverse the PUCO. In some instances (off-system sales) a remand will be necessary, with instructions to the PUCO to correct the error. All other errors will require a reversal. In order to ensure that customers are made whole, the Court should direct AEP Ohio to refund those portions of the rate increase found to be unlawful.

Generally, such refunds in the post-appellate process are not ordered in Ohio. This can be attributed to a 1958 holding of this Court, *Keco Indus. v. Cincinnati & Suburban Bell Tel. Co.*¹⁴² *Keco* prevented customers from seeking restitution for that portion of rate increases originally PUCO approved, but later found to unlawful by the Court. In *Keco* this Court foreclosed such equitable post-appellate relief, especially in light of R.C. 4903.16. The Court

¹⁴¹ R.C. 4928.141(A).

¹⁴² *Keco Indus. Inc. v. Cincinnati & Suburban Bell Tel. Co.*, 166 Ohio St. 254.

reasoned that R.C. 4903.16 established a stay as the exclusive means to seek protection during the appellate process, and the appellant in *Keco* had foregone such means.

Notwithstanding *Keco*, OCC's request for a refund should be permitted. The *Keco* principle does not apply based on the facts, law, and circumstances presented specifically in this case.

First, the balance that the Court was unwilling to interfere with, that underlie *Keco*, is not present here. In *Keco* the Court described the equities under the statutes between the utility and consumer and found a statutory balance: ““under present statutes *a utility may not charge increased rates during proceedings before the commission seeking same and losses sustained thereby may not be recouped*. Likewise, a consumer is not entitled to a refund of excessive rates paid during proceedings before the PUCO seeking a reduction in rates. Thus, while keeping its broad objectives in mind, the Legislature has attempted to keep the equities between the utility and the consumer in balance***.”¹⁴³ Here however, the PUCO has not adhered to the statutes that preclude a utility from charging increased rates during pending proceedings and recouping losses sustained during that period. Contrary to the precedent of *Keco*, the PUCO did permit the Companies to essentially recoup increased rates for losses sustained when the ESP proceeding was pending. It did so, by extending the term of the ESP back to January 1, 2009, and charging customers \$63 million for the losses sustained when continued rates, not first-authorized rates were in effect. Without the balance that was the cornerstone of *Keco*, there is a reason to conclude that *Keco* is not directly applicable and should not preclude refunds during the post-appellate process.

¹⁴³ Id. at 259 (emphasis added).

Second, the appellants in *Keco* did not seek a stay to protect their interests during the appeals process. In the case at hand, OCC took extraordinary efforts to protect customers' interests. These efforts started with an initial request for a stay at the PUCO, followed by an original action in prohibition, and a request for a stay at the Supreme Court. OCC has currently exhausted all means of seeking a remedy for customers, something the appellants in *Keco* failed to do. This is another reason to distinguish the holding of *Keco* from the case at hand.

There is also another ground to single out this case as distinguishable from *Keco*. In *Keco*, the rates were set under traditional regulation, and were in effect indefinitely until the utility chose to modify them by filing an application under R.C. 4909.18. Although the relief accorded to customers in *Keco* was prospective only-lawful rates were established on a going forward basis minus the unlawful elements-it did afford, nonetheless, some remedy, although incomplete from the customers' perspective.

Unlike the rates under review in *Keco*, here the rates are of limited duration, by the utility's choice. Under the Companies' approved ESP, the rates being reviewed by this Court will be in effect only until December 31, 2011. With the short duration of the rates, it is difficult for parties appealing to obtain a remedy for the financial harm unless refunds are permitted. Indeed in the case at hand, even with appeals being prosecuted at the earliest available time,¹⁴⁴ it is likely that 2/3 of the ESP rates will have been collected before the Court issues an opinion on the lawfulness of the PUCO's actions. And if remand is required, with further proceedings

¹⁴⁴ Several times in the proceeding below the PUCO deferred substantive rulings on applications for rehearing, by issuing Entries on rehearing for the purpose of allowing more time for review. See (R. 251, 274). Such action by the PUCO lengthens the time before an appeal can be pursued, since appeals must be filed from "final" orders, which require consideration of applications for rehearing. Indeed, although the Opinion and Order was issued on March 18, 2009, it was not until approximately eight months later that the PUCO issued a "final" order in this case, on November 4, 2009. All this time, the ESP rates approved in March were in effect and being collected from customers.

subject to the PUCO's discretion for scheduling¹⁴⁵ the prospective relief becomes even less likely. Thus, if Appellants are limited to prospective relief only under *Keco*, in the form of prospective lower rates that exclude the illegal elements, such a remedy under the specific circumstances of this appeal is practically non-existent. This situation significantly diminishes (or eliminates) for customers the value of the right of appeal that is part of the General Assembly's statutory scheme.

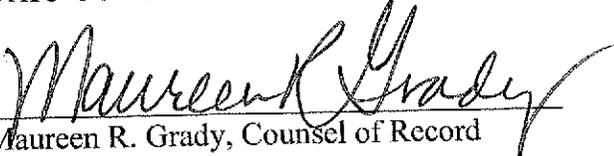
VI. CONCLUSION

As demonstrated above, the PUCO committed several errors in its Opinion and Order. OCC asks this Court to reverse the PUCO on these errors, and order a refund so that customers can be afforded a viable remedy in connection with their appellate rights established by the General Assembly. Only then will customers be afforded a remedy for the unlawful and unreasonable rates they continue to pay until the Court reverses and new rates are set reflecting appropriate reductions in rates to customers.

¹⁴⁵ See *Cleveland Electric Illuminating Co. v. Pub. Util. Comm.* (1976), 46 Ohio St.2d 105, 346 N.E.2d 778.

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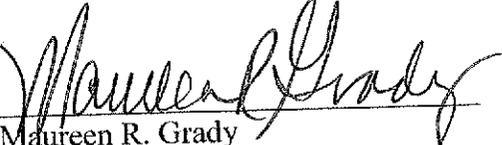
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CERTIFICATE OF SERVICE

The undersigned hereby certifies that a true and correct copy of the foregoing *Merit Brief of Appellant the Office of the Ohio Consumers' Counsel* has been served upon the below-named counsel via First Class mail, postage prepaid this 25th day of January, 2010.


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