

**In The  
Supreme Court of Ohio**

**The Ohio Energy Group,  
Industrial Energy Users-Ohio,**  
  
Appellants,  
  
and  
  
**Columbus Southern Power Company,**  
  
Cross-Appellant,  
  
v.  
  
**The Public Utilities Commission of  
Ohio,**  
  
Appellee.

Case No. 11-751  
  
On appeal from the Public Utilities  
Commission of Ohio, Case No. 10-  
1261-EL-UNC, *In the Matter of the  
Annual 2009 Filing of Columbus  
Southern Power Company and Ohio  
Power Company Required by Rule  
4901:2-35-10, Ohio Administrative  
Code.*

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**MERIT BRIEF  
SUBMITTED IN RESPONSE TO CROSS-APPEAL  
SUBMITTED ON BEHALF OF APPELLEE,  
THE PUBLIC UTILITIES COMMISSION OF OHIO**

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## TABLE OF CONTENTS

	Page	
TABLE OF AUTHORITIES .....	ii	
INTRODUCTION.....	1	
STATEMENT OF THE FACTS AND CASE.....	3	
ARGUMENT .....	4	
Proposition of Law No. I:		
A civil statute that does not implicate the First Amendment is unconstitutionally vague only where it is so vague and indefinite that it sets forth no standard or rule or if it is substantially incomprehensible. <i>Columbia Gas Transm. Corp. v. Levin</i> , 117 Ohio St. 3d 122, 130, 882 N.E.2d 400 (2008) quoting <i>Hoffman Estates v. Flipside, Hoffman Estates, Inc.</i> , 455 U.S. at 495, 102 S. Ct. 1186 (1982).....		4
Proposition of Law No. II:		
Appellant may not devise its own ratemaking formula upon appeal, but must confine its arguments to the ratemaking scheme enacted by the General Assembly. <i>Toledo Edison Co. v. Pub. Util. Comm'n</i> , 12 Ohio St. 3d 143, 146, 465 N.E.2d 886 (1984).....		11
CONCLUSION .....	13	
PROOF OF SERVICE .....	14	
APPENDIX	PAGE	
Ohio Rev. Code Ann. § 4909.15 (West 2011) .....	1	
Ohio Rev. Code Ann. § 4928.141 (West 2011) .....	4	
Ohio Rev. Code Ann. § 4928.142 (West 2011) .....	5	
Ohio Rev. Code Ann. § 4928.143 (West 2011) .....	8	

## TABLE OF AUTHORITIES

	Page(s)
<b>Cases</b>	
<i>City of Cincinnati v. Pub. Util. Comm'n</i> , 153 Ohio St. 56, 90 N.E.2d 681 (1950).....	7
<i>Cleveland Elec. Illuminating. v. Pub. Util. Comm'n</i> , 4 Ohio St. 3d 107, 447 N.E.2d 746 (1983).....	10
<i>Cleveland Electric Illuminating Co. v. Pub. Util. Comm'n</i> , 42 Ohio St. 2d 403, 300 N.E.2d 1 (1975).....	6
<i>Columbia Gas Transm. Corp. v. Levin</i> , 117 Ohio St. 3d 122, 882 N.E.2d 400 (2008).....	4, 5
<i>Consumers' Counsel v. Pub. Util. Comm'n</i> , 109 Ohio St. 3d 328 (2006).....	3
<i>Consumers' Counsel v. Pub. Util. Comm'n</i> , 6 Ohio St. 3d 405, 453 N.E.2d 584 (1983).....	6
<i>Consumers' Counsel v. Pub. Util. Comm'n</i> , 64 Ohio St. 2d 71, 413 N.E.2d 799 (1980).....	7
<i>Dayton Power and Light Co. v. Pub. Util. Comm'n</i> , 61 Ohio St. 2d 215, 400 N.E.2d 396 (1980).....	6
<i>Gen. Tel. Co. of Ohio v. Pub. Util. Comm'n</i> , 46 Ohio St. 2d 281, 348 N.E.2d 339 (1976).....	6
<i>Gen. Tel. Co. Of Ohio v. Pub. Util. Comm'n</i> , 46 Ohio St. 2d 281, 348 N.E.2d 339 (1976).....	7
<i>Hoffman Estates v. Flipside, Hoffman Estates, Inc.</i> , 455 U.S. at 495, 102 S. Ct. 1186 (1982).....	4
<i>In re Columbus Southern Power</i> , 128 Ohio St. 3d 512, 947 N.E.2d 655 (2011).....	10
<i>Norwood v. Horney</i> , 110 Ohio St. 3d 353, 853 N.E.2d 1115 (2006).....	9

**TABLE OF AUTHORITIES (cont'd)**

**Page(s)**

*Ohio Bell Telephone Co. v. Pub. Util. Comm'n*, 106 Ohio St. 266, 139 N.E. 857 (1922)..... 7

*Toledo Edison Co. v. Pub. Util. Comm'n*, 12 Ohio St. 3d 143, 465 N.E.2d 886 (1984)..... 11

**Statutes**

Ohio Rev. Code Ann. § 4909.15 (West 2011) ..... 5

Ohio Rev. Code Ann. § 4928.141 (West 2011) ..... 3

Ohio Rev. Code Ann. § 4928.142 (West 2011) ..... 3, 11

Ohio Rev. Code Ann. § 4928.143 (West 2011) ..... *passim*

**Other Authorities**

*In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Administration of the Significantly Excessive Earnings Test under Section 4928.143(F), Revised Code, and Rule 4901:1-35-10, Ohio Administrative Code, Case No. 10-1261-EL-UNC (Opinion and Order) (January 11, 2011)*..... 6, 8, 9, 12

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**INTRODUCTION**

The General Assembly has given electric utilities a choice. A company can meet its obligation to provide a standard service offer in one of two ways. It could either hold an auction to obtain the needed power or it could enter into a negotiated arrangement

called an electric security plan (ESP). An ESP provides greater flexibility for a utility,<sup>1</sup> including automatic recovery of a variety of costs, CWIP for new plants, non-bypassable charges for completed plants, securitization, rate decoupling, and even the ability to adjust distribution rates to improve the company's infrastructure. Nothing is free in life and the ESP is no exception. The ESP comes with a significant statutory condition – the company's earnings are subject to annual review (SEET), and, if found to be significantly excessive, are to be credited back to customers.

Cross-Appellant (American Electric Power or AEP) voluntarily made its choice. It picked an ESP. Now it wants this Court to change the deal that it chose to make. Having obtained the various benefits of the ESP plan, it now wants the Court to void the annual review condition as "vague." AEP takes the statute as it finds it. It cannot accept the benefits and avoid the burdens. If AEP had concerns about the ESP statute, it should have chosen the auction. It did not. AEP voluntarily chose to file for an ESP.

The SEET is not vague; AEP simply does not like the result of its application. AEP asks this Court to take the place of the General Assembly, to create a new, third option for it, an ESP without an annual review. The request is baseless and the Commission should be affirmed.

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<sup>1</sup> ESPs are beneficial to ratepayers as well; in fact they must be superior to the auction to be approved by the Commission. Ohio Rev. Code Ann. § 4928.143(C)(1) (West 2011), App. at 10-11. (Hereinafter references to appellee's appendix attached hereto are denoted "App. at \_\_\_," and references to appellee's supplement are denoted "Supp. at \_\_\_.")

## STATEMENT OF THE FACTS AND CASE

Electric utilities have long had an obligation to serve. Indeed this obligation is one of the defining features that make an entity a public utility. When the General Assembly sought to restructure the style of regulation in the industry in 1999, it preserved this requirement through a now repealed code section which required both a negotiated standard service offer and an opportunity to buy power at a price determined through competitive means. See discussion in *Consumers' Counsel v. Pub. Util. Comm'n*, 109 Ohio St. 3d 328, 333 (2006). More recently, when the General Assembly again altered the form of regulation in the electric industry, it replaced this provision with R.C. 4928.142 and 4928.143 and offered the utility the choice of meeting its obligation to serve through either section. Ohio Rev. Code Ann. § 4928.141(A) (West 2011), App. at 4-5.

On July 31, 2008, AEP, acting for its operating subsidiaries Ohio Power Company and Columbus Southern Power Company, made its choice. It sought the approval of an ESP. The Commission ultimately granted its approval in March 2009. Although that approval has been subject to a variety of legal challenges subsequently, the ESP remains in force and AEP has enjoyed the benefits of it to the current date.

After two procedural extensions, the instant case was initiated with a filing by Cross Appellant for review pursuant to R.C. 4928.143(F) on September 1, 2010. A large number of parties intervened. A hearing was held where the testimony of six witnesses on direct and rebuttal was offered. Briefs and Reply briefs were submitted. The Com-

mission issued its decision by opinion and order dated January 11, 2011 and entry on rehearing dated March 9, 2011. Appeals and this cross appeal were taken subsequently.

## ARGUMENT

### Proposition of Law No. I:

**A civil statute that does not implicate the First Amendment is unconstitutionally vague only where it is so vague and indefinite that it sets forth no standard or rule or if it is substantially incomprehensible. *Columbia Gas Transm. Corp. v. Levin*, 117 Ohio St. 3d 122, 130, 882 N.E.2d 400 (2008) quoting *Hoffman Estates v. Flipside, Hoffman Estates, Inc.*, 455 U.S. at 495, 102 S. Ct. 1186 (1982).**

The cross-appellant claims that Ohio Revised Code Section 4928.143(F) is unconstitutionally vague. AEP comes to this conclusion rather late. Having enjoyed the various significant benefits of R.C. 4928.143, it now wishes to avoid the one portion of the section it does not like, the SEET. It attempts to manufacture a constitutional claim as a way to do so.

This Court has noted the steep difficulty confronting those who make such claims.

It has stated:

A court's power to invalidate a statute "is a power to be exercised only with great caution and in the clearest of cases." Laws are entitled to a "strong presumption of constitutionality," and the party challenging the constitutionality of a law "bears the burden of proving that the law is unconstitutional beyond a reasonable doubt." *Yajnik v. Akron Dept. of Health, Hous. Div.*, 101 Ohio St. 3d 106, 802 N.E.2d 632, ¶ 16

(2004); *Buckley v. Wilkins*, 105 Ohio St. 3d 350, 826 N.E.2d 811, ¶ 18 (2005).

*Columbia Gas Transm. Corp. v. Levin*, 117 Ohio St. 3d 122, 130 882 N.E.2d 400 (2008).

AEP has not and cannot meet this standard. R.C. 4928.143(F) is not vague.

The relevant portion of the statute is:

...the commission shall consider, following the end of each annual period of the plan, if any such adjustments resulted in excessive earnings as measured by whether the earned return on common equity of the electric distribution utility is significantly in excess of the return on common equity that was earned during the same period by publicly traded companies, including utilities, that face comparable business and financial risk, with such adjustments for capital structure as may be appropriate.

Ohio Rev. Code Ann. § 4928.143(F) (West 2011), App. at 12. The statute delineates the test to be applied. Examining each component of the test reveals that the test is quite clear. While the SEET is new, the decisions that must be made by the Commission to implement it are of the type and kind that the Commission has routinely made for decades.

The term “earned return on common equity” is easily understood. The Commission has long been making return on equity determinations. This is a necessary aspect of traditional ratemaking under R.C. 4909.15. The return on equity is a component of the overall rate of return which statutorily the Commission must determine in every rate increase proceeding. See, *Ohio Edison Co. v. Pub. Util. Comm'n*, 63 Ohio St. 3d 555, 561 (1992). Additionally, the calculation required by the statute is simpler than what the Commission has traditionally be required to perform. As this analysis is historic, the

earnings and equity values are simply reported and the “earned return on common equity” is just the quotient of them. This calculation is not controversial. *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Administration of the Significantly Excessive Earnings Test under Section 4928.143(F), Revised Code, and Rule 4901:1-35-10, Ohio Administrative Code*, Case No. 10-1261-EL-UNC (hereinafter *In re AEP SEET*) (Opinion and Order 21-22) (January 11, 2011), Supp. at 21-22.

Determining a group of companies “. . . that face comparable business and financial risk,” is likewise. The Commission has long been presented with arguments founded in comparisons between a specific utility and others. *See, Dayton Power and Light Co. v. Pub. Util. Comm’n*, 61 Ohio St. 2d 215, 216, 400 N.E.2d 396 (1980) (group of nominally comparable utilities), *Gen. Tel. Co. of Ohio v. Pub. Util. Comm’n*, 46 Ohio St. 2d 281, 284, 348 N.E.2d 339 (1976) (comparison to another company), *Cleveland Electric Illuminating Co. v. Pub. Util. Comm’n*, 42 Ohio St. 2d 403, 407, 300 N.E.2d 1 (1975) (comparable group of utilities), *Consumers’ Counsel v. Pub. Util. Comm’n*, 6 Ohio St. 3d 405, 453 N.E.2d 584 (1983) (use of aggregate utility indices). This is simply a factual matter to be decided by the Commission based upon evidence presented.

The Commission must also distinguish between “excessive” and “significantly excessive.” R.C. 4928.143(F) does not contain an explicit formula for calculating “significantly.” This is not problematic. It simply reflects the General Assembly’s delegation to the Commission of discretion. It is directly analogous to that given to the

Commission regarding rate of return determination in rate cases about which this Court has said:

By omitting a specific formula in R.C. 4909.15 for determining an appropriate rate of return, the General Assembly has vested the commission with broad discretion. Similarly, this court has consistently deferred to the expertise of the commission in determining an appropriate rate of return unless such determination is “manifestly against the weight of the evidence and . . . so clearly unsupported by the record as to show misapprehension or mistake or willful disregard of duty.”

Limited judicial review of a rate of return determination is sound for reason that while “cost of capital analyses . . . have an aura of precision about them, . . . they are fraught with judgments and assumptions.”

*Consumers' Counsel v. Pub. Util. Comm'n*, 64 Ohio St. 2d 71, 79, 413 N.E.2d 799 (1980) (citations omitted). The Court should likewise defer to the Commission's judgment here.

Making this sort of factual judgment is fundamental to what the Commission does and has done for years. Distinguishing between reasonable and unreasonable, deciding how much is enough and how much is too much, is the Commission's job and always has been. As early as 1922 the Commission was distinguishing between reasonable and excessive rates of return. *Ohio Bell Telephone Co. v. Pub. Util. Comm'n*, 106 Ohio St. 266, 139 N.E. 857 (1922). It has continued. *Gen. Tel. Co. Of Ohio v. Pub. Util. Comm'n*, 46 Ohio St. 2d 281, 348 N.E.2d 339 (1976); *City of Cincinnati v. Pub. Util. Comm'n*, 153 Ohio St. 56, 90 N.E.2d 681 (1950). As the Commission found;

Moreover, the fact that there may be disagreement about how to define and apply this benchmark is not new. Parties frequently present the Commission with different views about a utility's return on common equity. The Commission has extensive experience adjudicating this issue. Utility regulation is not so mechanical that it can be performed without any expert judgment. The General Assembly has directed the Commission to utilize its experience and technical expertise in deciding a broad range of ratemaking issues. We do not find this issue to be fundamentally different from those which the Commission regularly decides under Ohio's statutory provisions for utility regulation. For these reasons, we find that Section 4928.143(F), Revised Code, provides sufficiently definitive guidance to the Commission to conduct the SEET.

*In re AEP SEET* (Opinion and Order at 10) (January 11, 2011), Supp. at 10. There is no vagueness. The statute requires the Commission to exercise its judgment to decide how much is too much, just as it has done for decades.

AEP complains that R.C. 4928.143(F) provides the Commission with no guidance.

This is not the case. As the Commission stated:

Contrary to AEP-Ohio's argument. Section 4928.143(F), Revised Code, provides a clear benchmark for identifying "excessive earnings." For example, the statute defines earnings as excessive "as measured by whether the earned return on common equity of the electric utility is significantly in excess of the return on common equity that was earned during the same period by publicly traded companies, including utilities, that face comparable business and financial risk." Additionally, the statute directs the Commission to make "such adjustments for capital structure as may be appropriate." Further, the Commission is to consider "the capital requirements of future committed investments in this state." Finally, the Commission is directed to "not consider, directly or indirectly, the revenue, expenses, or earnings of any affiliate or parent company." These concepts are not new or novel and have been traditionally applied in the regulatory rate-

making process. *Federal Power Commission v. Hope Natural Gas Co.*, (1944), 320 U.S. 591.

*Id.* Not only is the Commission tasked under R.C. 4928.143(F) with making the same sorts of decisions it always has, it is actually given *more* guidance from the General Assembly than it had under the traditional rate setting statutes. Appellant's argument has no weight.

Appellant claims that R.C. 4928.143(F) is void because it does not give AEP fair notice of what actions it must take or avoid and it results in the taking of private property, citing *Norwood v. Horney*, 110 Ohio St. 3d 353, 853 N.E.2d 1115 (2006). This argument underscores AEP's misunderstanding of the situation presented under R.C. 4928.143. There is no action that AEP could take or avoid. R.C. 4928.143(F) is directed at the *Commission*. The directives are made to *the Commission*. The statute needs to be clear enough that the *Commission* can understand it and it is clear as discussed above. The SEET is a comparison between the achieved earnings of the utility and those of other companies. There is no action that AEP could take to control the outcome. R.C. 4928.143(F) passes the *Norwood* test because the Commission has fair notice of what is required.

Likewise there is no taking of private property. The earnings a company achieves pursuant to an ESP are provisional and retaining them is conditioned on the SEET outcome. ~~The same statute that allows those earnings requires the SEET review of the~~ earnings. You cannot have the one without the other. The SEET is in the nature of a true-up, not a penalty. Such true-up mechanisms are common in the utility arena. In fact,

the ESP under review in this case contains just such a mechanism, called the fuel adjustment component or FAC. The FAC has been reviewed by this Court, *In re Columbus Southern Power*, 128 Ohio St. 3d 512, 526, 947 N.E.2d 655 (2011). True-up mechanisms were used to collect fuel costs by electric utilities for many years and are still used to collect gas costs by natural gas companies. The earnings received because of the ESP do not ultimately belong to the company until after the review under the SEET. That is simply one of the statutory conditions upon which the availability of the ESP is conditioned. In *Norwood*, the property in question was owned previously and the local government was attempting to take the property. That situation is entirely different.

AEP misunderstands the test for confiscation of utility property in any event. As this Court has noted, the constitutional standard in the utility arena is:

. . . *Per se* confiscation in a utility rate case may exist as an abstract premise, but the constitutional cases make it clear that a successful challenge must demonstrate that the rate order when reviewed in its entirety falls outside the “broad zone of reasonableness” and the “heavy burden” of establishing unreasonableness must be borne by the challenger.

\* \* \*

. . . The rule is clear: “. . . If the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry . . . is at an end. . . .” Moreover, the Constitution imposes no methodological strictures on ratemaking authorities.

*Cleveland Elec. Illuminating v. Pub. Util. Comm’n*, 4 Ohio St. 3d 107, 109, 447 N.E.2d 746 (1983) (citations omitted). The Commission’s decision below easily meets this test.

Appellant has not merely earned the same as other similarly risky companies, it has

earned more. AEP retains earnings under the plan that are excessive. It has been required to return only that portion of those earnings that is "significantly" excessive. A constitutional claim of taking could only arise where the company was required to provide service at the other end of the scale, that is to say where its returns were very low.

In sum, R.C. 4928.143(F) is not vague. The section provides the Commission with clear guidelines to preform an analysis very similar to those done by the Commission for years. It contains a sufficient standard and is comprehensible. Utility property is not taken, rather the Commission is simply charged to true-up the results of an ESP to prevent unintended large windfalls. The Commission order should be affirmed.

**Proposition of Law No. II:**

**Appellant may not devise its own ratemaking formula upon appeal, but must confine its arguments to the rate-making scheme enacted by the General Assembly. *Toledo Edison Co. v. Pub. Util. Comm'n*, 12 Ohio St. 3d 143, 146, 465 N.E.2d 886 (1984).**

Appellant must take the law as it finds it. It had a choice. It could have met its obligation to provide a standard service offer in either of two ways, either an ESP under R.C. 4928.143 or an auction under R.C. 4928.142. It chose an ESP. An ESP is complex and multi-faceted and offers a utility many advantages, but it also contains significant protections for the public including the SEET. This test is integral to the ESP. As the Commission stated:

The Commission also determines that Section 4928.143(F), Revised Code, is part of a comprehensive regulatory framework for setting rates under the provisions of S.B. 221. S.B. 221 created an approach to establishing ESP rates with significant regulatory flexibility including flexibility in what the utility may propose, a scope that may include distribution as well as generation charges and the option for the utility to withdraw any rate plan modified by the Commission. *The SEET examination included in S.B. 221 provides a check to this flexible approach.*

*In re AEP SEET* (Opinion and Order at 9-10) (January 11, 2011), Supp. at 9-10 (emphasis added). You cannot have an ESP without the SEET. To do so would destroy the fundamental balance that the General Assembly established. AEP's argument would have this Court judicially establish and impose a third mechanism for a utility to meet its standard service obligation, an ESP without the SEET check. This is not a reasonable outcome. The decision in this case shows that the SEET is vital to protect the interests of consumers. AEP did have significantly excessive earnings under its ESP. Customers were charged too much.<sup>2</sup> They are entitled to get the benefit of that overcharge back. That is how the statute is intended to work.

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<sup>2</sup> This is not to suggest the AEP did anything wrongly. AEP did not. It merely charged the rates that were authorized.

## CONCLUSION

R.C. 4928.143(F) is clear. The Commission is directed to determine whether electric utilities with ESPs have significantly excessive earnings compared to similarly risky companies. The Commission is provided with sufficient guidance from the General Assembly as to how to accomplish this task. The Commission has long experience in making just these sorts of valuations. Appellant asks this Court to upset the balance that the General Assembly struck in the statute and judicially create an unbalanced ESP lacking in the vital SEET check. This very case shows the danger of such an unreasonable outcome. The public interest requires the protection and balance offered by the SEET. The Commission's decision should be affirmed.

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## PROOF OF SERVICE

I hereby certify that a true copy of the foregoing **Merit Brief in Response to Cross-Appeal**, submitted on behalf of appellee, the Public Utilities Commission of Ohio, was served by regular U.S. mail, postage prepaid, or hand-delivered, upon the following parties of record, this 14<sup>th</sup> day of November, 2011.



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# APPENDIX

**APPENDIX  
TABLE OF CONTENTS**

**Page**

Ohio Rev. Code Ann. § 4909.15 (West 2011) .....	1
Ohio Rev. Code Ann. § 4928.141 (West 2011) .....	4
Ohio Rev. Code Ann. § 4928.142 (West 2011) .....	5
Ohio Rev. Code Ann. § 4928.143 (West 2011) .....	8

## **§ 4909.15. Fixation of reasonable rate**

(A) The public utilities commission, when fixing and determining just and reasonable rates, fares, tolls, rentals, and charges, shall determine:

(1) The valuation as of the date certain of the property of the public utility used and useful or, with respect to a natural gas company, projected to be used and useful as of the date certain, in rendering the public utility service for which rates are to be fixed and determined. The valuation so determined shall be the total value as set forth in division (C)(8) of section 4909.05 of the Revised Code, and a reasonable allowance for materials and supplies and cash working capital as determined by the commission.

The commission, in its discretion, may include in the valuation a reasonable allowance for construction work in progress but, in no event, may such an allowance be made by the commission until it has determined that the particular construction project is at least seventy-five per cent complete.

In determining the percentage completion of a particular construction project, the commission shall consider, among other relevant criteria, the per cent of time elapsed in construction; the per cent of construction funds, excluding allowance for funds used during construction, expended, or obligated to such construction funds budgeted where all such funds are adjusted to reflect current purchasing power; and any physical inspection performed by or on behalf of any party, including the commission's staff.

A reasonable allowance for construction work in progress shall not exceed ten per cent of the total valuation as stated in this division, not including such allowance for construction work in progress.

Where the commission permits an allowance for construction work in progress, the dollar value of the project or portion thereof included in the valuation as construction work in progress shall not be included in the valuation as plant in service until such time as the total revenue effect of the construction work in progress allowance is offset by the total revenue effect of the plant in service exclusion. Carrying charges calculated in a manner similar to allowance for funds used during construction shall accrue on that portion of the project in service but not reflected in rates as plant in service, and such accrued carrying charges shall be included in the valuation of the property at the conclusion of the offset period for purposes of division (C)(8) of section 4909.05 of the Revised Code.

From and after April 10, 1985, no allowance for construction work in progress as it relates to a particular construction project shall be reflected in rates for a period exceeding forty-eight consecutive months commencing on the date the initial rates reflecting such allowance become effective, except as otherwise provided in this division.

The applicable maximum period in rates for an allowance for construction work in progress as it relates to a particular construction project shall be tolled if, and to the extent, a delay in the in-service date of the project is caused by the action or inaction of any federal, state, county, or

municipal agency having jurisdiction, where such action or inaction relates to a change in a rule, standard, or approval of such agency, and where such action or inaction is not the result of the failure of the utility to reasonably endeavor to comply with any rule, standard, or approval prior to such change.

In the event that such period expires before the project goes into service, the commission shall exclude, from the date of expiration, the allowance for the project as construction work in progress from rates, except that the commission may extend the expiration date up to twelve months for good cause shown.

In the event that a utility has permanently canceled, abandoned, or terminated construction of a project for which it was previously permitted a construction work in progress allowance, the commission immediately shall exclude the allowance for the project from the valuation.

In the event that a construction work in progress project previously included in the valuation is removed from the valuation pursuant to this division, any revenues collected by the utility from its customers after April 10, 1985, that resulted from such prior inclusion shall be offset against future revenues over the same period of time as the project was included in the valuation as construction work in progress. The total revenue effect of such offset shall not exceed the total revenues previously collected.

In no event shall the total revenue effect of any offset or offsets provided under division (A)(1) of this section exceed the total revenue effect of any construction work in progress allowance.

(2) A fair and reasonable rate of return to the utility on the valuation as determined in division (A)(1) of this section;

(3) The dollar annual return to which the utility is entitled by applying the fair and reasonable rate of return as determined under division (A)(2) of this section to the valuation of the utility determined under division (A)(1) of this section;

(4) The cost to the utility of rendering the public utility service for the test period used for the determination under division (C)(1) of this section, less the total of any interest on cash or credit refunds paid, pursuant to section 4909.42 of the Revised Code, by the utility during the test period.

(a) Federal, state, and local taxes imposed on or measured by net income may, in the discretion of the commission, be computed by the normalization method of accounting, provided the utility maintains accounting reserves that reflect differences between taxes actually payable and taxes on a normalized basis, provided that no determination as to the treatment in the rate-making process of such taxes shall be made that will result in loss of any tax depreciation or other tax benefit to which the utility would otherwise be entitled, and further provided that such tax benefit as redounds to the utility as a result of such a computation may not be retained by the company, used to fund any dividend or distribution, or utilized for any purpose other than the defrayal of the operating expenses of the utility and the defrayal of the expenses of the utility in connection with construction work.

(b) The amount of any tax credits granted to an electric light company under section 5727.391 of the Revised Code for Ohio coal burned prior to January 1, 2000, shall not be retained by the company, used to fund any dividend or distribution, or utilized for any purposes other than the defrayal of the allowable operating expenses of the company and the defrayal of the allowable expenses of the company in connection with the installation, acquisition, construction, or use of a compliance facility. The amount of the tax credits granted to an electric light company under that section for Ohio coal burned prior to January 1, 2000, shall be returned to its customers within three years after initially claiming the credit through an offset to the company's rates or fuel component, as determined by the commission, as set forth in schedules filed by the company under section 4905.30 of the Revised Code. As used in division (A)(4) (b) of this section, "compliance facility" has the same meaning as in section 5727.391 of the Revised Code.

(B) The commission shall compute the gross annual revenues to which the utility is entitled by adding the dollar amount of return under division (A)(3) of this section to the cost, for the test period used for the determination under division (C)(1) of this section, of rendering the public utility service under division (A)(4) of this section.

(C)(1) Except as provided in division (D) of this section, the revenues and expenses of the utility shall be determined during a test period. The utility may propose a test period for this determination that is any twelve-month period beginning not more than six months prior to the date the application is filed and ending not more than nine months subsequent to that date. The test period for determining revenues and expenses of the utility shall be the test period proposed by the utility, unless otherwise ordered by the commission.

(2) The date certain shall be not later than the date of filing, except that it shall be, for a natural gas company, not later than the end of the test period.

(D) A natural gas company may propose adjustments to the revenues and expenses to be determined under division (C)(1) of this section for any changes that are, during the test period or the twelve-month period immediately following the test period, reasonably expected to occur. The natural gas company shall identify and quantify, individually, any proposed adjustments. The commission shall incorporate the proposed adjustments into the determination if the adjustments are just and reasonable.

(E) When the commission is of the opinion, after hearing and after making the determinations under divisions (A) and (B) of this section, that any rate, fare, charge, toll, rental, schedule, classification, or service, or any joint rate, fare, charge, toll, rental, schedule, classification, or service rendered, charged, demanded, exacted, or proposed to be rendered, charged, demanded, or exacted, is, or will be, unjust, unreasonable, unjustly discriminatory, unjustly preferential, or in violation of law, that the service is, or will be, inadequate, or that the maximum rates, charges, tolls, or rentals chargeable by any such public utility are insufficient to yield reasonable compensation for the service rendered, and are unjust and unreasonable, the commission shall:

(1) With due regard among other things to the value of all property of the public utility actually used and useful for the convenience of the public as determined under division (A)(1) of this section, excluding from such value the value of any franchise or right to own, operate, or enjoy

the same in excess of the amount, exclusive of any tax or annual charge, actually paid to any political subdivision of the state or county, as the consideration for the grant of such franchise or right, and excluding any value added to such property by reason of a monopoly or merger, with due regard in determining the dollar annual return under division (A)(3) of this section to the necessity of making reservation out of the income for surplus, depreciation, and contingencies, and;

(2) With due regard to all such other matters as are proper, according to the facts in each case,

(a) Including a fair and reasonable rate of return determined by the commission with reference to a cost of debt equal to the actual embedded cost of debt of such public utility,

(b) But not including the portion of any periodic rental or use payments representing that cost of property that is included in the valuation report under divisions (C)(4) and (5) of section 4909.05 of the Revised Code, fix and determine the just and reasonable rate, fare, charge, toll, rental, or service to be rendered, charged, demanded, exacted, or collected for the performance or rendition of the service that will provide the public utility the allowable gross annual revenues under division (B) of this section, and order such just and reasonable rate, fare, charge, toll, rental, or service to be substituted for the existing one. After such determination and order no change in the rate, fare, toll, charge, rental, schedule, classification, or service shall be made, rendered, charged, demanded, exacted, or changed by such public utility without the order of the commission, and any other rate, fare, toll, charge, rental, classification, or service is prohibited.

(F) Upon application of any person or any public utility, and after notice to the parties in interest and opportunity to be heard as provided in Chapters 4901., 4903., 4905., 4907., 4909., 4921., and 4923. of the Revised Code for other hearings, has been given, the commission may rescind, alter, or amend an order fixing any rate, fare, toll, charge, rental, classification, or service, or any other order made by the commission. Certified copies of such orders shall be served and take effect as provided for original orders.

#### **§ 4928.141. Distribution utility to provide standard service offer**

(A) Beginning January 1, 2009, an electric distribution utility shall provide consumers, on a comparable and nondiscriminatory basis within its certified territory, a standard service offer of all competitive retail electric services necessary to maintain essential electric service to consumers, including a firm supply of electric generation service. To that end, the electric distribution utility shall apply to the public utilities commission to establish the standard service offer in accordance with section 4928.142 or 4928.143 of the Revised Code and, at its discretion, may apply simultaneously under both sections, except that the utility's first standard service offer application at minimum shall include a filing under section 4928.143 of the Revised Code. 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; and that standard service offer shall serve as the utility's default standard service offer for the purpose of section 4928.14 of the Revised Code. Notwithstanding the foregoing

provision, 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, and, as applicable, pursuant to division (D) of section 4928.143 of the Revised Code, any rate plan that extends beyond December 31, 2008, shall continue to be in effect for the subject electric distribution utility for the duration of the plan's term. A standard service offer under 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.

(B) The commission shall set the time for hearing of a filing under section 4928.142 or 4928.143 of the Revised Code, send written notice of the hearing to the electric distribution utility, and publish notice in a newspaper of general circulation in each county in the utility's certified territory. The commission shall adopt rules regarding filings under those sections.

#### **§ 4928.142. Standard generation service offer price - competitive bidding**

(A) For the purpose of complying with section 4928.141 of the Revised Code and subject to division (D) of this section and, as applicable, subject to the rate plan requirement of division (A) of section 4928.141 of the Revised Code, an electric distribution utility may establish a standard service offer price for retail electric generation service that is delivered to the utility under a market-rate offer.

(1) The market-rate offer shall be determined through a competitive bidding process that provides for all of the following:

(a) Open, fair, and transparent competitive solicitation;

(b) Clear product definition;

(c) Standardized bid evaluation criteria;

(d) Oversight by an independent third party that shall design the solicitation, administer the bidding, and ensure that the criteria specified in division (A)(1)(a) to (c) of this section are met;

(e) Evaluation of the submitted bids prior to the selection of the least-cost bid winner or winners. No generation supplier shall be prohibited from participating in the bidding process.

(2) ~~The public utilities commission shall modify rules, or adopt new rules as necessary, concerning the conduct of the competitive bidding process and the qualifications of bidders, which rules shall foster supplier participation in the bidding process and shall be consistent with the requirements of division (A)(1) of this section.~~

(B) Prior to initiating a competitive bidding process for a market-rate offer under division (A) of this section, the electric distribution utility shall file an application with the commission. An electric distribution utility may file its application with the commission prior to the effective date of the commission rules required under division (A)(2) of this section, and, as the commission determines necessary, the utility shall immediately conform its filing to the rules upon their taking effect. An application under this division shall detail the electric distribution utility's proposed compliance with the requirements of division (A)(1) of this section and with commission rules under division (A)(2) of this section and demonstrate that all of the following requirements are met:

(1) The electric distribution utility or its transmission service affiliate belongs to at least one regional transmission organization that has been approved by the federal energy regulatory commission; or there otherwise is comparable and nondiscriminatory access to the electric transmission grid.

(2) Any such regional transmission organization has a market-monitor function and the ability to take actions to identify and mitigate market power or the electric distribution utility's market conduct; or a similar market monitoring function exists with commensurate ability to identify and monitor market conditions and mitigate conduct associated with the exercise of market power.

(3) A published source of information is available publicly or through subscription that identifies pricing information for traded electricity on- and off-peak energy products that are contracts for delivery beginning at least two years from the date of the publication and is updated on a regular basis. The commission shall initiate a proceeding and, within ninety days after the application's filing date, shall determine by order whether the electric distribution utility and its market-rate offer meet all of the foregoing requirements. If the finding is positive, the electric distribution utility may initiate its competitive bidding process. If the finding is negative as to one or more requirements, the commission in the order shall direct the electric distribution utility regarding how any deficiency may be remedied in a timely manner to the commission's satisfaction; otherwise, the electric distribution utility shall withdraw the application. However, if such remedy is made and the subsequent finding is positive and also if the electric distribution utility made a simultaneous filing under this section and section 4928.143 of the Revised Code, the utility shall not initiate its competitive bid until at least one hundred fifty days after the filing date of those applications.

(C) Upon the completion of the competitive bidding process authorized by divisions (A) and (B) of this section, including for the purpose of division (D) of this section, the commission shall select the least-cost bid winner or winners of that process, and such selected bid or bids, as prescribed as retail rates by the commission, shall be the electric distribution utility's standard service offer unless the commission, by order issued before the third calendar day following the conclusion of the competitive bidding process for the market rate offer, determines that one or more of the following criteria were not met:

(1) Each portion of the bidding process was oversubscribed, such that the amount of supply bid upon was greater than the amount of the load bid out.

(2) There were four or more bidders.

(3) At least twenty-five per cent of the load is bid upon by one or more persons other than the electric distribution utility. All costs incurred by the electric distribution utility as a result of or related to the competitive bidding process or to procuring generation service to provide the standard service offer, including the costs of energy and capacity and the costs of all other products and services procured as a result of the competitive bidding process, shall be timely recovered through the standard service offer price, and, for that purpose, the commission shall approve a reconciliation mechanism, other recovery mechanism, or a combination of such mechanisms for the utility.

(D) The first application filed under this section by an electric distribution utility that, as of July 31, 2008, directly owns, in whole or in part, operating electric generating facilities that had been used and useful in this state shall require that a portion of that utility's standard service offer load for the first five years of the market rate offer be competitively bid under division (A) of this section as follows: ten per cent of the load in year one, not more than twenty per cent in year two, thirty per cent in year three, forty per cent in year four, and fifty per cent in year five. Consistent with those percentages, the commission shall determine the actual percentages for each year of years one through five. The standard service offer price for retail electric generation service under this first application shall be a proportionate blend of the bid price and the generation service price for the remaining standard service offer load, which latter price shall be equal to the electric distribution utility's most recent standard service offer price, adjusted upward or downward as the commission determines reasonable, relative to the jurisdictional portion of any known and measurable changes from the level of any one or more of the following costs as reflected in that most recent standard service offer price:

(1) The electric distribution utility's prudently incurred cost of fuel used to produce electricity;

(2) Its prudently incurred purchased power costs;

(3) Its prudently incurred costs of satisfying the supply and demand portfolio requirements of this state, including, but not limited to, renewable energy resource and energy efficiency requirements;

(4) Its costs prudently incurred to comply with environmental laws and regulations, with consideration of the derating of any facility associated with those costs. In making any adjustment to the most recent standard service offer price on the basis of costs described in division (D) of this section, the commission shall include the benefits that may become available to the electric distribution utility as a result of or in connection with the costs included in the adjustment, including, but not limited to, the utility's receipt of emissions credits or its receipt of tax benefits or of other benefits, and, accordingly, the commission may impose such conditions on the adjustment to ensure that any such benefits are properly aligned with the associated cost responsibility. The commission shall also determine how such adjustments will affect the electric distribution utility's return on common equity that may be achieved by those adjustments. The commission shall not apply its consideration of the return on common equity to reduce any adjustments authorized under this division unless the adjustments will cause the electric distribution utility to earn a

return on common equity that is significantly in excess of the return on common equity that is earned by publicly traded companies, including utilities, that face comparable business and financial risk, with such adjustments for capital structure as may be appropriate. The burden of proof for demonstrating that significantly excessive earnings will not occur shall be on the electric distribution utility. Additionally, the commission may adjust the electric distribution utility's most recent standard service offer price by such just and reasonable amount that the commission determines necessary to address any emergency that threatens the utility's financial integrity or to ensure that the resulting revenue available to the utility for providing the standard service offer is not so inadequate as to result, directly or indirectly, in a taking of property without compensation pursuant to Section 19 of Article I, Ohio Constitution. The electric distribution utility has the burden of demonstrating that any adjustment to its most recent standard service offer price is proper in accordance with this division.

(E) Beginning in the second year of a blended price under division (D) of this section and notwithstanding any other requirement of this section, the commission may alter prospectively the proportions specified in that division to mitigate any effect of an abrupt or significant change in the electric distribution utility's standard service offer price that would otherwise result in general or with respect to any rate group or rate schedule but for such alteration. Any such alteration shall be made not more often than annually, and the commission shall not, by altering those proportions and in any event, including because of the length of time, as authorized under division (C) of this section, taken to approve the market rate offer, cause the duration of the blending period to exceed ten years as counted from the effective date of the approved market rate offer. Additionally, any such alteration shall be limited to an alteration affecting the prospective proportions used during the blending period and shall not affect any blending proportion previously approved and applied by the commission under this division.

(F) An electric distribution utility that has received commission approval of its first application under division (C) of this section shall not, nor ever shall be authorized or required by the commission to, file an application under section 4928.143 of the Revised Code.

#### **§ 4928.143. Application for approval of electric security plan - testing**

(A) For the purpose of complying with section 4928.141 of the Revised Code, an electric distribution utility may file an application for public utilities commission approval of an electric security plan as prescribed under division (B) of this section. The utility may file that application prior to the effective date of any rules the commission may adopt for the purpose of this section, and, as the commission determines necessary, the utility immediately shall conform its filing to those rules upon their taking effect.

(B) Notwithstanding any other provision of Title XLIX of the Revised Code to the contrary except division (D) of this section, divisions (I), (J), and (K) of section 4928.20, division (E) of section 4928.64, and section 4928.69 of the Revised Code:

(1) An electric security plan shall include provisions relating to the supply and pricing of electric generation service. In addition, if the proposed electric security plan has a term longer than three years, it may include provisions in the plan to permit the commission to test the plan pursuant to division (E) of this section and any transitional conditions that should be adopted by the commission if the commission terminates the plan as authorized under that division.

(2) The plan may provide for or include, without limitation, any of the following:

(a) Automatic 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;

(b) 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. Any such allowance shall be subject to the construction work in progress allowance limitations of division (A) of section 4909.15 of the Revised Code, except that the commission may authorize such an allowance upon the incurrence of the cost or occurrence of the expenditure. No such allowance for generating facility construction shall be authorized, however, unless the commission first determines in the proceeding that there is need for the facility based on resource planning projections submitted by the electric distribution utility. Further, no such allowance shall be authorized unless the facility's construction was sourced through a competitive bid process, regarding which process the commission may adopt rules. An allowance approved under division (B)(2)(b) of this section shall be established as a nonbypassable surcharge for the life of the facility.

(c) The establishment of a nonbypassable surcharge for the life of an electric generating facility that is owned or operated by the electric distribution utility, was sourced through a competitive bid process subject to any such rules as the commission adopts under division (B)(2)(b) of this section, and is newly used and useful on or after January 1, 2009, which surcharge shall cover all costs of the utility specified in the application, excluding costs recovered through a surcharge under division (B)(2)(b) of this section. However, no surcharge shall be authorized unless the commission first determines in the proceeding that there is need for the facility based on resource planning projections submitted by the electric distribution utility. Additionally, if a surcharge is authorized for a facility pursuant to plan approval under division (C) of this section and as a condition of the continuation of the surcharge, the electric distribution utility shall dedicate to Ohio Consumers' the capacity and energy and the rate associated with the cost of that facility. Before the commission authorizes any surcharge pursuant to this division, it may consider, as applicable, the effects of any decommissioning, deratings, and retirements.

(d) Terms, conditions, or 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;

(e) Automatic increases or decreases in any component of the standard service offer price;

(f) Provisions for the electric distribution utility to securitize any phase-in, inclusive of carrying charges, of the utility's standard service offer price, which phase-in is authorized in accordance with section 4928.144 of the Revised Code; and provisions for the recovery of the utility's cost of securitization.

(g) Provisions relating to transmission, ancillary, congestion, or any related service required for the standard service offer, including provisions for the recovery of any cost of such service that the electric distribution utility incurs on or after that date pursuant to the standard service offer;

(h) Provisions regarding the utility's distribution service, including, without limitation and notwithstanding any provision of Title XLIX of the Revised Code to the contrary, provisions regarding single issue ratemaking, a revenue decoupling mechanism or any other incentive rate-making, and provisions regarding distribution infrastructure and modernization incentives for the electric distribution utility. The latter may include a long-term energy delivery infrastructure modernization plan for that utility or any plan providing for the utility's recovery of costs, including lost revenue, shared savings, and avoided costs, and a just and reasonable rate of return on such infrastructure modernization. As part of its determination as to whether to allow in an electric distribution utility's electric security plan inclusion of any provision described in division (B)(2)(h) of this section, the commission shall examine the reliability of the electric distribution utility's distribution system and ensure that customers' and the electric distribution utility's expectations are aligned and that the electric distribution utility is placing sufficient emphasis on and dedicating sufficient resources to the reliability of its distribution system.

(i) Provisions under which the electric distribution utility may implement economic development, job retention, and energy efficiency programs, which provisions may allocate program costs across all classes of customers of the utility and those of electric distribution utilities in the same holding company system.

(C)(1) The burden of proof in the proceeding shall be on the electric distribution utility. The commission shall issue an order under this division for an initial application under this section not later than one hundred fifty days after the application's filing date and, for any subsequent application by the utility under this section, not later than two hundred seventy-five days after the application's filing date. Subject to division (D) of this section, the commission by order shall approve or modify and approve an application filed under division (A) of this section if it finds that the electric security plan so approved, including its pricing and all other terms and conditions, including any deferrals and any future recovery of deferrals, is more favorable in the aggregate as compared to the expected results that would otherwise apply under section 4928.142 of the Revised Code. Additionally, if the commission so approves an application that contains a surcharge under division (B)(2)(b) or (c) of this section, the commission shall ensure that the benefits derived for any purpose for which the surcharge is established are reserved and

made available to those that bear the surcharge. Otherwise, the commission by order shall disapprove the application.

(2)(a) If the commission modifies and approves an application under division (C)(1) of this section, the electric distribution utility may withdraw the application, thereby terminating it, and may file a new standard service offer under this section or a standard service offer under section 4928.142 of the Revised Code.

(b) If the utility terminates an application pursuant to division (C)(2)(a) of this section or if the commission disapproves an application under division (C)(1) of this section, the commission shall issue such order as is necessary to continue the provisions, terms, and conditions of the utility's most recent standard service offer, along with any expected increases or decreases in fuel costs from those contained in that offer, until a subsequent offer is authorized pursuant to this section or section 4928.142 of the Revised Code, respectively.

(D) Regarding the rate plan requirement of division (A) of section 4928.141 of the Revised Code, if an electric distribution utility that has a rate plan that extends beyond December 31, 2008, files an application under this section for the purpose of its compliance with division (A) of section 4928.141 of the Revised Code, that rate plan and its terms and conditions are hereby incorporated into its proposed electric security plan and shall continue in effect until the date scheduled under the rate plan for its expiration, and that portion of the electric security plan shall not be subject to commission approval or disapproval under division (C) of this section, and the earnings test provided for in division (F) of this section shall not apply until after the expiration of the rate plan. However, that utility may include in its electric security plan under this section, and the commission may approve, modify and approve, or disapprove subject to division (C) of this section, provisions for the incremental recovery or the deferral of any costs that are not being recovered under the rate plan and that the utility incurs during that continuation period to comply with section 4928.141, division (B) of section 4928.64, or division (A) of section 4928.66 of the Revised Code.

(E) If an electric security plan approved under division (C) of this section, except one withdrawn by the utility as authorized under that division, has a term, exclusive of phase-ins or deferrals, that exceeds three years from the effective date of the plan, the commission shall test the plan in the fourth year, and if applicable, every fourth year thereafter, to determine whether the plan, including its then-existing pricing and all other terms and conditions, including any deferrals and any future recovery of deferrals, continues to be more favorable in the aggregate and during the remaining term of the plan as compared to the expected results that would otherwise apply under section 4928.142 of the Revised Code. The commission shall also determine the prospective effect of the electric security plan to determine if that effect is substantially likely to provide the electric distribution utility with a return on common equity that is significantly in excess of the return on common equity that is likely to be earned by publicly traded companies, including utilities, that face comparable business and financial risk, with such adjustments for capital structure as may be appropriate. The burden of proof for demonstrating that significantly excessive earnings will not occur shall be on the electric distribution utility. If the test results are in the negative or the commission finds that continuation of the electric security plan will result in a return on equity that is significantly in excess of the return on common equity that is likely to be earned

by publicly traded companies, including utilities, that will face comparable business and financial risk, with such adjustments for capital structure as may be appropriate, during the balance of the plan, the commission may terminate the electric security plan, but not until it shall have provided interested parties with notice and an opportunity to be heard. The commission may impose such conditions on the plan's termination as it considers reasonable and necessary to accommodate the transition from an approved plan to the more advantageous alternative. In the event of an electric security plan's termination pursuant to this division, the commission shall permit the continued deferral and phase-in of any amounts that occurred prior to that termination and the recovery of those amounts as contemplated under that electric security plan.

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