

ORIGINAL

In The  
SUPREME COURT OF OHIO

<p><b>Ohio Power Company,</b></p> <p>Appellant,</p> <p>v.</p> <p><b>The Public Utilities Commission of Ohio,</b></p> <p>Appellee.</p>	<p>:</p>	<p>Case No. 12-2008</p> <p>On appeal from the Public Utilities Commission of Ohio, Case No. 11-4921-EL-RDR, <i>et al.</i>, <i>In the Matter of the Application of Columbus Southern Power Company for Approval of a Mechanism for Recover Deferred Fuel Costs Ordered Under Section 4928.144, Ohio Revised Code.</i></p>
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**MERIT BRIEF  
SUBMITTED ON BEHALF OF APPELLEE,  
THE PUBLIC UTILITIES COMMISSION OF OHIO**

**Matthew J. Satterwhite** (0071972)  
Counsel of Record  
**Steven T. Nourse** (0046705)  
American Electric Power Corporation  
1 Riverside Plaza, 29<sup>th</sup> Floor  
Columbus, OH 43215  
614.716.1915 (telephone)  
614.716.2950 (fax)  
[mjsatterwhite@aep.com](mailto:mjsatterwhite@aep.com)  
[stnourse@aep.com](mailto:stnourse@aep.com)

**Michael DeWine** (0009181)  
Ohio Attorney General

**William L. Wright** (0018010)  
Section Chief

**Thomas W. McNamee** (0017352)  
Counsel of Record

**Ryan P. O'Rourke** (0082651)  
Assistant Attorneys General  
Public Utilities Section  
180 East Broad Street, 6<sup>th</sup> Fl  
Columbus, OH 43215-3793  
614.466.4397 (telephone)  
614.644.8764 (fax)  
[thomas.mcnamee@puc.state.oh.us](mailto:thomas.mcnamee@puc.state.oh.us)  
[ryan.o'rourke@puc.state.oh.us](mailto:ryan.o'rourke@puc.state.oh.us)

**Daniel R. Conway** (0023058)  
**Kathleen R. Trafford** (0021753)  
Porter Wright Morris & Arthur  
41 South High Street  
Columbus, OH 43215  
614.227.2270 (telephone)  
614.227.2100 (fax)  
[dconway@porterwright.com](mailto:dconway@porterwright.com)  
[ktrafford@porterwright.com](mailto:ktrafford@porterwright.com)

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**Counsel for Appellee,  
The Public Utilities Commission of Ohio**

**Counsel for Appellant/Cross-Appellee,  
Ohio Power Company**

**Samuel C. Randazzo** (0016386)  
Counsel of Record

**Mark A. Whitt** (0067996)  
Counsel of Record  
**Andrew J. Campbell** (0081485)  
Whitt Sturtevant  
The KeyBank Building  
88 East Broad Street, Suite 1590  
Columbus, OH 43215  
614.224.3911 (telephone)  
614.224.3960 (fax)  
[whitt@whitt-sturtevant.com](mailto:whitt@whitt-sturtevant.com)  
[campbell@whitt-sturtevant.com](mailto:campbell@whitt-sturtevant.com)

**Counsel for *Amicus Curiae*,**  
**The East Ohio Gas Company d/b/a**  
**Dominion East Ohio**

**Frank P. Darr** (0025469)  
**Joseph E. Oliker** (0086088)  
**Matthew R. Pritchard** (0088070)  
McNees Wallace & Nurick  
21 East State Street, 17<sup>th</sup> Floor  
Columbus, OH 43215  
614.469.8000 (telephone)  
614.469.4653 (fax)  
[sam@mwncmh.com](mailto:sam@mwncmh.com)  
[fdarr@mwncmh.com](mailto:fdarr@mwncmh.com)  
[joliker@mwncmh.com](mailto:joliker@mwncmh.com)  
[mpritchard@mwncmh.com](mailto:mpritchard@mwncmh.com)

**Counsel for Appellee/Cross-Appellant,**  
**Industrial Energy Users-Ohio**

**Bruce J. Weston** (0016973)  
Ohio Consumers' Counsel  
**Terry L. Etter** (0067445)  
Counsel of Record  
**Maureen R. Grady** (0020847)  
Assistant Consumers' Counsel  
Office of the Ohio Consumers' Counsel  
10 West Broad Street, Suite 1800  
Columbus, OH 43215-3485  
614.466.7964 (telephone)  
614.466.9475 (fax)  
[etter@occ.state.oh.us](mailto:etter@occ.state.oh.us)  
[grady@occ.state.oh.us](mailto:grady@occ.state.oh.us)

**Counsel for Appellee/Cross-Appellant,**  
**Office of the Ohio Consumers' Counsel**

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**In The  
SUPREME COURT OF OHIO**

**Ohio Power Company,**

Appellant,

v.

**The Public Utilities Commission of  
Ohio,**

Appellee.

: Case No. 12-2008

:  
: On appeal from the Public Utilities  
: Commission of Ohio, Case No. 11-  
: 4921-EL-RDR, *et al.*, *In the Matter of*  
: *the Application of Columbus Southern*  
: *Power Company for Approval of a*  
: *Mechanism for Recover Deferred Fuel*  
: *Costs Ordered Under Section 4928.144,*  
: *Ohio Revised Code.*

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**MERIT BRIEF  
SUBMITTED ON BEHALF OF APPELLEE,  
THE PUBLIC UTILITIES COMMISSION OF OHIO**

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**INTRODUCTION**

Change is the essence of life. The law, and good sense, requires the Public Utilities Commission of Ohio (“Commission”) to recognize and embrace it. The Commission did so in this case. The Commission established a nonbypassable charge to collect phase-in deferrals as authorized by R.C. 4928.144. Previously, during the electric security plan period when deferrals were accruing, the Commission set the carrying charge rate by using the weighted-average-cost-of-capital

(“WACC”)<sup>1</sup> approach. When the plan ended and the Commission was about the business of establishing the nonbypassable mechanism to collect the deferrals, it recognized that the assumptions supporting the application of the WACC rate had changed. The risk associated with the collections of the deferrals had vanished; a statutory change made the elimination of the deferrals themselves feasible; and the magnitude of the deferrals exceeded all expectations.

All of these changes worked in the same direction and demanded a lower carrying charge rate. The Commission recognized this and lowered the carrying charge from the WACC rate to the rate that AEP-Ohio<sup>2</sup> pays on its long-term debt. The order was sensible and in keeping with the statute. It should be affirmed.

### **STATEMENT OF THE FACTS AND CASE**

This controversy traces back to the structure of AEP-Ohio’s first electric security plan (“ESP I”), thus we begin by briefly reviewing the relevant points

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<sup>1</sup> The WACC is a blended interest rate, which is calculated by taking “a company’s cost of debt and equity financing weighted by the percentage of debt and percentage of equity in a company’s capital structure.” *In re Heilig Meyers Co.*, 232 Fed. Appx. 240, 243 (4th Cir. 2007).

<sup>2</sup> The Columbus Southern Power Company (“CSP”) and the Ohio Power Company (“OP”) filed applications to recover deferred fuel costs in this case on September 1, 2011. Since that time, CSP merged into OP dba AEP-Ohio. *See In the Matter of the Application of the Ohio Power Company and Columbus Southern Power Company for Authority to Merge and Related Approvals*, Case No. 10-2376-EL-UNC (Entry) (Mar. 7, 2012), App. at 51-57. (Hereinafter, references to the Appendix to the First Merit Brief submitted by AEP-Ohio are denoted “AEP-Ohio App. at \_\_\_” and references to the Commission’s appendix are denoted “App. at \_\_\_.”)

from the Commission's opinion and order on AEP-Ohio's application for its ESP I. A discussion of the proceedings surrounding AEP-Ohio's application for approval of a mechanism to recover its deferred fuel costs will then follow.

**A. The Commission's opinion and order on AEP-Ohio's application for its ESP I.**

The Commission issued its opinion and order on AEP-Ohio's application for its ESP I on March 18, 2009 ("*ESP I Opinion and Order*").<sup>3</sup> There, the Commission, among other things, directed AEP-Ohio to phase-in a portion of the rate increase associated with its fuel costs (*i.e.*, its generation costs). *ESP I Opinion and Order* at 22, AEP-Ohio App. at 104. Under R.C. 4928.144, the Commission may phase-in any electric distribution utility rate or price established by R.C. 4928.141 to 4928.143, inclusive of carrying charges, through the creation of a regulatory asset. Any deferrals resulting from the phase-in are collected through a nonbypassable surcharge. R.C. 4928.144, App. at 11.

The Commission's principal reason for authorizing a phase-in was to "ensure rate or price stability and to mitigate the impact on customers during this

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<sup>3</sup> The full case-caption for the Commission's *ESP I Opinion and Order* is: *In the Matter of the Application of Columbus Southern Power Company for Approval of an Electric Security Plan; an Amendment to its Corporate Separation Plan; and the Sale or Transfer of Certain Generating Assets*, Case No. 08-917-EL-SSO (Opinion and Order) (Mar. 18, 2009) and *In the Matter of the Application of Ohio Power Company for Approval of its Electric Security Plan; and an Amendment to its Corporate Separation Plan*, Case No. 08-918-EL-SSO (Opinion and Order) (Mar. 18, 2009), AEP-Ohio App. at 83-160.

difficult economic period \* \* \*.” *ESP I Opinion and Order* at 22, AEP-Ohio App. at 104. While AEP-Ohio initially proposed to cap the rate increase at 15%, the Commission still deemed this too high and therefore lowered the cap even further. *Id.* The Commission ordered that any amounts exceeding this lowered cap must be deferred with carrying charges. *Id.* The carrying charge was set at the WACC rate, and was ordered by the Commission to be calculated on a gross-of-tax basis. *Id.* at 23-24, AEP-Ohio App. at 104-105. Any deferrals remaining at the end of AEP-Ohio’s ESP I were ordered by the Commission to be recovered from 2012 to 2018. *ESP I Opinion and Order* at 23, AEP-Ohio App. at 105. Importantly though, the Commission did not expressly set the carrying charge rate that would apply during the recovery period.

**B. The Commission’s decision on AEP-Ohio’s application for approval of a mechanism to recover its deferred fuel costs.**

Following the issuance of the Commission’s *ESP I Opinion and Order*, and after a decision and remand from this Court<sup>4</sup>, AEP-Ohio filed an application with the Commission in Case Nos. 11-4920-EL-RDR and 11-4921-EL-RDR seeking approval of a mechanism to recover deferred fuel costs as previously directed by

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<sup>4</sup> See *In re Application of Columbus Southern Power Co.*, 128 Ohio St.3d 512, 2011-Ohio-1788.

the Commission in its *ESP 1 Opinion and Order*. The recovery mechanism sought by AEP-Ohio took the form of a nonbypassable phase-in recovery rider (“PIRR”).

The Commission largely approved AEP-Ohio’s application, but modified the time period over which the WACC rate could be applied to the deferrals. *PIRR Finding and Order*<sup>5</sup> at 17, AEP-Ohio App. at 25. Specifically, the Commission directed AEP-Ohio “to collect carrying charges on the deferral balance based on the WACC rate, but only until such time as the recovery period begins. Thereafter, AEP-Ohio should be authorized to collect carrying charges at its long-term cost of debt rate.” *Id.* at 18, AEP-Ohio App. at 26. In other words, the Commission confined the application of the WACC rate to the duration of AEP-Ohio’s ESP I; upon the termination of the ESP I, carrying charges on the deferrals were to be calculated at AEP-Ohio’s long-term debt rate.

It is unreasonable, the Commission explained, to apply the WACC rate to the deferral balance once collection begins – that is, upon the termination of AEP Ohio’s ESP I – because at that point the “risk of non-collection is significantly reduced \* \* \*.” *Id.* at 18, AEP-Ohio App. at 26. Citing a long-line of its own

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<sup>5</sup> The full case-caption for the Commission’s *PIRR Finding and Order* is: *In the Matter of the Application of Columbus Southern Power Company for Approval of a Mechanism to Recover Deferred Fuel Costs Ordered Under Section 4928.144, Ohio Revised Code*, Case No. 11-4920-EL-RDR (Finding and Order) (Aug. 1, 2012) and *In the Matter of the Application of Ohio Power Company for Approval of a Mechanism to Recover Deferred Fuel Costs Ordered Under Section 4928.144, Ohio Revised Code*, Case No. 11-4921-EL-RDR (Finding and Order) (Aug. 1, 2012), AEP-Ohio App. at 9-31.

precedent, the Commission noted that its approach was congruent with sound regulatory practice. *Id.* at 18, fn. 10, AEP-Ohio App. at 26. The Commission also observed that it was inappropriate to apply the WACC rate to the deferral balance once collection begins because of the lingering economic recession faced by ratepayers. *Id.* at 18, AEP-Ohio App. at 26. While the Commission acknowledged that it was modifying the course taken in its *ESP I Opinion and Order*, it supported the modification based upon this Court's precedent, which authorizes the Commission to change or modify earlier orders so long as the change is accompanied by a justification. *Id.* at 19, AEP-Ohio App. at 27.

In its fifth entry on rehearing, the Commission addressed but ultimately rejected AEP-Ohio's argument that the Commission lacked authority to modify the time period over which the WACC rate could be applied to the deferrals. *In the Matter of the Columbus Southern Power Company and Ohio Power Company for Approval of a Mechanism to Recover Deferred fuel Costs Ordered Under Section 4928.144, Ohio Revised Code*, Case Nos. 11-4920-EL-RDR and 11-4921-EL-RDR (Fifth Entry on Rehearing at 13) (Oct. 3, 2012), AEP-Ohio App. at 48. AEP-Ohio filed an appeal with this Court. IEU-Ohio and OCC filed cross-appeals.

## ARGUMENT

### Proposition of Law No. I:

**When the Commission provides for a phase-in to ensure rate or price stability for consumers, it meets its statutory duty under R.C. 4928.144 by authorizing the utility to collect carrying charges on deferred amounts that are ultimately recoverable through a nonbypassable charge.**

R.C. 4928.144 authorizes the Commission to phase-in a standard service offer established under R.C. 4928.143 if three conditions are met. First, it may do so if it believes that such a phase-in is necessary to “...ensure rate or price stability for consumers.” R.C. 4928.144, App. at 11. Having made that finding, the Commission must do two additional things. Specifically, it must “...authoriz[e] the deferral of incurred costs equal to the amount not collected, plus carrying charges on that amount...” and also “...authorize the collection of those deferrals through a nonbypassable surcharge...” *Id.*

The Commission did all three. The Commission made the finding that the phase-in was necessary in its order. *ESP I Opinion and Order* at 22, AEP-Ohio App. at 104. Further the Commission established an initial carrying charge rate set at the WACC rate. *Id.* at 23, AEP-Ohio App. at 105. Here, the Commission adjusted this carrying cost rate to reflect the change in AEP-Ohio’s risk profile (caused by the beginning of collection through a nonbypassable charge and the availability of securitization) and lowered the rate to the cost of AEP-Ohio’s long-

term debt. *PIRR Finding and Order* at 18, AEP-Ohio App. at 26.<sup>6</sup> In this way the Commission set carrying charges just as R.C. 4928.144 requires. Finally, the Commission established a nonbypassable charge to collect the deferrals. *ESP I Opinion and Order* at 22-23, AEP-Ohio App. at 104-105. The Commission has done what the General Assembly required and its decision should be affirmed.

Fundamental to AEP-Ohio's argument is an incorrect reading of the statute. AEP-Ohio would read the statute to say that the Commission must provide deferrals "plus a carrying charge on that amount." That is not what the statute says. The statute actually requires that the Commission must provide deferrals "...plus carrying *charges* on that amount." R.C. 4928.144, App. at 11 (emphasis added). The term is plural; more than one carrying charge rate can be applied, exactly as the Commission ordered.

The use of a plural term is not accidental. It reflects the recognition that different periods and circumstances may necessitate different rates. During the period of the plan, while the deferrals are accruing, the utility may or may not be collecting anything toward amortization of these amounts, thus the WACC rate is appropriate. The deferrals are a long-term item with risk of non-collection in no

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<sup>6</sup> The Commission's explanation that the change in AEP-Ohio's risk profile warranted a downward adjustment to the carrying rate therefore belies AEP-Ohio's assertion that "[t]he only rationale the Commission gave for changing its finding is that these are hard economic times and that the modification follows the Commission's precedent." See AEP-Ohio's Brief at 15.

small part due to the vagaries of shopping inherent in the current regulatory structure.

Once the plan ended, this scenario changed entirely. The risk of non-collection vanished. The utility is assured of recovery because that recovery occurs through a nonbypassable charge. *PIRR Finding and Order* at 18, AEP-Ohio App. at 26. Shopping rates no longer make a difference. This change in the risk embodied in the regulatory asset is a basis for the application of a different carrying charge rate. *Id.*

That is not all that has changed in the situation below. After the Commission issued the *ESP I Opinion and Order*, the General Assembly enacted H.B. 364, codified in R.C. 4928.23, *et seq.*, which permits the utility to securitize phase-in deferrals. This is to say that the utility may turn the regulatory asset created by a phase-in into immediate cash. This is done by the utility selling bonds that are serviced by the nonbypassable charge. The utility retains the cash proceeds from the sale turning the potential money represented by the regulatory asset into real money. This is highly significant because the entire reason that carrying charges are required at all is to pay the utility for not receiving the cash it was otherwise, but for the phase-in, entitled to receive. Securitization obviates the need to compensate the utility with a carrying charge because it provides the utility with the cash to which it was entitled and it provides that cash immediately.

The existence of securitization as an option represents a sea change in the risk profile that the phase-in deferral presents. The Commission recognized this as a basis to change the carrying cost rate and even suggested that AEP should explore this option for dealing with these amounts. *PIRR Finding and Order* at 18-19, AEP-Ohio App. at 26-27. AEP has availed itself of this securitization option regarding other deferrals (those associated with the deferred asset recovery rider) by filing an application to securitize them. *In the Matter of the Application of the Ohio Power Company for Authority to Issue Phase-in Recovery-Bonds, and Impose, Charge and Collect Phase-in-Recovery Charges and for Tariff and Bill Format Changes*, Case No. 12-1969-EL-ATS (Application) (July 31, 2012), App. at 15.

Even the assumptions about the way these deferrals would develop have not proven to be accurate. When the Commission first established the deferrals, it believed that there would be no deferrals at all for Columbus Southern Power after the end of the plan period (and therefore no matter to be discussed in this case) and that the deferrals for Ohio Power Company would be fully amortized in two or three years. *ESP I* (Entry on Rehearing at 7) (Mar. 23, 2009), AEP-Ohio App. at 167. This has proven to be inaccurate.

In sum, the Commission has implemented R.C. 4928.144 correctly. The statute requires the Commission to establish carrying charges. It has done so, set-

ting two different charges, each commensurate with the risk profile of the relevant time period.

Of course that is not all that has changed. With the end of its ESP I, AEP-Ohio lost the ability to terminate that plan. This is presented as a reason that the Commission should not have adjusted the carrying cost rate. The argument is very difficult to understand and ultimately is just a red herring. Understanding why requires some explanation.

When the Commission modifies and approves a utility's ESP application, as happened in *ESP I*, the utility has a unilateral right to terminate that application and end the plan. R.C. 4928.143(C)(2)(a), App. at 9 AEP-Ohio did not exercise that option regarding *ESP I*. It is obvious that this right to terminate itself terminates with the end of the plan (there no longer being a plan to eliminate). When a utility exercises its ability to terminate an ESP, the Commission, by statute, must issue an order to revert back to the rates *before* the plan was put into place. R.C. 4928.143(C)(2)(b), App. at 9. It will be remembered that the effect of the ESP I for AEP-Ohio was to increase the rates and increase them to such an extent that the Commission believed a phase-in, and the attendant deferrals that are at issue here, was necessitated to protect the public. What AEP-Ohio lost when it did not terminate the ESP was the *ability to unilaterally reduce its own income*. Its argument is then, essentially, because it no longer can reduce its rates as it could

have in the past, it is entitled to make more money today, or, stated more directly, because it made more money in the past, it should make more money today. This is no argument at all.

In reality AEP-Ohio's argument is irrelevant. The question today is "what is the correct carrying charge for these phase-in deferrals now?" Nothing from the ESP period has a bearing on this question. The matter is current and only current information is relevant to it. The presence or absence of a right to terminate has no bearing. The Commission looked to current information to make its decision and its conclusion was reasonable.

The above reasons also explain why AEP-Ohio's reliance on the doctrine of res judicata (more specifically, issue preclusion) is misplaced. "The doctrines of res judicata and collateral estoppel preclude relitigation of law or fact that was at issue in a former action between the same parties and was passed upon by a court of competent jurisdiction." *Vectren Energy Delivery of Ohio v. Pub Util. Comm.*, 113 Ohio St.3d 180, 2007-Ohio-1386, ¶ 30. Here, there is no relitigation of a fact that was at issue in a prior proceeding. The *ESP I Opinion and Order* did not expressly address the carrying charge that would apply during the collection period. That issue was first expressly addressed in this proceeding when AEP-Ohio filed its application seeking approval of a mechanism to recover its deferred

fuel costs. Given the dissimilarity between the *ESP I Opinion and Order* and this proceeding, res judicata should not apply.

Moreover, res judicata will not bar the consideration of an issue where, as here, a change in facts raises a new material issue or would have been relevant to the disposition of a material issue from the prior action. *State ex rel. Westchester Estates v. Bacon*, 61 Ohio St.2d 42, syllabus at ¶ 2 (1980). Here, the facts surrounding AEP-Ohio's risk profile have changed since the Commission issued its *ESP I Opinion and Order*. Before, AEP-Ohio faced the risk of non-collection during the deferral period, and the application of the WACC rate to the deferrals compensated AEP-Ohio for taking on that risk. But now, that risk has vanished because AEP-Ohio is assured of recovery through a nonbypassable charge. AEP-Ohio should not be compensated with a rate of return (*i.e.*, the WACC rate) that is incommensurate with its current risk profile.

AEP-Ohio's res judicata argument is weakened further still because the Commission retains ongoing jurisdiction over the phase-in. *See State ex rel. B.O.C. Group v. Indus. Comm.*, 58 Ohio St.3d 199, 200-201, 569 N.E.2d 496 (1991) (res judicata applies with diminished force where the agency retains ongoing jurisdiction).

## Proposition of Law No. II:

**A long-line of this Court's precedent instructs that the Commission may revisit one of its prior decisions and modify the course previously taken so long as the Commission explains its reasons for doing so.**

AEP-Ohio argues that the Commission, having once made a decision, cannot depart from that decision. The law is quite to the contrary. This Court has stated "as a general rule, the commission has discretion to revisit earlier regulatory decisions and modify them prospectively." *In re Application of Columbus S. Power*, 129 Ohio St.3d 568, 569, 2011-Ohio-4129, 954 N.E.2d 1183, 2011 Ohio LEXIS 1926. The Commission should follow its precedent, "[y]et the commission must, when appropriate, be willing to change its policies." *Luntz Corp. v. Pub. Util. Comm.*, 79 Ohio St.3d 509, 513, 684 N.E.2d 43 (1997). When it does so it must, however, provide an explanation. *Util. Serv. Partners, Inc. v. Pub. Util. Comm.*, 124 Ohio St.3d 284, 2009-Ohio-6764, ¶ 18. As has been discussed above, and will be discussed again below, the Commission has provided overwhelming reasons for its decision. The legal standard has been met and the order should be affirmed.

Utilities are regulated entities. This means a number of things, including that their activities *qua* public utilities are subject to continuing jurisdiction and oversight by the Commission. For example,

The public utilities commission is hereby vested with the power and jurisdiction to supervise and regulate public utilities and railroads, to require all public utilities to fur-

nish their products and render all services exacted by the commission or by law \* \* \* . [R.C. 4905.04, App. at 1.]

Additionally the law provides:

The jurisdiction, supervision, powers, and duties of the public utilities commission extend to every public utility and railroad, the plant or property of which lies wholly within this state and when the property of a public utility or railroad lies partly within and partly without this state to that part of such plant or property which lies within this state; to the persons or companies owning, leasing, or operating such public utilities and railroads; to the records and accounts of the business thereof done within this state; and to the records and accounts of any companies which are part of an electric utility holding company system exempt under section 3(a)(1) or (2) of the "Public Utility Holding Company Act of 1935," 49 Stat. 803, 15 U.S.C. 79c, and the rules and regulations promulgated thereunder, insofar as such records and accounts may in any way affect or relate to the costs associated with the provision of electric utility service by any public utility operating in this state and part of such holding company system \* \* \* . [R.C. 4905.05, App. at 1.]

Additionally the General Assembly has provided that:

The public utilities commission has general supervision over all public utilities within its jurisdiction as defined in section 4905.05 of the Revised Code, and may examine such public utilities and keep informed as to their general condition, capitalization, and franchises, and as to the manner in which their properties are leased, operated, managed, and conducted with respect to the adequacy or accommodation afforded by their service, the safety and security of the public and their employees, and their compliance with all laws, orders of the commission, franchises, and charter requirements \* \* \* . [R.C. 4905.06, App. at 1-2.]

Although the General Assembly has provided that these quoted sections do not apply to a utility's competitive activities, the matter at issue here arises from the provision of the regulated standard service offer under R.C. 4928.143 to which the sections still apply. R.C. 4928.05, App. at 6-7.

This Court is very familiar with this body of law and has determined that the general rule is that the Commission may depart from its prior decisions when it explains the reason for the departure. *Util. Serv. Partners, Inc. v. Pub. Util. Comm.*, 124 Ohio St.3d 284, 2009-Ohio-6764, ¶ 18; *Consumers' Counsel v. Pub. Util. Comm.*, 16 Ohio St.3d 21, 21-22, 475 N.E.2d 786 (1985); *In re Application of Columbus S. Power*, 128 Ohio St.3d 512, 2011-Ohio-1788, ¶ 52. "Agencies undoubtedly may change course, provided that the new regulatory course is permissible". *In re Application of Columbus S. Power Co.*, 2011-Ohio-1788, ¶ 52.

There are few instances in which the General Assembly has determined it appropriate to depart from this general rule. Where the Commission has granted a natural gas company an exemption or an alternative rate regulation the order making the grant cannot be altered if that order has been in place more than eight years unless the natural gas company agrees. R.C. 4929.08(A)(2), App. at 14. Under the securitization process, a final financing order issued by the Commission is irrevocable and the public utilities commission may not reduce, impair, postpone, or terminate the phase-in-recovery charges authorized in the final financing order

or impair the property or the collection or recovery of phase-in costs. R.C. 4928.235(B), App. at 13. When the General Assembly wants the Commission not to change a decision already made, departing from the general rule, it says so. It did not say so in the situation at bar. The general rule applies here and the Commission can change an earlier decision if it provides its rationale for doing so.

The Commission has made its reasons for lowering the carrying cost rate for these deferrals abundantly clear. As noted previously, everything surrounding these deferrals has changed since the decision in *ESP I*. The risk of non-collection of the deferred amounts has dropped to zero. Once the plan period has ended, the collection of the deferrals occurs through a nonbypassable charge. This means that all customers will pay these amounts regardless of whether those customers buy their electricity from AEP-Ohio or from a competitive supplier. The charge can no longer be avoided by purchasing electricity from a different supplier. AEP-Ohio will get its money with certainty. This alone would be a sufficient reason to justify the change in the carrying charge rate, but there is more.

Although there was no way to anticipate it at the time of the *ESP I Opinion and Order*, the General Assembly entered into the situation as well by creating an entirely new and highly detailed mechanism to securitize deferrals by enacting what has been codified as R.C. 4928.23, *et seq.* By utilizing this new securitization process, a utility can transmute the phase-in deferrals on its books, which indicate

the promise of cash in the future<sup>7</sup>, into actual cash in the present. If this mechanism were utilized<sup>8</sup>, AEP-Ohio would sell these deferrals, keeping the proceeds, and there would be nothing on which to impose a carrying charge at all. This legislation only became effective on March 22, 2012, and thus could not have been anticipated on March 18, 2009 when the Commission issued its order establishing the phase-in which generated the deferrals.

As noted previously, even the level of the deferrals has turned out to be substantially different than was anticipated. Rather than no deferrals for Columbus Southern and only two or three years of amortization for Ohio Power, there are significant deferrals for both. *ESP I* (Entry on Rehearing at 7) (Mar. 23, 2009), AEP-Ohio App. at 167. The magnitude of the deferrals is quite different from the *a priori* expectation.

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<sup>7</sup> It should be noted that phase-in deferrals under R.C. 4928.144 are fundamentally different than the normal kind of accounting deferrals that the Court has seen in previous cases. In the more traditional kind of accounting deferral authorized by the Commission, the grant of a deferral only preserves the ability to argue about the recovery of the amounts deferred for a future case. There is no assurance that any portion of the amounts deferred will actually be allowed for recovery in that future case. *See, Elyria Foundry Co. v. Pub. Util. Comm.*, 114 Ohio St.3d 305, 2007-Ohio-4164. Deferrals pursuant to R.C. 4928.144 must be collected through a nonbypassable charge after the end of the electric security plan under which they were created.

<sup>8</sup> As noted previously, AEP-Ohio has initiated a proceeding to securitize certain other deferrals. *In the Matter of the Application of the Ohio Power Company for Authority to Issue Phase-in Recovery-Bonds, and Impose, Charge and Collect Phase-in-Recovery Charges and for Tariff and Bill Format Changes*, Case No. 12-1969-EL-ATS (Application) (July 31, 2012), App. at 15.

In sum, the record shows ample reasons for why the Commission adjusted the carrying cost rate to reflect current conditions. The Commission can change a prior decision if it explains its reasons for doing so. It has done this. The legal requirement has been met and the Commission's decision should be affirmed.

**Proposition of Law No. III:**

**A utility is not guaranteed a specific return on its investment nor is it permitted to attack, in isolation, an individual rate.**

AEP-Ohio's argument, as well as that of its amicus, is based on a faulty, tacit premise. They believe that AEP-Ohio is entitled to a specific return on a particular activity. This has never been the law in Ohio. Even when setting rates<sup>9</sup>, the cost of providing a service is a permissive factor that may be used to set the charge for that service. R.C. 4909.151, App. at 6. This Court has recognized that regulation does not guarantee the utility a particular return:

In *Hope*, the court recognized that " 'regulation does not insure that the business shall produce net revenues,' " 320 U.S. at 603, 64 S.Ct. at 288, 88 L.Ed. at 345, quoting *Fed. Power Comm. v. Natural Gas Pipeline Co.* (1942), 315 U.S. 575, 590, 62 S.Ct. 736, 745, 86 L.Ed.2d 1037, 1052, and in the latter case the court stated that "the hazard that the property will not earn a profit remains on the company in the case of a regulated, as well as an unregulated, business." *Id.* See, also, *Market Street Ry. Co. v. RR. Comm. of California* (1945), 324 U.S. 548, 65 S.Ct.

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<sup>9</sup> As opposed to setting a carrying charge which will be used to calculate a gross deferral amount which will be collected through a rate, as is the case herein. Overall rates are determined in a base rate case.

770, 89 L.Ed. 1171 (regulation does not insure a utility's profit). From a review of this language, the Supreme Court of Pennsylvania stated that "since the risk of non-profitability remains upon regulated utility companies, it follows that the consequence of that lack of profitability, to wit diminished financial integrity, also rests upon utility companies." *Pennsylvania Elec. Co. v. Pennsylvania Pub. Util. Comm.* (1985), 509 Pa. 324, 332, 502 A.2d 130, 134, appeal dismissed for want of substantial federal question *sub nom. Metropolitan Edison Co. v. Pennsylvania Pub. Util. Comm.* (1986), 476 U.S. 1137, 106 S.Ct. 2239, 90 L.Ed.2d 687. Indeed, in DP&L we stated that the court's summary dismissals of repeated appeals on this issue suggest that the court has implicitly recognized that "the Constitution no longer provides any special protection for the utility investor." (4 Ohio St.3d at 100, 4 OBR at 349, 447 N.E.2d at 740, quoting Bernstein, *Utility Rate Regulation: The Little Locomotive That Couldn't* [1970], Wash.U.L.Q. 223, 259-260.).

*Ohio Edison Co. v. Pub. Util. Comm.*, 63 Ohio St.3d 555, 565, 589 N.E.2d 1292, (1992). In fact, a utility is only entitled to "a fair and reasonable rate of return" on its investment. R.C. 4909.15(A)(2), App. at 3. This Court has recognized the same. *Dayton Power and Light Co. v. Pub. Util. Comm.*, 4 Ohio St.3d 91, 103, 447 N.E.2d 733 (1983).

This determination is based on the entirety of the regulated activities of the utility. This Court has noted, "If the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry \* \* \* is at an end." *Toledo Edison Co. v. Pub. Util. Comm.*, 12 Ohio St.3d 143, 146, 465 N.E.2d 886, (1984) (quoting *Federal Power Comm. v. Hope Natural Gas Co.*, 320 U.S. 591, 601 (1944)). No

individual rate is to be examined. It is the entire rate making order that must be considered. As this Court has noted “any rate selected \* \* \* from the broad zone of reasonableness \* \* \* cannot be attacked as confiscatory.” *Cleveland Elec. Illum. Co. v. Pub. Util. Comm.*, 4 Ohio St.3d 107, 110, 447 N.E.2d 746 (1983) (quoting *Permian Basin Area Rate Cases*, 390 U.S. 747, 770 (1968)).

AEP-Ohio made no such showing of unreasonableness below. Indeed, the carrying charge rate imposed by the Commission is reasonable because it is the level of return actually provided for on the company’s own long-term debt. Because the rate is reasonable, it cannot be confiscatory. This Court has reasoned that:

To prevail [on issues of confiscation], appellant must prove not only the unreasonableness of the [underlying statutory determinations] but also the confiscatory effect [these determinations] had on the rates established by the commission, viewing the rate order in its entirety.

*Ohio Edison Co. v. Pub. Util. Comm.*, 63 Ohio St.3d 555, 564, 589 N.E.2d 1292, (1992) (quoting *Dayton Power and Light Co.*, 4 Ohio St.3d at 106) (brackets in original, cites and quotes omitted). AEP-Ohio has shown neither unreasonableness nor confiscatory effect and therefore the Commission’s order must stand.

The principles from above also illustrate the fallacy with the arguments of amicus curiae the East Ohio Gas Co. dba Dominion East Ohio (“DEO”). DEO contends that the Commission’s *PIRR Finding and Order* retroactively modified

the structure of AEP-Ohio's ESP I. DEO's objections are grounded in Ohio Constitution, Article II, Section 28 (prohibition on retroactive laws) and R.C. 1.48 (presumption that laws are prospective unless expressly made retrospective). DEO is mistaken.

First, the Commission did not do anything retroactive—the modification from the WACC rate to AEP-Ohio's long-term debt rate was forward looking. The *ESP I Opinion and Order* did not expressly address the issue of what the carrying charge would be once the collection period commenced. That issue, rather, was first expressly addressed in this proceeding when the Commission issued its *PIRR Finding and Order* on AEP-Ohio's application for a mechanism to recover its deferred fuel costs. Thus, the notion that the Commission effected a retroactive modification is belied by the divergent characteristics of the *ESP I* and *PIRR* proceedings.

Second, even if the Commission's *PIRR Finding and Order* could be construed as having retroactive effect, this Court has repeatedly recognized that the Commission is clothed with the authority to modify prior orders so long as the modification is accompanied by an explanation. *See, e.g., Util. Serv. Partners, Inc.*, 2009-Ohio-6764 at ¶ 18. Here, the Commission met this standard. It explained that downward pressure on AEP-Ohio's risk profile necessitated a downward adjustment to its carrying charge rate. Indeed, fundamental principles

of finance and economics dictate that AEP-Ohio should not be compensated with a rate of return (*i.e.*, the WACC rate) that is incommensurate with its current risk profile.

Finally, DEO misapprehends the distinction between substantive and remedial rights in the regulatory context. While DEO is largely correct to say that the government cannot retroactively impair a substantive right, a utility's specific rate of return (such as the WACC rate) does not constitute a substantive right. *See, e.g., Ohio Edison Co.*, 63 Ohio St.3d at 565. Utilities are not guaranteed a specific rate of return; it is the totality of the ratemaking order that counts, viewed through the broad zone of reasonableness. *Id.* DEO is therefore wrong to suggest that, in the regulatory context, a guarantee of a specific amount of money constitutes a substantive right. *See* DEO's Brief at 6 (citing *State ex rel. Bd. of Ed. of Kenton City School Dist. v. State Bd. of Ed.*, 174 Ohio St. 257, 261, 189 N.E. 72 (1963)). There is no substantive right at issue here.

The case below is not even the correct vehicle for the determination that AEP-Ohio seeks. As noted previously, a utility is entitled to a reasonable return on its investment. This can only be determined when the entire investment is considered. Individual components cannot be viewed in isolation. *Cleveland Elec. Illum. Co. v. Pub. Util. Comm.*, 4 Ohio St.3d 107, 110, 447 N.E.2d 746 (1983) (quoting *Permian Basin Area Rate Cases*, 390 U.S. 747, 770 (1968)). This is the purpose of

filing a rate case under R.C. 4909.18: it affords the Commission the opportunity to examine the entirety of a utility's operation to assure that the company receives a reasonable return on its investment and the return of its costs. *Dayton Power and Light Co.*, 4 Ohio St.3d at 103.

Unlike a rate case, the purpose of the case below was much more limited. It only sought to design a mechanism to recover phase-in deferrals, merely one of myriads or components of the overall rate structure. It was not an undertaking to assess the entirety of the company's operations.

The reason that returns need to be examined in their entirety is quite obvious. If we consider a highly simplified situation, a utility that has only two activities, one earning a high return and the other a low return, that utility will obtain an overall reasonable rate. If the company were permitted to have only the low-earning service examined and its rate adjusted in isolation, it would be able to achieve an overall high rate. Consumers would pay too much. State law does not allow this. It requires only that the rates *in toto* provide a reasonable return and the rate case is the mechanism to achieve that assurance. R.C. 4909.15(A)(2), App. at 3.

This is the ultimate answer to AEP-Ohio's concern. If it believes that it is not being compensated adequately, its legal recourse is not through appeal of this order, but rather through the filing of a rate case under R.C. 4909.18. Such a case would be the correct vehicle to assure that AEP-Ohio is being treated fairly; such a

case would be the correct place to vet AEP-Ohio's concerns; and such a case would provide this Court with the appropriate information to review and apply its standards so as to fulfill its important role in assuring that the Commission implements the law correctly. It is up to AEP-Ohio to choose when to file a rate case. *Dayton Power and Light Co.*, 4 Ohio St.3d at 96. It has not chosen to do so as of yet. AEP-Ohio's concerns must wait until it does.

## CONCLUSION

The Commission must adjust its decisions to match the facts on the ground. It did so in this case. The circumstances at the time of the case below warranted the application of a different carrying charge to the phase-in deferrals. The Commission recognized this and made the adjustment. This was the only reasonable course and the Commission took it. The decision should be affirmed.

Respectfully submitted,

**Michael DeWine** (0009181)  
Ohio Attorney General

**William L. Wright** (0018010)  
Section Chief



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**Thomas W. McNamee** (0017352)

Counsel of Record

**Ryan P. O'Rourke** (0082651)

Assistant Attorneys General

Public Utilities Section

180 East Broad Street, 6<sup>th</sup> Fl

Columbus, OH 43215-3793

614.466.4397 (telephone)

614.644.8764 (fax)

[thomas.mcnamee@puc.state.oh.us](mailto:thomas.mcnamee@puc.state.oh.us)

[ryan.o'rourke@puc.state.oh.us](mailto:ryan.o'rourke@puc.state.oh.us)

**Counsel for Appellee,  
The Public Utilities Commission of Ohio**

## PROOF OF SERVICE

I hereby certify that a true copy of the foregoing Merit Brief, 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 19<sup>th</sup> day of April, 2013.



**Thomas W. McNamee**  
Assistant Attorney General

### Parties of Record:

**Matthew J. Satterwhite**  
**Steven T. Nourse**  
American Electric Power Corporation  
1 Riverside Plaza, 29<sup>th</sup> Floor  
Columbus, OH 43215

**Daniel R. Conway**  
**Kathleen R. Trafford**  
Porter Wright Morris & Arthur  
41 South High Street  
Columbus, OH 43215

**Mark A. Whitt**  
**Andrew J. Campbell**  
Whitt Sturtevant  
The KeyBank Building  
88 East Broad Street, Suite 1590  
Columbus, OH 43215

**Samuel C. Randazzo**  
**Frank P. Darr**  
**Joseph E. Olikier**  
**Matthew R. Pritchard**  
McNees Wallace & Nurick  
21 East State Street, 17<sup>th</sup> Floor  
Columbus, OH 43215

**Bruce J. Weston**  
**Terry L. Etter**  
**Maureen R. Grady**  
Assistant Consumers' Counsel  
Office of the Ohio Consumers' Counsel  
10 West Broad Street, Suite 1800  
Columbus, OH 43215-3485

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#### **4905.04 Power to regulate public utilities and railroads.**

The public utilities commission is hereby vested with the power and jurisdiction to supervise and regulate public utilities and railroads, to require all public utilities to furnish their products and render all services exacted by the commission or by law, and to promulgate and enforce all orders relating to the protection, welfare, and safety of railroad employees and the traveling public, including the apportionment between railroads and the state and its political subdivisions of the cost of constructing protective devices at railroad grade crossings.

#### **4905.05 Scope of jurisdiction.**

The jurisdiction, supervision, powers, and duties of the public utilities commission extend to every public utility and railroad, the plant or property of which lies wholly within this state and when the property of a public utility or railroad lies partly within and partly without this state to that part of such plant or property which lies within this state; to the persons or companies owning, leasing, or operating such public utilities and railroads; to the records and accounts of the business thereof done within this state; and to the records and accounts of any companies which are part of an electric utility holding company system exempt under section 3(a)(1) or (2) of the "Public Utility Holding Company Act of 1935," 49 Stat. 803, 15 U.S.C. 79c, and the rules and regulations promulgated thereunder, insofar as such records and accounts may in any way affect or relate to the costs associated with the provision of electric utility service by any public utility operating in this state and part of such holding company system.

Nothing in this section, or section 4905.06 or 4905.46 of the Revised Code pertaining to regulation of holding companies, grants the public utilities commission authority to regulate a holding company or its subsidiaries which are organized under the laws of another state, render no public utility service in the state of Ohio, and are regulated as a public utility by the public utilities commission of another state or primarily by a federal regulatory commission, nor do these grants of authority apply to public utilities that are excepted from the definition of "public utility" under divisions (A)(1) to (3) of section 4905.02 of the Revised Code.

#### **4905.06 General supervision.**

The public utilities commission has general supervision over all public utilities within its jurisdiction as defined in section 4905.05 of the Revised Code, and may examine such public utilities and keep informed as to their general condition, capitalization, and franchises, and as to the manner in which their properties are leased, operated, managed, and conducted with respect to the adequacy or accommodation afforded by their service, the safety and security of the public and their employees, and their compliance with all laws, orders of the commission, franchises, and charter requirements. The commission has general supervision over all other companies referred to in section 4905.05 of the Revised Code to the extent of its jurisdiction as defined in that section, and may examine such companies and keep informed as to their general condition and capitalization, and as to the manner in which their properties are leased, operated, managed, and conducted with respect to the adequacy or accommodation afforded by their service, and their compliance with all laws and orders of the commission, insofar as any of such matters may

relate to the costs associated with the provision of electric utility service by public utilities in this state which are affiliated or associated with such companies. The commission, through the public utilities commissioners or inspectors or employees of the commission authorized by it, may enter in or upon, for purposes of inspection, any property, equipment, building, plant, factory, office, apparatus, machinery, device, and lines of any public utility. The power to inspect includes the power to prescribe any rule or order that the commission finds necessary for protection of the public safety. In order to assist the commission in the performance of its duties under this chapter, authorized employees of the motor carrier enforcement unit, created under section 5503.34 of the Revised Code in the division of state highway patrol, of the department of public safety may enter in or upon, for inspection purposes, any motor vehicle of any motor carrier .

In order to inspect motor vehicles owned or operated by a motor carrier engaged in the transportation of persons, authorized employees of the motor carrier enforcement unit, division of state highway patrol, of the department of public safety may enter in or upon any property of any motor carrier engaged in the intrastate transportation of persons.

#### **4909.15 [Effective Until 3/27/2013] 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.

#### **4909.151 Consideration of costs attributable to service.**

In fixing the just, reasonable, and compensatory rates, joint rates, tolls, classifications, charges, or rentals to be observed and charged for service by any public utility, the public utilities commission may consider the costs attributable to such service. The utility shall file with the commission an allocation of the cost, except cost related to sparsity of population, for services for which a change in rates is proposed when evidence relating thereto is presented which indicates that the rate or rates do not generally reflect the cost of providing these services. As used in this section, "costs" includes [include] operation and maintenance expense, depreciation expense, tax expense, and return on investment as actually incurred by the utility. The costs allocated to each service shall include only those costs used by the public utilities commission to determine total allowable revenues.

#### **4928.05 Extent of exemptions.**

(A)

(1) On and after the starting date of competitive retail electric service, a competitive retail electric service supplied by an electric utility or electric services company shall not be subject to supervision and regulation by a municipal corporation under Chapter 743. of the Revised Code or by the public utilities commission under Chapters 4901. to 4909., 4933., 4935., and 4963. of the Revised Code, except sections 4905.10 and 4905.31, division (B) of section 4905.33, and sections 4905.35 and 4933.81 to 4933.90 ; except sections 4905.06, 4935.03, 4963.40, and 4963.41 of the Revised Code only to the extent related to service reliability and public safety; and except as otherwise provided in this chapter. The commission's authority to enforce those excepted provisions with respect to a competitive retail electric service shall be such authority as is provided for their enforcement under Chapters 4901. to 4909., 4933., 4935., and 4963. of the Revised Code and this chapter. Nothing in this division shall be construed to limit the commission's authority under sections 4928.141 to 4928.144 of the Revised Code. On and after the starting date of competitive retail electric service, a competitive retail electric service supplied by an electric cooperative shall not be subject to supervision and regulation by the commission under Chapters 4901. to 4909., 4933., 4935., and 4963. of the Revised Code, except as otherwise expressly provided in sections 4928.01 to 4928.10 and 4928.16 of the Revised Code.

(2) On and after the starting date of competitive retail electric service, a noncompetitive retail electric service supplied by an electric utility shall be subject to supervision and regulation by the commission under Chapters 4901. to 4909., 4933., 4935., and 4963. of the Revised Code and this chapter, to the extent that authority is not preempted by federal law. The commission's authority to enforce those provisions with respect to a noncompetitive retail electric service shall be the authority provided under those chapters and this chapter, to the extent the authority is not preempted by federal law. Notwithstanding Chapters 4905. and 4909. of the Revised Code, commission authority under this chapter shall include the authority to provide for the recovery, through a reconcilable rider on an electric distribution utility's distribution rates, of all transmission and transmission-related costs, including ancillary and congestion costs, imposed on or charged to the utility by the federal energy regulatory commission or a regional transmission

organization, independent transmission operator, or similar organization approved by the federal energy regulatory commission. The commission shall exercise its jurisdiction with respect to the delivery of electricity by an electric utility in this state on or after the starting date of competitive retail electric service so as to ensure that no aspect of the delivery of electricity by the utility to consumers in this state that consists of a noncompetitive retail electric service is unregulated. On and after that starting date, a noncompetitive retail electric service supplied by an electric cooperative shall not be subject to supervision and regulation by the commission under Chapters 4901. to 4909., 4933., 4935., and 4963. of the Revised Code, except sections 4933.81 to 4933.90 and 4935.03 of the Revised Code. The commission's authority to enforce those excepted sections with respect to a noncompetitive retail electric service of an electric cooperative shall be such authority as is provided for their enforcement under Chapters 4933. and 4935. of the Revised Code.

(B) Nothing in this chapter affects the authority of the commission under Title XLIX of the Revised Code to regulate an electric light company in this state or an electric service supplied in this state prior to the starting date of competitive retail electric service.

#### **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) Consistent with sections 4928.23 to 4928.2318 of the Revised Code, both of the following:

(i) 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; (ii) 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.

#### **4928.144 Phase-in of electric distribution utility rate or price.**

The public utilities commission by order may authorize any just and reasonable phase-in of any electric distribution utility rate or price established under sections 4928.141 to 4928.143 of the Revised Code, and inclusive of carrying charges, as the commission considers necessary to ensure rate or price stability for consumers. If the commission's order includes such a phase-in, the order also shall provide for the creation of regulatory assets pursuant to generally accepted accounting principles, by authorizing the deferral of incurred costs equal to the amount not collected, plus carrying charges on that amount. Further, the order shall authorize the collection of those deferrals through a nonbypassable surcharge on any such rate or price so established for the electric distribution utility by the commission.

#### **4928.23 Definitions for standards for securitization of costs for electric distribution utilities.**

As used in sections 4928.23 to 4928.2318 of the Revised Code: (A) "Ancillary agreement" means any bond insurance policy, letter of credit, reserve account, surety bond, swap arrangement, hedging arrangement, liquidity or credit support arrangement, or other similar agreement or arrangement entered into in connection with the issuance of phase-in-recovery bonds that is designed to promote the credit quality and marketability of the bonds or to mitigate the risk of an increase in interest rates. (B) "Assignee" means any person or entity to which an interest in phase-in-recovery property is sold, assigned, transferred, or conveyed, other than as security, and any successor to or subsequent assignee of such a person or entity. (C) "Bond" includes debentures, notes, certificates of participation, certificates of beneficial interest, certificates of ownership or other evidences of indebtedness or ownership that are issued by an electric distribution utility or an assignee under a final financing order, the proceeds of which are used directly or indirectly to recover, finance, or refinance phase-in costs and financing costs, and that are secured by or payable from revenues from phase-in-recovery charges. (D) "Bondholder" means

any holder or owner of a phase-in-recovery bond. (E) "Financing costs" means any of the following: (1) Principal, interest, and redemption premiums that are payable on phase-in-recovery bonds; (2) Any payment required under an ancillary agreement; (3) Any amount required to fund or replenish a reserve account or another account established under any indenture, ancillary agreement, or other financing document relating to phase-in-recovery bonds; (4) Any costs of retiring or refunding any existing debt and equity securities of an electric distribution utility in connection with either the issuance of, or the use of proceeds from, phase-in-recovery bonds; (5) Any costs incurred by an electric distribution utility to obtain modifications of or amendments to any indenture, financing agreement, security agreement, or similar agreement or instrument relating to any existing secured or unsecured obligation of the electric distribution utility in connection with the issuance of phase-in-recovery bonds; (6) Any costs incurred by an electric distribution utility to obtain any consent, release, waiver, or approval from any holder of an obligation described in division (E)(5) of this section that are necessary to be incurred for the electric distribution utility to issue or cause the issuance of phase-in-recovery bonds; (7) Any taxes, franchise fees, or license fees imposed on phase-in-recovery revenues; (8) Any costs related to issuing or servicing phase-in-recovery bonds or related to obtaining a financing order, including servicing fees and expenses, trustee fees and expenses, legal, accounting, or other professional fees and expenses, administrative fees, placement fees, underwriting fees, capitalized interest and equity, and rating-agency fees; (9) Any other similar costs that the public utilities commission finds appropriate. (F) "Financing order" means an order issued by the public utilities commission under section 4928.232 of the Revised Code that authorizes an electric distribution utility or an assignee to issue phase-in-recovery bonds and recover phase-in-recovery charges. (G) "Final financing order" means a financing order that has become final and has taken effect as provided in section 4928.233 of the Revised Code. (H) "Financing party" means either of the following: (1) Any trustee, collateral agent, or other person acting for the benefit of any bondholder; (2) Any party to an ancillary agreement, the rights and obligations of which relate to or depend upon the existence of phase-in-recovery property, the enforcement and priority of a security interest in phase-in-recovery property, the timely collection and payment of phase-in-recovery revenues, or a combination of these factors. (I) "Financing statement" has the same meaning as in section 1309.102 of the Revised Code. (J) "Phase-in costs" means costs, inclusive of carrying charges incurred before, on, or after the effective date of this section, authorized by the commission before, on, or after the effective date of this section to be securitized or deferred as regulatory assets in proceedings under section 4909.18 of the Revised Code, sections 4928.141 to 4928.143, or 4928.144 of the Revised Code, or section 4928.14 of the Revised Code as it existed prior to July 31, 2008, pursuant to a final order for which appeals have been exhausted. "Phase-in costs" excludes the following: (1) With respect to any electric generating facility that, on and after the effective date of this section, is owned, in whole or in part, by an electric distribution utility applying for a financing order under section 4928.231 of the Revised Code, costs that are authorized under division (B)(2)(b) or (c) of section 4928.143 of the Revised Code; (2) Costs incurred after the effective date of this section related to the ongoing operation of an electric generating facility, but not environmental clean-up or remediation costs incurred by an electric distribution utility because of its ownership or operation of an electric generating facility prior to the effective date of this section, which such clean-up or remediation costs are imposed or incurred pursuant to federal or state law rules, or regulations and for which the commission approves recovery in accordance with section 4909.18 of the Revised Code, sections 4928.141 to 4928.143, or 4928.144 of the Revised Code, or section 4928.14 of the Revised Code as it existed

prior to July 31, 2008. (K) "Phase-in-recovery property" means the property, rights, and interests of an electric distribution utility or an assignee under a final financing order, including the right to impose, charge, and collect the phase-in-recovery charges that shall be used to pay and secure the payment of phase-in-recovery bonds and financing costs, and including the right to obtain adjustments to those charges, and any revenues, receipts, collections, rights to payment, payments, moneys, claims, or other proceeds arising from the rights and interests created under the final financing order. (L) "Phase-in-recovery revenues" means all revenues, receipts, collections, payments, moneys, claims, or other proceeds arising from phase-in-recovery property. (M) "Successor" means, with respect to any entity, another entity that succeeds by operation of law to the rights and obligations of the first legal entity pursuant to any bankruptcy, reorganization, restructuring, or other insolvency proceeding, any merger, acquisition, or consolidation, or any sale or transfer of assets, regardless of whether any of these occur as a result of a restructuring of the electric power industry or otherwise.

#### **4928.235 Duration of final financing order.**

(A) (1) A final financing order shall remain in effect until the phase-in-recovery bonds issued under the final financing order and all financing costs related to the bonds have been paid in full. (2) A final financing order shall remain in effect and unabated notwithstanding the bankruptcy, reorganization, or insolvency of the electric distribution utility or any affiliate of the electric distribution utility or the commencement of any judicial or nonjudicial proceeding on the final financing order. (B) A final financing order is irrevocable and the public utilities commission may not reduce, impair, postpone, or terminate the phase-in-recovery charges authorized in the final financing order or impair the property or the collection or recovery of phase-in costs. (C) (1) Except as provided in division (C)(2) of this section, under a final financing order, the electric distribution utility retains sole discretion regarding whether to assign, sell, or otherwise transfer phase-in-recovery property, or to cause phase-in-recovery bonds to be issued, including the right to defer or postpone such assignment, sale, transfer, or issuance. (2) Subsequent to a financing order being issued or becoming final and taking effect, but before phase-in-recovery bonds have been issued, if market conditions are such that customers will not realize cost savings from the issuance of the phase-in-recovery bonds, the electric distribution utility shall not proceed with the securitization under the issued or final financing order.

#### **4929.08 Abrogation or modification of order.**

(A) The public utilities commission has jurisdiction over every natural gas company that has been granted an exemption or alternative rate regulation under section 4929.04 or 4929.05 of the Revised Code. As to any such company, the commission, upon its own motion or upon the motion of any person adversely affected by such exemption or alternative rate regulation authority, and after notice and hearing and subject to this division, may abrogate or modify any order granting such an exemption or authority only under both of the following conditions:

(1) The commission determines that the findings upon which the order was based are no longer valid and that the abrogation or modification is in the public interest;

(2) The abrogation or modification is not made more than eight years after the effective date of the order, unless the affected natural gas company consents.

(B) After receiving an exemption or alternative rate regulation under section 4929.04 or 4929.05 of the Revised Code, no natural gas company shall implement the exemption or alternative rate regulation in a manner that violates the policy of this state specified in section 4929.02 of the Revised Code. Notwithstanding division (A) of this section, if the commission determines that a natural gas company granted such an exemption or alternative rate regulation is not in substantial compliance with that policy, that the natural gas company is not in compliance with its alternative rate plan, or that the exemption or alternative rate regulation is affecting detrimentally the integrity or safety of the natural gas company's distribution system or the quality of any of the company's regulated services or goods, the commission, after a hearing, may abrogate the order granting such an exemption or alternative rate regulation.

### **Ohio Constitution, Article II, § 2.28 Retroactive laws**

The general assembly shall have no power to pass retroactive laws, or laws impairing the obligation of contracts; but may, by general laws, authorize courts to carry into effect, upon such terms as shall be just and equitable, the manifest intention of parties, and officers, by curing omissions, defects, and errors, in instruments and proceedings, arising out of their want of conformity with the laws of this state.



*Ohio Power Company, Individually and, if Their Proposed Merger is Approved, as a Merged Company (collectively AEP Ohio) for an Increase in Electric Distribution Rates, Case Nos. 11-351-EL-AIR, 11-352-EL-AIR (the "Distribution Rate Case").* The Opinion and Order was issued in a proceeding commenced under Section 4909.18, Revised Code, and is a final order from which no appeal was taken.

The distribution regulatory assets being recovered through the DARR are comprised of the following costs or charges (the "Phase-In Costs"):

- Consumer education, customer choice implementation, and transition plan filing costs plus carrying charges, approved in Case Nos. 99-1729-EL-ETP and 99-1730-EL-ETP;
- Rate Stabilization Plan rate case expenses plus carrying charges, approved in Case No. 04-169-EL-UNC;
- Carrying charges on distribution line extension charges, approved in Case No. 01-2708-EL-COI;
- Monongahela Power Company transfer integration costs plus carrying charges and acquired net regulatory assets, approved in Case No. 05-765-EL-UNC;
- AEP Ohio's voluntary Ohio Green Power Pricing Program costs plus carrying charges, approved in Case No. 06-1153-EL-UNC; and
- Storm costs related to the Hurricane Ike windstorm experienced in September 2008 plus debt carrying costs, approved in Case No. 08-1301-EL-AAM.

The deferral balance of the Phase-In Costs collectable through the existing DARR, as of June 30, 2012 was \$309 million. The estimated deferral balance of the Phase-In Costs collectable through the DARR, as of November 30, 2012, is \$ 291.5 million. November 30 is currently estimated as the date of the Phase-In Costs deferral balance that will be used for the calculation of the Phase-In-Recovery Bonds, but the actual date will depend on a number of factors which will influence the timing of the bond issuance, including, among others, whether the registration statement is reviewed, the timing of the issuance of the Financing Order and its becoming final, and financial market developments.

The Phase-In-Recovery Bonds will constitute "Bonds" within the meaning of Section 4928.23(C), Revised Code. The proposed issuance of Phase-In-Recovery Bonds will benefit customers by providing both cost savings and rate impact mitigation through reducing the overall cost of these regulatory assets and by reducing the rates customers currently are paying toward their recovery through the existing DARR. The proposed securitization transaction should, based upon current market conditions, significantly reduce the carrying charges over the recovery period for these Phase-In Costs resulting in customer savings through the issuance of the Phase-In-Recovery Bonds (even after including Financing Costs as discussed below) as compared to the cost recovery method previously approved by the Commission. Based upon the proposed recovery period of seven years, the estimated nominal costs savings to customers is approximately \$11.8 million in the aggregate as shown on Exhibit A. The net present value of expected customer savings is estimated to be \$20.4 million based on current interest rates and market conditions. In addition, the proposed securitization is expected to mitigate rate impacts to customers by flowing the cost savings through to customers in a manner that yields lower associated rates compared to the cost recovery method previously approved by the Commission,

i.e., the DARR which provides for a carrying charge of 5.34%, and consumers will benefit on a net present value basis so long as the weighted average interest rate of the Phase-In-Recovery Bonds does not exceed 3.32%, as shown on page 2 of Exhibit A.

Exhibit A to this Application compares the benefits arising from the lower costs of the securitization contrasted to the carrying charge authorized in the DARR. The expected rate mitigation is based on current interest rates, market conditions and the existing DARR as approved by the Commission. In order to reach a settlement agreement in the Distribution Rate Case, OPCo agreed to waive the traditional utility method of recovery that would have allowed OPCo to earn a carrying charge on the DARR based on its weighted average cost of capital (WACC), including the gross-up impact of income taxes on equity portion of the carrying charge rate. OPCo agreed to forgo a pre-tax WACC of approximately 10.77%, and agreed to accept a lower carrying charge of 5.34%, its cost of debt. If OPCo compared the benefits of securitization to OPCo's pre-tax weighted average cost of capital, the benefits to customers would be approximately \$52 million on a nominal basis.

The proceeds from the issuance of the Phase-In-Recovery Bonds, after the payment of upfront Financing Costs (i.e., costs of issuance for the Phase-In-Recovery Bonds, as described herein), will be applied to the reduction of OPCo's existing debt through avoidance of refinancing long-term debt maturing in 2013 and defeasance of other long-term debt.

## **II. Securitization Transaction**

1. OPCo is an Ohio corporation engaged in the distribution of electricity for sale to retail customers in Ohio under rates and tariffs approved by this Commission and an electric distribution utility pursuant to Section 4928.01(A)(6), Revised Code. CSP and OPCo were merged effective December 31, 2011 and OPCo is the surviving entity.

2. The Act provides for electric distribution utilities to securitize certain costs previously authorized to be securitized or deferred as regulatory assets through the issuance of Phase-In-Recovery Bonds pursuant to a Financing Order issued by the Commission. The Act directs the Commission to issue a Financing Order if, at the time the Financing Order is issued, the Commission finds, consistent with market conditions, that the securitization will measurably enhance cost savings to OPCo's customers and mitigate rate impacts to those customers as compared with the Commission's previously-approved recovery methods or traditional financing mechanisms, and is consistent with Ohio policy as set forth in Section 4928.02, Revised Code. Section 4928.232(D), Revised Code.
3. OPCo requests that the Commission issue a Financing Order pursuant to the provisions of Sections 4928.232(C)(1) and (D)(2), Revised Code, authorizing the issuance of up to an aggregate amount of \$320, million of Phase-In-Recovery Bonds, in one or more series and one or more tranches. For purposes of estimating the benefits from securitization, OPCo has estimated a \$291.5 million deferral balance of Phase-In Costs collectable through the DARR at the assumed date of the issuance (January 15, 2013) and estimated \$16 million of upfront Financing Costs, for an approximate issuance amount of \$307.5 million. The actual timing of issuance will depend on a number of factors, including, among others, whether the registration statement for the Phase-In-Recovery Bonds is approved, the timing of the issuance of the Financing Order and its becoming final and financial market conditions. The actual amount of Phase-In-Recovery Bonds issued will be an amount equal to (i) the deferral balance of Phase-In Costs collectable through the DARR as of the month-end which is at least 20 days prior to the date of the pricing of the Phase-In-Recovery Bonds (the "DARR Balance Amount") and (ii) the estimated upfront

Financing Costs described in Exhibit B. The proceeds from the issuance of the Phase-In-Recovery Bonds will allow full collection of the associated upfront Financing Costs and compensate OPCo for Phase-In Costs described in Section I of this Application. The Phase-In-Recovery Bonds will be issued at an effective interest rate (after taking into account upfront and ongoing Financing Costs) lower than OPCo's Commission-authorized carrying charge for such regulatory assets. The benefits to customers of the lower effective interest rate versus the current authorized carrying charge in the DARR are reflected in a reduction in the expected amount payable by customers on both a nominal and a net present value basis as compared with the existing recovery mechanism.

4. All of OPCo's customers will be responsible for repayment of the Phase-In-Recovery Bonds through separate, non-bypassable charges called Phase-In-Recovery Charges. Sections 4928.231(A)(2) and 4928.239(B)(1), Revised Code. For purposes of this proceeding, "Phase-In-Recovery Charges" are those charges to be set forth in a rider to be approved by the Commission in this proceeding, which, together with the adjustment mechanism to be authorized by the Commission pursuant to Section 4928.238, Revised Code, will provide for the full and timely recovery of all costs associated with the proposed Phase-In-Recovery Bonds including, without limitation, debt service and all other Financing Costs.
5. OPCo intends to use the proceeds from the issuance and sale of Phase-In-Recovery Bonds, net of upfront Financing Costs, to redeem, retire, repay or defease a portion of its existing debt. The Phase-In-Recovery Bonds will not be included in the regulatory capital structure of OPCo going forward. For GAAP purposes, the Phase-In-Recovery Bonds will be recorded as long term debt on the balance sheet of OPCo's bankruptcy-

remote special purpose entity, which will be a subsidiary of OPCo. Because the SPE will be consolidated with OPCo for financial reporting purposes, the Phase-In-Recovery Bonds will, under GAAP, also be reflected on the consolidated balance sheet of OPCo.

6. Notwithstanding that the Phase-In-Recovery Bonds' scheduled recovery period (and potential tranching, if any, resulting in multiple tranches of Phase-In-Recovery Bonds with different maturity dates) will be determined by reference to rating agency considerations and market conditions. As illustrated in Exhibit C, the Indicative Transaction Structure, OPCo intends that the overall scheduled (or expected) recovery period for the Phase-In-Recovery Bonds will not exceed 7.5 years. The Phase-In-Recovery Bonds (and each tranche, if applicable), however, will have a later final legal maturity date (no more than 1 year after the expected maturity date for such Bonds or tranche of Bonds) by which the Phase-In-Recovery Bonds must be paid in full in the event collections of the Phase-In-Recovery Charges are lower than projected prior to the expected maturity date. Based upon the market conditions as of the date of filing this Application, the recommended tranches with initial principal amounts, first scheduled principal payment dates, expected maturity dates, final legal maturity dates and average lives are shown in Exhibit D. OPCo intends to issue the Phase-In-Recovery Bonds at one time. Assuming no material changes in market conditions, OPCo would expect to issue the Phase-In-Recovery Bonds within one hundred twenty (120) days of the Financing Order becoming a Final Financing Order as defined in Section 4928.23(G), Revised Code. For illustrative purposes, Exhibit D assumes an issuance date of January 15, 2013. The final number of tranches, payment and maturity dates and average lives may differ

from those set forth in Exhibit D due to market conditions on the date of pricing of the Phase-In-Recovery Bonds.

7. An estimate of the upfront and ongoing Financing Costs is set forth in Exhibit B. Most of the Financing Costs set forth in Exhibit B may vary from the estimates. For instance, the most significant ongoing financing cost, debt service on the Bonds, cannot be known until the Bonds are priced in the market. Even after pricing, debt service requirements can change because scheduled debt service could differ from actual debt service if delays in payments are so severe as to cause a shortfall in payments of scheduled principal and interest. Accordingly, there can be no cap on the amount of ongoing Financing Costs which may be paid from Phase-In-Recovery Charges. As for upfront Financing Costs, these costs as well will vary from the estimates set forth in Exhibit B as a result of changes in market conditions, the SEC registration process, and other factors (e.g., the actual costs of defeasing or otherwise retiring existing long-term debt), none of which can be known at this time. Because the actual structure and pricing of the Phase-In-Recovery Bonds will not be known at the time the Financing Order is issued, following determination of the final terms of the Phase-In-Recovery Bonds and prior to issuance of the Phase-In-Recovery Bonds, OPCo will file with the Commission, no later than the close of business on the second business day after pricing the Phase-In-Recovery Bonds, an issuance advice letter in the form attached as Exhibit I (the "Issuance Advice Letter") that provides a final estimate of upfront Financing Costs as well as the estimated ongoing Financing Costs. OPCo's current estimate of such upfront Financing Costs is approximately \$16 million in the aggregate, including debt retirement/defeasance costs, currently estimated at approximately \$11 million, and approximately \$5 million of other

upfront Financing Costs described on Exhibit B. If the actual upfront Financing Costs are less than the estimated upfront Financing Costs included in the principal amount securitized, such unused funds will be deposited into the Collection Account (as described below) to be available for payment of debt service on the Phase-In-Recovery Bonds and with the result that the periodic billing requirement following such deposit would be reduced to take into account the availability of such unused funds (together with interest earned thereon through investment by the trustee in eligible investments). If the actual issuance costs are more than the estimated upfront Financing Costs set forth in the Issuance Advice Letter, OPCo may request recovery of the remaining upfront Financing Costs through traditional ratemaking mechanisms.

- a) In the case of debt defeasance costs, these costs may vary significantly in response to market conditions and as a result of the terms of the various debt securities to be defeased (e.g. the cost of securities deposited to defease the debt securities).
- b) In addition, the cost of debt retirement or tender is impacted by changes in interest rates. The lower prevailing interest rates are at the time of retirement or tender, the higher the cost will be to effect such retirement or successful tender. However, the impact of any increase in debt retirement costs caused by lower market interest rates should be somewhat offset by a lower cost of debt on the Phase-In-Recovery Bonds. Therefore, OPCo requests that the Commission authorize it to retire its debt with the proceeds from the Phase-In-Recovery Bonds in any manner, consistent with market conditions, that does not impede the securitization

transaction from achieving measurably enhanced cost savings and mitigating rate impacts for customers.

### **III. Retail Rate Impact and Phase-In-Recovery Charges**

8. The proposed securitization will provide customers with the benefit of lower cost financing compared to the existing DARR. Exhibit A shows the expected debt service associated with the Phase-In-Recovery Bonds based upon market conditions as of the date of this Application and compares those amounts to the current expected costs of recovery for the uncollected Phase-In Costs under the DARR. Exhibit A shows the projected savings to customers on both a nominal and a net present value basis. As demonstrated on Exhibit A, the proposed issuance of Phase-In-Recovery Bonds, consistent with the market conditions as of the date of filing this Application, will both measurably enhance cost savings to customers and mitigate rate impacts to customers as compared with recovery of such uncollected Phase-In Costs under the DARR. In comparing the estimated Phase-In-Recovery Charges to the rates under the DARR, it is important to acknowledge that such rates are not directly comparable (e.g., current rates do not reflect customer uncollectibles which are recovered separately, while Phase-In-Recovery Charges must be adjusted (through the adjustment mechanism described below) to reflect uncollectibles in order to assure the timely payment of the Phase-In-Recovery Bonds). While all amounts shown below: (i) are dependent upon a number of assumptions; (ii) are based on current estimates and market conditions; and (iii) will periodically change throughout the recovery period in accordance with the approved adjustment mechanism, upon issuance of the proposed Phase-In-Recovery Bonds, OPCo customers are expected to have an estimated initial Phase-In-Recovery Charge of

7.4597% of base distribution revenue. (Base distribution revenue excludes rider or surcharge revenue incurred as part of distribution service.) If the DARR continues as previously approved, OPCo customers will continue to pay a monthly charge of 8.501% of base distribution revenue. See Exhibit F for the typical bill impacts for customer classes and usage levels.

9. Consistent with Section 4928.231(B)(5), Revised Code, Exhibit A provides OPCo's initial estimate of the amount of Phase-In-Recovery Charges necessary to recover all Phase-In Costs and Financing Costs. Attached as Exhibit G are proposed tariff sheets reflecting Phase-In-Recovery Charges that are expected to approximate the final tariff charges, based upon currently available information related to the terms of the proposed issuance of Phase-In-Recovery Bonds (the "Proposed Tariff Sheets"). Exhibit G also includes the DARR tariff sheets red-lined to reflect the withdrawal of that rider upon the successful implementation of the proposed tariff. Upon pricing of the Phase-In-Recovery Bonds, the Proposed Tariff Sheets will be updated and attached to the Issuance Advice Letter to reflect actual debt service, other Financing Costs and any other revised assumptions (e.g., electricity consumption) and will be filed with the Commission pursuant to Section 4928.232(H), Revised Code (as so updated, the "Final Tariff Sheet"). Upon the issuance of the Phase-In-Recovery Bonds, OPCo will reduce the DARR deferral balance by the DARR Balance Amount to reflect the recovery of those Phase-In Costs through securitization. OPCo will make a final reconciliation filing, in a future regulatory proceeding to be commenced within ninety days after the date of bond issuance, to address the remaining deferral balance of the DARR.

10. As reflected in the description on the adjustment mechanism shown in Exhibit E, the determination of the Phase-In-Recovery Charges will take into account (a) the timing and amounts of principal, interest and other ongoing Financing Costs of the Phase-In-Recovery Bonds and (b) the expected monthly electricity consumption by customers. The Phase-In-Recovery Charges shall also take into account factors such as (i) expected delays between the billing and collection of Phase-In-Recovery Charges and (ii) expected Phase-In-Recovery Charge uncollectibles, which factors will impact the amount of Phase-In-Recovery Charges which will actually be available for the payment of Phase-In-Recovery Bonds in any period. The methodology proposed for allocating the amounts to be collected under the Phase-In-Recovery Charges among customer classes will be the same as the methodology used to allocate the DARR. For each upcoming payment period, OPCo will estimate the revenue requirement needed to be billed (the "periodic billing requirement" or "PBR") to assure that all revenues, receipts, collections, claims or other proceeds arising from the Phase-In Recovery Property (the "Phase-In-Recovery Revenues") will be sufficient to pay on a timely basis all principal and interest on the Phase-In-Recovery Bonds together with other ongoing Financing Costs during such period, and will divide such amount by the projected base distribution revenues for the same period. The resulting percentage will then be multiplied by the base distribution charges otherwise charged to each class of customers in order to generate the amount of Phase-In-Recovery Charges to be billed with the result that each rate schedule will be paying approximately the same proportion of the total Phase-In-Recovery Charges as it otherwise would for the DARR under the existing recovery methodology.

11. Because the Phase-In-Recovery Charges are recovered on a nonbypassable basis, the methodology proposed for allocating the Phase-In-Recovery Charges applicable to governmental aggregation customers is the same as for all other customers. The nonbypassability of the Phase-In-Recovery Charges ensures that all customers, including governmental aggregation customers, receive a proportion of the benefits generally consistent with the proportion of the charges they are paying under the existing recovery methodology.
12. The Phase-In-Recovery Bonds would be structured in the manner provided for in the Financing Order consistent with the Act, thus enabling the Phase-In-Recovery Bonds to achieve the highest credit rating and a lower cost than OPCo's existing, Commission-approved carrying charge, thereby both measurably enhancing cost savings to customers and mitigating rate impacts to customers as compared with the current Commission-approved recovery method, the DARR. The Phase-In-Recovery Bonds would also be structured, except for the first payment, to result in levelized debt payments. The Phase-In-Recovery Bonds will be issued with a fixed rate of interest. OPCo believes that any potential benefits of issuing the Phase-In-Recovery Bonds at a floating interest rate would be outweighed by potential risks due to volatile market conditions. The Phase-In-Recovery Bonds shall not constitute a debt or a pledge of the faith and credit or taxing power of the State of Ohio or any county, municipal corporation or other political subdivision of the State of Ohio. Section 4928.2314, Revised Code.
13. OPCo requests that the Financing Order establish the nonbypassable Phase-In-Recovery Charges in accordance with the Proposed Tariff Sheets, described in paragraph 9 above. Such charges, following the issuance of the Phase-In-Recovery Bonds, will be imposed

and collected from all customers pursuant to Section 4928.239(B)(1), Revised Code, as updated through the Final Tariff Sheet. Pursuant to Section 4928.232(H), Revised Code, the initial Phase-In-Recovery Charges will be determined by OPCo prior to the issuance of the Phase-In-Recovery Bonds and filed with the Commission in the Final Tariff Sheet as an attachment to the Issuance Advice Letter. These charges shall be final and effective upon the issuance of the Phase-In-Recovery Bonds, without further Commission action, provided that OPCo may delay imposition of such charges to the first day of the billing cycle of the revenue month next following the issuance date of the Phase-In-Recovery Bonds or such other date not more than 30 days following the date of issuance which is set forth in the Issuance Advice Letter.

14. The property, rights and interests of OPCo or its SPE assignee (further discussed below) under the Financing Order, including, among other things, the right to impose, charge and collect the Phase-In-Recovery Charges and the right to obtain adjustments to those charges, pursuant to Section 4928.238, Revised Code, together with the revenues, receipts, collections, rights to payment, payments, moneys, claims or other proceeds arising from the rights and interests created under the Financing Order, shall constitute, until fully collected, Phase-In-Recovery Property as defined in Section 4928.23(K), Revised Code. The Phase-In-Recovery Charges will be included in customers' bills, and OPCo will note on customers' bills that the right to impose, charge and collect Phase-In-Recovery Charges is owned by the SPE.
15. OPCo seeks approval of a bill message that includes the following (or substantially similar) language: "In Case No. 12-1969-EL-ATS the Commission approved recovery of previously incurred costs, including PUCO-approved Phase-In-Recovery Charges, Ohio

Power Company collects from all customers on behalf of its subsidiary, Ohio Power Phase-In Recovery Bonds I, which owns the right to impose and collect such charges." OPCo may also include similar language in billing inserts or other communication to customers. Such notation is important to preserve the "bankruptcy remote" nature of the securitization by respecting the legal ownership of the Phase-In-Recovery Property.

**IV. Securitization Structure and Documentation.**

16. OPCo will form a wholly-owned limited liability company, which is expected to be organized in Delaware, as a SPE for purposes of the securitization transaction. OPCo will then transfer, sell or assign its Phase-In-Recovery Property to the SPE. See H for a structure/transaction flow chart. OPCo requests that the Financing Order confirm the formation of the SPE, the sale of Phase-In-Recovery Property to the SPE, and the issuance by the SPE of Phase-In-Recovery Bonds secured by the Phase-In-Recovery Property, including Phase-In-Recovery Charges and other assets and property owned by the SPE.

- a) The SPE will be a bankruptcy-remote, special purpose limited liability company, with its activities generally limited to (i) purchasing, owning, administering and servicing the Phase-In-Recovery Property transferred, sold or assigned to it, (ii) issuing the Phase-In-Recovery Bonds, (iii) making payments on the Phase-In-Recovery Bonds, (iv) managing, selling, assigning, pledging, collecting amounts due on, and otherwise dealing with the Phase-In-Recovery Property and (v) granting a first priority security interest in the Phase-In-Recovery Property to secure such Phase-In-Recovery Bonds. Restrictions will be imposed on the SPE's ability to commence a bankruptcy case or other insolvency proceeding. The SPE

will have no employees, and it will engage with other parties to undertake the activities necessary to issue the Phase-In-Recovery Bonds and perform other functions in connection with the issuance of the Bonds.

- b) The SPE will establish one or more segregated trust accounts (collectively, the "Collection Account") into which all Phase-In-Recovery Charge remittances shall be deposited. The indenture trustee will on a timely basis apply moneys in this Collection Account to pay principal and interest on the Bonds and other Financing Costs. The Collection Account will include one or more subaccounts, including a general subaccount which will hold all collections of Phase-In-Recovery Charges pending distribution to bondholders, a capital subaccount as described below, and an excess funds subaccount. The excess funds subaccount will hold any Phase-In-Recovery Charge remittances and investment earnings received by the Servicer during any payment period which are in excess of the amounts needed to pay Financing Costs accrued and payable. The Collection Account may, if required by the rating agencies, also include an overcollateralization subaccount to hold additional cash collections of Phase-In-Recovery Charges in order to provide more funds available to pay Financing Costs in the event of a shortfall.
- (c) OPCo will capitalize the SPE in an amount anticipated to be 0.50 percent of its initial principal balance of Phase-In-Recovery Bonds, based upon guidance from the Internal Revenue Service. Such amount will be held in a capital subaccount and will be pledged to secure the Phase-In-Recovery Bonds. This equity contribution helps assure that OPCo will not recognize gross income upon the sale of the Phase-In-Recovery Property to the SPE. OPCo intends to finance the

contribution of the capital amount to the SPE with cash from working capital. The amount in the capital subaccount will, however, be available to pay ongoing Financing Costs that may vary from estimates due to unexpected shortfalls in collections or increases in such Financing Costs, in which event additional Phase-In-Recovery Charges may be assessed to replenish the withdrawals from the capital subaccount. OPCo will be authorized to recover its average long term debt rate without reduction for accumulated deferred income taxes on the capital contribution to the SPE as an ongoing miscellaneous Financing Cost. Upon the full payment of the Phase-In-Recovery Bonds, the SPE will return to OPCo all amounts remaining in the Collection Account. . Any excess (or deficit) of such amounts as compared to the amount of capital contributed to OPCo should be addressed in OPCo's other regulatory proceedings.

- d) The sale of Phase-In-Recovery Property by OPCo to the SPE, as authorized under the Financing Order, will occur concurrently with the issuance of the Phase-In-Recovery Bonds. Concurrently with such sale, there will arise an existing, present property right and interest in such Phase-In-Recovery Property, which shall continue to exist until the Phase-In-Recovery Bonds and all applicable Financing Costs are paid in full. Section 4928.234(C), Revised Code. Consistent with Section 4928.232(G), Revised Code, OPCo requests that the Financing Order confirm the creation of its Phase-In-Recovery Property and that such creation shall be simultaneous with the sale of that property to its SPE, and the grant of a security interest in its Phase-In-Recovery Property, among other SPE assets and property, to secure the repayment of Phase-In-Recovery Bonds and

Financing Costs. Additionally, consistent with Section 4928.234(D), Revised Code, the Financing Order should confirm that all such Phase-In-Recovery Property shall continue to exist regardless of whether Phase-In-Recovery Charges have been billed, have accrued or have been collected and notwithstanding any requirement that value or amount of the property is dependent on the future provision of service to customers, and shall continue to exist until the Phase-In-Recovery Bonds and all Financing Costs are paid in full.

- e) The SPE will acquire the Phase-In-Recovery Property from OPCo using the net proceeds from the Phase-In-Recovery Bonds. The repayment of the Phase-In-Recovery Bonds by the SPE will be secured by a first priority pledge and security interest in all right, title, and interest of the SPE in (i) the Phase-In-Recovery Property, (ii) the transaction documents, (iii) the collection account and all subaccounts established in the Indenture (discussed below) under which the Phase-In-Recovery Bonds will be issued, (iv) the cash used to capitalize the SPE, (v) all other property owned by the SPE (with limited exceptions as may be appropriate) and (vi) all proceeds of each of the foregoing. The SPE's Phase-In-Recovery Bonds will be non-recourse to OPCo and its assets (i.e., OPCo will have no obligation to pay any of the principal, interest or other amounts payable on the Phase-In-Recovery Bonds or any Financing Costs); provided, however, that OPCo could be liable to holders of Phase-In-Recovery Bonds in the event that it breached representations, warranties or covenants made by it in connection with its Sale Agreement (discussed below) or otherwise to such holders in connection with the securitization.

- f) The SPE will be an "Assignee" of Phase-In-Recovery Property as defined in Section 4928.23(B), Revised Code, and as provided for in Section 4928.234(A), Revised Code.
  - g) The Indenture pursuant to which the Phase-In-Recovery Bonds are issued shall have a "priority of payments" that shall establish how collections of Phase-In-Recovery Charges and any other amounts are applied to pay principal, interest on, and other costs related to the Phase-In-Recovery Bonds. The right to impose, charge and collect Phase-In-Recovery Charges, although owned by the SPE, will be accorded similar treatment with OPCo's own charges under applicable statutes, the Commission's rules, and OPCo's tariffs, rules and practices, including for purposes of priority of customer payments and termination/reconnection of service.
17. The Phase-In-Recovery Bonds contemplated by the transactions described in this Application will be "asset-backed securities." A key feature of any asset-backed security is that the SPE owning the asset or group of assets underlying those securities be "bankruptcy remote" from the entity originating such asset or group of assets, which in this case will be OPCo. More specifically, an asset-backed security must be secured by, and payable from, a cash flow stream associated with an identifiable asset, the collections from which are sufficient to pay debt service and related costs, and the ownership of that asset is normally vested in a limited purpose entity, such as a limited liability company or corporation, which is insulated from the credit risks, including the possible bankruptcy, of the originating entity. This structure helps to ensure that the Phase-In-Recovery Bonds will have less credit risk than debt securities issued by OPCo, and investors should

therefore be willing to accept a lower carrying charge for the asset-backed security than for other debt of OPCo. If such criteria are satisfied in the proposed securitization, the Phase-In-Recovery Bonds secured by the Phase-In-Recovery Property should receive a triple-A (or equivalent) credit rating from applicable rating agencies.

18. In order to assure that the Phase-In-Recovery Bonds receive the highest ratings and to enhance their marketability, there are a number of other structural elements and express regulatory authorizations and confirmations customarily included in a Financing Order even though some may be repetitive of provisions in the Act. These structural elements, authorizations and confirmations are described in this Application and include, among others, those described in paragraphs (a) through (j) below. For the Commission's convenience and to maximize the rating and marketability of Phase-In-Recovery Bonds, a proposed Financing Order, incorporating all the necessary and customary structural elements, authorizations and confirmations, is included in this Application as Exhibit J. OPCo requests that the Commission adopt the proposed Financing Order without material modification because any such modification could negatively impact the rating and marketability of the Phase-In-Recovery Bonds.

- (a) Irrevocability: Consistent with Section 4928.235(B), Revised Code, the Financing Order should provide that it is irrevocable when final and the Commission may not reduce, impair, postpone, or terminate the Phase-In-Recovery Charges authorized in the Financing Order or impair the Phase-In-Recovery Property or the collection of Phase-In-Recovery Charges or the recovery of the DARR Balance Amount and Financing Costs. The Financing Order should further confirm, consistent with the Act, that no adjustment (described in Section

4928.238, Revised Code) approved by the Commission shall affect the irrevocability of the Financing Order.

- (b) State Pledge: Consistent with Section 4928.2315, Revised Code, the Financing Order should confirm that the State of Ohio pledges to and agrees with the bondholders, any assignee, and any financing parties under the Financing Order that the State of Ohio will not take or permit any action that impairs the value of Phase-In-Recovery Property under the Financing Order or revises the DARR Balance Amount or, except as allowed under Section 4928.238, Revised Code (i.e., the adjustment mechanism) reduces, alters or impairs Phase-In-Recovery Charges until all principal, interest and premium, if any, of the Phase-In-Recovery Bonds, all Financing Costs, and all other amounts to be paid under any ancillary agreement are paid or performed in full. The Financing Order should further confirm, consistent with Section 4928.2315(B), Revised Code, that the SPE is permitted to include the above-described pledge in the Phase-In-Recovery Bonds, ancillary agreements, and documentation relating to the issuance and marketing of the Phase-In-Recovery Bonds.
- (c) True Sale: Consistent with Section 4928.2313, Revised Code the Financing Order should confirm that any sale, assignment, or transfer of Phase-In-Recovery Property under a Financing Order shall be an absolute transfer and true sale of, and not a pledge of or secured transaction relating to, the seller's right, title and interest in, to, and under the Phase-In-Recovery Property.
- (d) Successor Utility: Consistent with Section 4928.2311, Revised Code, the Financing Order should confirm that any successor to an electric distribution

utility subject to a Financing Order shall perform and satisfy all obligations of the electric distribution utility under the Financing Order.

- (e) Security Interest: Consistent with Section 4928.2312, Revised Code, the Financing Order should confirm that a valid and binding security interest in the Phase-In-Recovery Property, will be created, perfected and enforced to secure the repayment of the principal of and interest on Phase-In-Recovery Bonds, amounts payable under any ancillary agreement, and other Financing Costs. The security interest will have priority over any other lien that may subsequently attach to the Phase-In-Recovery Property. The Financing Order should further confirm that the priority of such security interest is not affected by the commingling of Phase-In-Recovery Charges with other amounts as provided in Section 4923.2312(D)(2), Revised Code, and that no application of the adjustment mechanism (described in Section 4928.238, Revised Code) shall affect the validity, perfection, or priority of a security interest in or the transfer of Phase-In-Recovery Property under the Financing Order, as provided in Section 4923.2312(D)(3), Revised Code.
- (f) Bankruptcy of the electric distribution utility: Consistent with Section 4928.2310(A)(1), Revised Code, the Financing Order should confirm that if an electric distribution utility subject to a Financing Order defaults on any required payment of Phase-In-Recovery Revenues to any SPE, a court, upon application by an interested party and without limiting any other remedies available to the applicant, shall order the sequestration and payment of the Phase-In-Recovery Charges to the applicable SPE for the benefit of Bondholders, any assignee and any financing parties. The Financing Order should further confirm, consistent

with Section 4928.2310(A)(2), Revised Code, that, customers of an electric distribution utility and the SPE shall be held harmless for the electric distribution utility's failure to remit any required payment of Phase-In-Recovery Charges, and such failure shall in no way affect the Phase-In-Recovery Property or the rights to impose, collect and adjust the Phase-In-Recovery Charges.

- (g) Nonbypassability: Consistent with Section 4928.239, Revised Code, the Financing Order should confirm that the Phase-In-Recovery Charges cannot be avoided by any customer or other person obligated to pay the charges and that, if a customer subsequently receives retail electric distribution service from another electric distribution utility operating in the same service area, the Phase-In-Recovery Charges shall continue to apply to that customer.
- (h) Third Party Billing Agents: Consistent with the nonbypassable nature of the Phase-In-Recovery Charges, the Financing Order should further provide that (i) regardless of who is responsible for billing, the customers of that electric distribution utility shall continue to be responsible for Phase-In-Recovery Charges, (ii) if a third party meters and bills for the Phase-In-Recovery Charges, the electric distribution utility (as servicer) must have access to information on billing and usage by customers to provide for proper reporting to the SPE and to perform its obligations as servicer, (iii) in the case of a third party default, billing responsibilities must be promptly transferred to another party to minimize potential losses; and (iv) the failure of customers to pay Phase-In-Recovery Charges shall allow service termination by the electric distribution utility on behalf of the SPE of the customers failing to pay Phase-In-Recovery Charges in

accordance with Commission-approved service termination rules and orders. To ensure that the highest ratings on the bonds will be achieved, the Commission should provide in the Financing Order that the Phase-In-Recovery Charges will be collected in a manner that will not adversely affect the ratings on the Phase-In-Recovery Bonds.

- (i) Validity of the Financing Order: Consistent with Section 4928.235, Revised Code, the Financing Order should confirm that it shall remain in effect until the Phase-In-Recovery Bonds issued under the Financing Order are paid in full and all Financing Costs relating to the Phase-In-Recovery Bonds have been paid in full, and the Financing Order shall remain in effect and unabated notwithstanding the bankruptcy, reorganization, or insolvency of the electric distribution utility or any affiliate of the electric distribution utility or the commencement of any judicial or nonjudicial proceeding on the Financing Order.
- (j) Treatment of Phase-In-Recovery Charges: Consistent with Section 4928.232(E)(7), Revised Code, to ensure the full and timely collection of Phase-In-Recovery Charges, including minimizing the likelihood that customer defaults in the payment of Phase-In-Recovery Charges would result in additional charges being borne by other non-defaulting customers, the Financing Order should provide that the electric distribution utility or other servicer, on behalf of the SPE, shall terminate service of any customer who defaults in the payment of Phase-In-Recovery Charges in accordance with applicable statutes, Commission rules and orders and OPCo's rules, tariffs, and practices applicable to other charges owed directly to the electric distribution utility.

19. OPCo seeks approval to issue and sell the Phase-In-Recovery Bonds through a registered public offering under the U.S. Securities Act of 1933, as amended (the "Securities Act"). OPCo believes that a registered public offering will provide access to the most liquid market for the Phase-In-Recovery Bonds, and therefore the best method to achieve the savings for ratepayers. In connection with the public offering, OPCo and/or the SPE will enter into several agreements with respect to the securitization transaction. The material agreements listed below will be filed as exhibits to the registration statement filed with the SEC. In addition, the material terms of each agreement will also be summarized in the related prospectus included in the registration statement and used to offer and sell the Phase-In-Recovery Bonds.

- a) The SPE's LLC (Limited Liability Company) Agreement is the key organizational and governing document for the SPE and contains customary SPE provisions related to its restricted purposes. The LLC Agreement will not permit the SPE to engage in any activity not related to its restricted purposes and will contain provisions regarding separateness, independent managers and restrictions on commencing bankruptcy and insolvency proceedings. It is expected that the SPE will be managed by five managers, at least two of which will be independent managers, in each case appointed by OPCo. Only independent managers are expected to be paid compensation, and this cost, which is expected to be minimal, will be recovered through the Phase-In-Recovery Charges.
- b) The Administration Agreement will provide for the administrative functions that OPCo will provide to its SPE subsidiary, including services relating to the preparation of financial statements, any required filings with the SEC, any tax

returns required to be filed under applicable law, qualifications to do business and minutes of managers' meetings. OPCo (or any successor administrator thereof) will receive a periodic administration fee, expected to be \$50,000 annually, for performing these services, which, together with costs and expenses incurred by the administrator, will be recovered through Phase-In-Recovery Charges as Financing Costs.

- c) The Sale Agreement will provide for the terms and conditions of the absolute transfer and true sale of OPCo's right, title and interest in, to, and under the Phase-In-Recovery Property to the SPE, consistent with the provisions of Section 4928.2313, Revised Code. The SPE's obligation to purchase, and OPCo's obligation to sell, the Phase-In-Recovery Property is subject to numerous conditions in the Sale Agreement, including: (i) OPCo's delivery of a bill of sale identifying the Phase-In-Recovery Property, (ii) receipt of a Financing Order from the Commission creating the Phase-In-Recovery Property, (iii) certain conditions related to the solvency of OPCo, and (iv) delivery by OPCo of appropriate opinions of counsel and officers' certificates. The Sale Agreement will further provide that OPCo has taken all actions required to transfer ownership of the Phase-In-Recovery Property to the SPE, free and clear of all liens, and to perfect such transfer, and that the Phase-In-Recovery Bonds have received a rating or ratings as required by the Financing Order. The Sale Agreement will also contain customary representations, warranties and covenants of OPCo and the SPE.
- d) The Servicing Agreement describes the services that OPCo, as servicer, will provide to the SPE with respect to calculating, billing and collecting the Phase-In-

Recovery Charges. OPCo will be responsible for (among other things): (i) posting all collections, (ii) responding to inquiries by the trustee, customers, competitive retail electric suppliers (if any), third party billing agents (if any), the Commission or others regarding Phase-In-Recovery Charges, (iii) calculating historical electricity usage and customer payment information (e.g., uncollectibles, typical lags between billing and collection of charges), (iv) projecting future electricity usage and customer payment information, (v) accounting for collections, (vi) furnishing periodic certifications, reports and statements as specified in the transaction documents or required under applicable law, including filings under SEC Regulation AB and filings with the Commission, (vii) making certain filings as necessary to perfect the trustee's lien on the Phase-In-Recovery Property and (viii) taking all necessary action in connection with true-up adjustments. OPCo (or any successor servicer thereof) will receive a periodic servicing fee, which will be recovered through Phase-In-Recovery Charges as a Financing Cost. Based upon market precedent for such fees, the annual servicing fee shall be 0.10% of the initial principal amounts of the Phase-In-Recovery Bonds issued by the SPE, which fee will be paid to OPCo or a successor electric distribution utility company. OPCo, as servicer, will also be entitled to retain interest earnings and late charges on Phase-In-Recovery Charges pending disbursement to the trustee, as well as reimbursement for costs and expenses incurred by the servicer to third parties (i.e., accountants, attorneys). Customary for transactions of this type, in the unlikely event that there is no electric distribution utility successor willing or able to assume such servicing duties, a non-utility servicer may need to be

engaged. Given the incremental costs for such an entity to perform the servicing function (i.e., an entity not already billing and collecting the same customer base for other charges), the annual servicing fee for such non-utility successor shall not exceed 0.75% of the initial principal amount of the Phase-In-Recovery Bonds issued by the SPE, unless otherwise approved by the Commission.

- e) The Phase-In-Recovery Bonds issued by the SPE will be issued pursuant to an Indenture between the SPE and a third party trustee, which will describe the particular terms of the Phase-In-Recovery Bonds, including the principal amount, interest rate, payment dates, issuance date, collateral, authorized denominations, principal repayment schedule and other material terms of the Phase-In-Recovery Bonds. The Indenture will provide for certain covenants on the part of the SPE, including covenants restricting the SPE's ability to: (i) merge or consolidate with any other entity, (ii) sell, convey, transfer or otherwise dispose of its assets or property, (iii) terminate its existence or dissolve or liquidate, (iv) permit any lien, charge, security interest or other encumbrance (other than the lien and security interest granted under the Indenture) to be created, (v) engage in any business other than financing, purchasing, owning and managing the Phase-In-Recovery Property, and (vi) issue, incur, assume, guarantee or otherwise become liable for any indebtedness except for the Phase-In-Recovery Bonds and any other secured obligations arising under the transaction documents.

- 20. The fixed interest rates and yields for each series or tranche will not be known until the Phase-In-Recovery Bonds are priced. Based upon current market conditions, typical structural features, and assuming an SEC-registered offering of securities rated in the

highest category by the rating agencies, the weighted average annual interest cost of the Phase-In-Recovery Bonds is estimated to be less than 1.75%. In the absence of an extraordinary change in market conditions between the date of this Application and the issuance date of the Phase-In-Recovery Bonds, significant cost savings and mitigation of rate impacts through the proposed Phase-In-Recovery Bond issuance are expected to result. Based on the Phase-In-Recovery Bond expected principal repayment schedule reflected in Exhibit D (which is based upon level debt service), only a weighted average rate on the Phase-In-Recovery Bonds in excess of 3.32% would overcome on a net present value basis the benefits associated with OPCo's proposal so as to deny cost savings to customers. Consistent with Section 4928.232(F), Revised Code, OPCo requests that the Commission, in the Financing Order, afford it the flexibility in establishing the terms and conditions for the Phase-In-Recovery Bonds to accommodate changes in market conditions, including repayment schedules, the fixed interest rates, Financing Costs, collateral requirements, required debt service and other reserves. OPCo covenants, consistent with Section 4928.235(C)(2), Revised Code, that it will not proceed with the issuance of Phase-In-Recovery Bonds if it determines that market conditions are such that customers will not realize cost savings.

21. It is expected that the Phase-In-Recovery Bonds would be sold pursuant to a negotiated sale to investors, coordinated through one or more underwriters. The complexity of the Phase-In-Recovery Bonds and the resulting need for sophisticated marketing make it customary for securities of this type to be structured by the utility with the assistance of a financial advisor and offered pursuant to a negotiated sale in a public offering. After completing a request for proposals process and follow-up interviews, OPCo engaged

Citigroup Global Markets, Inc., an investment banking firm frequently involved in the underwriting of this type of securities, to assist in the process of structuring the transaction. OPCo's selection of a financial advisor to assist it in the issuance of Phase-In-Recovery Bonds took into account many attributes. OPCo considered each advisor's previous experience with securitization bonds, previous modeling and structuring experience, rating agency advisory capabilities, experience in marketing and distributing of securitization bonds, proposed advisory fees, and key personnel on each advisory team.

22. Certain of the Financing Costs to be recovered from the proceeds of the Phase-In-Recovery Bonds will be costs of issuing the Phase-In-Recovery Bonds and applying the proceeds thereof. These Financing Costs, which are referred to as "upfront Financing Costs", include, without limitation, estimated costs associated with the retiring, refunding or defeasing of OPCo's existing long-term debt, counsel fees, structural advisory fees, underwriting fees, rating agency fees, independent auditor's fees, SEC registration fees, printing and marketing expenses and other fees and expenses approved in the Financing Order. An estimate of the upfront Financing Costs is included as Exhibit B hereto. Other Financing Costs will constitute costs necessary to support, repay and service the Phase-In-Recovery Bonds. These Financing Costs, which are referred to as "ongoing Financing Costs" include principal and interest and redemption premium (if any) on the Bonds, servicer fees and expenses, trustee fees and expenses, SPE administrative fees and expenses, independent managers fees, rating agency surveillance fees, ongoing SEC compliance costs, accounting fees, the cost of maintaining or replenishing overcollateralization or other reserves or accounts (if any) established under

the indenture, any ancillary agreement or other financing document relating to the Phase-In-Recovery Bonds, and any other Financing Costs approved under the Financing Order. An estimate of the ongoing Financing Costs for the initial payment period is included in Exhibit B. While the ongoing Financing Costs are expected to be relatively stable over time, they may increase or decrease based upon factors beyond OPCo's control. Actual debt service payments, for example, may be different from scheduled debt service payments if projected Phase-In-Recovery Charges collections deviate from actual collections in a manner causing shortfalls in scheduled principal payments. Other ongoing Financing Costs, such as rating agency surveillance fees, trustee fees, and legal and accounting costs may change from time to time. In addition, ongoing Financing Costs include the recovery of all tax liabilities associated with the collection of the Phase-In-Recovery Charges or otherwise arising due to the securitization. All ongoing Financing Costs must be recovered through the imposition and collection and adjustment (or true up), from time to time, of the Phase-In-Recovery Charges.

**V. Adjustment Mechanism.**

23. OPCo has included in Exhibit E a proposed mechanism for making expeditious periodic adjustments in the Phase-In-Recovery Charges. Such adjustments, or true-up filings, must be made annually to correct for any undercollections or overcollections during the preceding period and to ensure that the Phase-In-Recovery Charges continue to generate amounts sufficient to timely pay all scheduled payments of principal and interest and any other amounts due in connection with the Phase-In-Recovery Bonds for the twelve month period following the true-up adjustment. Further, the servicer shall make a mandatory interim true-up filing semi-annually (quarterly after the last scheduled maturity date of

any Phase-In-Recovery Bonds) if the servicer forecasts that the Phase-In-Recovery Revenues will be insufficient to make all scheduled payments of principal, interest and other ongoing Financing Costs on a timely basis during the current or next succeeding payment period; provided that in the case of any quarterly true-up adjustment following the last scheduled maturity date of any Phase-In-Recovery Bonds, the true-up filing will be calculated to ensure that Phase-in-Recovery Charges are sufficient to pay such Phase-In-Recovery Bonds in full on the next succeeding payment date. In addition to mandatory annual and semi-annual (and quarterly after the last scheduled maturity date) true-up filings, the servicer will be permitted to file a true-up filing more frequently if it determines that such filing is necessary to ensure the expected recovery of amounts sufficient to pay scheduled principal and interest and ongoing Financing Charges. To implement any required annual adjustment, OPCo, within forty-five days of the anniversary of the issuance date, will file with the Commission a request for approval of adjusted Phase-In-Recovery Charges which shall go into effect on a bills rendered basis on no earlier than 15 days thereafter. Any other adjustment will be filed by OPCo at least 15 days prior to its proposed effective date. All such adjustments shall go into effect on a bills rendered basis on the date specified therein, which will be no earlier than 15 days after the filing of the request. Consistent with Section 4928.238(B), Revised Code, the Commission's review of any adjustment request would be limited to determining whether there is any mathematical error in the application of the adjustment mechanism approved in the Financing Order. Each adjustment will take into account revised projections of base distribution revenues, electricity consumption and customer payment information (e.g., uncollectibles, lags between customer billing and collection). Further, each

adjustment will take into account differences between estimated and actual revenue collections as well as differences between estimated and actual payment requirements for all ongoing Financing Costs. Each adjustment will ensure the recovery of adequate revenues sufficient to provide for the timely payment of scheduled principal and interest on the Phase-In-Recovery Bonds and all ongoing Financing Costs. Finally, pursuant to Section 4928.232(H), Revised Code, the initial Phase-In-Recovery Charges will be determined by OPCo prior to the issuance of the Phase-In-Recovery Bonds and filed with the Commission in the Final Tariff Sheet as an attachment to the Issuance Advice Letter. These charges shall be final and effective upon the issuance of the Phase-In-Recovery Bonds, without further Commission action, provided that OPCo may delay imposition of such charges to the first day of the billing cycle of the revenue month next following the issuance date of the Phase-In-Recovery Bonds or such other date not more than 30 days following the date of issuance which is set forth in the Issuance Advice Letter.

**VI. Timing of Commission Action.**

24. Issuance of a Financing Order as proposed herein is consistent with Section 4928.02, Revised Code. Customers will benefit from the provision of reasonably-priced retail electric service. Section 4928.02(A), Revised Code. Because securitization will reduce the overall cost of the nonbypassable DARR being replaced by the Phase-In-Recovery Charges and will result in cost savings and rate mitigation, securitization promotes customer choice and the diversity of electric supplies and suppliers. Section 4928.02(B) and (C), Revised Code. Securitization also recognizes the continuing emergence of competitive electricity markets through the development and implementation of flexible

regulatory treatment and facilitates the state's effectiveness in the global economy.  
Section 4928.02(G) and (N), Revised Code.

25. OPCo requests that the Commission consider and approve the securitization and all related matters requested in this Application on an expedited basis by October 1, 2012, which is within the 135-day timeline set forth in Section 4928.232(C)(1), Revised Code. Such expedited treatment will permit the Phase-In-Recovery Bonds to be issued in a timely fashion to take advantage of historically low interest rates and the currently functioning credit markets, and that the savings for customers expected to arise from the implementation of this Application may start being realized as soon as possible.

**WHEREFORE**, for the reasons set forth above, OPCo respectfully requests that the Commission:

- (1) Approve OPCo's proposed securitization and, pursuant to the Act, issue a Financing Order, substantially in the form of the proposed Financing Order attached as Exhibit J, granting any and all authorizations and approvals that may be required under the Act, for the consummation of the securitization transaction and related matters (all as described in this Application), including, without limitation, (a) the recovery of Phase-In Costs and upfront Financing Costs, through the issuance of up to an aggregate amount of \$320 million of Phase-In-Recovery Bonds payable from collections from Phase-In-Recovery Charges, and the execution, delivery and performance of all documentation necessary to consummate the securitization transaction, (b) the imposition, charging, and collection of Phase-In-Recovery Charges, (c) the creation of the Phase-In-Recovery Property (such creation to be simultaneous with the sale of such Phase-In-Recovery Property to the SPE and the issuance of the Phase-In-Recovery Bonds), (d) the

establishment of an adjustment mechanism as described herein to be applied from time to time to adjust the Phase-In-Recovery Charges to ensure the timely payment of Phase-In-Recovery Bonds and all ongoing Financing Costs, (e) the calculation and allocation of the Phase-In-Recovery Charges among customer classes, (f) the maximum term of the Phase-In-Recovery Bonds, (g) the organization and capitalization of the SPE to which Phase-In-Recovery Property will be sold, (h) the servicing of Phase-In-Recovery Charges by OPCo as initial servicer or any successor servicer under the servicing agreement, (i) flexibility in establishing the terms and conditions for the Phase-In-Recovery Bonds to accommodate changes in market conditions, (j) the ability to issue Phase-In-Recovery Bonds and to effect correlated assignments, sales, pledges, and other transfers of Phase-In-Recovery Property (k) approval of the Final Tariff Sheet and associated adjustment mechanism, (l) approval of the proposed bill message, and (m) all of the determinations and descriptions required by Section 4928.232, Revised Code;

(2) Find that the proposed securitization, consistent with market conditions, measurably provides cost savings to customers and mitigates rate impacts to customers as compared to the existing cost recovery method for the Deferred Balance Amount;

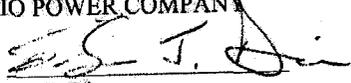
(3) Require that OPCo file with the Commission, no later than the end of the second business day after the pricing date for a series of Phase-In-Recovery Bonds, an Issuance Advice Letter (in the form attached as Exhibit I) that reports the actual dollar amount of the initial Phase-In-Recovery Charges and other information specific to the Phase-In-Recovery Bonds to be issued, including the Final Tariff Sheet;

(4) Make such other findings and issue such other orders as requested by OPCo in this Application; and

(5) Grant such other and further orders and approvals as it may deem necessary or proper under the circumstances.

Respectfully submitted,

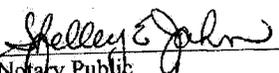
OHIO POWER COMPANY

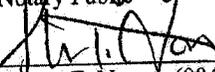
By:   
Selwyn J. Dias  
Vice-President of Regulatory and Finance

STATE OF OHIO     )  
                              )  
FRANKLIN COUNTY )

Before me a notary public, in and for Franklin County in the State of Ohio, personally appeared Selwyn J. Dias, a vice president of Ohio Power Company, and he being duly sworn says that the facts herein contained are true to the best of his knowledge and belief.

Dated: July 31, 2012

  
Notary Public

  
Steven T. Nourse (0046705)  
David C. House (0059706)  
AMERICAN ELECTRIC POWER CORPORATION  
1 Riverside Plaza, 29<sup>th</sup> Floor  
Columbus, Ohio 43215  
Telephone: 614-716-1608  
Fax: 614-716-2950  
stnourse@aep.com  
dchouse@aep.com

Daniel R. Conway (0023058)  
Kathleen M. Trafford (0021753)  
PORTER WRIGHT MORRIS & ARTHUR LLP  
41 South High Street  
Columbus, Ohio 43215  
Telephone: 614-227-1915  
Fax: 614-227-2100  
dconway@porterwright.com  
ktrafford@porterwright.com

Counsel of Record for Ohio Power Company

BEFORE

THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Ohio )  
Power Company and Columbus Southern ) Case No. 10-2376-EL-UNC  
Power Company for Authority to Merge )  
and Related Approvals. )

In the Matter of the Application of )  
Columbus Southern Power Company and )  
Ohio Power Company for Authority to ) Case No. 11-346-EL-SSO  
Establish a Standard Service Offer Pursuant ) Case No. 11-348-EL-SSO  
to Section 4928.143, Revised Code, in the )  
Form of an Electric Security Plan. )

In the Matter of the Application of )  
Columbus Southern Power Company and ) Case No. 11-349-EL-AAM  
Ohio Power Company for Approval of ) Case No. 11-350-EL-AAM  
Certain Accounting Authority. )

In the Matter of the Application of )  
Columbus Southern Power Company and ) Case No. 10-343-EL-ATA  
Ohio Power Company to Amend their ) Case No. 10-344-EL-ATA  
Emergency Curtailment Service Riders. )

In the Matter of the Commission Review of )  
the Capacity Charges of Ohio Power ) Case No. 10-2929-EL-UNC  
Company and Columbus Southern Power )  
Company. )

In the Matter of the Application of )  
Columbus Southern Power Company and )  
Ohio Power Company for Approval of ) Case No. 11-4920-EL-RDR  
Mechanisms to Recover Deferred Fuel ) Case No. 11-4921-EL-RDR  
Costs Ordered Under Section 4928.144, )  
Revised Code. )

ENTRY

The Commission finds:

- (1) On January 27, 2011, in Case Nos. 11-346-EL-SSO, 11-348-EL-SSO, 11-349-EL-AAM and 11-350-EL-AAM, Columbus Southern Power Company (CSP) and Ohio Power Company (OP) (jointly, AEP-Ohio or the Companies) filed an application for a standard service offer (SSO) pursuant to Section 4928.141, Revised Code (ESP 2).
- (2) On September 7, 2011, a Stipulation and Recommendation (Stipulation) was filed for the purpose of resolving all the issues raised in the ESP 2 cases and several other AEP-Ohio cases pending before the Commission, Case No. 10-2376-EL-UNC, *In the Matter of the Application of Ohio Power Company and Columbus Southern Power Company for Authority to Merge and Related Approvals* (Merger Case); Case No. 10-343-EL-ATA, *In the Matter of the Application of Columbus Southern Power Company to Amend its Emergency Curtailment Service Riders* and Case No. 10-344-EL-ATA, *In the Matter of the Application of Ohio Power Company to Amend its Emergency Curtailment Service Riders* (jointly Curtailment Cases); Case No. 10-2929-EL-UNC, *In the Matter of the Commission Review of the Capacity Charges of Ohio Power Company and Columbus Southern Power Company* (Capacity Case); and Case No. 11-4920-EL-RDR, *In the Matter of the Application of Columbus Southern Power Company for Approval of a Mechanism to Recover Deferred Fuel Costs Pursuant to Section 4928.144, Revised Code*, and Case No. 11-4921-EL-RDR, *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of a Mechanism to Recover Deferred Fuel Costs Pursuant to Section 4928.144, Revised Code* (jointly Deferred Fuel Cost Cases).
- (3) On December 14, 2011, the Commission issued its Opinion and Order in the consolidated cases, finding that the Stipulation, as modified, be adopted and approved.
- (4) However, on February 23, 2012, the Commission issued its Entry on Rehearing determining that the Stipulation, as a package, did not benefit ratepayers and the public interest and, thus, did not satisfy the three-part test for the consideration of stipulations. The Commission directed AEP-Ohio to file new proposed tariffs to continue the provisions, terms, and conditions of its previous electric security plan no later than February 28, 2012.

- (5) On February 28, 2012, AEP-Ohio submitted its proposed compliance tariffs containing the provisions, terms, and conditions of its previous electric security plan, as approved in Case No. 08-917-EL-SSO (ESP 1) et al. *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Authority to Establish a Standard Service Offer Pursuant to Section 4928.143, Revised Code, in the Form of an Electric Security Plan.* AEP-Ohio further explains that the implementation of the phase-in recovery rider (PIRR), as approved in ESP 1, was recalculated on its January and February collections and carrying costs for those two months based on the long term debt rate. Therefore, AEP-Ohio states that the new PIRR rates are designed to collect the revised balance over the remaining 82 months of the amortization period.
- (6) On March 2, 2012, Industrial Energy Users-Ohio (IEU-Ohio) filed objections to AEP-Ohio's compliance tariffs. In its objections, IEU-Ohio asserts that AEP-Ohio's compliance tariffs contain a blended fuel adjustment clause (FAC) transmission cost recovery rider (TCRR) for both Ohio Power Company and Columbus Southern Power Company instead of individual provisions, improperly included the PIRR in its compliance tariffs, and failed to file an appropriate application of its capacity charges. IEU-Ohio also maintains that AEP-Ohio incorrectly omitted key terms and conditions of service.
- (7) On March 5, 2012, Ormet filed an objection to AEP-Ohio's compliance tariffs. Ormet contends that the inclusion of the PIRR in the compliance tariffs is improper and unauthorized.
- (8) On March 5, 2012, AEP-Ohio filed a Notice of Intent that it intends to submit a modified ESP pursuant to Section 4928.143, Revised Code, by March 30, 2012.
- (9) On March 6, 2012, the Ohio Consumers' Counsel and the Appalachian Peace and Justice Network (collectively OCC/APJN) filed a motion to reject portions of AEP-Ohio's compliance filing that implement the PIRR. In the alternative, OCC/APJN request that the Commission issue an order to stay the collection of the PIRR rates or order the PIRR rates be collected subject to refund.

- (10) Also on March 6, 2012, FirstEnergy Solutions (FES) filed objections to AEP-Ohio's proposed tariffs. FES opines that no recovery mechanism for the PIRR has been authorized, and AEP-Ohio failed to include a TCRR rate for its IRP-D customers.
- (11) AEP-Ohio filed revised tariffs on March 6, 2012, that reinserted terms and conditions that were omitted from the proposed tariffs filed on February 28, 2012. Also on March 6, 2012, AEP-Ohio filed a reply to objections filed by IEU-Ohio, Ormet, and OCC/APJN. AEP-Ohio asserts that the Commission already merged the FAC in a separate docket in Case No. 11-5906-EL-FAC (11-5906), and it would be impractical and unnecessary to revise not only the FAC provisions, but also the TCRR implementation. AEP-Ohio argues the inclusion of the PIRR was appropriate, and the capacity charges are appropriate as they do not relate to the implementation of the prior retail rate plan. Further, AEP-Ohio urges the Commission to reject OCC's requests to stay the prior rate plan or make the rates subject to refund.
- (12) The Commission finds that, with the exception of the tariffs for the PIRR, FAC, and TCRR, the tariffs filed by AEP-Ohio are consistent with its February 23, 2012, Entry on Rehearing, do not appear to be unjust or unreasonable, and should be approved, effective March 9, 2012.
- (13) Regarding the FAC and TCRR, the Commission finds that, pursuant to AEP-Ohio's application in the Merger Case, the approval of the merger will not affect CSP and OP's rates. Specifically, the application provides that CSP and OP shall continue service to customers within the pre-merger certified territories in accordance with their respective rates and terms and conditions in effect until such time as the Commission approves new rates and terms and conditions. While AEP-Ohio is correct that its FAC rates were approved in 11-5906, the rates were approved in light of the Commission's approval of the Stipulation in the ESP 2 proceedings, which was subsequently disapproved on February 23, 2012. Accordingly, OP shall file final unblended TCRR and FAC rates to be effective March 7, 2012, subject to subsequent Commission review. Further, FES correctly points out that AEP-Ohio failed

to include a TCRR rate for its IRP-D customers. Therefore, we direct AEP-Ohio to amend Original Sheet No. 475-1 to make it consistent with ESP 1's terms and conditions.

- (14) With respect to the PIRR, AEP-Ohio is directed to file, in final form, new tariffs removing the PIRR at this time. The Commission will address AEP-Ohio's application to establish the PIRR by subsequent entry in the Deferred Fuel Cost Cases.
- (15) Further, as AEP-Ohio filed corrections to its compliance filing on March 6, 2012, we do not need to address IEU-Ohio's objection that AEP-Ohio incorrectly omitted key terms and conditions of service.
- (16) In addition, as the captioned cases were consolidated by the Stipulation which the Commission disapproved, all future filings should be made in the appropriate case docket, as the consolidated case matters will no longer be docketed in all of the above-captioned cases.
- (17) Finally, the Commission notes that, on March 5, 2012, AEP-Ohio filed its notice of intent to file a modified ESP application. The Commission expects that such modified ESP application will include a thorough discussion of: any plans of AEP-Ohio to divest its generation assets, including provisions to ensure that adequate capacity will be available on an on-going basis to Ohio customers, notwithstanding any potential plant retirements; provisions to address rate design concerns for small commercial customers and residential customers in the former CSP service territory using more than 800 kWh in winter months; provisions regarding plans to take advantage of a territory-wide deployment of emerging metering technology to provide ample choices regarding pricing, information, and electric energy services for customers in a competitive market, including provisions that AEP-Ohio does not foreclose the possibility of working collaboratively with other utilities, retail energy suppliers, and interested stakeholders to explore cost saving and market development opportunities; provisions to take advantage of the deployment of emerging distribution system technologies in all locations where they can cost-effectively improve the efficiency of the distribution system or enhance reliability consistent with the value customers place on

service reliability; provisions for reasonable support for the development of technologies that could provide significant economic benefits; provisions ensuring that AEP-Ohio has the ability to meet Ohio's renewable energy standards over the long-term; provisions that any proposed retail stability charge be applied to all customers within AEP-Ohio service territory; provisions addressing the prompt modification or termination of the AEP Interconnection Agreement to reflect State law and policies; or provisions that provide for market-based pricing for standard service offer customers in a manner more expeditious than proposed within AEP-Ohio's Notice of Intent. The Commission further expects that AEP-Ohio will look to recent Commission precedent for guidance in formulating its modified ESP in considering how to best ensure its customers have market-based standard service offer pricing in an efficient and expeditious manner. (See *In the Matter of Application of Duke Energy Ohio, Inc. for Authority to Establish a Standard Service Offer Pursuant to Section 4928.143, Revised Code*, Case No. 11-3549-EL-SSO; *In the Matter of Application of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Authority to Establish a Standard Service Offer Pursuant to Section 4928.143, Revised Code*, Case No. 10-388-EL-SSO.)

It is, therefore,

ORDERED, That, with the exception of the tariffs for the PIRR, TCRR, and FAC, the tariffs filed on February 28, 2012, by AEP-Ohio be approved, effective for bills rendered on or after March 9, 2012. It is, further,

ORDERED, That OP file unblended TCRR and FAC rates to be effective March 9, 2012, subject to Commission review. It is, further,

ORDERED, That OP file tariffs including a TCRR rate for IRP-D customers, consistent with ESP 1's terms and conditions. It is, further,

ORDERED, That AEP-Ohio file new tariffs removing the PIRR at this time. The Commission will address AEP-Ohio's applications in the Deferred Fuel Cost Cases. It is, further,

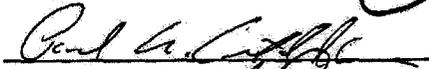
ORDERED, That the Companies file in final form four complete copies of tariffs. One copy shall be filed with this case docket, one shall be filed with each company's TRF docket, and the remaining two copies shall be designated for distribution to the Rates and Tariffs Division of the Commission's Utilities Department. The Companies shall also update their respective tariffs previously filed electronically with the Commission's Docketing Division. It is, further,

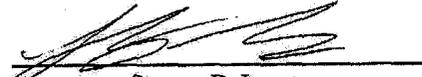
ORDERED, That the Companies shall notify their customers of the changes to the tariff via bill message or bill insert within 30 days of the effective date. A copy of this notice shall be submitted to the Commission's Service Monitoring and Enforcement Department prior to its distribution to customers. It is, further,

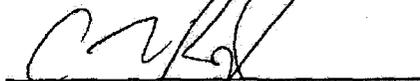
ORDERED, That a copy of this entry be served on all parties of record.

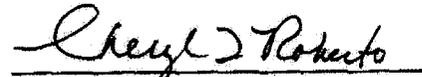
THE PUBLIC UTILITIES COMMISSION OF OHIO

  
Todd A. Snitchler, Chairman

  
Paul A. Centofella

  
Steven D. Lesser

  
Andre T. Porter

  
Cheryl L. Roberto

JJT/sc

Entered in the Journal

MAR 07 2012



Barcy F. McNeal  
Secretary