

ORIGINAL

IN THE SUPREME COURT OF OHIO

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| In the Matter of the Commission Review | : | Case No. 2013-0228 |
| of the Capacity Charges of Ohio Power | : | Case No. 2012-2098 |
| Company and Columbus Southern | : | |
| Power Company | : | On Appeal from the Public Utilities |
| | : | Commission of Ohio |
| | : | PUCO Case No. 10-2929-EL-UNC |

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TABLE OF CONTENTS

| | |
|--|----|
| INTRODUCTION | 1 |
| STATEMENT OF THE FACTS | 2 |
| A. Ohio’s Restructuring Legislation and Move Towards Retail Competition | 2 |
| B. The Role of PJM and its Capacity Resource Obligation | 3 |
| 1. RPM-Based Pricing | 6 |
| 2. FRR Alternative | 7 |
| C. The Commission Proceedings Regarding Compensation for Capacity Resources | 8 |
| ARGUMENT | 19 |
| Proposition of Law I: The Capacity Case Decisions are unlawful and unreasonable because the Commission’s only authority to regulate prices for competitive retail electric services is contained in R.C. 4928.141 to R.C. 4928.144. The Commission, however, held it could regulate a competitive service under R.C. Chapters 4905 and 4909 in direct contradiction with R.C. 4928.05 | 19 |
| 1. The Commission’s ratemaking authority over competitive retail electric services is limited to R.C. 4928.141 to R.C. 4928.144 | 20 |
| 2. The Commission cannot bypass the specific ratemaking requirements in R.C. 4928.141 to R.C. 4928.144 by relying upon its general supervisory powers in R.C. Chapter 4905 including, but not limited to, its authority to hear complaints under R.C. 4905.26 | 22 |
| 3. The RAA does not provide the Commission with any authority to invent and apply a cost-based ratemaking methodology | 28 |
| 4. Conclusion Regarding Proposition of Law I | 29 |
| Proposition of Law II: The Capacity Case Decisions are unlawful and unreasonable because the Commission’s jurisdiction under R.C. Chapter 4905 and its ratemaking authority under R.C. Chapters 4909 and 4928 extends to an electric light company, only when it is “engaged in the business of supplying electricity for light, heat, or power purposes to consumers within this state.” | 29 |
| Proposition of Law III: The Capacity Case Decisions are unlawful and unreasonable because the Commission is without authority to “adjudicate controversies between parties as to contract rights.” The Commission’s Capacity Case Decisions rest upon the Commission’s assessment of legal rights and liabilities under PJM’s RAA, a contract approved by FERC, which is subject to Delaware law. | 31 |

Proposition of Law IV: If the Commission has authority to regulate AEP-Ohio's capacity-related compensation, the Capacity Case Decisions are unreasonable and unlawful because AEP-Ohio failed to present the required evidence and the Commission failed to comply with the substantive and procedural requirements contained in R.C. Chapter 4909.....32

Proposition of Law V: The authorization of the deferred above-market compensation in excess of the market-based RPM compensation is unlawful and unreasonable for the reasons below:35

1. The deferred above-market compensation is unlawful and unreasonable because it allows AEP-Ohio to collect transition revenue or its equivalent and because it violates the terms of AEP-Ohio's Commission-approved settlement commitment to not impose lost generation-related revenue charges on shopping customers35

2. The deferred above-market compensation is unlawful and unreasonable because it conflicts with the policies contained in R.C. 4928.02, which prohibit anticompetitive subsidies and which rely upon market forces, customer choice, and prices disciplined by market forces to regulate prices for competitive retail electric services.....38

3. The deferred above-market compensation is unlawful and unreasonable because the Commission is prohibited under R.C. 4928.05(A) from regulating or otherwise creating a deferral associated with a competitive retail electric service under R.C. 4905.13. The Commission may only authorize deferred collection of a generation service-related price under R.C. 4928.144, but failed to comply with the requirements in R.C. 4928.14439

4. The deferred above-market compensation is unlawful and unreasonable because the Commission authorized AEP-Ohio to increase the above-market revenue supplement by adding carrying charges without any evidence that carrying charges, or any specific level of carrying charges, are lawful or reasonable40

5. The deferred above-market compensation is unlawful and unreasonable because the Commission failed to recognize that non-shopping customers are paying rates for capacity service in excess of \$188.88/MW-day and it failed to establish a mechanism to credit such excess compensation obtained from non-shopping customers against any deferred balance created by the Capacity Case Decisions41

Proposition of Law VI: The Capacity Case Decisions are unlawful and unreasonable because the Commission failed to restore RPM-Based Pricing as required by R.C. 4928.143(C)(2)(b) when it rejected the ESP Stipulation42

Proposition of Law VII: The Capacity Case Decisions are unlawful and unreasonable because the temporary two-tiered rates established by the March 7, 2012 Entry and May 30, 2012 Entry were not based upon the record from this proceeding.....43

Proposition of Law VIII: The Capacity Case Decisions are unlawful and unreasonable inasmuch as the Commission failed to direct AEP-Ohio to refund the above-market portion of capacity charges in place since January 2012 or credit the excess collection against regulatory asset balances otherwise eligible for amortization through retail rates and charges.45

Proposition of Law IX: In addition to the individual errors committed by the Commission which are referenced or identified herein, the totality of the Commission’s conduct throughout this proceeding is arbitrary and capricious, an abuse of discretion, otherwise outside the law and “... at variance with ‘the rudiments of fair play’ long known to our law. The Fourteenth Amendment condemns such methods and defeats them.” *West Ohio Gas Co. v. Public Utilities Commission*, 294 U.S. 63, 71 (1935) (quoting *Chicago, Milwaukee, & St. Paul Ry. Co. v. Polt*, 232 U.S. 165, 168 (1917)).....46

CONCLUSION..... 49

TABLE OF AUTHORITIES

| <u>Cases</u> | <u>Page</u> |
|--|-------------|
| <i>Columbus S. Power Co. v. Pub. Util. Comm.</i> , 67 Ohio St.3d..... | 22, 23 |
| <i>Consumers' Counsel v. Pub. Util. Comm.</i> , 61 Ohio St.3d 396, 406 (1991) <i>dissenting opinion of Justice Herbert Brown (quoting Columbus v. Pub. Util. Comm.</i> , 58 Ohio St.2d 103, 104 (1979))..... | 48 |
| <i>DiFranco v. FirstEnergy Corp.</i> , 34 Ohio St.3d 144, 2012-Ohio-5445, ¶20 (<i>citing State ex. rel Dayton Power & Light Co. v. Riley</i> , 53 Ohio St.2d 168, 170 (1978))..... | 31 |
| <i>Fox v. Eaton Corp.</i> , 48 Ohio St.2d 236, 238 (1976)..... | 29 |
| <i>FPC v. Florida Power & Light Co.</i> , 404 U.S. 453, 454-455 (1972)..... | 30 |
| <i>FPC v. Sierra Pacific Power Co.</i> , 350 U.S. 348 (1956)..... | 27 |
| <i>Indus. Energy Users-Ohio v. Pub. Util. Comm.</i> , 117 Ohio St.3d 486, 2008-Ohio-990..... | 21, 48 |
| <i>In re Kerry Ford, Inc.</i> , 106 Ohio App.3d 643, 651 (10th Dist. Ct. App. 1995)..... | 29 |
| <i>Lucas County Commissioners v. Pub. Util. Comm.</i> , 80 Ohio St.3d 344, 347-348 (1997)..... | 23 |
| <i>New Bremen v. Pub. Util. Comm.</i> , 103 Ohio St.23, 30-31 (1921)..... | 31 |
| <i>New York et al. v. FERC et al.</i> , 535 U.S. 1 (2002)..... | 30 |
| <i>Ohio Bell Tel. Co. v. Pub. Util. Comm.</i> , 301 U.S. 292, 300 (1937)..... | 47 |
| <i>Ohio Utilities Company v. Pub. Util. Comm.</i> , 58 Ohio St.2d 153, 157-159 (1979)..... | 23-24 |
| <i>Pub. Util. Comm. v. Pollak</i> , 343 U.S. 451, 465 (1952)..... | 47 |
| <i>Tongren v. Pub. Util. Comm.</i> 85 Ohio St.3d 87 (1999)..... | 29, 41, 48 |
| <i>United Gas Co. v. Mobile Gas Corp.</i> , 350 U.S. 332 (1956)..... | 27 |
| <i>Vectren Energy Delivery of Ohio, Inc. v. Pub. Util. Comm.</i> , 113 Ohio St.3d 180, 863 N.E.2d 599; 2006-Ohio-1386 at ¶ 53..... | 47 |
| <i>West Ohio Gas Co. v. Pub. Util. Comm.</i> , 294 U.S. 63, 71 (1935) (<i>quoting Chicago, Milwaukee & St. Paul Ry. Co. v. Polt</i> , 232 U.S. 165, 168 (1914))..... | 46, 48 |

Other Authorities

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 Assets,
Case Nos. 08-917-EL-SSO, *et al.*, Order on Remand (Oct. 3, 2011)45

In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of a Post-Market Development Rate Stabilization Plan,
Case No. 04-169-EL-UNC, Opinion and Order (Jan. 26, 2005)36

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,
Case Nos. 11-346-EL-SSO, *et al.*, Opinion and Order (Aug. 8, 2012)18

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,
Case Nos. 11-346-EL-SSO, *et al.*, Entry (Sept. 16, 2011)43, 44

In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of an Electric Transition Plan and Application for Receipt of Transition Revenues,
Case Nos. 99-1729-EL-ETP, *et al.*, Opinion and Order (Sept. 28, 2000)37

In the Matter of the Application of Ohio Power Company for Approval of the Shutdown of Unit 5 of the Philip Sporn Generating Station and to Establish a Plant Shutdown Rider,
Case No. 10-1454-EL-RDR, Finding and Order (Jan. 11, 2012)39

In the Matter of the Application of Ohio Power Company to cancel certain special power agreements and for other relief,
Case No. 75-161-EL-SLF, Opinion and Order (Aug. 4, 1976)27

In the Matter of the Commission Review of the Capacity Charges of Ohio Power Company and Columbus Southern Power Company,
Case No. 10-2929-EL-UNC, Entry (Dec. 8, 2010).....9, 10, 26, 41, 42

In the Matter of the Commission Review of the Capacity Charges of Ohio Power Company and Columbus Southern Power Company,
Case No. 10-2929-EL-UNC, Entry on Rehearing (Feb. 2, 2011).....46

In the Matter of the Commission Review of the Capacity Charges of Ohio Power Company and Columbus Southern Power Company,
Case No. 10-2929-EL-UNC, Opinion and Order (Dec. 14, 2011)8, 12

In the Matter of the Commission Review of the Capacity Charges of Ohio Power Company and Columbus Southern Power Company,
Case No. 10-2929-EL-UNC, Entry on Rehearing (Feb. 23, 2012).....12, 13

In the Matter of the Commission Review of the Capacity Charges of Ohio Power Company and Columbus Southern Power Company,
Case No. 10-2929-EL-UNC, Entry (Mar. 7, 2012)13, 44

In the Matter of the Commission Review of the Capacity Charges of Ohio Power Company and Columbus Southern Power Company,
Case No. 10-2929-EL-UNC, Entry (May 30, 2012).....14, 26, 45

In the Matter of the Commission Review of the Capacity Charges of Ohio Power Company and Columbus Southern Power Company,
Case No. 10-2929-EL-UNC, Opinion and Order (July 2, 2012)....7, 15, 16, 17, 20, 26, 27,
.....28, 29, 30, 32, 38, 39, 40, 41

In the Matter of the Commission Review of the Capacity Charges of Ohio Power Company and Columbus Southern Power Company,
Case No. 10-2929-EL-UNC, Entry on Rehearing (Oct. 17, 2012).....16, 25, 26, 30, 37

In the Matter of the Complaint of the Office of Consumers' Counsel, State of Ohio, on Behalf of the Residential Customers of West Ohio Gas Company v. West Ohio Gas Company, Case No 88-1743-GA-CSS, Entry (Jan. 31, 1988).....25

In the Matter of the Self-Complaint of Suburban Natural Gas Company Concerning its Existing Tariff Provisions, Case No. 11-5846-GA-SLF, Opinion and Order.....24

PJM Interconnection, L.L.C., 115 FERC ¶ 61,079 (2006).....26

PJM Interconnection, L.L.C., 117 FERC ¶ 61,331 (2006).....6, 26

PJM Interconnection, L.L.C., 119 FERC ¶ 61,318 (2007).....26

PJM Interconnection, L.L.C., 121 FERC ¶ 61173 (Nov. 15, 2007)6, 27

Statutes

Ohio Revised Code

| | |
|------------------------------|----------------------------|
| R.C. 4901.02 | 22 |
| R.C. 4905.02 | 30 |
| R.C. 4905.03 | 30 |
| R.C. 4905.03(C)..... | 29, 31 |
| R.C. 4905.04 | 21, 22, 30 |
| R.C. 4905.05 | 21, 22, 30 |
| R.C. 4905.06 | 21, 22, 30 |
| R.C. 4905.10 | 21 |
| R.C. 4905.13 | 40 |
| R.C. 4905.15 | 24 |
| R.C. 4905.26 | 22, 23, 24, 25, 27, 28, 30 |
| R.C. 4905.31 | 21 |
| R.C. 4905.33(B)..... | 21 |
| R.C. 4905.35 | 21 |
| R.C. 4909.18 | 33 |
| R.C. 4909.19(C)..... | 44 |
| R.C. 4909.43 | 33 |
| R.C. 4928.01(A)(27) | 20 |
| R.C. 4928.02 | 12, 38, 39 |
| R.C. 4928.02(B)..... | 42 |
| R.C. 4928.02(H)..... | 39 |
| R.C. 4928.03 | 3, 20, 26 |
| R.C. 4928.04 | 3 |
| R.C. 4928.05 | 40 |
| R.C. 4928.05(A)(1)..... | 19, 20, 21 |
| R.C. 4928.06 | 38 |
| R.C. 4928.12(A)..... | 3 |
| R.C. 4928.141 | 19, 20, 22, 23, 29, 36, 40 |
| R.C. 4928.142 | 19, 20, 22, 23, 29, 40 |
| R.C. 4928.143 | 19, 20, 22, 23, 29, 40 |
| R.C. 4928.143(C)(2)(b)..... | 12, 13, 42, 43 |
| R.C. 4928.144 | 19, 20, 22, 23, 29, 40 |
| R.C. 4928.15 | 42 |
| R.C. 4928.17 | 3 |
| R.C. 4928.31(A)..... | 36 |
| R.C. 4928.35(C)..... | 42 |
| R.C. 4928.38 | 36, 37, 38 |
| R.C. 4933.81 – 4933.90 | 21 |
| R.C. 4935.03 | 21 |
| R.C. 4963.40 | 21 |
| R.C. 4963.41 | 21 |

Ohio Administrative Code

Ohio Adm.Code 4901:1-35-01(L)42

INTRODUCTION

At issue in this proceeding is the Public Utilities Commission of Ohio's ("Commission") unlawful and unreasonable invention and application of a cost-based ratemaking methodology that significantly increased the compensation that Ohio Power Company ("AEP-Ohio")¹ receives for satisfying a wholesale capacity obligation imposed upon all load serving entities ("LSE"), which includes AEP-Ohio, that operate within PJM Interconnection, L.L.C. ("PJM").² The Commission's unlawful and unreasonable invented and applied cost-based ratemaking methodology displaced the market-based compensation that AEP-Ohio had been receiving and which had been found to be "just and reasonable" by the Commission as well as the Federal Energy Regulatory Commission ("FERC").

As discussed herein, the Commission patently and unambiguously lacks the authority to invent and apply a cost-based ratemaking methodology to authorize a significant above-market increase in the compensation AEP-Ohio receives for satisfying the wholesale capacity obligation imposed on AEP-Ohio by PJM. AEP-Ohio has also argued throughout the litigation below and before FERC that the Commission lacks this jurisdiction to address AEP-Ohio's capacity-related compensation.³ Nonetheless, the Commission ignored its jurisdictional limitations and has

¹ As used herein, AEP-Ohio refers to Ohio Power Company ("OP") and Columbus Southern Power Company ("CSP") on a merged basis. The merger of OP and CSP was initially authorized in 2011 and was reauthorized in March 2012.

² PJM is a regional transmission organization ("RTO") that coordinates the movement of wholesale electricity in all or parts of Delaware, Illinois, Indiana, Kentucky, Maryland, Michigan, New Jersey, North Carolina, Ohio, Pennsylvania, Tennessee, Virginia, West Virginia and the District of Columbia. Information on PJM is available *via* the Internet at <http://www.pjm.com/home.aspx> (last visited July 11, 2013).

³ *American Electric Power Service Corporation*, FERC Docket No. ER13-1164-000, American Electric Power Service Corporation, on behalf of its utility affiliate Ohio Power Company, Proposed Appendix to the Reliability Assurance Agreement at 15 (Mar. 25, 2013), available at: <http://www.pjm.com/~media/documents/ferc/2013-filings/20130325-er13-1164-000.ashx> ("[FERC] has the exclusive authority to establish wholesale FRR capacity charges.").

authorized a significant unlawful and unreasonable rate increase for AEP-Ohio that deprives customers of the opportunity that would otherwise exist to reduce their electric bills through the customer choice rights guaranteed by Ohio law

As discussed below, the Court should reverse the Commission's decisions in the case below (the "Capacity Case Decisions")⁴ and should direct the Commission to restore the lawful market-based pricing that was in place prior to the Commission's unlawful and unreasonable actions. Additionally, the Court should direct the Commission to credit the above-market charges AEP-Ohio collected in excess of the market prices against regulatory asset balances otherwise eligible for amortization through retail rates.

STATEMENT OF THE FACTS

A. Ohio's Restructuring Legislation and Move Towards Retail Competition

In 1999, the General Assembly enacted Amended Substitute Senate Bill 3 ("SB 3"), which restructured Ohio's regulation of the electric industry. SB 3 unbundled generation, transmission, and distribution into three separate service components.⁵ SB 3 declared generation service a competitive retail electric service and opened up the generation function to retail

⁴ The Industrial Energy Users-Ohio ("IEU-Ohio") seek a reversal of the March 7, 2012 Entry, May 30, 2012 Entry, July 2, 2012 Opinion and Order, October 17, 2012 Entry on Rehearing, December 12, 2012 Entry on Rehearing, and January 30, 2013 Entry on Rehearing issued in the proceeding below. Collectively, these decisions are referred to herein as the "Capacity Case Decisions."

⁵ *In the Matter of the Commission Review of the Capacity Charges of Ohio Power Company and Columbus Southern Power Company*, Case No. 10-2929-EL-UNC (hereinafter, "Capacity Case"), IEU-Ohio Ex. 102A at 16 (Supp. at 186).

competition.⁶ SB 3 also required the incumbent vertically-integrated electric utilities to separate competitive lines of business from non-competitive lines of business.⁷

Following the passage of the restructuring legislation, competitive retail electric service (“CRES”) providers compete with one another to serve customers that elect to exercise their customer choice rights. Customers that do not exercise their rights to obtain the supply of competitive retail electric service (*i.e.*, generation service) from a CRES provider are supplied such service through an electric distribution utility’s (“EDU”) standard service offer (“SSO”). The generation supply function of an EDU such as AEP-Ohio is confined by operation of law to meeting the needs of customers that are not receiving generation supply from a CRES provider.

B. The Role of PJM and its Capacity Resource Obligation

Under FERC’s supervision, RTOs, such as PJM, are managing the operation of regional electricity markets to secure economies of scale and scope with independent market-monitoring oversight to determine if, and when, RTO or FERC intervention is needed to address anticompetitive behavior or circumstances in which competition is not adequate to produce “just and reasonable” rates.⁸ The RTOs also function to assure the stability and reliability of the electric grid.⁹ Ohio specifically requires that that owners of transmission facilities transfer control of such facilities to an RTO.¹⁰ The RTO in which the Ohio EDUs participate is PJM, which includes members from 13 states and the District of Columbia.

⁶ R.C. 4928.03 (Appx. at 504). SB 3 also provided the Commission with the authority to declare additional services as competitive services and allow for competition for such service. R.C. 4928.04 (Appx. at 505).

⁷ R.C. 4928.17 (Appx. at 521-522). This requirement became effective on January 1, 2001, the start date of competitive retail electric service.

⁸ IEU-Ohio Ex. 102A at 5 (Supp. at 175).

⁹ *Id.* at 6 (Supp. at 176).

¹⁰ R.C. 4928.12(A) (Appx. at 509).

PJM's market structure is governed by comprehensive FERC-approved documents including PJM's Reliability Assurance Agreement ("RAA") and provisions of the Open Access Transmission Tariff ("OATT"). The RAA, by its terms, has a pro-competitive and region-wide focus.¹¹ Within PJM, the current FERC-approved and supervised market structure includes separate generation products or services for capacity and energy as well as various ancillary services.¹²

Under the RAA, PJM's capacity market is intended to ensure the availability of necessary resources that can be called upon to maintain the necessary supply and demand balance for the entire footprint of PJM, not just the distribution service area of AEP-Ohio.¹³ The resources that are committed to PJM for this reliability objective are defined as Capacity Resources under the RAA and include generation facilities, transmission to bring energy from nearby resources, demand reduction, and energy efficiency.¹⁴ Each LSE within PJM is responsible for contributing owned or controlled Capacity Resources to the common pool of resources that are available to PJM to satisfy PJM's reliability mission.¹⁵

Under the RAA, there are two means by which an LSE can satisfy its Capacity Resource obligation to PJM. The first and default means is through the market-based Reliability Pricing Model ("RPM").¹⁶ The goal of RPM is to align capacity pricing with system, region-wide reliability requirements and to provide transparent information to all market participants far

¹¹ FirstEnergy Solutions Corp. ("FES") Ex. 110A at 21 (Supp. at 22).

¹² IEU-Ohio Ex. 102A at 5 (Supp. at 175).

¹³ FES Ex. 110A at 21, 106 (Supp. at 22, 107); IEU-Ohio Ex. 102A at 5-6 (Supp. at 175-176).

¹⁴ FES Ex. 110A at 6 (Supp. at 7); Tr. Vol. XI at 2531 (Supp. at 767); *see also* PJM Manual 18, *PJM Capacity Market* at 84, available at: <http://www.pjm.com/~media/documents/manuals/m18.ashx>.

¹⁵ IEU-Ohio Ex. 102A at 5-8 (Supp. at 175-178).

¹⁶ IEU-Ohio Ex. 102A at 6-9 (Supp. at 176-179).

enough in advance of transactions to allow time for potential buyers and sellers to respond to the information.¹⁷ RPM relies upon an auction to procure a sufficient level of Capacity Resource commitments from the auction participants and establishes the “just and reasonable” compensation for providers of Capacity Resources that clear or are accepted through the PJM auction process.¹⁸ Auctions are held each May three years in advance of the PJM delivery year, which runs from June 1 through the following May 31.¹⁹ Subsequently, PJM conducts up to three incremental auctions, if necessary, to procure additional Capacity Resources for the PJM delivery year.²⁰

As an alternative to participating in the RPM auctions, LSEs may elect to satisfy their Capacity Resource obligation to the PJM pool through a method known as the Fixed Resource Requirement (“FRR”) Alternative.²¹ An LSE electing the FRR Alternative is an FRR Entity. An FRR Entity commits in-kind Capacity Resources to PJM based upon its projected loads, rather than obtaining and paying for Capacity Resources through PJM’s RPM auction process.²² A CRES provider expected to serve load within an FRR Entity’s Service Area is also provided the opportunity to provide in-kind Capacity Resources.²³ If a CRES provider does not elect to provide in-kind Capacity Resources to PJM, the responsibility to provide in-kind Capacity Resources defaults to the FRR Entity.

¹⁷ *Id.* at 6 (Supp. at 176).

¹⁸ *Id.* at 6-9 (Supp. at 176-179).

¹⁹ *Id.* at 7 (Supp. at 177).

²⁰ *Id.* (Supp. at 177).

²¹ FES Ex. 110A at 13 (Supp. at 14); IEU-Ohio Ex. 102A at 9 (Supp. at 179). Definitions of “Capacity Resources,” “FRR Alternative,” “FRR Entity,” and “FRR Capacity Plan” are available in the Definitions Section of the RAA. FES Ex. 110A at 5-20 (Supp. at 6-21).

²² FES Ex. 110A at 109-110, 113-114 (Supp. at 110-111, 114-115).

²³ *Id.* at 10 (Supp. at 11) (defining FRR Service Area).

The RAA, RPM, and the FRR Alternative are byproducts of a FERC-approved settlement negotiated by many parties in a case in which PJM proposed changes to its market rules.²⁴ That settlement, which American Electric Power Service Corporation (“AEPSC”) signed on behalf of all the affiliated American Electric Power Co., Inc. operating companies in PJM including AEP-Ohio, was accepted by FERC on December 22, 2006.²⁵

I. RPM-Based Pricing

As mentioned above, RPM auctions are held to allow LSEs to secure sufficient Capacity Resources to satisfy their regional reliability-related capacity obligation to PJM and to do so through a market-based approach.²⁶ Capacity Resources that clear in the RPM auctions receive compensation at the auction clearing price. FERC has approved PJM’s approach under the “just and reasonable” standard in the Federal Power Act (“FPA”).²⁷ As will be discussed below, the Capacity Resource compensation established by RPM-Based Pricing is significantly less than the compensation which the Commission uniquely, unreasonably, and unlawfully authorized AEP-Ohio to collect for generation capacity service.

During the periods relevant to this proceeding, the RPM auction price specific to the AEP-Ohio zone was \$145.79/megawatt-day (“MW-day”) for the 2011/2012 PJM delivery year, \$20.01/MW-day for the 2012/2013 PJM delivery year, \$33.71/MW-day for the 2013/2014 PJM

²⁴ IEU-Ohio Ex. 102A at 10 (Supp. at 180).

²⁵ *PJM Interconnection, L.L.C.*, 117 FERC ¶ 61,331 (2006).

²⁶ IEU-Ohio Ex. 102A at 7-9 (Supp. at 177-179).

²⁷ *PJM Interconnection, L.L.C.*, 121 FERC ¶ 61173 at ¶ 1, 20-30 (Nov. 15, 2007) (“We again affirm our finding that the RPM program produces just and reasonable rates for capacity in PJM.”), available at: <http://elibrary.ferc.gov/idmws/common/OpenNat.asp?fileID=11506194>.

delivery year, and \$153.89/MW-day for the 2014/2015 PJM delivery year.²⁸ As used herein, RPM-Based Pricing refers to the prices established by the RPM auction process.

2. *FRR Alternative*

In states that do not have retail choice, FRR Entities do not receive any payments from PJM's markets for in-kind Capacity Resources they make available to PJM. However, in the case of an FRR Entity in states that have retail choice, if a retail customer elects to receive its electric generation service from a CRES provider (referred to as an Alternative LSE under the RAA), and that CRES provider did not also elect to provide in-kind Capacity Resources, PJM's rules require CRES providers to compensate the FRR Entity for a quantity of Capacity Resources commensurate with the amount of load served by the CRES provider.²⁹

The level of compensation an FRR Entity receives for supplying Capacity Resources based upon load that switches to a CRES provider is governed by Schedule 8.1, Section D.8, of the RAA.³⁰ RPM-Based Pricing is the default method of compensation for an FRR Entity;

²⁸ Opinion and Order at 10 (July 2, 2012) (Appx. at 54) (hereinafter "Capacity Order").

²⁹ See FES Ex. 101 at 9 (Supp. at 10); FES Ex. 110A at 111. (Supp. at 12). The Alternative LSE must make the election to participate in the RPM process and carve out a portion of the FRR Entity's capacity obligation three years in advance of the PJM delivery year. FES Ex. 110A at 108, 111 (Supp. at 109, 112).

³⁰ *Id.* at 111 (Supp. at 112). Schedule 8.1, Section D.8, of the RAA provides:

In a state regulatory jurisdiction that has implemented retail choice, the FRR Entity must include in its FRR Capacity Plan all load, including expected load growth, in the FRR Service Area, notwithstanding the loss of any such load to or among alternative retail LSEs. In the case of load reflected in the FRR Capacity Plan that switches to an alternative retail LSE, where the state regulatory jurisdiction requires switching customers or the LSE to compensate the FRR Entity for its FRR capacity obligations, such state compensation mechanism will prevail. In the absence of a state compensation mechanism, the applicable alternative retail LSE shall compensate the FRR Entity at the capacity price in the unconstrained portions of the PJM Region, as determined in accordance with Attachment DD to the PJM Tariff, provided that the FRR Entity may, at any time, make a filing with FERC under Sections 205 of the Federal Power Act proposing

however, other compensation methods may be established prospectively if certain conditions are satisfied. In states that permit retail customers to obtain generation supply from a competitive service provider, such as Ohio, a state's "state compensation mechanism" will prevail if one has been lawfully approved.³¹ In the absence of a lawful state compensation mechanism, the RAA allows an FRR Entity to seek FERC approval to change the methodology of compensation from the default RPM-Based Pricing method to another basis that is "just and reasonable."³² The FERC process is initiated by filing an application pursuant to Section 205 of the FPA.³³ An FRR Entity also may seek to exercise its rights under Section 206 of the FPA to seek revisions to the RAA or OATT.³⁴

C. The Commission Proceedings Regarding Compensation for Capacity Resources

The compensation AEP-Ohio received from CRES providers serving retail customers located in AEP-Ohio's service area was based on the RPM-Based Pricing method from 2007, when the RAA became effective, until January 2012.³⁵ Additionally, the RPM-Based Pricing method was used by AEP-Ohio to support the year-over-year escalating SSO rates that became

to change the basis for compensation to a method based on the FRR Entity's cost or such other basis shown to be just and reasonable, and a retail LSE may at any time exercise its rights under Section 206 of the FPA.

³¹ *Id.* (Supp. at 112).

³² *Id.* (Supp. at 112).

³³ *Id.* (Supp. at 112).

³⁴ *Id.* (Supp. at 112).

³⁵ Tr. Vol. II at 401 (Supp. at 747); Opinion and Order at 51-55 (Dec. 14, 2011) (approving an increase from RPM-Based Pricing to the two-tiered capacity charge structure effective January 1, 2012) (Appx. at 245-249).

effective in 2009 as a result of the Commission's approval of AEP-Ohio's first electric security plan ("ESP") in the *ESP I Case*.³⁶

Since November 2010, AEP-Ohio has attempted to uniquely delete the default and previously-approved RPM-Based Pricing method and insert a so-called cost-based ratemaking methodology to substantially increase the compensation available to AEP-Ohio from CRES providers making retail sales in AEP-Ohio's territory. AEP-Ohio's pursuit of compensation much higher than the compensation available from RPM-Based Pricing began with an application at FERC ("Section 205 Application") in November 2010.³⁷ Through this filing, AEPSC sought to invoke its status as an FRR Entity to displace the RPM-Based Pricing method through the introduction of a cost-based ratemaking methodology and, thereby, secure a significant increase in the compensation payable by CRES providers.³⁸ The cost-based formula that AEPSC proposed for AEP-Ohio was based upon a formula that used AEP-Ohio's generating assets as an input to the formula to produce the requested compensation of \$355/MW-day, an amount significantly in excess of the "just and reasonable" compensation established by the RPM process described herein.

Recognizing the danger that the Section 205 Application presented to retail customer choice, the Commission, on December 8, 2010, opened an investigation in the *Capacity Case*.

³⁶ Entry at 1-2 (Dec. 8, 2010) (Appx. at 182-183). As used herein, "*ESP I Case*" refers to *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 Nos. 08-917-EL-SSO, *et al.* In another proceeding, AEP-Ohio advocated for use of the RPM-Based Prices to drive state-wide SSO auctions. IEU-Ohio Ex. 102A at 10-11 (Supp. at 180-181).

³⁷ *American Electric Power Service Corporation*, FERC Docket ER11-2183-000, Section 205 Application (Nov. 24, 2010), available at: <http://elibrary.ferc.gov/idmws/common/OpenNat.asp?fileID=12494899>.

³⁸ See Entry at 1 (Dec. 8, 2010) (Appx. at 182).

After noting that it had approved AEP-Ohio's SSO rates in the *ESP I Case* based on the continuation of capacity pricing driven by the market-based RPM-Based Pricing method, the Commission explicitly "adopt[ed] as the state compensation mechanism for [AEP-Ohio] the current capacity charges established by the three-year capacity auction conducted by PJM, Inc. during the pendency of this review."³⁹ In other words, the Commission acted quickly to make it clear that the RPM-Based Pricing method, the default pricing method under the RAA, controlled for purposes of determining the compensation that AEP-Ohio could secure for the provision of wholesale generation capacity service to CRES providers.

In comments at FERC, the Commission further explained its position: "[a]lthough the state compensation mechanism has implicitly been in place since the inception of AEP-Ohio's current Standard Service Offer, the Ohio Commission expressly adopted as its state compensation mechanism the AEP Ohio Companies' charges established by the reliability pricing model's three-year capacity auction conducted by PJM."⁴⁰ Further, the Commission requested that AEPSC's application be dismissed because there was no need for FERC to advance the proceeding at FERC since the state compensation mechanism prevailed under the applicable provision of the RAA.⁴¹ On January 20, 2011, FERC dismissed AEPSC's Section 205 Application. Subsequently, AEPSC requested rehearing of FERC's decision to dismiss the Section 205 Application, advancing the claim that the Commission lacked jurisdiction to regulate the capacity-related compensation AEP-Ohio receives for satisfying PJM's Capacity Resource

³⁹ *Id.* at 2 (Appx. at 183).

⁴⁰ *American Electric Power Service Corporation*, FERC Docket No. ER11-2183-000, Comments Submitted on Behalf of the Public Utilities Commission of Ohio at 3 (Dec. 10, 2010), available at: http://elibrary.ferc.gov/idmws/File_list.asp?document_id=13872567.

⁴¹ *Id.* at 4.

Obligation.⁴² FERC granted rehearing for further consideration on March 24, 2011, but has not issued a final ruling on the request for rehearing.

AEP-Ohio also sought rehearing of the Commission's December 8, 2010 Entry and argued that "the Commission's Entry establishing an interim wholesale capacity rate [was] unreasonable and unlawful because the Commission is a creature of statute and *lacks jurisdiction under both Federal and Ohio law to issue an order affecting wholesale rates regulated by the Federal Energy Regulatory Commission.*"⁴³ AEPSC, on behalf of AEP-Ohio, also continued to seek FERC approval of its desired above-market compensation through a complaint under Section 206 of the FPA.⁴⁴ In the Section 206 Complaint, AEPSC sought to amend Section 8.1 of the RAA to displace and subordinate the role of any state compensation mechanism and RPM-Based Pricing.⁴⁵ It alleged, among other things, that the state compensation mechanism contained in Section 8.1 of the RAA was not just and reasonable because it would allow the Commission to establish a wholesale rate for capacity and circumvent AEPSC's ability to secure the specific type of cost-based compensation for capacity that AEPSC favored.⁴⁶ FERC has not addressed AEPSC's Section 206 Complaint.

⁴² Section 205 Application, Request for Rehearing of AEPSC at 13-14 (Feb. 22, 2011), available at: <http://elibrary.ferc.gov/idmws/common/OpenNat.asp?fileID=12569314>.

⁴³ Ohio Power Company's and Columbus Southern Power Company's Application for Rehearing at 3, 18-21 (Supp. at 345, 360-363) (emphasis added).

⁴⁴ *American Electric Power Service Corporation v. PJM Interconnection, L.L.C.*, FERC Docket No. EL11-32-000, Complaint (Apr. 4, 2011) ("Section 206 Complaint"), available at: http://elibrary.ferc.gov/idmws/File_list.asp?document_id=13906613.

⁴⁵ Section 16.4 of the RAA states that only the PJM Board may amend the RAA. FES Ex. 110A at 71 (Supp. at 72). Thus, the RAA bars AEPSC's effort to amend the RAA through its Section 206 Complaint.

⁴⁶ Section 206 Complaint at 2-4 available at: http://elibrary.ferc.gov/idmws/File_list.asp?document_id=13906613.

AEP-Ohio eventually tried to resolve its desire for a significant above-market increase in its capacity-related compensation through a strongly contested Stipulation and Recommendation (“ESP Stipulation”) submitted to the Commission on September 7, 2011 that, in addition to addressing AEP-Ohio’s ESP case, addressed AEP-Ohio’s capacity-related compensation. Despite AEP-Ohio’s position that the Commission lacked jurisdiction to regulate its capacity-related compensation, the ESP Stipulation provided for a two-tiered compensation structure applicable to CRES providers serving retail customers located in AEP-Ohio’s distribution service area.⁴⁷ The Commission approved the ESP Stipulation on December 14, 2011.⁴⁸

The first tier pricing was tied to RPM-Based Pricing and was limited to the first 21 percent of AEP-Ohio’s total load served by CRES providers.⁴⁹ Any load in excess of 21 percent served by CRES providers (the second tier) triggered compensation at an arbitrary amount of \$255/MW-day.⁵⁰ The purpose of the second tier pricing was to limit customer shopping,⁵¹ a purpose that offends both the letter and spirit of Ohio law.⁵² The two-tiered pricing scheme began on January 1, 2012. In response to applications for rehearing, however, the Commission granted rehearing and eventually rejected the ESP Stipulation on February 23, 2012, finding that it was not consistent with the public interest.⁵³ Upon rejecting the ESP Stipulation and in accordance with the requirements of R.C. 4928.143(C)(2)(b), the Commission ordered AEP-

⁴⁷ Opinion and Order at 25 (Dec. 14, 2011) (Appx. at 219).

⁴⁸ *Id.* at 67 (Appx. at 261).

⁴⁹ *Id.* at 25, 51-55 (Appx. at 219, 245-249).

⁵⁰ *Id.*

⁵¹ FES Ex. 102 at Exhibit TCB-4 (Supp. at 804) (at a presentation to financial investors, an AEP-Ohio executive indicated that “the thought and the theory is that the shopping will be constrained to” customers receiving RPM-Based Pricing under the first tier).

⁵² *See* R.C. 4828.02 (Appx. at 502).

⁵³ Entry on Rehearing at 12 (Feb. 23, 2012) (Appx. at 180).

Ohio to restore the prices, terms and conditions of the ESP approved in the *ESP I Case*.⁵⁴ The Commission accompanied the rejection of the ESP Stipulation with a directive that AEP-Ohio reduce its charges to CRES providers to the RPM-Based Price and further directed that the *Capacity Case* be set for hearing.⁵⁵

Despite R.C. 4928.143(C)(2)(b)'s mandate that the prior SSO's "provisions, terms, and conditions" continue and the Commission's order to restore the prior SSO's "provisions, terms, and conditions," AEP-Ohio refused, and continued to bill and collect for capacity under the ESP Stipulation's much higher two-tiered pricing scheme. On February 27, 2012, AEP-Ohio sought permission from the Commission to maintain the two-tiered pricing scheme.⁵⁶ Over the protests of IEU-Ohio and other parties pointing out that the Commission: (1) lacked jurisdiction to authorize a non-RPM-Based Price; (2) was required under R.C. 4928.143(C)(2)(b) to restore RPM-Based Pricing; and (3) could not act on AEP-Ohio's claims without a hearing or evidence, the Commission granted AEP-Ohio's motion to maintain the rejected ESP Stipulation's two-tiered capacity pricing. The Commission held that the two-tiered pricing scheme would remain in place through May 31, 2012, and directed that thereafter AEP-Ohio's compensation would be based on RPM-Based Pricing.⁵⁷ The practical effect of the Commission's ruling allowed AEP-Ohio to obtain significantly above-market compensation for wholesale generation capacity service at a level of compensation that was much higher than the level that the Commission was obligated to restore upon rejection of the ESP Stipulation.

⁵⁴ *Id.* at 12 (Appx. at 180).

⁵⁵ *Id.* at 12 (Appx. at 180).

⁵⁶ Motion for Relief and Request for Expedited Ruling (Feb. 27, 2012) (Supp. at 485).

⁵⁷ Entry at 17 (Mar. 7, 2012) (Appx. at 31).

As May 31, 2012 approached, AEP-Ohio filed a second motion seeking to extend and increase the rates of the two-tiered pricing scheme until the Commission resolved the pending *Capacity Case*.⁵⁸ Again over IEU-Ohio's and other parties' objections and over Commissioner Porter's dissent, the Commission granted AEP-Ohio's request.⁵⁹ As a result of the Commission's May 30, 2012 Entry, AEP-Ohio was authorized to continue charging the higher tier two price (\$255/MW-day) and was authorized to increase the first tier price from the RPM-Based Price (which on June 1, 2012 became \$20.01/MW-day) to an arbitrary amount of \$146/MW-day.⁶⁰ In each instance in which the Commission authorized the two-tiered pricing scheme, the Commission also ignored requests by IEU-Ohio to order that the above-market and illegal charges be collected subject to reconciliation.

Prior to the commencement of the evidentiary hearing, IEU-Ohio filed a motion to dismiss AEP-Ohio's proposal asserting that the Commission lacked jurisdiction to approve AEP-Ohio's formulaic methodology that produced a "cost" of wholesale capacity of roughly \$355/MW-day.⁶¹ And throughout the litigation below, AEP-Ohio continued to assert that the Commission lacked jurisdiction to address its capacity-related compensation, but nonetheless sought and obtained authorization from the Commission for a substantial rate increase.

The record established during the evidentiary hearing in the *Capacity Case* demonstrates that AEP-Ohio is not an FRR Entity; rather, AEPSC, acting on behalf of a group of affiliated AEP operating companies in PJM's territory including AEP-Ohio, made a single FRR election in

⁵⁸ Motion for Extension (Apr. 30, 2012) (Supp. at 511).

⁵⁹ Entry at 7-8 (May 30, 2012) (Appx. at 39-40). Commissioner Porter's dissenting opinion noted that AEP-Ohio's requested relief following the rejection of the ESP Stipulation was to maintain the status quo, which made RPM-Based Pricing available to the first 21 percent of customers shopping. *Id.* at 1-2 (Appx. at 41-42).

⁶⁰ *Id.* (Appx. at 39-40).

⁶¹ Motion to Dismiss of IEU-Ohio at 1, 6-11 (Apr. 11, 2012) (Supp. at 526, 531-536).

2007 for the combined group of affiliated companies.⁶² The FRR election for all of the affiliated AEP operating companies in PJM will remain in place through May 31, 2015, at which time AEP-Ohio will participate in the RPM auction process.⁶³ The record also demonstrates that AEP-Ohio's and the Commission's assumption that AEP-Ohio's owned or controlled generating assets were the source of capacity that was made available to CRES providers is complete fiction.⁶⁴ The record demonstrates that Capacity Resources are committed to PJM to satisfy region-wide reliability and are *not* "dedicated" to specific customer loads.⁶⁵ The record further demonstrates that whatever Capacity Resources were committed to PJM to meet the overall capacity obligation of the entire FRR Entity, those Capacity Resources would have included Capacity Resources other than AEP-Ohio's owned or controlled generating facilities.⁶⁶ AEP-Ohio did not, however, introduce evidence regarding what Capacity Resources had been committed to PJM.

Following the hearing, the Commission issued its opinion and order in the proceeding (the "Capacity Order"), denied IEU-Ohio's motion to dismiss, and found that it had jurisdiction to use a cost-based ratemaking methodology to set AEP-Ohio's capacity-related compensation.⁶⁷ The Commission pointed to its general supervisory authority in R.C. 4905.04, 4905.05, and

⁶² Tr. Vol. II at 436-437 (Supp. at 750-751); Tr. Vol. XI at 2533-2534 (Supp. at 769-770).

⁶³ See Capacity Order at 14 (Appx. at 58). AEP-Ohio will begin participating in the RPM process beginning June 1, 2015. *Id.*

⁶⁴ IEU-Ohio's Application for Rehearing of the July 2, 2012 Opinion and Order and Memorandum in Support at 29 (Aug. 1, 2012) (Appx. at 324); Tr. Vol. VI at 1346-1349 (Supp. at 759-762); Tr. Vol. IX at 2530-2534 (Supp. at 766-770).

⁶⁵ Tr. Vol. VI at 1346-1349 (Supp. at 759-762).

⁶⁶ Tr. Vol. IX at 2530-2534 (Supp. at 766-770) (the affiliated AEP companies pooled their resources to meet the FRR Entity's capacity obligation and did not rely solely on AEP-Ohio's generating units).

⁶⁷ Capacity Order at 9 (Appx. at 53).

4905.06 as its authority to regulate generation capacity service.⁶⁸ Then, on rehearing, the Commission held that R.C. 4905.26 also provided the Commission jurisdiction.⁶⁹

The Commission then found that “pursuant to [its] regulatory authority under Chapter 4905, Revised Code, as well as Chapter 4909, Revised Code, [] it is necessary and appropriate to establish a cost-based state compensation mechanism,” and that this exercise of authority was “consistent with the governing section of the RAA,” Section D.8 of Schedule 8.1.⁷⁰ In resorting to the cost-based ratemaking principles in R.C. Chapter 4909, however, the Commission ignored the detailed procedural and substantive requirements that are specifically set out in R.C. Chapter 4909. Thus, the Commission invented its own ratemaking methodology, found nowhere in Ohio law, and substituted the results of this invented and applied ratemaking methodology for the results of the previously-approved and default RPM-Based Pricing method, all to authorize AEP-Ohio to significantly increase its compensation for wholesale generation capacity service. And, along the way there was no finding that the previously-approved and default RPM-Based Pricing method was unlawful or unreasonable. Instead, the Commission explained the virtues of the RPM-Based Pricing method on the way to depriving customers of the lower electric bills produced by the RPM-Based Pricing method.⁷¹

Using its invented cost-based ratemaking methodology, the Commission found AEP-Ohio’s “cost” of capacity was \$188.88/MW-day.⁷² Although the record demonstrated that the assumptions embedded in AEP-Ohio’s \$355/MW-day formula rate were complete fiction, the

⁶⁸ *Id.* at 12 (Appx. at 56).

⁶⁹ Entry on Rehearing at 9-10 (Oct. 17, 2012) (Appx. at 98-99).

⁷⁰ *Id.* at 13, 22 (Appx. at 57, 66); *see also Id.* at 10 (Oct. 17, 2012) (Appx. at 99).

⁷¹ Capacity Order at 23 (Appx. at 67).

⁷² *Id.* at 36 (Appx. at 80).

Commission nonetheless relied upon AEP-Ohio's claimed cost of capacity as a starting point of its invented ratemaking methodology.⁷³ The Commission then adopted several of the Commission Staff's ("Staff") recommended adjustments to AEP-Ohio's \$355/MW-day rate, which reduced AEP-Ohio's "cost" of capacity to \$188.88/MW-day.⁷⁴

The Commission, however, also held that it would not permit AEP-Ohio to bill CRES providers for the full amount of the \$188.88/MW-day price. Instead, it ordered AEP-Ohio to bill CRES providers the RPM-Based Price and stated it would authorize accounting changes under R.C. 4905.13 to allow AEP-Ohio to defer the difference between what it collected through the RPM-Based Pricing charges applicable to CRES providers and \$188.88/MW-day (the "deferred above-market compensation").⁷⁵ The Commission then held it would establish a mechanism for the collection of the portion of the \$188.88/MW-day not collected from CRES providers in AEP-Ohio's pending ESP case (the "*ESP II Case*").⁷⁶

Despite there being different parties in the *Capacity Case* and the *ESP II Case*, and despite the evidentiary record having already been closed in the *ESP II Case* when the Commission issued its Capacity Order, the Commission moved the issue regarding collection of the deferred above-market compensation to the *ESP II Case*.⁷⁷ The Commission then

⁷³ *Id.* at 33 (Appx. at 77) ("Staff followed its traditional process of making reasonable adjustments to AEP-Ohio's proposed capacity pricing mechanism.").

⁷⁴ *Id.* at 33-35 (Appx. at 77-79) (the Commission accepted some of Staff's recommended adjustments to AEP-Ohio's proposed rate and rejected several others).

⁷⁵ *Id.* at 23 (Appx. at 67).

⁷⁶ *Id.* at 23-24 (Appx. at 67-68). As used herein, "*ESP II Case*" refers to *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*, Case Nos. 11-346-EL-SSO, *et al.*, available at: <http://dis.puc.state.oh.us/CaseRecord.aspx?CaseNo=11-346&x=0&y=0>.

⁷⁷ Capacity Order at 23 (Appx. at 67).

substantially modified AEP-Ohio's request in the *ESP II Case* for a non-bypassable generation-related rider called the Retail Stability Rider ("RSR") which, as proposed, applied to retail customers (shopping and non-shopping customers). AEP-Ohio requested that the RSR be designed to maintain AEP-Ohio's total company revenue at a certain level so as to insulate AEP-Ohio's competitive generation business from the discipline of the market.⁷⁸ The Commission rejected AEP-Ohio's proposal but unilaterally repurposed the RSR; the Commission authorized an RSR, in part, for the purpose of collecting, on a non-bypassable basis and from retail customers, a portion of the deferred above-market compensation, which the Commission had concocted in the separate *Capacity Case*.⁷⁹

More specifically, the Commission authorized AEP-Ohio to increase electric bills by collecting, on a non-bypassable basis from shopping and non-shopping customers, \$508 million through the RSR over the term of the ESP. And, the Commission directed AEP-Ohio to apply roughly 25% of the \$508 million collected from retail customers towards payment of the deferred above-market compensation.⁸⁰ The Commission held that any amount of the \$188.88/MW-day revenue that was not collected by the RPM-Based Price applied to CRES providers and the RSR applied to all retail customers would be paid by retail customers through yet another non-bypassable rider.⁸¹

⁷⁸ *ESP II Case*, Opinion and Order at 27 (Aug. 8, 2012) available at: <http://dis.puc.state.oh.us/TiffToPDF/A1001001A12H08B40046F08138.pdf>.

⁷⁹ *Id.* at 35.

⁸⁰ *Id.* To collect the \$508 million RSR charge, the Commission authorized AEP-Ohio to charge customers \$3.50/megawatt-hour ("MWh") and directed AEP-Ohio to credit \$1/MWh to the portion of the \$188.88/MW-day price not paid by CRES providers. From June 1, 2014 through June 1, 2015, the Commission authorized AEP-Ohio to increase the RSR charge to \$4/MWh; the credit will remain at \$1/MWh. *Id.* at 36, 75 n.32.

⁸¹ *Id.* at 52.

The Commission's orders in the *Capacity Case* and the *ESP II Case* substantially increase AEP-Ohio's generation-related compensation through the introduction of immediate and future non-bypassable charges that transfer the risk of AEP-Ohio's above-market generation supply prices to AEP-Ohio's shopping and non-shopping customers during a period of time when the previously-approved RPM-Based Pricing method provided and provides the greatest opportunity for such customers to reduce their electric bills. In other words, the Commission's orders wall off customers' ability to capture the electric bill reduction opportunities otherwise available through the exercise of the customer choice rights guaranteed by Ohio law.

ARGUMENT

Proposition of Law I: The Capacity Case Decisions are unlawful and unreasonable because the Commission's only authority to regulate prices for competitive retail electric services is contained in R.C. 4928.141 to R.C. 4928.144. The Commission, however, held it could regulate a competitive service under R.C. Chapters 4905 and 4909 in direct contradiction with R.C. 4928.05.

The Capacity Case Decisions are unlawful and unreasonable because the Commission is prohibited from inventing and applying cost-based ratemaking principles or resorting to R.C. Chapter 4905 or 4909 to supervise and regulate competitive retail electric services. As discussed in Proposition of Law II below, the Commission's authority in R.C. Chapter 4905, and its ratemaking authority in R.C. Chapters 4909 and 4928, only extend to retail services. Furthermore, R.C. 4928.05(A)(1) limits the Commission's ratemaking authority over competitive retail electric services to its authority to authorize the default SSO for EDUs under R.C. 4928.141 to R.C. 4928.143. Because Ohio law has deemed generation service competitive, from the point of production to the point of consumption, the Commission's reliance on R.C. Chapters 4905 and 4909 to invent and apply a cost-based ratemaking methodology to increase AEP-Ohio's capacity-related compensation is unlawful and unreasonable.

1. *The Commission's ratemaking authority over competitive retail electric services is limited to R.C. 4928.141 to R.C. 4928.144*

The scope of the Commission's jurisdiction over retail electric service is contained in the definitions and statutory limitations contained in R.C. Chapter 4928. R.C. 4928.01(A)(27) contains the definition of "retail electric service," which is defined as:

any service involved in supplying or arranging for the supply of electricity to ultimate consumers in this state, *from the point of generation to the point of consumption*. For the purposes of this chapter, retail electric service includes one or more of the following "service components": generation service, aggregation service, power marketing service, power brokerage service, transmission service, distribution service, ancillary service, metering service, and billing and collection service. (emphasis added)

A component of retail electric service, retail electric generation service, is deemed competitive as a matter of law:

Beginning on the starting date of competitive retail electric service, *retail electric generation*, aggregation, power marketing, and power brokerage services supplied to consumers within the certified territory of an electric utility are competitive retail electric services that the consumers may obtain subject to this chapter from any supplier or suppliers.⁸² (emphasis added).

The record in this proceeding makes it clear that capacity service is a generation service; and the so-called cost of this service, as defined by the method invented and applied by the Commission, is tied directly, albeit illegally, to AEP-Ohio's generating plants.⁸³

R.C. 4928.05(A)(1) provides that the Commission may only regulate a competitive retail electric service under: (1) R.C. 4928.141 to R.C. 4928.144 (authority to establish rates for an

⁸² R.C. 4928.03 (Appx. at 504). The definition of "retail electric service" (in combination with the balance of R.C. Chapter 4928) also makes it clear that a service component or function is either competitive or non-competitive. Because non-competitive service components are defined to be everything except competitive service components or functions, a service component must be either competitive or non-competitive.

⁸³ See Capacity Order at 24 (Appx. at 68); IEU-Ohio's Application for Rehearing of the July 2, 2012 Opinion and Order and Memorandum in Support at 29 (Aug. 1, 2012) (Appx. at 324); Tr. Vol. VI at 1346-1349 (Supp. at 759-762); Tr. Vol. IX at 2530-2534 (Supp. at 766-770).

EDU's SSO); (2) R.C. 4905.10 (regarding the funding of the Commission); (3) R.C. 4905.31 (allowing the Commission to establish reasonable arrangements between utilities or between a utility and a customer); (4) R.C. 4905.33(B) (prohibiting charging different rates for providing a like and contemporaneous service under substantially the same circumstances and conditions); (5) R.C. 4905.35 (prohibiting discrimination); (6) R.C. 4933.81 to 4933.90 (addressing utility and municipality territorial issues); and (7) R.C. 4905.06, 4935.03, 4963.40, and 4963.41, but "only to the extent related to service reliability and public safety." Outside of these narrowly defined categories, the Commission does not have authority to supervise or regulate any aspect of generation service.⁸⁴

From these definitions and limitations, it is apparent that the Commission cannot resort to or rely upon R.C. Chapter 4905 or 4909 to invent and apply a cost-based ratemaking methodology to increase AEP-Ohio's capacity-related compensation. In other cases, the Commission has also agreed that it cannot regulate "a utility's competitive activities" under R.C. 4905.04, R.C. 4905.05, and R.C. 4905.06.⁸⁵ Because Ohio law defines generation service, which encompasses capacity service, as a competitive retail electric service, and because Ohio law

⁸⁴ R.C. 4928.05(A)(1) (Appx. at 505); *Indus. Energy Users-Ohio v. Pub. Util. Comm.*, 117 Ohio St.3d 486, 2008-Ohio-990, ¶ 20.

It is well settled that the generation component of electric service is not subject to commission regulation. In *Constellation NewEnergy, Inc.*, 104 Ohio St.3d 530, 2004-Ohio-6767, 820 N.E.2d 885, ¶ 2, we stated that S.B. 3 'provided for restructuring Ohio's electric-utility industry to achieve retail competition with respect to the generation component of electric service.' R.C. 4928.03 specifies that retail electric-generation service is competitive and therefore not subject to commission regulation, and R.C. 4928.05 expressly removes competitive retail electric services from commission regulation.

⁸⁵ *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. 2012-2008, Merit Brief Submitted on Behalf of Appellee, The Public Utilities Commission of Ohio at 15-16 (Apr. 19, 2013), available at: http://www.sconet.state.oh.us/pdf_viewer/pdf_viewer.aspx?pdf=725902.pdf.

limits the Commission's ratemaking authority over competitive retail electric services to establishing rates for an EDU's SSO under R.C. 4928.141 to R.C. 4928.144, the Commission's reliance on R.C. Chapters 4905 and 4909 to regulate capacity service is unlawful and unreasonable.

2. *The Commission cannot bypass the specific ratemaking requirements in R.C. 4928.141 to R.C. 4928.144 by relying upon its general supervisory powers in R.C. Chapter 4905 including, but not limited to, its authority to hear complaints under R.C. 4905.26*

The Court has held that the Commission cannot use its general supervisory powers in contravention of the specific ratemaking processes that the General Assembly has developed and which are contained elsewhere in R.C. Title 49. As discussed above, the specific ratemaking statutes applicable to competitive retail electric services such as capacity service are located in R.C. 4928.141 to R.C. 4928.144.

In reviewing whether the seemingly broad grant of authority contained in R.C. 4901.02 provided the Commission with independent authority to establish rates outside the Commission's traditional ratemaking process, the Court held:

[t]he comprehensive ratemaking formula provided by the General Assembly is meant to protect and balance the interests of the public utilities and their ratepayers alike. *Dayton Power & Light Co. v. Pub. Util. Comm.*, *supra*, 4 Ohio St.3d 91, 4 OBR 341, 447 N.E.2d 733. We cannot conclude that it was the General Assembly's intent under the above enabling statute, R.C. 4901.02(A), to permit the PUCO to disregard *that very formula* in instances in which it simply did not agree with the result. Cf. *Consumers' Counsel*, *supra*, 67 Ohio St.2d at 165, 21 O.O.3d at 104, 423 N.E.2d at 828 ("the General Assembly undoubtedly did not intend to build into its recently revised [1976] ratemaking formula a means by which the PUCO may effortlessly abrogate that very formula").⁸⁶

Although in this instance the Commission suggests it has authority under R.C. 4905.04, 4905.05, 4905.06 and 4905.26, instead of the Section analyzed by the Court above, the same legal

⁸⁶ *Columbus S. Power Co. v. Pub. Util. Comm.*, 67 Ohio St.3d at 540 (emphasis in original).

principles apply. The General Assembly has established specific statutory requirements that the Commission must follow to authorize rates and charges for competitive retail electric services; and those specific requirements are contained in R.C. 4928.141 to R.C. 4928.144. Based on the Court's precedent, the Commission does not have the authority to bypass these specific requirements.⁸⁷

Further, the Commission's authority under R.C. 4905.26 to investigate rates that may be "unjust, unreasonable, unjustly discriminatory, unjustly preferential, or in violation of law," does not provide the Commission with the authority to invent and apply a ratemaking methodology to increase AEP-Ohio's capacity-related compensation. The determination as to whether a particular price or rate is unjust and unreasonable can be made only by reference to other provisions of R.C. Title 49 that describe the subject matter the Commission may address, the manner in which that subject matter may be addressed, and the criteria the Commission must apply to resolve the justness and reasonableness of a price or rate.

The Court has addressed this issue and held that R.C. 4505.26 does not provide the Commission with independent ratemaking authority. In *Lucas County Commissioners v. Pub. Util. Comm.*, 80 Ohio St.3d 344, 347-348 (1997), the Court held that R.C. 4905.26 did not provide the Commission with independent authority to order a refund of previous rates that the complainant argued were unjust and unreasonable. Instead, the Court looked elsewhere in R.C. Title 49 to see if another grant of statutory authority could be coupled with the Commission's investigatory powers under R.C. 4905.26 to order a refund of an allegedly unjust and unreasonable rate.⁸⁸ Finding no grant of authority to order the refund, the Court affirmed the Commission's dismissal of the complaint. Similarly in *Ohio Utilities Company v. Pub. Util.*

⁸⁷ *Id.*

⁸⁸ See *Lucas County*, 80 Ohio St.3d at 347-348.

Comm., 58 Ohio St.2d 153, 157-159 (1979), the Court held that the Commission could establish new rates in a complaint case by joining its authority to investigate the reasonableness of existing rates under R.C. 4905.26 with its ratemaking authority under R.C. 4905.15.

Finally, the Commission itself has ruled that complaint cases initiated under R.C. 4905.26 are not the primary method for the Commission to modify or approve rates. Historically, the Commission has only authorized rates in a complaint case initiated under R.C. 4905.26 in very “limited circumstances” and has only done so in accordance with grants of authority found elsewhere in R.C. Title 49, *e.g.*, R.C. Chapter 4909.⁸⁹ For instance, in an opinion and order regarding a self-complaint case filed by Suburban Natural Gas Company, the Commission stated that such “limited circumstances” exist:

only when the impact of the rate change has been directed to particular customer classes, has occurred during a rate proceeding, has been temporary in duration, or occurred in the context of an emergency rate proceeding, pursuant to Section 4909.16, Revised Code. Further, the Commission has, in prior cases, found that, if the proposed charges are not a general, across-the-board, rate increase, which would affect all of the company's customers and, if the self-complaint mechanism will protect the company's customers' interests, it is appropriate to consider the reasonableness of charges proposed by the utility.⁹⁰

Thus, contrary to the Commission's assertions in the October 17, 2012 Entry on Rehearing, the Commission has found that R.C. 4905.26 does *not* “provide[] the Commission with considerable authority to initiate proceedings to investigate the reasonableness of any rate or charge rendered

⁸⁹ *In the Matter of the Self-Complaint of Suburban Natural Gas Company Concerning its Existing Tariff Provisions*, Case No. 11-5846-GA-SLF, Opinion and Order at 6 available at: <http://dis.puc.state.oh.us/TiffToPDF/A1001001A12H15B40825J90050.pdf>. See also *Ohio Utilities*, 58 Ohio St.2d at 157-159.

⁹⁰ *In the Matter of the Self-Complaint of Suburban Natural Gas Company Concerning its Existing Tariff Provisions*, Case No. 11-5846-GA-SLF, Opinion and Order at 6 available at: <http://dis.puc.state.oh.us/TiffToPDF/A1001001A12H15B40825J90050.pdf>.

or proposed to be rendered by a public utility.”⁹¹ Instead, the Commission has held that “limited circumstances” exist that allow the Commission to alter rates through an investigation under R.C. 4905.26 and even then the Commission’s authority to modify rates was tied back to the substantive ratemaking criteria found elsewhere in R.C. Title 49.

Further, the Commission has not identified the criteria, *i.e.*, the ratemaking authority, by which to judge whether current rates are “unjust, unreasonable, unjustly discriminatory, unjustly preferential, or in violation of law.”⁹² Without reference to the statutory ratemaking authority, it is simply impossible for the Commission to conclude that an existing rate – such as a rate established by the previously-approved RPM-Based Pricing method -- is unjust or unreasonable inasmuch as there is nothing to compare the current rates against. Thus, because there has never been an allegation that AEP-Ohio was not receiving what would otherwise be authorized by law, the Commission was required, based upon its own precedent, to dismiss the case.⁹³

Of course, the Commission cannot point to any provision of R.C. Title 49 which authorizes the Commission to invent and apply a cost-based ratemaking methodology for the purpose of uniquely and significantly increasing AEP-Ohio’s capacity-related compensation because no such statute exists. R.C. Chapter 4909 is the only chapter of R.C. Title 49 that provides for a cost-based methodology for increasing an EDU’s compensation; however, that Chapter only applies to non-competitive retail electric services. Because generation capacity service has been deemed a competitive retail electric service by operation of law, it cannot be

⁹¹ Entry on Rehearing at 9 (Oct. 17, 2012) (Appx. at 98).

⁹² R.C. 4905.26 (Appx. at 485).

⁹³ *In the Matter of the Complaint of the Office of Consumers’ Counsel, State of Ohio, on Behalf of the Residential Customers of West Ohio Gas Company v. West Ohio Gas Company*, Case No 88-1743-GA-CSS, Entry at 10-11 (Jan. 31, 1988) (dismissing a complaint on grounds that the complainant failed to allege facts that if true would support a finding that the current rates exceed those which would have otherwise have been authorized by law) (Supp. at 801-802).

regulated under R.C. Chapter 4909.⁹⁴ Additionally, the Commission's claim that capacity service is a wholesale, rather than retail, service would also prevent the Commission from regulating capacity service under R.C. Chapters 4905, 4909, and 4928.⁹⁵

Furthermore, throughout the roughly two-year history of the *Capacity Case*, the Commission has never alleged that the existing RPM-Based rates were unreasonable, unjust, unduly discriminatory or preferential, or otherwise in violation of law. In fact, the Commission directed the continued use of RPM-Based Pricing in its initial order opening the investigation in this case,⁹⁶ and authorized the use of RPM-Based Pricing from January 1, 2012 through May 30, 2012.⁹⁷ The Commission has determined that public policy requires that AEP-Ohio charge CRES providers the RPM-Based Price through May 31, 2015.⁹⁸ Additionally, RPM-Based Pricing has been determined to be reasonable through FERC's approval of the RAA,⁹⁹ through the use of RPM-Based Pricing by all other EDUs in Ohio, and through AEP-Ohio's previous reliance on RPM-Based Pricing to develop the expected results of a market rate offer ("MRO") to satisfy R.C. 4928.143(C)(1)'s requirement that an ESP be more favorable in the aggregate

⁹⁴ R.C. 4928.03 (Appx. at 504).

⁹⁵ Capacity Order at 13 (Appx. at 57); *Capacity Case*, Entry on Rehearing at 19-20 (Oct. 17, 2012) (Appx. at 108-109). See Proposition of Law II, *infra* at 29 (Commission's jurisdiction under R.C. Chapters 4905, 4909, and 4928 extends to a public utility that is in the business of supplying electricity to consumers, i.e., it must be supplying a *retail* service).

⁹⁶ Entry at 2 (Dec. 8, 2010) (Appx. at 183).

⁹⁷ RPM-Based Pricing was the sole method of compensation for AEP-Ohio through December 31, 2011. Beginning January 1, 2012 and continuing through May 30, 2012, AEP-Ohio received compensation for generation-related capacity service based on two pricing tiers. The first tier, however, remained tied to RPM-Based Pricing. See, e.g., Entry at 1-8 (May 30, 2012) (Appx. at 33-40).

⁹⁸ Capacity Order at 23 (Appx. at 67).

⁹⁹ See *PJM Interconnection, L.L.C.*, 115 FERC ¶ 61,079 (2006) (finding preexisting pricing model to be unjust and unreasonable); *PJM Interconnection, L.L.C.*, 117 FERC ¶ 61,331 (2006) (approving, with conditions, the RPM); *PJM Interconnection, L.L.C.*, 119 FERC ¶ 61,318 (2007) (clarifying nature and extent of order approving the RPM).

than an MRO. FERC has also concluded that the RPM-Based Pricing method establishes a just and reasonable rate.¹⁰⁰ Thus, by all accounts, the RPM-Based Pricing method produces a just and reasonable result, it is the method that the Commission was obligated to restore when it pulled the plug on the ESP Stipulation and this method may not be displaced by an invented and applied cost-based ratemaking method to protect AEP-Ohio's competitive generation business and deprive customers of the opportunity that would otherwise exist to reduce their electric bills through the customer choice rights guaranteed by Ohio law.

AEP-Ohio's claim that RPM-Based Pricing does not yield just and reasonable compensation requires AEP-Ohio to satisfy a *Mobile-Sierra* standard of review.¹⁰¹ That doctrine requires that a party to a contract (*e.g.*, the RAA) demonstrate that its current agreed-to compensation under the agreement is not in the public interest before it can seek an increase in its compensation.¹⁰² AEP-Ohio did not demonstrate, nor did the Commission find, that continuation of RPM-Based Pricing is contrary to the public interest. Quite the contrary, the Commission found that the continuation of RPM-Based Pricing is in the public interest.¹⁰³

In sum, R.C. 4905.26 does not provide the Commission with ratemaking authority; it is a procedural statute. While the Commission can, in "limited circumstances" establish rates in a

¹⁰⁰ *PJM Interconnection, L.L.C.*, 121 FERC ¶ 61173 at ¶ 1 (Nov. 15, 2007) ("We again affirm our finding that the RPM program produces just and reasonable rates for capacity in PJM."), available at: <http://elibrary.ferc.gov/idmws/common/OpenNat.asp?fileID=11506194>.

¹⁰¹ *FPC v. Sierra Pacific Power Co.*, 350 U.S. 348 (1956); *United Gas Co. v. Mobile Gas Corp.*, 350 U.S. 332 (1956); *In the Matter of the Application of Ohio Power Company to cancel certain special power agreements and for other relief*, Case No. 75-161-EL-SLF, Opinion and Order at 6 (Aug. 4, 1976) (Supp. at 777) (applying the *Mobile-Sierra* doctrine to bilateral agreements approved by the Commission).

¹⁰² *FPC v. Sierra Pacific Power Co.*, 350 U.S. 348 (1956); *United Gas Co. v. Mobile Gas Corp.*, 350 U.S. 332 (1956); *In the Matter of the Application of Ohio Power Company to cancel certain special power agreements and for other relief*, Case No. 75-161-EL-SLF, Opinion and Order at 6 (Aug. 4, 1976) (Supp. at 777).

¹⁰³ Capacity Order at 23 (Appx. at 67).

complaint case initiated pursuant to R.C. 4905.26, the Commission's ratemaking authority comes from R.C. Chapters 4909 and 4928. Because the requirements of R.C. Chapters 4909 and 4928 were not met, there was no basis to establish any rate in the *Capacity Case*. Although the Commission concluded that RPM-Based Pricing would be insufficient to yield reasonable compensation for AEP-Ohio, the Commission failed to identify how it was measuring just and reasonable compensation and this omission effectively bypasses the statutory obligations in R.C. 4905.26 which the Commission must satisfy before it can increase utility bills.¹⁰⁴ Accordingly, the Capacity Case Decisions are unlawful and unreasonable.

3. ***The RAA does not provide the Commission with any authority to invent and apply a cost-based ratemaking methodology***

The Commission held that its exercise of jurisdiction was consistent with the RAA;¹⁰⁵ but the RAA does not provide the Commission any authority to invent a cost-based ratemaking methodology to increase the capacity-related compensation AEP-Ohio receives from CRES providers. The RAA is a FERC-approved contract (governed by the laws of Delaware) between and among its signatories.¹⁰⁶ It does not and cannot authorize the Commission to invent or apply a cost-based ratemaking methodology to increase AEP-Ohio's capacity-related compensation.¹⁰⁷ The RAA only recognizes that a state compensation mechanism shall control if a state regulator

¹⁰⁴ *Id.* (Appx. at 67).

¹⁰⁵ Capacity Order at 13 (Appx. at 57).

¹⁰⁶ FES Ex. 110A at 21, 69 (Supp. at 22, 70).

¹⁰⁷ Previously, AEP-Ohio has argued to both the Commission and FERC that the RAA does not permit the Commission to establish a wholesale capacity charge. Ohio Power Company's and Columbus Southern Power Company's Application for Rehearing at 21 (Jan. 7, 2011) (Supp. at 363); *American Electric Power Service Corporation*, Docket No. ER11-2183-001, Request for Rehearing of American Electric Power Service Corporation at 11-14 (Feb. 22, 2011), available at: <http://elibrary.ferc.gov/idmws/common/OpenNat.asp?fileID=12569314>).

has adopted a state compensation mechanism in accordance with its lawful authority.¹⁰⁸ Because there is no basis in Ohio law for the Commission to assert jurisdiction through the RAA, the RAA standing alone cannot extend the jurisdiction of the Commission to permit it to authorize an increase in AEP-Ohio's capacity-related compensation.¹⁰⁹

4. *Conclusion Regarding Proposition of Law I*

The Commission can only exercise the authority conferred upon it by the General Assembly; the RAA cannot expand that jurisdiction.¹¹⁰ The Commission must also rely on the specific ratemaking statutes enacted into Ohio law and cannot bypass those specific statutes by relying on its general supervisory authority. The Commission's ratemaking authority over competitive retail electric services is contained in R.C. 4928.141 to R.C. 4928.144, and these Sections do not provide the Commission with jurisdiction to invent and apply a cost-based ratemaking methodology to increase the capacity-related compensation that AEP-Ohio receives from CRES providers. Thus, the Capacity Case Decisions are unlawful and unreasonable.

Proposition of Law II: The Capacity Case Decisions are unlawful and unreasonable because the Commission's jurisdiction under R.C. Chapter 4905 and its ratemaking authority under R.C. Chapters 4909 and 4928 extends to an electric light company, only when it is "engaged in the business of supplying electricity for light, heat, or power purposes to consumers within this state."¹¹¹

In the Capacity Order, the Commission asserted that capacity service is not a retail service:

[i]n this case, the electric service in question (*i.e.*, capacity service) is provided by AEP-Ohio for CRES providers, with CRES providers compensating the Company in return for its [Fixed Resource Requirement ("FRR")] capacity obligations.

¹⁰⁸ FES Ex. 110A at 111 (Supp. at 112).

¹⁰⁹ *Fox v. Eaton Corp.*, 48 Ohio St.2d 236, 238 (1976); *In re Kerry Ford, Inc.*, 106 Ohio App.3d 643, 651 (10th Dist. Ct. App. 1995).

¹¹⁰ *Tongren v. Pub. Util. Comm.*, 85 Ohio St.3d 87, 88, 1999-Ohio-206.

¹¹¹ R.C. 4905.03(C) (Appx. at 475).

Such capacity service is not provided directly by AEP-Ohio to retail customers. Although the capacity service benefits shopping customers in due course, they are initially one step removed from the transaction, which is more appropriately characterized as an intrastate wholesale¹¹² matter between AEP-Ohio and each CRES provider operating in the Company's service territory.¹¹³

In the October 17, 2012 Entry on Rehearing, the Commission again asserted that its jurisdiction over capacity service was not governed by R.C. Chapter 4928 because "capacity service" is not a retail service:

AEP-Ohio's provision of capacity to CRES providers ... is not a retail electric service The capacity service in question is not provided directly by AEP-Ohio to retail customers, but is rather a wholesale transaction between the Company and CRES providers.¹¹⁴

The Commission's claim that generation-related capacity service is a wholesale service and not subject to limitations on its jurisdiction found in R.C. 4928.05(A)(1), however, offers the Commission no advantage. The Commission's reliance on R.C. Chapters 4905 and 4909 to regulate wholesale capacity service is unlawful and unreasonable because those Sections only apply to retail services.

R.C. 4905.04, 4905.05, 4905.06, and 4905.26, and R.C. Chapters 4909 and 4928 all apply to public utilities, and specifically to an electric services company, as that term is defined in R.C. 4905.02 and 4905.03. Those Sections specify that an electric services company subject

¹¹² It is unclear what the Commission means by the use of the words "intrastate wholesale." The United States Supreme Court has held that electricity is inherently in interstate commerce. *See New York et al. v. FERC et al.*, 535 U.S. 1 (2002); *FPC v. Florida Power & Light Co.*, 404 U.S. 453, 454-455 (1972). And, the RAA itself specifies that the capacity responsibility discussed therein is a regional responsibility for the entire multistate footprint of PJM. IEU-Ohio's Application for Rehearing of the July 2, 2012 Opinion and Order and Memorandum in Support at 45 (Aug. 1, 2012) (Appx. at 340); FES Ex. 110A at 4, 21 (Supp. at 5, 22); Tr. Vol. VI at 1346-1348 (Supp. at 759-761). In plainer words, there is no such thing as "intrastate wholesale" electric service.

¹¹³ Capacity Order at 13 (internal citations omitted) (Appx. at 57).

¹¹⁴ Entry on Rehearing at 19-20 (Oct. 17, 2012) (Appx. at 108-109).

to the Commission's jurisdiction under R.C. Chapters 4905, 4909, and 4928 must be a company engaged in the business of "supplying electricity to consumers," *i.e.*, it must be supplying a retail service. The definition of an electric services company also specifically exempts RTOs, such as PJM, the entity that actually bills CRES providers for capacity service.¹¹⁵ As mentioned above, the Commission held that it was not regulating a service provided to consumers; rather, it held it was regulating a wholesale service. Thus, based on the Commission's own findings, the Commission has no authority under R.C. Chapters 4905, 4909, or 4928 to regulate capacity service or increase the compensation available to AEP-Ohio for providing such service. Therefore, the Commission's assertion that it can regulate a wholesale rate under R.C. Chapters 4905 and 4909 is unlawful and unreasonable.

Proposition of Law III: The Capacity Case Decisions are unlawful and unreasonable because the Commission is without authority to "adjudicate controversies between parties as to contract rights."¹¹⁶ The Commission's Capacity Case Decisions rest upon the Commission's assessment of legal rights and liabilities under PJM's RAA, a contract approved by FERC, which is subject to Delaware law.

The Commission does not have jurisdiction to interpret and apply the RAA, a FERC-approved agreement. The Court recently held that the Commission "is not a court and has no power to ascertain and determine legal rights and liabilities." *DiFranco v. FirstEnergy Corp.*, 34 Ohio St.3d 144, 2012-Ohio-5445, ¶20 (citing *State ex. rel Dayton Power & Light Co. v. Riley*, 53 Ohio St.2d 168, 170 (1978); *New Bremen v. Pub. Util. Comm.*, 103 Ohio St. 23, 30-31 (1921)). In *New Bremen*, the Court held that the Commission does not have authority to "adjudicate controversies between parties as to contract rights ..."¹¹⁷ Despite the fact that the RAA is a

¹¹⁵ R.C. 4905.03(C) (Appx. at 475).

¹¹⁶ *New Bremen v. Pub. Util. Comm.*, 103 Ohio St.23, 30-31 (1921).

¹¹⁷ *New Bremen*, 103 Ohio St. at 30-31.

FERC-approved contract (governed by the laws of Delaware) between and among its signatories, the Commission unlawfully determined legal rights and liabilities under the RAA.¹¹⁸

In inventing and applying its cost-based ratemaking methodology, the Commission held that its actions were consistent with the RAA, concluding that AEP-Ohio was entitled to receive above-market compensation because “RPM-based capacity pricing would be insufficient to yield reasonable compensation for AEP-Ohio’s provision of capacity to CRES providers *in fulfillment of its FRR capacity obligations.*”¹¹⁹ But the source of any “FRR capacity obligation” stems from the RAA itself and, therefore, to determine what an appropriate level of compensation is, the Commission must interpret the rights and liabilities of a signatory party to that agreement. Again, it is important to note that AEP-Ohio did not make an FRR Alternative election; rather, AEPSC made that election on behalf of a group of affiliated companies that operate in PJM. Thus, whatever contract rights and liabilities exist relative to any “FRR capacity obligation,” those rights and liabilities are tied to AEPSC and not AEP-Ohio.

Accordingly, the Commission acted unlawfully and unreasonably when it concluded that AEP-Ohio was entitled to receive above-market capacity compensation based on the RAA.

Proposition of Law IV: If the Commission has authority to regulate AEP-Ohio’s capacity-related compensation, the Capacity Case Decisions are unreasonable and unlawful because AEP-Ohio failed to present the required evidence and the Commission failed to comply with the substantive and procedural requirements contained in R.C. Chapter 4909.

The Commission’s only authority to establish cost-based rates for an EDU is contained in R.C. Chapter 4909. That Chapter, however, only applies to non-competitive retail electric services. The Commission has not claimed that capacity service is a non-competitive retail electric service.

¹¹⁸ FES Ex. 110A at 21, 69 (Supp. at 22, 70).

¹¹⁹ Capacity Order at 23 (Appx. at 67) (emphasis added).

Furthermore, R.C. Chapter 4909 requires certain procedural and substantive requirements to be satisfied before the Commission may authorize a rate increase. It is undisputed that AEP-Ohio's proposed rate of \$355/MW-day and the Commission's \$188.88/MW-day rate are both greater than what AEP-Ohio would have collected if RPM-Based Pricing remained in place; thus, it is undisputed that AEP-Ohio sought, and the Commission authorized, a rate increase.¹²⁰ But, none of the requirements to obtain an increase in rates under R.C. Chapter 4909 have been met.

R.C. 4909.43 provides that the first mandatory step in securing an increase in rates under R.C. Chapter 4909 is to file a notice of intent to file an application to increase rates. R.C. 4909.43 requires that the notice of intent be sent to the mayor and legislative authority of each municipality served by the EDU. R.C. 4909.18 specifies that no earlier than thirty days later, the public utility may then file its application to increase rates. R.C. 4909.18 also requires that the president or vice-president and the secretary or treasurer of the public utility must verify the accuracy of the application. The application itself must also contain extensive details.

R.C. 4909.05 provides that an application to increase rates of a non-competitive service must include a description and valuation of the property used and useful in rendering service to the public. R.C. 4909.18 provides that an application to increase rates must also include a list of current and proposed rate schedules the public utility seeks to establish. R.C. 4909.18 also requires that the application contain a "complete operating statement of its last fiscal year, showing in detail all its receipts, revenues, and incomes from all sources, all of its operating costs and other expenditures, and any analysis such public utility deems applicable to the matter referred to in said application;" "a statement of the income and expense anticipated under the

¹²⁰ The applicable RPM-Based Pricing for the timeframe at issue in this case ranges from a low of \$20/MW-day to a high of \$153/MW-day. *Supra*, at 6-7.

application filed;” and “a statement of financial condition summarizing assets, liabilities, and net worth.”

Once the EDU has filed a proper application with all the appropriate information with the Commission, R.C. 4909.19(C) requires the Staff at the Commission to investigate the facts contained in the rate increase application. Once the Staff has completed its review, R.C. 4909.19(C) requires the Staff Report of Investigation to be docketed with the Commission and served on the mayors of all municipalities within the public utility’s service territory. R.C. 4909.19(C) also states that parties that have intervened in the proceeding are afforded a statutory right to object to the Staff Report of Investigation.

AEP-Ohio did not attempt to satisfy any of the ratemaking requirements contained in R.C. Chapter 4909. AEP-Ohio did not file a notice of intent to file an application for a rate increase. AEP-Ohio did not present any evidence that it served a notice on the mayor and legislative authority of each municipality served by the EDU. AEP-Ohio did not present any evidence as to what property was used and useful in rendering capacity service to the public. Nor did AEP-Ohio have any of the information it presented in the *Capacity Case* verified by the proper personnel. The Attorney General’s office representing the Staff also admitted that the Staff had not prepared a Staff Report of Investigation under R.C. 4909.19(C).¹²¹

The Commission likewise failed to comply with the requirements of R.C. Chapter 4909. It made no findings regarding the test year, the value of AEP-Ohio’s used and useful property, the inadequacy of AEP-Ohio’s current compensation, or the other elements of the cost-based ratemaking methodology that apply to non-competitive electric services.

¹²¹ Tr. Vol. IX at 1948 (Supp. at 764).

Therefore, even if R.C. Chapter 4909 could somehow be made relevant to the proceeding below, the Commission and AEP-Ohio failed to comply with any of the mandatory steps to seek, obtain, and authorize a rate increase.

Proposition of Law V: The authorization of the deferred above-market compensation in excess of the market-based RPM compensation is unlawful and unreasonable for the reasons below:

- 1. The deferred above-market compensation is unlawful and unreasonable because it allows AEP-Ohio to collect transition revenue or its equivalent and because it violates the terms of AEP-Ohio's Commission-approved settlement commitment to not impose lost generation-related revenue charges on shopping customers***

The cost-based ratemaking methodology invented and applied by the Commission will allow AEP-Ohio to collect, on a non-bypassable basis, generation plant-related transition revenue for many years into the future in violation of Ohio law and AEP-Ohio's prior Commission-approved agreements.¹²² IEU-Ohio's witnesses Hess and Murray testified that AEP-Ohio's proposed above-market capacity charges would fall within the definition of transition revenue or its equivalent.¹²³ Although AEP-Ohio claimed that the transition revenue analysis and its request to increase its capacity charges were two distinct issues, AEP-Ohio's "cost-based" calculation in this proceeding was based on the same assumptions as the transition revenue claim AEP-Ohio previously made and agreed to forgo in its electric transition plan ("ETP") proceeding.¹²⁴ Both calculations were based on AEP-Ohio's total net book value of its generation assets, and both included assumptions on the generation-related revenue that AEP-Ohio would be able to receive in the electric market (wholesale and retail).¹²⁵ Despite the legal

¹²² IEU-Ohio Ex. 101 at 8-9, 11-13, 18 (Supp. at 146-147, 149-151, 156).

¹²³ *Id.* 101 at 4-20 (Supp. at 142-158); IEU-Ohio Ex. 102A at 16-20 (Supp. at 186-190).

¹²⁴ IEU-Ohio Ex. 101 at 8-9, 11-13, 18 (Supp. at 146-147, 149-151, 156).

¹²⁵ *Id.* (Supp. at 146-147, 149-151, 156).

bar to collecting transition revenue and AEP-Ohio's prior Commission-approved agreements, the Commission authorized AEP-Ohio to collect the above-market supplement, which amounts to the collection of transition revenue or its equivalent.

Pursuant to R.C. 4928.38, AEP-Ohio's opportunity to obtain recovery of above-market generation plant-related transition charges terminated with the end of its market development period ("MDP") in 2005. This new generation plant-related transition revenue claim also comes well after the expiration of the 90-day time period specified by Ohio law for filing a transition revenue claim.¹²⁶ The deferred above-market compensation also fundamentally conflicts with R.C. 4928.38 which mandates that AEP-Ohio's generation business shall be fully on its own in the competitive market which, as argued by AEP-Ohio and upheld by the Commission, means AEP-Ohio's earnings do not matter for purposes of establishing generation rates.¹²⁷ The above-market supplement also offends the General Assembly's directive in R.C. 4928.141 requiring the Commission to remove any transition charges from future rate plans. Thus, the Commission's invention and application of a cost-based ratemaking methodology to authorize AEP-Ohio to collect above-market charges for capacity service is prohibited by Ohio law.

Beyond these statutory limits on the Commission's ability to provide AEP-Ohio transition revenue or its equivalent, the Commission's decision is precluded by the binding settlement agreement approved by the Commission in AEP-Ohio's ETP case. In that settlement agreement, AEP-Ohio agreed that it would forego recovery of any generation-related transition revenue and that it would not impose any lost generation-related revenue charges on shopping

¹²⁶ R.C. 4928.31(A) (an ETP, including requests for transition revenue, had to be filed within 90 days of October 5, 1999) (Appx. at 523).

¹²⁷ *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of a Post-Market Development Rate Stabilization Plan*, Case No. 04-169-EL-UNC, Opinion and Order at 18 (Jan. 26, 2005) available at: [http://dis.puc.state.oh.us/TiffToPDF/KLHCU8\\$9OVLJO676.pdf](http://dis.puc.state.oh.us/TiffToPDF/KLHCU8$9OVLJO676.pdf).

customers.¹²⁸ The Commission is without jurisdiction to abridge the rights of consumers under the terms of a previously approved settlement agreement by inventing and applying a cost-based ratemaking methodology to substantially and uniquely authorize AEP-Ohio to collect above-market compensation for generation-related capacity service through non-bypassable charges that apply to shopping and non-shopping customers.

In its October 17, 2012 Entry on Rehearing, the Commission finally addressed the issue of whether the deferred above-market compensation violated the statutory and contractual bar on the recovery of transition revenue raised by IEU-Ohio.¹²⁹ According to the Commission, the deferred above-market compensation is not transition revenue because the above-market capacity charges are not “directly assignable or allocable to retail electric generation service provided to electric consumers in this state” because capacity service is a wholesale rather than retail service.¹³⁰ The Commission’s analysis is deeply flawed.

R.C. 4928.38 prohibits not just the authorization and collection of transition revenue but the authorization and collection of “transition revenues or any equivalent revenues.” As mentioned above, AEP-Ohio’s prior transition revenue analysis addressed all revenue (wholesale and retail) that was placed at risk by the deregulation of generation service.¹³¹ To date, the Commission has ignored this reality and has instead offered conclusory statements that above-

¹²⁸ *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of an Electric Transition Plan and Application for Receipt of Transition Revenues*, Case Nos. 99-1729-EL-ETP, *et al.*, Opinion and Order at 18 (Sept. 28, 2000) available at: <http://dis.puc.state.oh.us/TiffToPDF/YZE52O@NG17PZP8X.pdf>. This provision of the ETP settlement was incorporated into AEP-Ohio’s subsequent rate plan, the Rate Stabilization Plan (“RSP”), which was in effect until March 18, 2009 when the Commission approved AEP-Ohio’s first ESP.

¹²⁹ The Commission failed to address this issue in the Capacity Order.

¹³⁰ Entry on Rehearing at 19-20, 56 (Oct. 17, 2012) (Appx. at 108-109, 145).

¹³¹ IEU-Ohio Ex. 101 at 8-9, 11-13, 18 (Supp. at 146-147, 149-151, 156).

market capacity charges are not transition revenue because they are not retail charges, and has done so despite the fact that the Commission authorized AEP-Ohio to collect the deferred above-market compensation through current and future non-bypassable retail riders. As R.C. 4928.38 makes clear, the Commission cannot authorize transition revenue or its equivalent. Accordingly, the above-market supplement is unlawful and unreasonable.

2. *The deferred above-market compensation is unlawful and unreasonable because it conflicts with the policies contained in R.C. 4928.02, which prohibit anticompetitive subsidies and which rely upon market forces, customer choice, and prices disciplined by market forces to regulate prices for competitive retail electric services*

R.C. 4928.02 contains state policies which the Commission is obligated to effectuate pursuant to R.C. 4928.06. These policies generally support reliance on market-based approaches to set prices for competitive services such as generation service and strongly favor competition to discipline prices of competitive services.

In this proceeding, the Commission confirmed that R.C. 4928.02 favors market-based approaches to set prices and compensation for competitive services. The Commission rejected imposing the significantly above-market \$188.88/MW-day charge on CRES providers, and instead held that AEP-Ohio would have to charge CRES providers the market-based RPM-Based Pricing to “promote retail electric competition.”¹³² The Commission found that “RPM-based capacity pricing will stimulate true competition among suppliers in AEP-Ohio’s service territory” and will “incent shopping.”¹³³ The Commission also found that RPM-Based Pricing has “been used successfully throughout Ohio and the rest of the PJM region and puts electric utilities and CRES providers on a level playing field.”¹³⁴ Thus, the Commission found that

¹³² Capacity Order at 23 (Appx. at 67).

¹³³ *Id.* (Appx. at 67).

¹³⁴ *Id.* (Appx. at 67).

RPM-Based Pricing promoted state policy and competition in line with Ohio law and policy and the Commission's duty to effectuate that policy. The Commission did not find that an above-market capacity charge could comply with R.C. 4928.02 and the Commission's reasoning implicitly rejects such a finding.

Furthermore, the deferred above-market compensation violates the state policy contained in R.C. 4928.02(H) by providing AEP-Ohio an anticompetitive subsidy. In a previous AEP-Ohio proceeding, the Commission was confronted with a similar circumstance and held that R.C. 4928.02(H):

requires the Commission to avoid subsidies flowing from a noncompetitive retail electric service to a competitive retail electric service. [AEP-Ohio] seeks to establish a nonbypassable charge that would be collected from all distribution customers by way of the [Plant Closure Cost Recovery Rider]. Approval of such a charge would effectively allow the Company to recover competitive, generation-related costs through its noncompetitive, distribution rates, in contravention of the statute.¹³⁵

Despite the plain meaning of R.C. 4928.02(H) and the Commission's refusal to authorize the recovery of generation-related costs through a non-bypassable charge assed to all of AEP-Ohio's distribution customers, the Commission nonetheless has authorized AEP-Ohio to recover the deferred above-market compensation through non-bypassable charges.

Because the deferred above-market compensation does not comply with R.C. 4928.02, the Commission's authorization of the above-market supplement is unlawful and unreasonable.

3. ***The deferred above-market compensation is unlawful and unreasonable because the Commission is prohibited under R.C 4928.05(A) from regulating or otherwise creating a deferral associated with a competitive retail electric service under R.C. 4905.13. The Commission may only authorize deferred collection of a generation service-related price under***

¹³⁵ *In the Matter of the Application of Ohio Power Company for Approval of the Shutdown of Unit 5 of the Philip Sporn Generating Station and to Establish a Plant Shutdown Rider*, Case No. 10-1454-EL-RDR, Finding and Order at 16-17 (Jan. 11, 2012), available at: <http://dis.puc.state.oh.us/ViewImage.aspx?CMID=A1001001A12A11B35831F43601>.

R.C. 4928.144, but failed to comply with the requirements in R.C. 4928.144

As part of the Capacity Order, the Commission held it was authorizing AEP-Ohio to defer for future collection the difference between RPM-Based Pricing and \$188.88/MW-day under R.C. 4905.13.¹³⁶ The Commission, however, has no authority to modify accounting practices related to generation services under that Section. R.C. 4928.05 limits the Commission's authority to defer generation-related costs for future collection to its authority in R.C. 4928.144; however, that Section is inapplicable because it requires the underlying rate to be authorized as part of an SSO under R.C. 4928.141 to R.C. 4928.143. Thus, the Commission's reliance on R.C. 4905.13 is unlawful and unreasonable.

4. ***The deferred above-market compensation is unlawful and unreasonable because the Commission authorized AEP-Ohio to increase the above-market revenue supplement by adding carrying charges without any evidence that carrying charges, or any specific level of carrying charges, are lawful or reasonable***

The Commission unlawfully and unreasonably authorized AEP-Ohio to add carrying charges (interest) to the deferred above-market compensation without any evidence in the record to support any level of carrying charges. Despite the lack of record support, the Commission held that AEP-Ohio could defer the difference in rates with a carrying charge on the deferral based on AEP-Ohio's "weighted average cost of capital [WACC], until such time as a recovery mechanism is approved" in the *ESP II Case*.¹³⁷ Thereafter, the Commission held AEP-Ohio could collect carrying charges at its long-term cost of debt.¹³⁸ The Court has held it is reversible

¹³⁶ Capacity Order at 23 (Appx. at 67).

¹³⁷ *Id.* at 23-24 (Appx. at 67-68).

¹³⁸ *Id.* at 24 (Appx. at 68).

error when the Commission acts without any evidentiary record.¹³⁹ Because there was no evidence introduced to support any level of carrying charges, the Commission acted unlawfully and unreasonably.

5. *The deferred above-market compensation is unlawful and unreasonable because the Commission failed to recognize that non-shopping customers are paying rates for capacity service in excess of \$188.88/MW-day and it failed to establish a mechanism to credit such excess compensation obtained from non-shopping customers against any deferred balance created by the Capacity Case Decisions*

The Commission initiated this proceeding to determine: (1) if the Commission should authorize AEP-Ohio to charge a capacity rate other than RPM-Based Pricing; (2) “the degree to which AEP-Ohio’s capacity charges are currently being recovered through retail rates approved by the Commission or other capacity charges;” and (3) the impact of AEP-Ohio’s capacity charges on CRES providers and retail competition.¹⁴⁰ The Commission addressed the first and third issue, as discussed herein, but failed to address the second issue. According to AEP-Ohio, current SSO rates provide AEP-Ohio with compensation for capacity service on par with a \$355/MW-day charge.¹⁴¹ Thus, SSO customers are paying excessive amounts for capacity service that are not based upon either market (RPM-Based Pricing) or cost (\$188.88/MW-day as determined by the Commission).

Ohio law and the Commission’s rules, however, require capacity service prices in AEP-Ohio’s SSO to be comparable and non-discriminatory relative to the prices applicable to CRES

¹³⁹ *Tongren v. Pub. Util. Comm.* 85 Ohio St.3d 87 (1999) (quoting *Cleveland Elec. Illum. Co. v. Pub. Util. Comm.*, 76 Ohio St.3d 163 (1996)).

¹⁴⁰ Entry at 2 (Dec. 8, 2010) (Appx. at 183).

¹⁴¹ Tr. Vol. III at 635-637 (Supp. at 754-756).

providers/shopping customers.¹⁴² To ensure comparability and non-discrimination, the Commission should have unbundled the generation capacity service embedded in the SSO, established a comparable and non-discriminatory price and rate design for the unbundled components, and should have held that the capacity service compensation that AEP-Ohio has obtained through the SSO that is above the \$188.88/MW-day price would offset the above-market deferred revenue supplement. Because the Commission failed to do so, the Capacity Case Decisions produce a non-comparable and discriminatory result that is unlawful and unreasonable.

Proposition of Law VI: The Capacity Case Decisions are unlawful and unreasonable because the Commission failed to restore RPM-Based Pricing as required by R.C 4928.143(C)(2)(b) when it rejected the ESP Stipulation

As discussed above, AEP-Ohio's rates under its first ESP were benchmarked to and were based upon AEP-Ohio charging RPM-Based Pricing for capacity service.¹⁴³ After AEP-Ohio sought to increase its capacity charges through the Section 205 Application at FERC, the Commission eliminated any doubt, and held it had adopted the RPM-Based Pricing methodology as the state compensation mechanism.¹⁴⁴ Thus, AEP-Ohio's SSO rates, as established in the *ESP I Case*, included RPM-Based Pricing for generation capacity service and that pricing controlled until the Commission authorized new SSO rates for AEP-Ohio.

On December 14, 2011, the Commission approved the ESP Stipulation and adopted the ESP Stipulation's recommended two-tiered pricing for capacity service.¹⁴⁵ Subsequently, the

¹⁴² See R.C. 4928.02(B) (Appx. at 502), R.C. 4928.15 (Appx. at 520); R.C. 4928.35(C) (Appx. at 524); Ohio Adm. Code 4901:1-35-01(L) (Appx. at 468).

¹⁴³ IEU-Ohio Ex. 103 at 11, 13-14 (Supp. at 288, 290-291).

¹⁴⁴ Entry at 2 (Dec. 8, 2010) (Appx. at 183).

¹⁴⁵ *ESP II Case*, Stipulation and Recommendation at 20-22 (Sept. 7, 2011) available at: <http://dis.puc.state.oh.us/TiffToPDF/A1001001A11I07B05057D70465.pdf>.

Commission determined the ESP Stipulation was not in the public interest and rejected the Stipulation. Upon rejecting the ESP Stipulation, the Commission was required, in accordance with R.C. 4928.143(C)(2)(b), to restore the “the provisions, terms, and conditions of the utility’s most recent standard service offer.”

Although the Commission recognized that it was bound by R.C. 4928.143(C)(2)(b) when it rejected the ESP Stipulation, the Commission nonetheless sustained AEP-Ohio’s lawless demand to continue to charge for capacity service under the two-tiered pricing provision of the then-rejected ESP Stipulation. Thus, the March 7, 2012 Entry and May 30, 2012 Entry, which permitted the two-tiered charges to remain in place following the rejection of the ESP Stipulation, are unlawful and unreasonable.

Proposition of Law VII: The Capacity Case Decisions are unlawful and unreasonable because the temporary two-tiered rates established by the March 7, 2012 Entry and May 30, 2012 Entry were not based upon the record from this proceeding.

On September 7, 2011, AEP-Ohio, along with a number of other parties, submitted the ESP Stipulation to resolve issues in AEP-Ohio’s *ESP II Case* and several other pending cases, including this proceeding. On September 8, 2011, a number of parties that had signed the ESP Stipulation filed a joint motion to consolidate the *Capacity Case* and other cases *for purposes of considering the adoption of the ESP Stipulation*.¹⁴⁶ On September 16, 2011, an Attorney Examiner issued an Entry granting the September 8, 2011 motion to consolidate *for the purpose of considering the ESP Stipulation* and staying the procedural schedule in this proceeding.¹⁴⁷ The Attorney Examiner’s September 16, 2011 Entry was *not* issued or filed in this proceeding.

¹⁴⁶ Joint Motion to Consolidate at 6 (Sept. 8, 2011) (Supp. at 734).

¹⁴⁷ *ESP II Case*, Entry at 6 (Sept. 16, 2011) (“ORDERED, That the motion to consolidate the hearing on the Stipulation in the ESP 2 cases with the Merger Case, the Capacity Charges Case, the Energy Curtailment Cases, and the Fuel Deferral Cases *for purpose of considering the*

Under the short-lived ESP Stipulation, AEP-Ohio was authorized to implement the two-tiered pricing scheme for its capacity charges to CRES providers. Despite the limited purpose of the consolidation, the Commission cited the record from the consolidated hearing on the ESP Stipulation to support its authorization of a continuation of the two-tiered capacity pricing scheme from the then-rejected ESP Stipulation.¹⁴⁸ Specifically, the Commission claimed that continued use of RPM-Based Pricing as the state compensation mechanism could result in an unjust and unreasonable result.¹⁴⁹ The Commission cited evidence from the ESP Stipulation hearing to claim that RPM-Based Pricing did not permit AEP-Ohio to recover its capacity costs.¹⁵⁰ Further, the Commission noted that AEP-Ohio was no longer collecting provider of last resort (“POLR”) charges as a result of the remand in the *ESP I Case* and may have to share off-system sales (“OSS revenues”) with its affiliates.¹⁵¹ The Commission’s reasoning and reliance on this “record” is unlawful and unreasonable.

The Commission improperly relied on testimony from the ESP Stipulation hearing concerning capacity costs.¹⁵² Without this reference to the record of the ESP Stipulation hearing, the Commission had no basis to suggest that RPM-Based Pricing was below AEP-Ohio’s “cost” to provide capacity or the Commission’s conclusion that RPM-Based Prices could lead to an unjust and unreasonable result.¹⁵³

Stipulation, is granted.”) available at:

<http://dis.puc.state.oh.us/ViewImage.aspx?CMID=A1001001A11116B14424C32193>.

¹⁴⁸ Entry at 15-16 (Mar. 7, 2012) (Appx at 29-30).

¹⁴⁹ *Id.* at 16 (Appx. at 30).

¹⁵⁰ *Id.* (Appx. at 30).

¹⁵¹ *Id.* (Appx. at 30).

¹⁵² *Id.* at 15-16 (Appx. at 29-30).

¹⁵³ *Id.* at 16 (Appx. at 30).

The Commission also improperly relied on the fact that AEP-Ohio is no longer authorized to collect POLR charges. Previously, the Commission determined that AEP-Ohio was not entitled to POLR charges because it had failed to demonstrate that it had any POLR-related costs.¹⁵⁴ The Commission's suggestion that AEP-Ohio should be permitted to raise its capacity charges to make up for a cost the Commission previously found had not been proven defies reason. Finally, there was no evidence to address what shortfall might occur because of AEP-Ohio's decision to agree to share OSS revenue with its affiliates.

The lack of record support for the March 7, 2012 Entry was further compounded in the Commission's May 30, 2012 Entry when the Commission authorized AEP-Ohio to extend and increase the two-tiered pricing scheme.¹⁵⁵ The pricing scheme authorized in the May 30, 2012 Entry was not subject to any hearing and no evidence was cited to support increasing the tier one charges from RPM-Based Pricing to an arbitrary \$146/MW-day.¹⁵⁶ Accordingly, the March 7, 2012 and May 30, 2012 Entries are unlawful and unreasonable.

Proposition of Law VIII: The Capacity Case Decisions are unlawful and unreasonable inasmuch as the Commission failed to direct AEP-Ohio to refund the above-market portion of capacity charges in place since January 2012 or credit the excess collection against regulatory asset balances otherwise eligible for amortization through retail rates and charges.

¹⁵⁴ *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 Assets*, Case Nos. 08-917-EL-SSO, *et al.*, Order on Remand at 33 (Oct. 3, 2011), available at: <http://dis.puc.state.oh.us/TiffToPDF/A1001001A11J03B20528I67558.pdf>.

¹⁵⁵ The pricing scheme authorized in the ESP Stipulation that continued through May 31, 2012 had a tier one price set at the then-current RPM-Based Price and a tier two price set at \$255/MW-day. The pricing scheme authorized in the May 30, 2012 Entry had a tier one price of \$146/MW-day and a tier two price of \$255/MW-day. Beginning June 1, 2012, the RPM-Based Price was roughly \$20/MW-day.

¹⁵⁶ See Entry at 7-8 (May 30, 2012) (Appx. at 39-40).

For the reasons expressed herein, the Commission's authorization of an increase in AEP-Ohio's compensation from the market-based RPM-Based Pricing to the two iterations of the two-tiered pricing scheme and now to the above-market \$188.88/MW-day pricing scheme was and is unlawful and unreasonable. Because the Commission patently and unambiguously lacked jurisdiction to approve these charges, as AEP-Ohio repeatedly argued,¹⁵⁷ the Court should direct the Commission to credit the above-market charges AEP-Ohio collected in excess of RPM-Based Pricing against regulatory asset balances otherwise eligible for amortization through retail rates in order to provide consumers with some "rough justice" for the Commission's patent and unambiguous violation of its statutory duty.

Proposition of Law IX: In addition to the individual errors committed by the Commission which are referenced or identified herein, the totality of the Commission's conduct throughout this proceeding is arbitrary and capricious, an abuse of discretion, otherwise outside the law and "... at variance with 'the rudiments of fair play' long known to our law. The Fourteenth Amendment condemns such methods and defeats them." West Ohio Gas Co. v. Pub. Util. Comm., 294 U.S. 63, 71 (1935) (quoting Chicago, Milwaukee, & St. Paul Ry. Co. v. Polt, 232 U.S. 165, 168 (1917)).

As described herein, the totality of the Commission's actions during the course of this proceeding combine to violate IEU-Ohio's due process rights under the Fourteenth Amendment of the U.S. Constitution. Throughout this proceeding, the Commission has repeatedly granted applications for rehearing, indefinitely tolling them, preventing parties from taking an unobstructed appeal to the Ohio Supreme Court.¹⁵⁸ Additionally, the Commission granted AEP-Ohio authority to temporarily impose various forms of the two-tiered capacity charges without

¹⁵⁷ See e.g. Ohio Power Company's and Columbus Southern Power Company's Application for Rehearing at 21 (Jan. 7, 2011) (Supp. at 363).

¹⁵⁸ In fact, AEP-Ohio's application for rehearing challenging the Commission's jurisdiction to regulate its capacity-related compensation was tolled from February 2, 2011 through October 17, 2012; the Commission issued its decision on the merits (on July 2, 2012) before it addressed AEP-Ohio's threshold argument that the Commission lacked jurisdiction to proceed. Entry on Rehearing at 2 (Feb. 2, 2011) (Appx. at 167).

any record support for the charges. The Commission also unlawfully and unreasonably created an incomplete deferral (the deferred above-market compensation) without any evidence in the record to support a deferral, and then moved the resolution of the deferred above-market compensation to a separate proceeding (the *ESP II Case*) where the evidentiary record had already closed. Finally, the Commission unlawfully and unreasonably authorized carrying charges on the deferral without record support. The totality of the Commission's actions is a violation of IEU-Ohio's due process rights.

When the Commission has engaged in ratemaking based on evidence not in the record or failed to allow parties to refute evidence, the United States Supreme Court has held that the Commission violated the due process rights of parties: “[t]his is not the fair hearing essential to due process. It is condemnation without trial.”¹⁵⁹ The United States Supreme Court has also held that regulation by a public utilities commission in accordance with the jurisdiction's applicable law “meets the requirements both of substantive and procedural due process *when it is not arbitrarily and capriciously exercised.*”¹⁶⁰

Similarly, this Court has held due process in a Commission proceeding occurs *when* a party is given: (1) “ample notice;” (2) “permitted to present evidence through the calling of its own witnesses;” (3) permitted to “cross-examin[e] the other parties’ witnesses;” (4) introduce exhibits; (5) “argue its position through the filing of posthearing briefs;” and (6) “challenge the PUCO’s findings through an application for rehearing.”¹⁶¹ Further, this Court has held that the Commission must, in order to comply with the law, provide “in sufficient detail, the facts in the

¹⁵⁹ *Ohio Bell Tel. Co. v. Pub. Util. Comm.*, 301 U.S. 292, 300 (1937).

¹⁶⁰ *Pub. Util. Comm. v. Pollak*, 343 U.S. 451, 465 (1952) (emphasis added).

¹⁶¹ *Vectren Energy Delivery of Ohio, Inc. v. Pub. Util. Comm.*, 113 Ohio St.3d 180, 863 N.E.2d 599; 2006-Ohio-1386 at ¶ 53.

record upon which the order is based, and the reasoning followed by the PUCO in reaching its conclusion.”¹⁶² As a dissenting opinion of Justice Herbert Brown eloquently explains:

The commission cannot decide cases on subjective belief, wishful thinking, or folk wisdom. Its decision must be based on a record containing “sufficient probative evidence to show that the commission’s determination is not manifestly against the weight of the evidence and is not so clearly unsupported by the record as to show misapprehension, mistake or willful disregard of duty.”¹⁶³

The Commission abuses its discretion if it renders an opinion without record support.¹⁶⁴

The Commission’s conduct throughout this proceeding has subjected parties objecting to AEP-Ohio’s demands to condemnation without trial. Throughout this proceeding, the Commission has taken it upon itself to rewrite the law to claim authority it does not have. Repeatedly, the Commission has acceded to AEP-Ohio’s demands, granting rehearing, delaying any final decision for years. The Commission has also repeatedly refused to make its AEP-Ohio-friendly decisions subject to reconciliation and refund so as to protect the interests of parties injured by the Commission’s AEP-Ohio-inspired rush to judgment. The totality of the Commission’s conduct throughout this proceeding is arbitrary and capricious, an abuse of discretion, otherwise outside the law and “at variance with ‘the rudiments of fair play’ long known to our law. The Fourteenth Amendment condemns such methods and defeats them.”¹⁶⁵

¹⁶² *Tongren v. Pub. Util. Comm.* 85 Ohio St.3d 87, 89 (1999).

¹⁶³ *Consumers' Counsel v. Pub. Util. Comm.*, 61 Ohio St.3d 396, 406 (1991) *dissenting opinion of Justice Herbert Brown (quoting Columbus v. Pub. Util. Comm.*, 58 Ohio St.2d 103, 104 (1979)).

¹⁶⁴ *Tongren v. Pub. Util. Comm.* 85 Ohio St. 3d 87, 1999-Ohio-206 (*quoting Cleveland Elec. Illum. Co. v. Pub. Util. Comm.*, 76 Ohio St.3d 163 (1996)); *Indus. Energy Users-Ohio v. Pub. Util. Comm.*, 117 Ohio St.3d 486, 2008-Ohio-990 at ¶ 30.

¹⁶⁵ *West Ohio Gas Co. v. Pub. Util. Comm.*, 294 U.S. 63, 71 (1935) (*quoting Chicago, Milwaukee & St. Paul Ry. Co. v. Polt*, 232 U.S. 165, 168 (1914)).

CONCLUSION

For the reasons described herein, the Commission's actions in the proceeding below are unlawful and unreasonable. Accordingly, IEU-Ohio requests that the Court reverse the Commission and remand this proceeding back to the Commission with directions to revoke its approval of the above-market supplement to RPM-Based Pricing. IEU-Ohio also requests that the Court direct the Commission to reduce AEP-Ohio's outstanding regulatory asset balances by the unlawful and unreasonable above-market capacity charges AEP-Ohio has collected through the two-tiered pricing scheme and through the \$1/MWh portion of the RSR.

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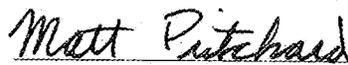
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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing *Merit Brief of Appellant/Cross-Appellee, Industrial Energy Users-Ohio* was served upon the parties of record this 15th day of July 2013 via electronic transmission, hand-delivery, or ordinary U.S. mail, postage prepaid.



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