ORIGINAL

IN THE SUPREME COURT OF OHIO

INDUSTRIAL ENERGY USERS – OHIO,	:	**Consolidated Case Nos. 2012-2098**
	:	**2013-0228**
Appellant,	:	
	:	**Appeals from the Public Utilities Commission of Ohio**
v.	:	
	:	
THE PUBLIC UTILITIES COMMISSION OF OHIO,	:	**Public Utilities Commission of Ohio Case No. 10-2929-EL-UNC**
	:	
Appellee.	:	

FOURTH MERIT BRIEF OF APPELLEE/CROSS-APPELLANT OHIO POWER COMPANY

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

CASES

INTRODUCTION

The State Compensation Mechanism (SCM) adopted by the Commission goes a long way toward establishing a capacity rate that balances the needs and interests of a variety of stakeholders, including consumers, CRES providers, and AEP Ohio. But the SCM incorporates a dramatically overstated energy credit that artificially suppresses the net capacity charges. In calculating that credit, the Commission used a static estimate of the shopping rate that was well below empirical experience even before the Commission ruled. The Commission also improperly incorporated revenue that is unrelated to the capacity sales to CRES providers at issue here; and the Commission used a black-box model from another (undisclosed) context that was never calibrated to AEP Ohio and the circumstances here. Public welfare and the Constitution alike require that AEP Ohio receive just compensation for the capacity it provides to CRES providers. If the Court does not allow AEP Ohio to defer incurred capacity costs not recovered from CRES providers, at the very least the Court must provide some mechanism for affording AEP Ohio the "just compensation" – the difference between AEP Ohio's capacity costs and below-cost RPM rate – that the U.S. Constitution requires.

LAW AND ARGUMENT

Proposition of Law No. VIII: The PUCO may not reduce AEP Ohio's cost-based capacity rate using an energy credit that incorporates demonstrably inaccurate inputs.

A. The Commission Adopted A Static Shopping Assumption That Is Against The Manifest Weight Of The Evidence And Results In An Unreasonably And Unlawfully Overstated Energy Credit.

As AEP Ohio explained in its Second Merit Brief, the Commission produced a dramatically inflated energy credit by incorporating a static, 26.1% shopping assumption that was against the manifest weight of the evidence. (AEP Ohio Second Br. at 42-47.) In response, the Commission points to its finding on rehearing that "the level of shopping will continually fluctuate in both directions." (PUCO Third Merit Br. at 12, citing First Rehearing Entry at 35, IEU Appx. at 124.) But that "finding" has no basis in – and disregards – the record evidence. The record evidence showed that the Commission expected and, indeed, insured by its actions that shopping would go only in one direction – upward.

No evidence was adduced at hearing that suggested shopping would decrease or would remain at or near 26.1% during the term of AEP Ohio's ESP. To the contrary, AEP Ohio presented evidence that the shopping rate in its service territory had increased substantially above the Commission's chosen 26.1% figure *even before the hearing regarding AEP Ohio's capacity charge concluded* – increasing at a rate of more than 4% in one month. (*See* AEP Ohio Ex. 142 at 21 (shopping in AEP Ohio's service territory increased from 26.1% as of March 31, 2012, to 30.19% as of April 30, 2012).) Other evidence likewise demonstrated that shopping will continue to increase – up to as high as 71.3% due, in part, to the low prices for capacity that the Commission ordered AEP Ohio to charge CRES providers. (*See* RESA Ex. 102 at 3, Add. Supp. at 2 ((16,942 GWh + 17,490 GWh)/(48,261 GWh) = 71.3%).) The Commission simply disregarded this evidence when it chose to adopt a 26.1% static shopping assumption that was already incorrect by the time the hearing concluded.

The Commission's contrary finding that shopping could fluctuate not only above but also below the 26.1% rate during the term of AEP Ohio's ESP has no merit. That finding contradicts the Commission's stated intention that its decision in the *Capacity* Case "stimulate competition among suppliers in AEP Ohio's service territory" and thereby increase shopping. *Capacity* Order at 23, IEU Appx. at 67; *see also* First Rehearing Entry at 6, IEU Appx. at 95 (noting that the Commission "directed that AEP-Ohio's capacity charge to CRES providers should be the RPM-based rate * * * on the basis that the RPM-based rate will promote retail electric competition");

id. at 40, IEU Appx. at 129 ("[W]e believe that a capacity charge assessed to CRES providers on the basis of RPM pricing will advance the development of true competition in AEP-Ohio's service territory."). Indeed, the Commission concedes that its adopted shopping assumption "reflected the current level of shopping in AEP-Ohio's service territory at the time of EVA's analysis," but does *not* reflect the actual shopping taking place at the time of its decision or account for its projected future *increases*. (*See* PUCO Third Br. at 12)

The impact is significant. The Commission should account for actual shopping levels in the record at the time of the Commission's decision. It should also account for the Commission's own findings that shopping levels will substantially increase – not decrease – under the RPM pricing regime. The failure of the Commission's energy credit to reflect those changes in shopping renders its ruling contrary to the manifest weight of the evidence and, as a result, unreasonable and unlawful. The Court should remand this case with instructions to the Commission to correct this failure by adjusting the energy credit based on an appropriate, non-static shopping assumption. At a minimum, the Court should instruct the Commission to adjust the rate to actual shopping levels in the record at the time of the Commission's decision.

B. The Commission Fails To Refute That Its Energy Credit Methodology Is Based On A Model Whose Inputs Cannot Be Meaningfully Evaluated Or Tested.

The Commission argues that the model it adopted used "known AEP-Ohio specific inputs that can be meaningfully evaluated." (PUCO Third Br. at 13-14.) The witness who originally sponsored the model, however, testified that all the data that was used in the model was either embedded, off-the-shelf, already default data, or was provided by somebody else who was not present to testify about it. (Tr. IX at 1865, Add. Supp.[1] at 5.) He could not identify or describe, among other things, what data was used in the model's coal forecast (*id.* at 1844, Add. Supp. at

[1] "Add. Supp." refers to AEP Ohio's Additional Supplemental being filed contemporaneously with this brief.

4), what reserve margin the model utilized (*id.* at 1872, Add. Supp. at 6), or the vintage of the data used in the modeling. (*Id.* at 1873-1874, Add. Supp. at 7-8)

Ms. Medine, the second witness called to defend the model, and whom the Commission characterizes as "the better witness for the model inputs" (PUCO Third Br. at 14), also could not answer even basic questions such as the reserve margin used in the model. (*See, e.g.*, Tr. X at 2208, Add. Supp. 10) Moreover, her hearing testimony directly contradicts the Commission's contention that the model used AEP Ohio-specific inputs. (*See, e.g., id.* at 2257-2258, Add. Supp. at 14-15 (stating that the model used 2011 coal purchase data from the U.S. Energy Information Administration, not AEP Ohio-specific data).) One of the only things that is certain about the Commission's method is that many of its inputs were *not* based on known AEP Ohio-specific inputs. Simply put, the Commission has not demonstrated that its adopted model is supported by the record. For this reason, its adoption of the model was unreasonable and unlawful.

C. The Commission's Adopted Model Was Not Properly Calibrated.

The Commission's contention that the Aurora model it adopted for calculating the energy credit was properly calibrated (PUCO Third Br. at 15-16) is also devoid of any record support. To the contrary, the record evidence before the Commission clearly demonstrates that the model was not properly calibrated. (*See* AEP Ohio Ex. 144 at 10-11, Supp. at 380-381; Tr. X at 2210-2211, 2163-2164, Supp. at 597-598, 593-594.) Indeed, one of the Commission Staff's witnesses sponsoring the model testified at hearing that the model *was not calibrated for AEP Ohio*. (Tr. X at 2210-2211, Add. Supp. at 12-13) And, although she claimed (and the Commission now argues) that the model was calibrated for some other project for the federal government, she refused to discuss what that project was, what was done to calibrate the model to that project, or whether the outputs from that engagement were benchmarked to historical market performance or clearing prices. That denied AEP Ohio and the Commission any meaningful opportunity to evaluate the model's accuracy *for the purpose to which it was put in this case*. (*See id.* at 2209-2210, Add. Supp. at 11-12) The failure to properly calibrate the model was a critical error, caused the model to be unsuitable for its intended use, and resulted in outputs that were inaccurate. (AEP Ohio Second Br. at 45.) Moreover, had this "most basic step" in any modeling analysis been undertaken, it would have revealed that the model's final run overstated gross energy margins by more than 20%. (*Id.*) "[C]alibration is a 'critical' and 'valuable' step that ensures that model simulation matches the field observation to a reasonable degree." *Abarca v. Franklin County Water Dist.*, 761 F.Supp.2d 1007, 1060 (E.D. Cal. 2011).

As with the Company's other concerns about the energy credit model, AEP Ohio's challenges to the model's calibration fell on deaf ears. Those concerns were not challenged by any other party to the case, and the Commission did not address them. Rather, in response to all of AEP Ohio's comments, the Commission stated only: "[W]e do not believe that the Company has demonstrated that the inputs actually used by EVA are unreasonable." *Capacity Case*, Entry on Rehearing at 35, Add. Supp. at 16. But that does not address the model's lack of calibration – *i.e.*, the undisputed fact that there was no effect to recalibrate it from its prior (undisclosed) use on a government project to its current use of calculating an energy credit for AEP Ohio. Because the energy credit is based on the results of that uncalibrated and unreliable model, this Court should set aside the Commission's calculation of the energy credit and remand for further proceedings.

D. The Commission's Adopted Model Erroneously Incorporates Traditional OSS Margins, Unreasonably Captures Margins from Non-Shopping Customers, and Disregards The Impact of the AEP Pool on Such Margins.

The Commission's adopted energy credit suffers from three further, fatal, defects. It (1) erroneously incorporates OSS margins not associated with capacity used to support shopping load; (2) improperly imputes a market-based margin for non-shopping customers; and (3) does not adjust OSS margins to take into account AEP Ohio's 40% Member Load Ratio ("MLR") under the FERC-approved Pool agreement between the companies in the AEP East System. Those errors, both individually and in the aggregate, significantly overstate the energy credit and, correspondingly, result in an understatement of the Company's cost-based capacity rate. Presented with these errors, the Commission, characterized the issue as a mere "difference in methodology," *Capacity Case*, Order at 36, and said nothing further. The Commission takes a similarly dismissive approach in its Third Merit Brief. (*See* PUCO Third Br. at 16-19.) But any energy credit that incorporates these plain errors is by definition unreasonable and unlawful.

1. The adopted energy credit improperly reflects more than the Incremental OSS margins created by "freed up" energy associated with the capacity supplied to CRES providers.

The approach that the Commission adopted to set the energy credit incorrectly assumes that AEP Ohio's MLR share (currently 40%) of *all* OSS margins is retained and available to offset the costs of capacity that is furnished to CRES providers. In other words, the energy credit does not just incorporate profits from wholesale energy sales made possible, *i.e.*, "freed up," as a result of capacity furnished to CRES providers (as is ordinarily appropriate). Instead, it also commandeers profits from wholesale energy sales made using *other* surplus generation capacity (traditional OSS energy margins) unrelated to the capacity sold to CRES providers.

That is inappropriate. Incorporating AEP Ohio's margins realized from wholesale OSS energy sales that are completely separate and independent from its supply of capacity to CRES providers confiscates those margins. If the energy credit must account for OSS margins, only those attributable to "freed up" energy associated with the capacity being sold to a CRES provider should be included. An analogy makes that clear: If Ford Motor Company were required to provide gasoline car engines to competitors, it might be appropriate to reduce the compensation it received to account for the fact that doing so allowed Ford to generate additional revenue by selling more scrap metal on the market and providing buyers with replacement parts. But one would never reduce the compensation to be paid because Ford also makes money by selling scrap metal from and supplying replacement parts in connection with its separate diesel truck division. That would in effect confiscate unrelated profits. Yet that is in essence what the Commission did to AEP Ohio here.

Because the Commission disregarded AEP Ohio's arguments on this point and adopted an energy credit that unreasonably strips from the Company the margins from its traditional OSS revenues, its decision is arbitrary, unreasonable, and against the manifest weight of the evidence. This Court should not sanction the Commission's confiscation of unrelated margins. The case should be remanded with instructions that, to the extent any OSS margins are included as an offset in determining the energy credit, only those margins actually attributable to wholesale energy sales "freed up" by capacity sold to CRES providers should be used.

2. The energy credit unreasonably imputes a fictional market-based margin for non-shopping customers and incorporates that credit to offset the capacity charge for shopping load, creating an unreasonable and unlawful subsidy and confiscating margin to which AEP Ohio is entitled through its SSO rates.

There is no dispute that the Commission's energy credit methodology assumed that 100% of the retail energy margins it imputed is available and can be used to offset the cost of capacity that AEP Ohio is required to furnish to CRES providers. This aspect of the energy credit methodology is patently unreasonable for multiple reasons. First, the energy credit should not include an offset for OSS margins related to non-shopping load. Such an offset confiscates a portion of the SSO generation revenue collected from non-shopping customers, under Commission-approved SSO rates, and forces AEP Ohio to use those revenues to offset the costs of capacity that CRES providers and retail customers are jointly responsible for paying. Moreover, when it proposed the energy credit, Commission Staff did not explain why *any*, let alone *all* of the Company's imputed retail SSO margins should be co-opted for the benefit of CRES providers. Second, the Commission's adoption of a methodology that funds a capacity charge discount through the use of SSO revenues also amounts to a subsidy of a competitive service and, therefore, conflicts with Ohio's energy policy and basic economic principles.

3. The adopted energy credit unlawfully fails to reflect operation of the FERC-approved Pool.

The Commission's methodology of imputing 100% of non-shopping SSO margins as an offset to CRES providers' capacity costs also unlawfully disregards the correct operation of the FERC-approved Pool, of which AEP Ohio is a member. AEP Ohio demonstrated at hearing that imputing non-shopping SSO energy margins as "Retail Margins," and then providing 100% of those margins to CRES providers, effectively increases the Member Load Ratio ("MLR") from an actual 40% (the level that AEP Ohio is allowed to retain under the Pool) to about 92% (a level not permitted by the Pool). (AEP Ohio Ex. 143 at 10, Add. Supp.at 20) This greatly overstates the amount of margin that AEP Ohio retains under the FERC-approved AEP Pool Agreement and provides a windfall at AEP Ohio's expense, particularly at the unreasonably low level of shopping that the Commission's model assumes. (*Id.* at 10-11,Add. Supp. at 20-21.) The Pool is under the FERC's jurisdiction and infringement upon its operation is preempted by federal law. (*See id.* at 2, Add. Supp. at 18); *Mississippi Power & Light Co. v. Mississippi ex rel. Moore,* 487 U.S. 354, 357 (1988); *American Electric Power Service Corp.*, 32 FERC ¶ 61,363 (1985).

In substance, the Commission's flawed methodology confiscates revenues from AEP Ohio's retail SSO sales and uses them to subsidize the lower wholesale rate paid to AEP Ohio for capacity. (AEP Ohio Ex. 143 at 6,11, Add. Supp. At 19, 21.) This fictional imputation and retention of energy margins substantially inflates AEP Ohio's retained energy margins and, ultimately, the Commission's adopted energy credit, resulting in a cost-based capacity rate that is substantially understated. For this reason too, the Commission's adopted energy credit cannot stand.

In light of the record and the Commission's failure to substantively address the numerous problems with its energy credit methodology and model, the Court should find that the Commission's energy credit is unreasonable, unlawful, and against the manifest weight of the evidence, and it should remand the energy credit to the Commission with instructions to correct it and to modify AEP Ohio's capacity rate accordingly.

Proposition of Law No. IX: Precluding AEP Ohio from recovering the difference between its cost of capacity and the auction rate would constitute a regulatory taking.

The Supreme Court has confirmed that the Constitution places limits upon the government's power to regulate in a way that amounts to a "taking" of property without just compensation – even if the regulation deprives the owner of less than 100% of its interest. *Penn Cent. Transp. Co. v. New York City*, 438 U.S. 104, 123-128, 98 S. Ct. 2646, 57 L. Ed. 2d 631 (1978). Before the Commission and this Court, AEP Ohio invoked *Penn Central*'s test and showed, with record support, that: (1) the Commission's adoption of a non-compensatory price for capacity would have a pernicious economic impact upon AEP Ohio; (2) no investor's expectations would be met if a utility commission could find that a certain capacity rate is just and reasonable, but then preclude the party generating the capacity from recovering anything close to that rate; and (3) the character of such a regulation would compel an order of just compensation. (*See* AEP Ohio App. for Rehearing at 50-56 (July 20, 2013); *see also* AEP Ohio Second Br. at 47-49.) IEU, FES, and OCC all challenge AEP Ohio's takings claim, but their contentions lack merit.

A. IEU, FES, And OCC Conflate Analytically Distinct Legal Theories.

Disputing AEP Ohio's *Penn Central* takings claim, IEU, FES, and OCC all rely upon the U.S. Supreme Court's decision in *Fed. Power Comm. v. Hope Natural Gas Co.*, 320 U.S. 591, 602 (1944) and its progeny, such as *Market St. R. Co. v. R.R. Comm. of California*, 324 U.S. 548, 567 (1945). (*See* IEU Br. at 48 (describing *Hope Natural Gas* as the "pinnacle case on this issue"); *see also id.* at 49, citing *Market St. R. Co.*; FES Merit Br. at 36; OCC Merit Br. at 19.) But *Hope Natural Gas* predated *Penn Central* by more than three decades. And it relates to an analytically distinct legal theory also presented in AEP Ohio's Application for Rehearing – that the Commission's Order is confiscatory, unjust, and unreasonable under the "end result" standard. (*See* AEP Ohio App. for Rehearing at 45-50 (July 20, 2013.) The Supreme Court has noted that *Hope Natural Gas* was "reviewed *pursuant to statute* rather than under the Fourteenth Amendment." (Emphasis added.) *Market St. R. Co.*, 324 U.S. at 566. And the *en banc* D.C. Circuit has confirmed that *Hope Natural Gas* sets the "standard of judicial review when rates ordered by an agency are challenged in court as failing to meet the *statutory requirement* that they be 'just and reasonable.'" (Emphasis added.) *Jersey Cent. Power & Light Co. v. Federal Energy Regulatory Comm.*, 810 F.2d 1168 (D.C. Cir. 2004).

AEP Ohio's Ninth Proposition of Law invokes *Penn Central*'s test to determine whether a property deprivation is unsound because of constitutional requirements. *Hope Natural Gas*, by contrast, involved the *statutory* requirement of "just and reasonable" rates. Appellants have muddled that distinction. But those two inquiries, while related, are "analytically distinct claims." *P.R. Tel. Co. v. Telecomms. Regulatory Bd. of P.R.*, 665 F.3d 309 (1st Cir. 2011). For this Court to assess the merits of AEP Ohio's constitutional takings claim, it should apply *Penn Central*'s three-part test and authority construing that test.

For example, the New Hampshire Supreme Court has cited *Penn Central* in support of its holding that a public utility commission order placing conditions upon the utility's future issuance of securities resulted in an unconstitutional taking because it frustrated distinct investment-backed expectations. *Pub. Serv. Co. of New Hampshire v. New Hampshire Pub. Util. Comm.*, 122 N.H. 1062, 1071-73, 454 A.2d 435 (1982). That case, like this one, stemmed from an investigatory docket initiated by the state commission itself. *Id.* at 1064. And that case, like this one, resulted in an order mandating that the utility conduct certain future transactions under specific terms and conditions, which the utility contended would amount to a partial taking. *Id.* at 1065. Quoting Justice Holmes for the proposition that courts are "'in danger of forgetting that a strong public desire to improve the public condition is not enough to warrant achieving the desire by a shorter cut than the constitutional way of paying for the change,'" the New Hampshire Supreme Court held that the commission could not deny the utility the financial means to complete construction of a new generating unit "*without adequately compensating the utility.*" (Emphasis added.) *Id.* at 1071. This Court should reach the same conclusion here. *Penn Central* and the Takings Clause preclude the Commission from denying AEP Ohio adequate compensation for the capacity it generates, and must provide to CRES providers, even if the Commission's Order stems from a "strong public desire to improve the public condition."

B. IEU, FES, And OCC Fail To Rebut AEP Ohio's Application Of The *Penn Central* Three-Part Test.

Addressing the first factor of the *Penn Central* test – the economic impact of the regulation – AEP Ohio offered extensive witness testimony regarding the pernicious effect that a non-compensatory capacity price would have. (AEP Second Merit Brief at 48). One witness, for example, testified that "[t]he impact on AEP Ohio's ability to be compensated for its costs has become significant due to the trend in auction prices, as well as the growth in shopping by AEP Ohio customers whose CRES providers take advantage of the capacity supplied by AEP as opposed to supplying their own capacity." (AEP Ohio Ex. 101 at 7, Add. Supp. at 23) Aligning the SCM with the PJM RPM price, he explained, would undermine the Company's ability to provide customers with reliable and adequate service. AEP Ohio, he observed, "is not receiving adequate compensation for performing its FRR capacity obligations, and the gap between its costs and the compensation for those costs is increasing at an alarming rate," thereby "threatening AEP Ohio's financial stability." (*Id.* at 14, Add. Supp. at 24.) The Commission *itself* found that RPM rates were "substantially below all estimates provided by the parties regarding AEP Ohio's cost of capacity" and found that under RPM pricing AEP Ohio "may earn an unusually low return on equity * * * with a loss of $240 million between 2012 and 2013." *Capacity* Order at 23, IEU Appx. at 67.

As for interference with AEP Ohio's distinct investment-backed expectations, the second element of the *Penn Central* test, AEP Ohio asked the Commission to take notice of the fact that Standard & Poor's Ratings Service issued a statement *the following day* regarding the impact on AEP Ohio's credit metrics:

> [I]n the longer term we believe this change will likely erode credit quality. We would consider deferrals of changes in capacity prices to be unsupportive of credit quality because cash flow would decline, and could result in financial measures inconsistent with the current rating. In addition, the business risk profile of the company is pressured as it transitions to an unregulated model for generation in Ohio.

Standard & Poor's Research, July 3, 2012.[2] It cannot seriously be contested that the Commission's Order, if it precludes AEP Ohio from recovering the difference between its cost of capacity and the RPM rate, will interfere with AEP Ohio's distinct investment-backed expectations.

The third *Penn Central* factor – the character of the government regulation – would also be met if the Commission is allowed to preclude AEP Ohio from recovering reasonable compensation. Doing so would not "promote the common good," *Penn Central*, 438 U.S. at 124, because it would remove any incentive to develop capacity. Neither AEP Ohio nor anyone else would build up new capacity if there is no possibility of recovering reasonable compensation.

Given the strength of AEP Ohio's showing on these prongs of *Penn Central*'s test, it is not surprising that IEU, FES, and OCC all fail to rebut the Company's application of the test in their Third Merit Briefs. FES does not even cite *Penn Central*, much less dispute any of AEP Ohio's related evidence at all. (FES Third Br. at 35-36.) FES merely argues, wrongly, that AEP Ohio provides capacity "in a competitive market" and seeks "unprecedented guaranteed revenues as if capacity is noncompetitive and subject to traditional rate regulation." (*Id.* at 35.) Given that AEP Ohio is the sole and obligatory supplier of capacity, how FES can characterize the capacity market as "competitive" is anyone's guess, and contradicts the Commission's express findings.

IEU similarly ignores *Penn Central*. Nor does it challenge any of the evidence cited by AEP Ohio in support of the *Penn Central* test. Instead, IEU relies on inapposite authority. (IEU Third Br. at 48-49.) For example, IEU cites a 2012 FERC Order on Rehearing for the proposition that "[FERC] has also recognized that since it has moved to a market-based compensation approach for wholesale services, a traditional confiscation claim is no longer applicable." (*Id.* at

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[2] Available at http://www.reuters.com/article/2012/07/03/idUSWNA036120120703; *see also ESP II*, Case No. 2013-0521, Ex. A to AEP Ohio Reply Post-Hearing Br. (July 9, 2009).

49, citing *ISO New England, Inc. & New England Power Pool Participants Comm. New England Power Generators Assn.*, 138 FERC ¶ 61027 at ¶ 138-39 (Jan. 19, 2012).) But the Joint Complainants in that case did <u>not</u> base their claim upon *Penn Central*; they invoked *Hope Natural Gas* and its line of authority. 138 FERC ¶ 61027 at ¶ 138. FERC's conclusions in that matter, moreover, were expressly predicated upon the existence of a competitive market for capacity:

> As we emphasized, "the Commission has no obligation <u>in a competitive marketplace</u> to guarantee [a resource] its full traditional cost-of-service. Rather, <u>in a competitive market</u>, the Commission is responsible only for assuring that [the resource] is provided the *opportunity* to recover its costs."

Id. at ¶ 140, quoting 113 FERC ¶ 61,311 at ¶ 29 (underscoring added; italics in original). But in this case we have neither a competitive market nor the "opportunity to recover its costs" on which FERC's opinion rests. As the Commission found, a market with a single capacity supplier (here, AEP Ohio) can hardly be deemed competitive – and the evidence shows AEP Ohio is not and cannot recover its full costs. Finally, FERC's rejection of the confiscation claim in IEU's cited Order was expressly based on FERC's finding that the resources in question were "*not compelled* to provide service at a price that is unacceptable to them." (Emphasis added.) *Id.* Here, AEP Ohio must provide capacity to competitors. If AEP Ohio is precluded from recovering the difference between its cost of capacity and the auction rate, it will be compelled to provide service at an unreasonably low price – precisely the condition absent in the FERC proceeding FES invokes. That supports the Company's regulatory takings claim.

OCC alone cites *Penn Central* and its three-part test (OCC Third Br. at 18.) But OCC fails to challenge any of the evidence and testimony the Company proffered in support of that test. (*Id.* at 16-20.) Instead, OCC posits that because AEP Ohio "will be compensated for capacity from retail non-shopping customers and Marketers even if it does not collect the capacity deferrals," that somehow precludes a *Penn Central* claim. (OCC Merit Br. at 18.) It does not. But the *Penn Central* test allows those (like AEP Ohio) who have *not* suffered *complete* deprivations of all their property interests to pursue just compensation for *partial* takings. *Wymsylo v. Bartec, Inc.*, 132 Ohio St.3d 167, 2012-Ohio-2187, 970 N.E.2d 898, ¶ 55. And the fact that AEP receives proper compensation for some of the capacity it supplies does not permit the taking of capacity without just compensation elsewhere. Consequently, OCC's request to cancel the deferred recovery of AEP Ohio's capacity costs should be rejected. If it is accepted, then this Court should hold that "just compensation" (the difference between AEP Ohio's capacity costs and the RPM rate) is owed to AEP Ohio.

CONCLUSION

For the foregoing reasons and those set forth in AEP Ohio's Second Merit Brief, the Court should grant the relief that AEP Ohio seeks in its cross-appeal.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I certify that the foregoing *Fourth Merit Brief of Appellee/Cross-Appellant Ohio Power Company* was served by First-Class U.S. Mail or hand delivery upon counsel for parties to this proceeding, identified below, this 12th day of November, 2013.

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