

ORIGINAL

IN THE SUPREME COURT OF OHIO

In the Matter of the Application of	:	Case No. 2013-0521
Columbus Southern Power Company and	:	
Ohio Power Company for Authority to	:	Appeal from the Public Utilities
Establish a Standard Service Offer	:	Commission of Ohio
Pursuant to §4928.143, Ohio Rev. Code,	:	
in the Form of an Electric Security Plan.	:	Public Utilities Commission of Ohio
	:	Case No. 11-346-EL-SSO
	:	Case No. 11-348-EL-SSO
In the Matter of the Application of	:	Case No. 11-349-EL-AAM
Columbus Southern Power Company and	:	Case No. 11-350-EL-AAM
Ohio Power Company for Approval of	:	
Certain Accounting Authority.	:	
	:	
The Kroger Company,	:	
	:	
and	:	
	:	
Industrial Energy Users-Ohio,	:	
	:	
Appellants,	:	
	:	
v.	:	
	:	
Public Utilities Commission of Ohio,	:	
	:	
Appellee.	:	

THIRD MERIT BRIEF OF APPELLANT INDUSTRIAL ENERGY USERS-OHIO

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I. INTRODUCTION

In the ESP II Order,¹ the Public Utilities Commission of Ohio (“Commission”) authorized several nonbypassable riders that permit Ohio Power Company (“AEP-Ohio”)² to bill and collect above-market revenue for competitive generation-related services in an electric security plan (“ESP”). The Commission further found that the ESP was more favorable in the aggregate than the market-based alternative, a Market Rate Offer (“MRO”),³ even though the ESP was at least \$386 million less favorable than an MRO. It also conditionally approved the transfer of generating assets to an unregulated competitive affiliate and authorized the pass through of above-market generation-related revenue to the affiliate. As Industrial Energy Users-Ohio (“IEU-Ohio”) demonstrated in its First Brief (“IEU-Ohio Brief”), the orders increase customer costs by \$1 billion over the market alternative and were unlawful and reasonable.

In their responsive briefs,⁴ the Commission and AEP-Ohio urge this Court to affirm the Commission’s unlawful actions, claiming that the ESP II Order provides a benefit to customers.⁵ In a brief filed as amicus curiae, The Dayton Power and Light Company (“DP&L”) also defends the Commission’s authorization of one of the nonbypassable riders, the Retail Stability Rider

¹ *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) (Appendix. at 21) (“ESP II Order” or “ESP II Case” as the context requires). IEU-Ohio’s Appendix and Supplement filed with its First Brief are respectively designated “Appx.” and “Supp.” Its Second Supplement filed with this brief is designated as “Second Supp.”

² In December 2011, the Columbus Southern Power Company and Ohio Power Company merged. Ohio Power Company is the remaining electric distribution utility (“EDU”).

³ R.C. 4928.142 sets out the requirements for an MRO.

⁴ Second Merit Brief Submitted on Behalf of Appellee, the Public Utilities Commission of Ohio (Oct. 21, 2013) (“Commission Brief”); Merit Brief and Appendix of Appellee/Cross-Appellant Ohio Power Company (Oct. 21, 2013) (“AEP-Ohio Brief”).

⁵ Commission Brief at 4-11; AEP-Ohio Brief at 1.

("RSR"), and the Commission's application of the ESP versus MRO test.⁶ In its cross-appeal, AEP-Ohio further argues that the Commission should have authorized AEP-Ohio to recover additional above-market generation-related revenue and that the Commission infringed AEP-Ohio's right to withdraw its application for an ESP. As discussed below, these arguments are without merit.

Accordingly, the Court should reject AEP-Ohio's assignments of error that seek to extract additional above-market revenue from its customers. Further, the Court should reverse and remand the Commission's approval of the ESP and order the Commission to reject the ESP or substantially modify it. The Court also should reverse the Commission's authorization of nonbypassable generation-related charges. Finally, the Commission should reverse the Commission's order permitting AEP-Ohio to pass through above-market revenue to its unregulated competitive affiliate.⁷

⁶ Merit Brief of Amicus Curiae The Dayton Power and Light Company in Support of Appellee the Public Utilities Commission of Ohio (Oct. 21, 2013) ("DP&L Brief").

⁷ In addition to the ESP II Order, two additional Commission decisions currently pending before the Court ensure that AEP-Ohio's generation resources will not be subject to market discipline during the term of the ESP and for several years thereafter. In a decision issued in July 2012, the Commission invented and applied a cost-based ratemaking methodology to uniquely increase the compensation of AEP-Ohio for the provision of wholesale generation-related capacity service to competitive retail electric service ("CRES") providers. *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) (Supp. at 234) ("Capacity Case" or "Capacity Order" as the context requires), *appeal pending*, Sup. Ct. Case Nos. 2013-0228 & 2012-2098. In a decision issued in October 2012, the Commission confirmed its prior conditional order in the ESP II Order to transfer generation assets to an unregulated competitive affiliate and provide the affiliate with a guaranteed above-market revenue stream paid by AEP-Ohio's shopping and nonshopping customers. *In the Matter of the Application of Ohio Power Company for Approval of Full Legal Corporate Separation and Amendment to its Corporate Separation Plan*, Case No. 12-1126-EL-UNC, Finding and Order (Oct. 17, 2012) ("Corporate Separation Case") (Supp. at 687), *appeal pending*, Sup. Ct. Case No. 2013-1014.

II. ARGUMENT

- A. **Proposition of Law No. 1: The ESP II Order is unlawful and unreasonable because the ESP, including its pricing and all other terms and conditions, including any deferrals and any future recovery of deferrals, is not more favorable in the aggregate as compared to the expected results that would otherwise apply under R.C. 4928.142**

The test for approval of an ESP (“ESP versus MRO test”) is set out in R.C. 4928.143(C)(1). That section requires that the Commission find that the ESP, as modified by the Commission, “including its pricing and all other terms and conditions, including any deferrals and any future recovery of deferrals, is more favorable in the aggregate as compared to the expected results that would otherwise apply under section 4928.142 of the Revised Code.” As demonstrated in the IEU-Ohio Brief, the Commission’s determination that the ESP was more favorable in the aggregate than an MRO was unlawful in three ways. First, the Commission’s decision approves an ESP that is objectively worse than an MRO by at least \$386 million. The Commission’s estimate, moreover, is based on a substantial and illegal understatement of the quantitative costs of the ESP relative to the MRO. Second, the decision relies on subjective and unsubstantiated guesswork concerning “qualitative” benefits the Commission concludes “outweigh” \$386 million that the Commission found the ESP objectively fails the ESP versus MRO test. Third, it is premised on a rejection of the policy outcomes mandated by Ohio law.

In its brief, the Commission claims that the record shows that the ESP was more favorable in the aggregate than an MRO.⁸ In their briefs, AEP-Ohio and DP&L support the Commission’s claim that it lawfully applied the ESP versus MRO test.⁹ As discussed below, the Court should reject the arguments of the Appellees and DP&L that, if accepted, would approve an ESP that is more than \$1 billion worse in the aggregate than an MRO.

⁸ Commission Brief at 3.

⁹ AEP-Ohio Brief at 32-42; DP&L Brief at 12.

1. The Commission understated the amount the ESP fails the ESP versus MRO test by several hundred million dollars

By the Commission's estimate, the ESP has a \$386 million higher cost than an MRO.

Based upon that finding alone, the Commission should have rejected the ESP. The Commission, however, substantially underestimates the cost of the ESP.

a. The Commission overstated the cost of the MRO when it used the wrong price for generation capacity service

As IEU-Ohio demonstrated,¹⁰ the Commission used an overstated price for generation capacity to set the price of the MRO. The proper prices for generation capacity are based on the price of capacity that results from the auction process established by PJM Interconnection LLC ("PJM")¹¹ known as the RPM-Based Prices.¹² The prices set through the RPM process are \$20.01/MW-day for the June 2012 to May 2013 planning year, \$33.71/MW-day for the June 2013 to May 2014 planning year, and \$153.89/MW-day for the June 2014 to May 2015 planning year.¹³ Those prices are substantially below the \$188.88/megawatt-day ("MW-day") price authorized by the Commission in the Capacity Case and used by the Commission in this case to set the price of the MRO.¹⁴

¹⁰ IEU-Ohio Brief at 17-19.

¹¹ PJM is a regional transmission organization ("RTO") that establishes wholesale and capacity pricing for utilities operating in a region that covers 13 states and the District of Columbia.

¹² IEU-Ohio Ex. 125 at 55 (Supp. at 193) (successful bidders would have access to capacity at the RPM-Based Price because they are not serving customers as CRES providers, but instead selling generation services to the EDU). "RPM" refers to the Reliability Pricing Model, a market-based auction process used by PJM to set the price of wholesale generation-related capacity service ("Capacity Service").

¹³ Capacity Order at 10 (Supp. at 243).

¹⁴ ESP II Order at 74 (Appx. at 97).

In its brief, the Commission argues that it properly used \$188.88/MW-day as the price for capacity in estimating the cost of the MRO.¹⁵ To support its claim, the Commission misstates its findings in the Capacity Case. According to the Commission, AEP-Ohio's "obligation" to supply capacity *for all customers* required the Commission's use of \$188.88/MW-day to estimate the costs under an MRO.¹⁶ In the Capacity Case, however, the Commission determined that \$188.88/MW-day is the price of Capacity Service for load served by CRES providers only.¹⁷ By using \$188.88/MW-day as the price for the capacity instead of the much lower RPM-Based Prices, the ESP II Order significantly overstates the cost of the MRO's default generation supply and understates the difference between the cost of the MRO and the ESP.

b. The Commission understated the benefits of the MRO when it shortened the term of the MRO by ten months

The tariffs approved under the ESP II Order were effective with the first billing cycle in September 2012.¹⁸ The Commission, however, applied the ESP versus MRO test by delaying the start of the MRO until ten months later.¹⁹ By delaying the start of the MRO, the Commission again understated the difference between the higher cost ESP and the lower cost MRO.

The Commission argues the use of a shortened MRO is reasonable because AEP-Ohio needs at least ten months to implement an auction to support an MRO.²⁰ The Commission's

¹⁵ Commission Brief at 12.

¹⁶ *Id.*

¹⁷ Capacity Order at 36 (Supp. at 269).

¹⁸ ESP II Order at 77 (Appx. at 100).

¹⁹ *Id.* at 74 (Appx. at 97).

²⁰ Commission Brief at 15. In an attempt to lower the amount the ESP fails the ESP versus MRO test, AEP-Ohio states that the cost of the RSR included in the ESP is overstated because the Commission did not shorten the recovery period to the June 1, 2013 to May 31, 2015 period. AEP-Ohio Brief at 39-40. AEP-Ohio's argument fails for the same reason as the Commission's failure to account for the full benefit of the MRO: it misstates the term of the authorized ESP.

explanation to justify the shortened period, however, does not conform with the requirement of R.C. 4928.143(C)(1) which mandates that the Commission compare the ESP to an MRO as if the MRO was in effect. The Commission's delayed start-up time for the MRO for purposes of comparing the MRO to the ESP resulted in an MRO that is not authorized by R.C. 4928.142. Thus, the Commission acted unlawfully when it removed ten months of the MRO from the ESP versus MRO test.

c. The Commission understated the ESP side of the test by failing to include all estimated costs of the illegal nonbypassable riders

In the ESP II Order, the Commission approved several nonbypassable riders to collect above-market generation-related revenue including provisions to amortize the above-market portion of the price the Commission unlawfully authorized in the Capacity Case (the "Capacity Shopping Tax"). As IEU-Ohio demonstrated in its initial brief, the Commission understated the cost of the ESP by failing to account for all of the additional costs associated with the nonbypassable Generation Resource Rider ("GRR"), Pool Termination Rider ("PTR"), RSR, and a post-ESP mechanism to collect any remaining Capacity Shopping Tax not amortized through the RSR.²¹ In their briefs, the Commission and AEP-Ohio argue that the Commission's exclusions were lawful. Their arguments are unsupported by the applicable law and the record.

i. The cost of the GRR is understated in the estimate of costs of the ESP

Initially, the Commission argues that it properly excluded the cost of the Turning Point Solar Facility ("Turning Point") in excess of \$8 million from the GRR.²² The Commission asserts that the decision to include only \$8 million of the \$357 million cost of Turning Point

²¹ IEU-Ohio Brief at 19-23.

²² Commission Brief at 12-13.

“was reasonable and consistent with its analysis of other quantifiable costs of the ESP.”²³ Under R.C. 4928.143(C)(1), however, the Commission must account for all pricing, terms, and conditions of the ESP, both during and after the term of the ESP. At the time the Commission rendered the ESP II Order, AEP-Ohio was seeking approval of Turning Point and cost recovery under R. C. 4928.143(B)(2)(c) for “*the life of an electric generating facility.*” Since the Commission approved the GRR and the charge would have been effective for the life of Turning Point,²⁴ the Commission was required to recognize the entire cost of Turning Point to be collected through the GRR, \$357 million. By including only \$8 million of the \$357 million cost of Turning Point, the Commission unlawfully understated the cost of the ESP by \$349 million.

Moreover, the Commission’s exclusion of \$349 million in costs for Turning Point is inconsistent with its inclusion of alleged *post-ESP benefits* in the ESP versus MRO test. For example, the Commission attributes a benefit to “competitive market pricing” that it claims will occur after the term of the ESP in the ESP versus MRO test.²⁵ The Commission’s application of the test thus includes “qualitative” post-ESP benefits but excludes quantitative post-ESP costs. The effect of the Commission’s inclusion of post-ESP benefits and an exclusion of post-ESP costs biases the ESP versus MRO test in favor of the ESP side of the test by failing to account for the costs of all pricing and other terms of the ESP. As a result, the Commission has not looked at the ESP “in the aggregate.”

Further, the Commission has failed to provide an explanation for this biased application of the test. Without an explanation as to why post-term costs are excluded but post-term benefits

²³ *Id.* at 13.

²⁴ R.C. 4928.143(B)(2)(c).

²⁵ ESP II Order at 76 (Appx. at 99).

are included, the Commission has failed to provide a reasoned basis for its decision in violation of R.C. 4903.09.²⁶

ii. The costs of the PTR and Capacity Shopping Tax are excluded from the estimate of costs of the ESP

As noted above, the ESP II Order does not include costs of the PTR and the mechanism to recover any remaining balance of the Capacity Shopping Tax at the end of the ESP on the ESP side of the ESP versus MRO test.²⁷ (Because the Commission reduced the revenue effect of the RSR by \$144 million that it ordered AEP-Ohio to use to amortize the Capacity Shopping Tax discussed below, the Commission ignored *all* of the Capacity Shopping Tax in its application of the ESP versus MRO test.) The Commission and AEP-Ohio argue that it was proper to exclude the estimated costs of the riders because the expected costs were “speculative.”²⁸

There is nothing speculative about the effects of the riders the Commission excluded. The Commission authorized the riders. Based on the evidence presented to the Commission, the PTR could result in a known cost of \$410 million.²⁹ Likewise, the total Capacity Shopping Tax will increase the cost of the ESP by an estimated \$833 million,³⁰ a substantial portion of which will remain as a deferred balance at the end of the ESP’s term.³¹ Although the Commission authorized the riders and the evidence identified the likely amount of revenue that the riders would collect from customers both during and after the term of the ESP, the Commission ignored

²⁶ *In re Columbus S. Power Co.*, 128 Ohio St.3d 512, 519 (2011) (“*Remand Decision*”).

²⁷ IEU-Ohio Brief at 21-22.

²⁸ Commission Brief at 13-15; AEP-Ohio Brief at 41-42.

²⁹ FES Ex. 104 at 31 (Supp. at 423).

³⁰ ESP II Case, Reply Brief of Industrial Energy Users-Ohio at 12-13 (July 9, 2012) (Supp. at 336-37) (based on AEP-Ohio’s losses of SSO load due to shopping and the Commission’s determination that the price of Capacity Service is \$188.88/MW-day).

³¹ ESP II Order at 75 n.32 (Appx. at 98) (deferred balance amortized \$144 million during ESP).

the requirement of R.C. 4928.143(C)(1) to compare “pricing and all other terms and conditions, including any deferrals and any future recovery of deferrals” of an ESP compared to an MRO. As a result, the Commission unlawfully understated the cost of the ESP.

iii. The cost of the RSR is understated in the estimate of costs of the ESP

The Commission authorized AEP-Ohio to bill and collect \$508 million through the RSR, but excluded \$144 million of that amount when it estimated the cost of ESP in the ESP versus MRO test.³² The Commission argues that the Commission properly excluded the \$144 million because customers would be required to pay the Capacity Shopping Tax under either an ESP or an MRO, and therefore the Capacity Shopping Tax would have no quantifiable effect on the ESP versus MRO test.³³ As discussed in IEU-Ohio’s Brief, however, the statute defining the MRO, R.C. 4928.142, does not provide the Commission any authority to authorize a nonbypassable generation-related charge to collect the Capacity Shopping Tax.³⁴ As a result, there would not be a charge assignable to the MRO to balance the \$144 million AEP-Ohio is authorized to collect in the ESP. Thus, the exclusion resulted in an underestimate of the cost of the ESP relative to an MRO.

iv. The Commission unlawfully and unreasonably understated the cost of the ESP relative to the MRO by over \$1 billion

Even though the Commission tampered with the test, the Commission still found that ESP was less favorable than an MRO in the aggregate by \$386 million. Due to the many arbitrary quantitative mistakes the Commission committed in applying the ESP versus MRO test,

³² *Id.*

³³ Commission Brief at 14-15.

³⁴ IEU-Ohio Brief at 20-21.

however, the Commission's estimate is materially understated. Accounting for only the additional costs of the nonbypassable generation-related riders, the ESP will cost consumers over \$1 billion more than an MRO.³⁵ Under either the Commission's or the lawful application of the ESP versus MRO test, the Commission should have rejected the ESP, and the failure to do so was unlawful.

2. The Commission's reliance on qualitative benefits to conclude the ESP is more favorable than an MRO is unlawful and unreasonable

Rather than reject the ESP as required by R.C. 4928.143(C)(1) because the ESP is at least \$386 million less favorable than an MRO, the ESP II Order states that "qualitative" benefits outweigh the objective cost difference.³⁶ As IEU-Ohio demonstrated in its brief, the Commission's reliance on qualitative benefits was unlawful and unreasonable.³⁷ In their briefs, the Commission and AEP-Ohio respond that the Commission may not only manipulate the quantitative test so as to bias it in favor of the ESP but may also assign some indeterminate, but apparently significant, value to increased reliability, energy-only auctions, and a "quicker" move

³⁵ In addition to the \$386 million the ESP failed the ESP versus MRO test identified by the Commission, the Commission should have included total costs of Turning Point estimated at \$357.2 million by OCC using AEP-Ohio data, OCC Ex. 114 at 17-18 (based on the supplemental testimony of AEP-Ohio witnesses Thomas, Nelson, and Roush) (Supp. at 504-05), and \$833 million for the Capacity Shopping Tax, ESP II Case (*see* Reply Brief of Industrial Energy Users-Ohio at 12-13 (July 9, 2012) (Supp. at 336-37)). The \$144 million may be included separately, but should partially offset the \$833 million associated with the Capacity Shopping Tax. An additional cost of the ESP is up to \$410 million for the PTR, although the Commission found that testimony supporting this amount was not credible. FES Ex. 104 at 31 (Supp. at 423). The Commission does not explain why it found the testimony not credible. ESP II Case, Entry on Rehearing at 9 (Jan. 30, 2013) (Appx. at 115). The \$1 billion estimate does not include the effect of properly stating the term and capacity price of the MRO.

³⁶ ESP II Order at 76 (Appx. at 99).

³⁷ IEU-Ohio Brief at 13-17.

to “full competition” through an auction-based standard service offer (“SSO”).³⁸ The Commission also argues that price stability and a 12% cap on increases caused by the ESP are benefits.³⁹ Ohio law and the record in this case, however, require the Court to reverse the Commission’s determination that qualitative benefits “outweigh” an objective estimate that the ESP is at least \$386 million less favorable than an MRO.

a. The Commission’s reliance upon “qualitative” benefits unlawfully frustrates the stated policy of Ohio law by denying the benefits of choice to customers of AEP-Ohio and violates the requirements of R.C. 4903.09

As IEU-Ohio showed in its Brief, it is clear that the “qualitative” benefits on which the Commission relies to justify its findings rest on a fundamental misinterpretation of the statutory outcomes required by Chapter 4928.⁴⁰ The General Assembly has declared retail generation service to be a competitive service. Ohio law requires the Commission to ensure that individual customers have access to the benefits of competition and that the EDU does not deny these benefits to customers through its control of non-competitive delivery services.⁴¹ Ohio law also specifically limits the role of the EDU to that of a default supplier of competitive generation services and protects customer choice and the competition it is based on by subjecting the EDU to corporate separation requirements.⁴² Even the default service provided under an ESP must be

³⁸ See, e.g., Commission Brief at 3, citing *In re Columbus S. Power Co.*, 128 Ohio St.3d 402 (2011).

³⁹ *Id.* at 5.

⁴⁰ IEU-Ohio Brief at 13-17.

⁴¹ R.C. 4928.02(A) & (B).

⁴² R.C. 4928.17.

better in the aggregate than an MRO structured to include an auction-based price of generation service.⁴³

The ESP II Order, however, authorizes an ESP that enhances AEP-Ohio's revenue from competitive generation-related services through nonbypassable riders. Nonshopping customers lose because they pay substantially more for an ESP than what would be available under an MRO, and shopping does not provide any relief since the nonbypassable charges reduce or eliminate the benefits of shopping. Existing shopping customers similarly must pay the nonbypassable charges. Thus, the move to competitively based pricing (on which AEP-Ohio and the Commission rely) offers no benefit, qualitative or otherwise, to consumers that are served by a competitive supplier. Yet the Commission and AEP-Ohio's arguments are advanced as though competitive pricing of default generation supply is the core purpose of Chapter 4928 and that the law's customer-choice imperative must be subordinated to the Commission's and AEP-Ohio's demands to defer the benefits of customer choice to some future time so that AEP-Ohio's competitive generation business is protected from the very competition that the General Assembly enabled for the benefit of consumers. The result of this violation of state policy supporting customer choice is an ESP that fails the ESP versus MRO test by at least \$1 billion.

Further, the Commission contends that it may ignore the requirements of R.C. 4903.09 to reach this unlawful result. According to the Commission, "The Commission is not required to 'explain its math' regarding 'non-quantitative benefits' because, as the name suggests, these benefits cannot be quantified."⁴⁴ The problem with the Commission's decision making, however, is not only that it has not "explained its math"; it is that it has ignored the record and

⁴³ R.C. 4928.143(C)(1).

⁴⁴ Commission Brief at 17.

the law to prop up AEP-Ohio's generation-related earnings, thereby depriving consumers of the benefits to which they are entitled by Ohio law.

Ohio law requires the Commission to reject an ESP that in the aggregate is \$1 billion more costly than an MRO. The ESP versus MRO test requires the Commission to measure the objective costs and benefits of the ESP and approve the ESP only if the ESP is more favorable in the aggregate than an MRO. In support of its decision approving an ESP, the Commission must explain its reasoning based on the record.⁴⁵ The Commission, however, failed to apply the ESP versus MRO test objectively and symmetrically. Had it properly applied the ESP versus MRO test as defined by the General Assembly, the Commission should have found that the ESP was at least \$1 billion worse than an MRO and rejected the ESP as a matter of law.

b. AEP-Ohio has not committed to an auction based SSO and the energy-only auctions will increase the cost of the ESP

Beyond the unlawful introduction of subjective guesswork into the ESP versus MRO test, the findings of the ESP II Order regarding the alleged qualitative benefits are baseless. For example, the Commission and AEP-Ohio both argue it was lawful to approve an ESP that was \$386 million worse than an MRO because AEP-Ohio will move more quickly to competitively based pricing and an SSO with generation pricing established through an auction.⁴⁶ Contrary to the Commission's assumption, however, AEP-Ohio may reject an future ESP.⁴⁷ Further, AEP-Ohio has not made a commitment to a future ESP with SSO rates established through a competitive auction process after the term of the ESP.⁴⁸ As AEP-Ohio made clear in a post-ESP II Order pleading, "No firm presumptions or assumptions can be made about the next SSO rate

⁴⁵ R.C. 4903.09.

⁴⁶ Commission Brief at 6-9; AEP-Ohio Brief at 35-36.

⁴⁷ R.C. 4928.143(C)(2).

⁴⁸ IEU-Ohio Brief at 15.

plan, how the competitive bidding process will work post-June 2015, or the rates to be paid by any particular customer group.”⁴⁹ The alleged future benefit of a move to competitively-priced default generation supply is not a benefit of the ESP approved by the Commission.

Further, an energy-only auction-based SSO that was approved by the Commission works to increase the cost of the as-approved ESP.⁵⁰ The Commission attempts to dismiss IEU-Ohio’s demonstration of the likely results of the auctions as “conclusory,”⁵¹ but the demonstration was based on information provided by AEP-Ohio.⁵² Once again, the Commission has chosen to selectively ignore evidence for the purpose of tampering with the scale that the General Assembly requires the Commission to use to weigh the ESP against the MRO for the purposes of advancing the policy contained in R.C. 4928.02.

c. Customers realize no additional benefit from distribution charges

The Commission further argues that the authorization of distribution riders has a qualitative benefit that exceeds their cost to customers. According to the Commission, it “recognized the qualitative benefits of these distribution programs because these programs provide benefits that would not necessarily occur through a distribution rate case.”⁵³

The Commission’s claim is faulty in two respects. First, the Commission does not state what the additional benefits are. The Commission recognizes that customers will pay

⁴⁹ *In the Matter of the Commission’s Review of Customer Rate Impacts from Ohio Power Company’s Transition to Market Based Rates*, Case No. 13-1530-EL-UNC, AEP Ohio Comments at 2 (Aug. 12, 2013) (viewed at <http://dis.puc.state.oh.us/TiffToPDF/A1001001A13H12B65519C35144.pdf>).

⁵⁰ IEU-Ohio Ex. 125 at 57 (Supp. at 195).

⁵¹ Commission Brief at 9 n.7.

⁵² IEU-Ohio Ex. 125 at 72-74 (Supp. at 210-12) (relying on discovery responses provided by AEP-Ohio).

⁵³ Commission Brief at 11.

distribution-related riders,⁵⁴ but does not demonstrate how any presumed reliability benefits exceed the costs customers will pay.⁵⁵ Second, the Commission's claim that the distribution benefits would not necessarily occur in a distribution case stands in stark contrast to the position the Commission has taken before the Court in a pending appeal of an ESP order for the FirstEnergy ("FE") EDUs. In its brief in the FE case, the Commission argued that the alleged costs of a distribution rider in an ESP should be not recognized when evaluating an ESP because the same costs could be realized through a hypothetical distribution case under an MRO.⁵⁶ Thus, benefits of distribution riders approved as part of an ESP count while costs are ignored. The inconsistent treatment of costs and benefits is unreasonable, and the Court should reverse the unlawful finding that the distribution riders benefits customers.

d. The ESP does not provide price stability, and the 12% rate cap does not provide a qualitative benefit to customers

The Commission points to price certainty as a qualitative benefit of the ESP. As discussed throughout this brief and IEU-Ohio's initial brief, the ESP increases charges for all customers and has eight adjustable riders in addition to the GRR and PTR. The Commission's argument that the ESP provides price stability is completely divorced from what is actually happening in the electric bills received by consumers as a consequence of the Commission's ESP II Order.

⁵⁴ IEU-Ohio Brief at 14-15.

⁵⁵ ESP II Order at 76 (Appx. at 99).

⁵⁶ *In the Matter of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Authority to Provide for a Standard Service Offer Pursuant to Section 4928.143, Revised Code, in the Form of an Electric Security Plan*, Sup. Ct. Case No. 2013-513, Merit Brief Submitted on Behalf of Appellee, the Public Utilities Commission of Ohio at 17-18 (Aug. 19, 2013).

Additionally, the Commission argues that the ESP provides a qualitative benefit (not identified in the ESP II Order as such a benefit) because it reduces the impacts of potential rate increases by establishing a 12% cap.⁵⁷ The practical implications of this provision of the ESP II Order, however, do not support the Commission's claim that the 12% cap provides a benefit to customers : (1) rate increases are delayed, not reduced; (2) the "items" that are covered by this provision are narrowly defined and the cap does not apply to many of the moving parts of the customer bill that can increase;⁵⁸ and (3) the Commission must also authorize a carrying charge, *i.e.*, interest, on the amounts deferred as required by R.C. 4928.144. Because the Commission must consider the effects of deferrals in the ESP versus MRO test, a delayed increase with interest cannot reduce the weight of the \$1 billion by which ESP is heavier than an MRO.

Even if the Commission was authorized to weigh "qualitative" benefits against the objective quantifiable costs in applying the ESP versus MRO test, the Commission is required to provide a record-based and reasoned explanation as to how those qualitative benefits "outweigh at least \$386 million."⁵⁹ Contrary to the Commission's position in its brief, it is required to explain its math. As demonstrated above, however, the Commission has failed to do so. Accordingly, the Commission's conclusion that the ESP is more favorable in the aggregate than an MRO is neither lawful nor reasonable and should be reversed.

B. Proposition of Law No. II: The ESP II Order is unlawful and unreasonable because the nonbypassable RSR, Capacity Shopping Tax, and PTR cannot be included in an ESP as a matter of law

⁵⁷ Commission Brief at 5.

⁵⁸ ESP II Case, Entry on Rehearing at 40 (Appx. at 146).

⁵⁹ R.C. 4903.09; *Remand Decision*, 128 Ohio St.3d at 519.

In its second Proposition of Law, IEU-Ohio showed that the Commission acted unlawfully when it authorized the RSR, Capacity Shopping Tax, and PTR for several reasons.⁶⁰ First, the generation-related riders cannot be authorized on a nonbypassable basis because they do not meet the requirements of R.C. 4928.143(B)(2)(b) or (c). Second, the findings on which the Commission authorized the RSR and PTR under R.C. 4928.143(B)(2)(d) are legally insufficient. Third, R.C. 4928.144 does not provide the Commission authority to approve riders to amortize the Capacity Shopping Tax. Finally, the riders violate the prohibition on generation-related nonbypassable charges set out in R.C. 4928.02(H) and 4928.17.

1. The ESP II Order is unlawful and unreasonable because it authorizes nonbypassable generation-related riders which are not included in the list of permissive provisions contained in R.C. 4928.143(B)(2)

As the Court has already held, the Commission has no authority to expand the list of provisions under R.C. 4928.143(B)(2) that may be included in an ESP.⁶¹ An ESP may include a nonbypassable generation-related rider under R.C. 4928.143(B)(2)(b) to recover costs associated with construction work in progress that occurs on or after January 1, 2009 or under R.C. 4928.143(B)(2)(c) to recover the costs associated with an electric generating facility that is newly used and useful on or after January 1, 2009.⁶² Because the General Assembly clearly and unambiguously provided that the Commission has authority to approve a nonbypassable generation-related rider in only two instances, the specific mention of those instances implies the exclusion of any others.⁶³ The RSR, the PTR, and a mechanism to recover the portion of the

⁶⁰ IEU-Ohio Brief at 23-33.

⁶¹ *Remand Decision*, 128 Ohio St.3d at 519-20.

⁶² R.C. 4928.143(B)(2)(b) & (c). The EDU must demonstrate that other detailed requirements also are satisfied.

⁶³ *Montgomery County Bd. Of Comm'rs v. Pub. Util. Comm'n of Ohio*, 28 Ohio St.3d 171, 175 (1986).

Capacity Shopping Tax not collected during the ESP were not and cannot be approved under R.C. 4928.143(B)(2)(b) or (c) since they do not recover costs of construction work in progress incurred on or after January 1, 2009 or costs of an electric generating facility newly used and useful on or after January 1, 2009. Thus, the Commission's authorization of these nonbypassable riders was not lawful, as IEU-Ohio demonstrated in its brief.⁶⁴

In response, the Commission and AEP-Ohio (in this instance because it suits the outcome AEP-Ohio seeks⁶⁵) focus on the RSR and argue that the Commission can expand its authority to approve a nonbypassable rider under R.C. 4928.143(B)(2)(d). In its brief, the Commission asserts that nothing in Chapter 4928 prohibits the Commission from approving the RSR on a nonbypassable basis and argues that the Court should defer to the Commission's statutory interpretation.⁶⁶ Similarly, AEP-Ohio argues that "[t]he fact that the statute *requires* charges approved under (B)(2)(b) and (c) to be nonbypassable provides no basis for concluding that the Commission lacks authority to approve a nonbypassable charge under (B)(2)(d)."⁶⁷ AEP-Ohio also claims that the Commission can authorize the RSR because the Commission has authorized nonbypassable generation-related charges in a case pending before the Commission and in a settlement for another EDU.⁶⁸

Initially, there is no reason to "interpret" R.C. 4928.143(B)(2)(d) so as to expand the Commission's authority to approve generation-related nonbypassable riders. "If the meaning of

⁶⁴ IEU-Ohio Brief at 24-25.

⁶⁵ Later in its brief, AEP-Ohio argues that the Commission must strictly abide by the requirements of R.C. 4928.143(F) regarding the application of the Significantly Excessive Earnings Test. AEP-Ohio Brief at 42-44.

⁶⁶ Commission Brief at 25-26.

⁶⁷ AEP-Ohio Brief at 12 (emphasis in original).

⁶⁸ *Id.*

a statute is unambiguous and definite, then it must be applied as written and no further interpretation is appropriate.”⁶⁹ R.C. 4928.143(B)(2)(d), in sharp contrast to the authorization the General Assembly provided in R.C. 4928.143(B)(2)(b) and (c), does not provide for authorization of a nonbypassable rider. Because R.C. 4928.143(B)(2) is unambiguous and definite on the scope of the Commission’s authority to authorize nonbypassable riders, there is no basis or need to interpret R.C. 4928.143(B)(2)(d).

Further, the Court should reject the request that the Court defer to the Commission’s interpretation of its own authority. On matters of statutory interpretation, the Court’s review is *de novo*, and the Court defers to the Commission’s statutory interpretation only if there is disparate competence on issues that are highly specialized.⁷⁰ In this instance, the Commission simply ignored the statutory structure; it is providing no special competence to which deference is warranted.

If there were need to interpret R.C. 4928.143(B)(2)(d), the section must be interpreted in a manner consistent with the pro-competitive and customer choice mission set forth in R.C. 4928.02. Such an approach leads to the rejection of arguments advanced by the Appellees because nonbypassable generation related riders deprive consumers of the benefit that they can otherwise obtain by obtaining generation supply from a competitive supplier.

Likewise, the Court should reject AEP-Ohio’s reliance on the Commission’s decision regarding the ESP of DP&L (“Dayton ESP Case”) to support its claim that the Commission lawfully expanded its authority. At the time these briefs were filed, the Dayton ESP Case was the subject of applications for rehearing and likely appeal challenging the lawfulness of the

⁶⁹ *State, ex rel. Herman, v. Klopfleisch*, 72 Ohio St.3d 581, 584 (1995).

⁷⁰ *In re Application of Columbus S. Power Co.*, 134 Ohio St.3d 392, 400 (2012).

nonbypassable riders the Commission approved in that case.⁷¹ The fact that the Commission acted unlawfully in the Dayton ESP Case does not immunize the Commission's unlawful decision in this case.

AEP-Ohio's reliance on the settlement in an ESP case for Duke Energy Ohio, Inc. ("Duke ESP Case") to demonstrate consistent construction of R.C. 4928.143(B)(2)(d) also is unwarranted. The Commission may not exceed its statutory authority through reliance on a stipulation.⁷² Further, the Duke ESP Case settlement contains an explicit term stating that it may not be considered or used as precedent in other proceedings.⁷³ Thus, it is not indicative of Commission practice. Moreover, if the Court relies on a settlement to affirm the Commission's decision here, the Court's action will undermine the use of settlements in future proceedings. No party will agree to a settlement when it may be used in a way to preclude a party from advancing the unlawfulness of a claim in another proceeding.

2. The ESP II Order is unlawful and unreasonable because the record does not support the Commission's conclusion that the RSR has the effect of making retail electric service stable or certain

As IEU-Ohio's Brief demonstrated, the Commission did not make findings to support its authorization of the RSR under R.C. 4928.143(B)(2)(d) which requires a showing that the charge

⁷¹ *In the Matter of the Application of The Dayton Power and Light Company for Approval of its Market Rate Offer*, Case Nos. 12-426-EL-SSO, *et al.*, Application for Rehearing and Memorandum in Support of Industrial Energy Users-Ohio (Oct. 4, 2013) (available at <http://dis.puc.state.oh.us/TiffToPDF/A1001001A13J04B31645B67696.pdf>).

⁷² *Monongahela Power Co. v. Pub. Util. Comm'n of Ohio*, 104 Ohio St.3d 571, 577 (2004).

⁷³ *In the Matter of the Application of Duke Energy Ohio for Authority to Establish a Standard Service Offer Pursuant to Section 4928.143, Revised Code, in the Form of an Electric Security Plan, Accounting Modifications and Tariffs for Generation Service*, Case Nos. 11-3549-EL-SSO, *et al.*, Stipulation at 2 (Oct. 24, 2011) (available at <http://dis.puc.state.oh.us/TiffToPDF/A1001001A11J25A75953G79485.pdf>).

has the effect of stabilizing or providing certainty regarding retail electric service.⁷⁴ In its response, the Commission argues that the statutory requirement is satisfied because “[t]he RSR freezes any non-fuel generation rate increase that might not otherwise occur absent the RSR, allowing current customer rates to remain stable throughout the term of the modified ESP.”⁷⁵

Although the Court has already admonished the Commission for its failure to conform the provisions of an ESP to the requirements of R.C. 4928.143(B)(2),⁷⁶ the Commission again legislates rather than implements Ohio law by its reliance on claimed price stability to support its authorization of the RSR.⁷⁷ Ohio law, however, differentiates charges providing for *price stability* from those that have the effect of making retail electric service *stable and certain*. Under R.C. 4928.144, the Commission can authorize a phase-in of rates or prices to produce *price stability*. In contrast to the language used in R.C. 4928.144, R.C. 4928.143(B)(2)(d) requires that a charge approved under that provision have the effect of stabilizing or providing certainty regarding retail electric service. Retail electric service refers to the “supplying or arranging” of that service.⁷⁸ Thus, the section requires a showing that supplying or arranging of retail electric service is made stable or certain. When the Commission ignored the terms of R.C. 4928.143(B)(2)(d) and chose instead to graft “price stability” to the provision to justify its authorization, the Commission acted unlawfully.

Even if a finding that the RSR provides price stability could satisfy the statutory requirement, the ESP II Order does not stabilize prices: though one part of the SSO customers’

⁷⁴ IEU-Ohio Brief at 25-30.

⁷⁵ Commission Brief at 20.

⁷⁶ *Remand Decision*, 128 Ohio St.3d at 519-20.

⁷⁷ Commission Brief at 20-21; AEP-Ohio Brief at 9.

⁷⁸ R.C. 4928.01(A)(27).

rates is “frozen,” their rates in total increase and the various reconcilable riders will change periodically. Shopping customers are not “benefiting” from alleged price stability because they will pay higher prices through the imposition of the nonbypassable charges. Thus, all customers will suffer because of the authorization of above-market generation-related nonbypassable charges explicitly designed to stabilize AEP-Ohio’s total revenue.

The Commission’s reliance on the fact that non-fuel generation rate is frozen also ignores additional increases the Commission authorized that were not reflected as a cost of the ESP in the ESP II Order. For example, the Commission authorized AEP-Ohio to raise electric bills further for the expansion of gridSMART.⁷⁹ In a recent application, AEP-Ohio has requested a gridSMART expansion with 15-year costs estimated at \$465 million.⁸⁰

More generally, the Commission was so concerned about the resulting price increases authorized by the ESP II Order that it capped individual customer bill increases *caused by the provisions authorized in this ESP* to 12%, but allowed AEP-Ohio to defer and request collection of any deferred collections with interest.⁸¹ The authorization of a price cap is another indication of the lack of price stability caused by the ESP II Order.

The Commission and AEP-Ohio further argue that the RSR satisfies the requirements of R.C. 4298.143(B)(2)(d) and can be authorized as a nonbypassable rider because the rider supports the Commission’s decision to authorize AEP-Ohio to “discount” Capacity Service to CRES providers, allows a quicker transition to an auction based SSO, and provides a stable rate

⁷⁹ ESP II Order at 62 (Appx. at 85).

⁸⁰ *In the Matter of the Application of Ohio Power Company to Initiate Phase 2 of its gridSMART Project and to Establish the gridSMART Phase 2 Rider*, Case No. 13-1939-EL-RDR, Application, Attachment A at 10 (Sept. 13, 2013) (viewed at <http://dis.puc.state.oh.us/TiffToPDF/A1001001A13I13B70029D86441.pdf>).

⁸¹ ESP II Order at 37 (Appx. at 60).

for customers who return to the SSO.⁸² The argument that the RSR advances certain policies ignores that the Commission cannot expand its statutory authority based on its policy choices.⁸³

Moreover, the policy claims the Commission makes are themselves based on mistakes of law and fact. The first claim, that RSR supports the Commission's decision to set a price for Capacity Service, assumes that the Commission's decision to invent and apply a cost-based ratemaking methodology to increase AEP-Ohio's compensation for Capacity Service was lawful.⁸⁴ It was not.⁸⁵ The claim that the RSR will lead to a faster transition to an auction-based SSO is contradicted by the fact that the Commission has not ordered and AEP-Ohio has not committed to an auction-based SSO after the ESP term ends. Finally, the claim that the RSR provides stable and certain prices for customers returning to the SSO is contradicted by the ESP II Order itself; there is nothing stable in the ESP rates and the only certainty is that rates for all customers will increase because the ESP II Order requires customers to subsidize AEP-Ohio's revenue through unlawful nonbypassable charges. Finally, none of these arguments demonstrates that the Commission can lawfully authorize a nonbypassable charge under R.C. 4928.143(B)(2)(d). As discussed above, it cannot.

⁸² Commission Brief at 20 & 24; AEP-Ohio Brief at 9-10.

⁸³ *Industrial Energy Users-Ohio v. Pub. Util. Comm'n of Ohio*, 117 Ohio St.3d 486, ¶ 23 (2008) (“[A] concern for the future of the competitive market does not empower the commission to create remedies beyond the parameters of the law.”).

⁸⁴ The Commission's jurisdiction regarding both competitive and noncompetitive electric service is limited to retail services. See, R.C. 4905.03 (definition of electric light company is limited to a company supplying electricity for “consumers”) and R.C. 4928.01(A)(27) (“retail electric service” limited to the supplying or arranging for the supply of electricity to ultimate consumers).

⁸⁵ IEU-Ohio Brief at 38-42; *In the Matter of the Commission Review of the Capacity Charges of Ohio Power Company and Columbus Southern Power Company*, Sup. Ct. Case Nos. 2012-2098 & 2013-228, Merit Brief of Appellant/Cross-Appellee Industrial Energy Users-Ohio (July 15, 2013).

3. The ESP II Order is unlawful and unreasonable because the Commission's findings do not support the authorization of the PTR under R.C. 4928.143(B)(2)(d)

IEU-Ohio's Brief demonstrated that the Commission unlawfully authorized the PTR, a rider designed to replace lost wholesale revenue resulting from termination of the AEP Interconnection Agreement ("Pool Agreement").⁸⁶ The Commission indicates that it intended to respond to IEU-Ohio's argument, but its brief addresses only the Commission's authorization of the GRR to collect the costs of Turning Point.⁸⁷ In contrast to the Commission's lack of response, AEP-Ohio advances two arguments to support the authorization of the PTR. First, it states that a challenge to the rider is not ripe because the Commission did not authorize a charge. Second, it argues that the record supports authorization of the nonbypassable generation-related rider.⁸⁸ Neither argument is correct.

The lawfulness of the PTR is properly before the Court in this appeal. The PTR is designed to recover a decline in wholesale generation-related revenue that AEP-Ohio may experience because the Pool Agreement is being terminated.⁸⁹ The key triggering event, notice of termination of the Pool Agreement, has occurred.⁹⁰ Although the Commission set the initial rate at \$0, the Commission's authorization has placed customers at risk that they may be charged an additional \$410 million in PTR charges during the term of the ESP upon satisfaction of some additional conditions.⁹¹ As this Court has previously concluded, the Commission's retention of

⁸⁶ IEU-Ohio Brief at 29-30.

⁸⁷ The Commission's brief references IEU-Ohio Proposition of Law No. II (3), but does not address it. Commission Brief at 39-40.

⁸⁸ AEP-Ohio Brief at 30-32.

⁸⁹ ESP II Order at 47-49 (Appx. at 70-73).

⁹⁰ AEP-Ohio Ex. 104 at 21 (Second Supp. at 33).

⁹¹ IEU-Ohio Brief at 29; ESP II Order at 49 (Appx. at 72).

future review of the charges that AEP-Ohio may seek under the rider does not preclude the Court from reviewing the lawfulness of the rider.⁹²

Additionally, the findings on which AEP-Ohio relies to justify the PTR are not a lawful basis for approval of the charge under R.C. 4928.143(B)(2)(d). As AEP-Ohio concedes, the Commission found that the charge was lawful because termination of the Pool Agreement was a prerequisite for effective competition and that AEP-Ohio faced a potential decline in wholesale generation-related revenue.⁹³ Neither explanation demonstrates that the PTR will have the effect of making retail electric service stable or certain. Because the Commission approved the PTR without making the required finding of fact, the Court must reverse the Commission's authorization of the rider.

4. The ESP II Order is unlawful and unreasonable because it concludes that the Capacity Shopping Tax can be imposed and collected under R.C. 4928.144

As demonstrated in IEU-Ohio's Brief,⁹⁴ the Commission's order authorizing the recovery of the Capacity Shopping Tax violates the requirements of R.C. 4928.144. That section applies to only the "phase-in of any electric distribution utility rate or price *established under sections 4928.141 to 4928.143 of the Revised Code.*" (Emphasis added.) In the ESP II Order, the Commission phased in the above-market charge for Capacity Service, a wholesale service

⁹² *Elyria Foundry Co. v. Pub. Util. Comm'n of Ohio*, 114 Ohio St.3d 305, 316-17 (2007).

⁹³ AEP-Ohio Brief at 31. To the extent that the Commission is authorizing AEP-Ohio to increase its compensation for the provision of a wholesale generation-related service, the authorization of the PTR is also unlawful because the Commission's authorization increasing AEP-Ohio's compensation for wholesale capacity service is preempted. *PPL Energyplus, LLC v. Nazarian*, 2013 WL 5432346 (D. Md. Sept. 30, 2013) ("*PPL I*"); *PPL Energyplus, LLC v. Hanna*, 2013 WL 5603896 (D.N.J. Oct. 11, 2013) ("*PPL II*").

⁹⁴ IEU-Ohio Brief at 30-31.

provided to CRES providers, that was authorized in the Capacity Order.⁹⁵ In the Capacity Order, the Commission established the price for Capacity Service pursuant to authority it claimed existed under Chapter 4905 and 4909.⁹⁶ Further, the Commission approved accounting changes under R.C. 4905.13 that would permit AEP-Ohio to defer the difference, with carrying charges, between what it collected at the RPM-Based Price and \$188.88/MW-day (the “Capacity Shopping Tax”). Because the price for Capacity Service and the resulting Capacity Shopping Tax were not authorized pursuant to R.C. 4928.141 to 4928.143, the Commission was without authority to phase-in the recovery of the Capacity Shopping Tax under R.C. 4928.144.

In response, the Commission and AEP-Ohio argue that the Commission had authority to implement a charge to recover the deferred amounts under R.C. 4928.143(B)(2)(d). Both rely on the Commission’s finding that the RSR provides price stability to allow “CRES suppliers to purchase capacity at market prices while allowing AEP Ohio to continue to offer reasonably priced electric service to customers who choose not to shop.”⁹⁷

As discussed above, the RSR does not provide for stable prices, and the response of the Commission and AEP-Ohio does not address the limitation contained in R.C. 4928.144 that the Commission’s authority to phase-in a price applies to only an “electric distribution utility rate or charge established under sections 4928.141 to 4928.143 of the Revised Code.” The charge being phased in is not the RSR; AEP-Ohio is authorized to bill and collect \$508 million in revenue through the RSR over the term of the ESP; \$144 million of this RSR revenue will be applied towards the total amount payable (now and later) by consumers as a consequence of the Capacity

⁹⁵ ESP II Order at 51-52 (Appx. at 74-75).

⁹⁶ Capacity Order at 12 (Supp. at 245); Capacity Case, Entry on Rehearing at 9 (Oct. 17, 2012) (Supp. at 721).

⁹⁷ Commission Brief at 22; AEP-Ohio Brief at 16.

Shopping Tax.⁹⁸ This demonstrates it is the Capacity Shopping Tax that is being phased in, and the Commission authorized the wholesale price and the accounting treatment that resulted in the Capacity Shopping Tax under Chapter 4905 and 4909.⁹⁹ Thus, R.C. 4928.144 cannot serve as lawful authority for the Commission to authorize AEP-Ohio to collect the Capacity Shopping Tax.¹⁰⁰

In AEP-Ohio's attempt to justify recovery of the Capacity Shopping Tax revenue, it adds that costs approved by the Federal Energy Regulatory Commission ("FERC") have to be recovered in retail rates and continues with a digression on the requirements applicable to traditional retail ratemaking that prevent "trapping" FERC-approved wholesale costs incurred by a utility.¹⁰¹ There are two problems with this digression. First, the Capacity Shopping Tax was unlawfully authorized by the Commission, not FERC. Second, the Commission-approved Capacity Shopping Tax is an amount in excess of the RPM-Based Price collected through nonbypassable retail charges; the FERC-approved price for Capacity Service is set at the RPM-Based Price.¹⁰² Thus, AEP-Ohio's digression on the role of the Commission to authorize FERC-approved costs is irrelevant to a decision on the lawfulness of the phase-in of the Commission-approved Capacity Shopping Tax under R.C. 4928.144.

⁹⁸ ESP II Order at 36 & 75 n.19 (Appx. at 59 & 98).

⁹⁹ Capacity Order at 12-13 & 23-24 (Supp. at 245-46 & 256-57).

¹⁰⁰ The Commission and AEP-Ohio raise a related argument later in their briefs that again relies on R.C. 4928.144 to justify authorization of accounting changes associated with the Capacity Shopping Tax. The argument is again addressed below.

¹⁰¹ AEP-Ohio Brief at 16-17.

¹⁰² *PJM Interconnection, L.L.C., et al.*, FERC Docket No. ER13-1164-000, Order Accepting Appendix to Reliability Assurance Agreement Subject to a Compliance Filing at ¶23 (May 23, 2013) ("the wholesale rate shall be equal to the adjusted final zonal PJM RPM rate in effect for the rest of the RTO region for the current PJM delivery year, and with the rate changing annually on June 1, 2013, and June 1, 2014 to match the then current adjusted final zonal PJM RPM rate in the rest of the RTO region.") (Second Supp. at 8).

5. The ESP II Order is unlawful and unreasonable because the RSR, PTR, and Capacity Shopping Tax will result in the recovery of generation-related revenue through nonbypassable charges which violates the State Energy Policy under R.C. 4928.02 and the requirements for corporate separation under R.C. 4928.17

The RSR, PTR, and Capacity Shopping Tax also violate prohibitions in R.C. 4928.02 and 4928.17 of the recovery of generation-related revenue through nonbypassable charges. R.C. 4928.02(H) “prohibit[s] the recovery of any generation-related costs through distribution or transmission rates.” R.C. 4928.17 requires that the EDU operate under a corporate separation plan that is consistent with the state policies including the prohibition contained in R.C. 4928.02(H). Despite these prohibitions, the Commission unlawfully authorized AEP-Ohio and its generation affiliate to secure above-market generation-related revenue through nonbypassable charges.¹⁰³

The Commission focuses only on the lawfulness of the RSR and argues there is no violation of state policy because the ESP II Order’s approval of the RSR is authorized by R.C. 4928.02(B)(2)(d).¹⁰⁴ The Commission fails to address this Court’s prior decisions applying R.C. 4928.02(H)¹⁰⁵ and the Commission’s own orders¹⁰⁶ on the issue. Based on these prior holdings, it is clear the Commission cannot authorize a charge that is prohibited by R.C. 4928.02(H).

AEP-Ohio focuses on the RSR and the Capacity Shopping Tax and asserts that the ESP II Order does not violate R.C. 4928.02(H) by offering its own definition of what constitutes an

¹⁰³ IEU-Ohio Brief at 31-33.

¹⁰⁴ Commission Brief at 25 n.19. The citation is inaccurate. R.C. 4928.02(B)(2)(d) does not exist; the intended reference apparently was R.C. 4928.143(B)(2)(d).

¹⁰⁵ See, e.g., *Elyria Foundry Co.*, 114 Ohio St.3d at 315-17.

¹⁰⁶ *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 19 (Jan. 11, 2012) (viewed at: <http://dis.puc.state.oh.us/ViewImage.aspx?CMID=A1001001A12A11B35831F43601>).

illegal cross-subsidy.¹⁰⁷ AEP-Ohio's attempt to define an unlawful subsidy, however, ignores the express prohibition of the collection of generation-related revenue through distribution or transmission rates in R.C. 4928.02(H). Despite that prohibition, the ESP II Order authorizes riders that permit AEP-Ohio to bill and collect generation-related revenue through distribution (nonbypassable) riders.

AEP-Ohio's attempt to define an unlawful cross-subsidy also does not provide an excuse for the violation of R.C. 4928.17. That section requires the corporate separation plan of AEP-Ohio to comply with state policies set out in R.C. 4928.02, including the prohibition of the collection of generation-related revenue through distribution charges. Because the Commission has permitted the pass through of the RSR revenue to the unregulated competitive affiliate, the ESP II Order also authorizes a violation of R.C. 4928.17.

Repeating prior arguments, the Commission and AEP-Ohio also argue that the RSR is justified because the RSR promotes competitive markets that may permit customers to lower their electric bills by shopping.¹⁰⁸ Initially, it is clear that the RSR reduces or eliminates any benefit customers might obtain by shopping by assuring that AEP-Ohio's earnings do not suffer. Further, the Appellees' argument assumes that the Commission's policy justification (even if it were correct) trumps the statutory prohibition of the recovery of generation-related revenues through distribution or transmission rates. As noted previously, the Commission's policy objectives cannot serve as a basis for ignoring the statutory prohibition contained in R.C. 4928.02(H).¹⁰⁹

¹⁰⁷ AEP-Ohio Brief at 18 ("A cross-subsidy involves either paying for something without receiving anything in return, or receiving a payment without a corresponding cost.").

¹⁰⁸ See, e.g., Commission Brief at 26-27.

¹⁰⁹ *Industrial Energy Users-Ohio v. Pub. Util. Comm'n of Ohio*, 117 Ohio St.3d 486, ¶ 23 (2008).

AEP-Ohio further argues that it has a constitutional entitlement to the revenue that it is authorized to collect through the RSR,¹¹⁰ citing *Federal Power Commission v. Hope Natural Gas Co.*¹¹¹ and *Bluefield Water Works & Improvement Co. v. Public Service Commission of West Virginia.*¹¹² No regulated utility, however, has a constitutional claim to increased compensation to offset losses due to market forces: “The due process clause has been applied to prevent governmental destruction of existing economic values. It has not and cannot be applied to insure values or to restore values that have been lost by the operation of economic forces.”¹¹³ As is evident in this case, the RSR, PTR, and Capacity Shopping Tax are designed to offset the effects of customer shopping and low market-based Capacity Service prices on AEP-Ohio’s generation-related revenues.¹¹⁴ Because the record demonstrates that market forces, not Commission intervention, are driving AEP-Ohio’s alleged reduced revenue, AEP-Ohio has no valid constitutional claim for additional financial support.

Even if the *Hope* analysis applied to this case, AEP-Ohio has not presented a judicially recognized basis for finding that a taking would occur if the Court correctly finds that the RSR is unlawful. *Hope* holds that in reviewing a takings claim “[i]t is not theory but the impact of the rate order which counts” and “[i]f the total effect of the rate order cannot be said to be unjust and unreasonable, judicial inquiry under the Act is at an end.”¹¹⁵ AEP-Ohio’s claim that it will suffer a constitutional taking if it does not recover RSR revenue fails to address the total effect of the order and instead seeks to apply an issue specific review that does not meet the *Hope* standard.

¹¹⁰ AEP-Ohio Brief at 20.

¹¹¹ 320 U.S. 591 (1944).

¹¹² 262 U.S. 679 (1923).

¹¹³ *Market Street R. Co. v. Railroad Comm'n of Cal.*, 324 U.S. 548, 567 (1945).

¹¹⁴ ESP II Order at 37-38 (Appx. at 60-61).

¹¹⁵ *Federal Power Comm'n v. Hope Natural Gas Co.*, 320 U.S. at 602.

Finally, the Commission and AEP-Ohio do not address the lawfulness of the PTR under R.C. 4928.02 and 4928.17.¹¹⁶ The charge is designed to permit AEP-Ohio to recover lost generation-related wholesale revenue through a nonbypassable rider. As discussed above, the Commission lacks the legal authority to approve the recovery of wholesale generation-related charges through a rider that is paid by all customers (a nonbypassable charge). Accordingly, the Commission's authorization of the PTR violates R.C. 4928.02(H) and should be reversed.

C. Proposition of Law No. III: The ESP II Order is unlawful and unreasonable because it authorizes AEP-Ohio to increase SSO prices so as to collect above-market generation-related revenue through the nonbypassable RSR, the Capacity Shopping Tax, and the PTR, thereby providing AEP-Ohio with the ability to collect transition revenue or its equivalent at a time when Ohio law commands that AEP-Ohio's generation business be fully on its own in the competitive market

In Proposition of Law No. III, IEU-Ohio demonstrated that the ESP II Order is unlawful because the RSR, Capacity Shopping Tax, and PTR permit AEP-Ohio to recover transition revenue or its equivalent when the time for the recovery of such revenue is long over and such recovery is barred by AEP-Ohio's Electric Transition Plan settlement ("ETP Stipulation").¹¹⁷

In response, the Commission and AEP-Ohio argue that AEP-Ohio did not seek and the Commission did not authorize transition revenue when it approved the RSR.¹¹⁸ Asserting that the RSR recovers the cost of Capacity Service, AEP-Ohio further argues that the riders have nothing to do with "retail generation transition charges."¹¹⁹ The Commission also claims that

¹¹⁶ As noted above, the Commission does not address IEU-Ohio's propositions of law regarding the PTR, instead presenting a response concerning the GRR that IEU-Ohio did not challenge. AEP-Ohio argues that the Commission lawfully approved the PTR under R.C. 4928.143(B)(2)(d), but fails to address the limitation on the Commission authority contained in R.C. 4928.02(H). AEP-Ohio Brief at 31.

¹¹⁷ IEU-Ohio Brief at 33-38.

¹¹⁸ Commission Brief at 33; AEP-Ohio Brief at 26-27.

¹¹⁹ AEP-Ohio Brief at 26.

AEP-Ohio did not seek or receive transition revenue in its electric transition plan (“ETP”) and that AEP-Ohio did not claim that its receipt of transition revenue was insufficient.¹²⁰ (The Commission and AEP-Ohio do not address IEU-Ohio’s argument that the PTR also authorizes the billing and collection of transition revenue.)

1. The nonbypassable riders provide AEP-Ohio the authority to collect transition revenue or its equivalent

Contrary to the Appellees’ claim, the nonbypassable generation-related riders provide AEP-Ohio with transition revenue or its equivalent as defined by Ohio law. Under R.C. 4928.39(C) and 4928.40, the amount of transition revenue that an EDU could recover through transition charges was limited to those transition costs that were unrecoverable in the competitive market.¹²¹

The nonbypassable riders authorized in the ESP II Order collect revenue that is not recoverable in the competitive market. For example, the RSR is authorized to collect a revenue target above what AEP-Ohio collects through its “market-based” generation rates and to make up for the losses it claims it will incur as a result of increased customer switching. The Capacity Shopping Tax, recovered through the nonbypassable RSR and a post-ESP rider, is the difference between what AEP-Ohio collects at market-based prices for the provision of Capacity Service and the “cost-based” price the Commission authorized in the Capacity Case. The PTR charge is calculated based on the revenue that AEP-Ohio would lose if it sold wholesale generation services in the market rather than recover revenue from other members of the Pool Agreement

¹²⁰ Commission Brief at 33.

¹²¹ To secure authorization for transition revenue, the EDU also had to establish that the costs were prudently incurred, legitimate, net, verifiable, and directly assignable or allocable to retail electric generation service provided to electric consumers in this state, and that the EDU would otherwise be entitled an opportunity to recover the costs. A separately identifiable portion of transition costs were regulatory assets. R.C. 4928.39(A), (B), and (D).

under a cost-based formula. Particularly in regard to the RSR and the Capacity Shopping Tax, the Commission has authorized AEP-Ohio to secure the kinds of revenue AEP-Ohio agreed to forego as part of its ETP settlement.¹²² Thus, the Commission has authorized AEP-Ohio to recover transition revenue or its equivalent.

2. AEP-Ohio is barred from recovering transition revenue or its equivalent

As discussed in IEU-Ohio's brief,¹²³ the Commission has violated R.C. 4928.38 and the ETP Stipulation by authorizing AEP-Ohio to bill and collect additional transition revenue or its equivalent. The Commission, however, attempts to justify its authorization by arguing that AEP-Ohio did not ask for or receive transition revenue in its ETP case and that AEP-Ohio did not complain that it had not received sufficient transition revenue.¹²⁴ What the Commission did or did not authorize in the ETP Order or whether AEP-Ohio complained about not recovering sufficient revenue previously, however, provides no basis for a finding that the Commission can authorize a new charge that operates to permit AEP-Ohio to collect transition revenue or its equivalent after the time for the collection of such revenue has expired and in violation of the Commission-approved ETP Stipulation. Simply put, the Commission has no legal authority to permit AEP-Ohio to collect above-market generation-related transition revenue or its equivalent.¹²⁵

¹²² See IEU-Ohio Ex. 124 at 16-17 (addressing AEP-Ohio's capacity pricing proposal) & 23-24 (addressing AEP-Ohio's RSR proposal) (Supp. at 111-12 & 118-19).

¹²³ IEU-Ohio Brief at 33-38.

¹²⁴ Commission Brief at 33.

¹²⁵ R.C. 4928.38.

Moreover, both claims about the evidence are incorrect. The Commission's order in the ETP case¹²⁶ and record in this case¹²⁷ are clear that AEP-Ohio asked for both a generation transition charge and the recovery of regulatory assets in its ETP cases. Further, AEP-Ohio agreed to forgo the recovery of a generation transition charge, but secured agreement for a transition charge for regulatory assets.¹²⁸ Additionally, AEP-Ohio argued that the Commission should authorize the RSR because the Commission acted to prevent it from collecting higher market-based rates in prior proceedings.¹²⁹ Thus, the Commission's justifications for allowing the RSR are not only irrelevant, but also are manifestly against the weight of the evidence.

Advancing its own alternative to justify the recovery of the Capacity Shopping Tax, AEP-Ohio argues that the revenue collected through the various charges authorized by the Commission has nothing to do with a *retail* generation transition charge¹³⁰ and further states that "AEP Ohio is seeking actual costs of capacity, not legacy generation costs."¹³¹ This argument is both inaccurate and meritless.

Initially, the RSR is designed to supplement AEP-Ohio's revenue based on the alleged shortfall of both retail and wholesale revenue relative to a revenue target.¹³² Thus, AEP-Ohio's description that the RSR is tied to wholesale capacity costs is not accurate.

¹²⁶ *In the Matter of the Applications of Columbus Southern Power Company and Ohio Power Company for Approval of Their Electric Transition Plans and for Receipt of Transition Revenues*, Case Nos. 99-1729-EL-ETP, *et al.*, Opinion and Order at 11 (Sept 28, 2000) (viewed at <http://dis.puc.state.oh.us/TiffToPDF/A1001001A13113B70029D86441.pdf>) ("ETP Order").

¹²⁷ IEU-Ohio Ex. 124 at 10-16 and Attached Ex. JEH-1 (Supp. at 105-11).

¹²⁸ ETP Order at 11.

¹²⁹ AEP-Ohio Ex. 101 at 7-9 (Supp. at 525-27).

¹³⁰ AEP-Ohio Brief at 26.

¹³¹ *Id.* at 27.

¹³² ESP II Order at 35 (Appx. at 58).

Additionally, as noted above, AEP-Ohio's original ETP case addressed the same kind of transition revenue claim as that presented in the case below.¹³³ The distinction that AEP-Ohio is trying to draw between the recovery of wholesale above-market capacity prices and retail transition charges is meaningless.

Further, if AEP-Ohio is suggesting that the Commission may approve the nonbypassable charges because AEP-Ohio is recovering revenue not recoverable in the wholesale generation capacity market, then it rests its entire claim on the theory that the Commission has lawful authority to set a wholesale capacity or energy price. Because the Commission's jurisdiction over an EDU's services is limited to its retail services by state law,¹³⁴ AEP-Ohio's claim that the RSR permits it to recover its cost of a wholesale service once again demonstrates the unlawfulness of the Commission's order.

AEP-Ohio's statement that the nonbypassable charges are related to an increase in compensation for Capacity Service also demonstrates that the Commission's order is preempted by the Federal Power Act ("FPA").¹³⁵ In a recent case decided by the Federal District Court of Maryland, the court concluded that the Maryland commission was preempted from authorizing cost-based compensation for wholesale capacity and energy services for a new generator. According to the district court, "[U]nder field preemption principles, the [Maryland commission] is impotent to take regulatory action to establish the price for wholesale energy and capacity sales. The FERC has exclusive domain in that field and has fixed the price for wholesale energy

¹³³ IEU-Ohio Ex. 124 at 16-17 (addressing AEP-Ohio's capacity pricing proposal) & 23-24 (addressing AEP-Ohio's RSR proposal) (Supp. at 111-12 & 118-19).

¹³⁴ IEU-Ohio Brief at 38-42.

¹³⁵ *PPL I*, 2013 WL 5432346 at *42; *PPL II*, 2013 WL 5603896 at *34.

and capacity sales in the PJM Markets as the market-based rate produced by the auction processes approved by the FERC and utilized by PJM.”¹³⁶

Based on the well-understood principles of federal preemption, the Commission’s orders in this and Capacity Case increasing AEP-Ohio’s compensation for Capacity Service likewise are preempted. As noted above, FERC has approved the RPM-Based Price for Capacity Service provided by AEP-Ohio. The Capacity Shopping Tax is the portion of the “cost-based” price of Capacity Service the Commission authorized in the Capacity Case in excess of the RPM-Based Price.¹³⁷ Because the Commission is preempted from increasing the compensation of AEP-Ohio for Capacity Service above FERC-approved prices, the Commission cannot lawfully authorize AEP-Ohio to bill and collect the Capacity Shopping Tax through the RSR or a mechanism after the term of the ESP.

Finally, DP&L argues in its amicus brief the Commission could authorize the recovery of transition revenue because R.C. 4928.143(B)(2)(d) was enacted after and implicitly repealed R.C. 4928.38.¹³⁸ This argument is meritless.¹³⁹ R.C. 4928.141, enacted with R.C. 4928.143(B)(2)(d) in Amended Substitute Senate Bill 221 (“SB 221”), expressly provides that “[a] standard service offer under section 4928.142 or 4928.143 of the Revised Code shall exclude any previously authorized allowances for transition costs, with such exclusion being effective on and after the date that the allowance is scheduled to end under the utility’s rate plan.” By enacting this provision of R.C. 4928.141, and not repealing R.C. 4928.38, the General

¹³⁶ *PPL I*, 2013 WL 5432346 at *35.

¹³⁷ The Commission had previously approved the RPM-Based Price as the “state compensation mechanism.” Capacity Case, Entry (Dec. 8, 2010) (Supp. at 231).

¹³⁸ DP&L Brief at 11.

¹³⁹ AEP-Ohio has acknowledged that the period for securing transition revenue has ended. IEU-Ohio Ex. 124 at 14-15 (Supp. at 109-10).

Assembly expressed a clear intention to terminate transition revenue recovery. Accordingly, the Court must reject DP&L's argument that R.C. 4928.143(B)(2)(d) repealed the prohibition contained in R.C. 4928.38.

D. Proposition of Law No. IV: The ESP II Order is unlawful and unreasonable because it assumes that the Commission may invent and apply a cost-based ratemaking methodology for purposes of authorizing a significant increase in the price for Capacity Service. It is similarly unlawful and unreasonable because it authorizes AEP-Ohio to defer the uncollected portion of this significant increase in the price for Capacity Service and then, after the term of the ESP, collect such portion plus interest charges through nonbypassable charges applicable to shopping and nonshopping customers

In its fourth Proposition of Law, IEU-Ohio demonstrated that the ESP II Order unlawfully increased AEP-Ohio's total compensation based on the invention and application of a cost-based ratemaking methodology, permitted a deferral of the amount above the competitive market price for Capacity Service without statutory authority, and then authorized AEP-Ohio to collect the unlawfully deferred amount with interest through nonbypassable charges.¹⁴⁰

The Commission and AEP-Ohio respond that the Commission can lawfully phase-in charges for Capacity Service because the Commission has authority to authorize the above-market prices for a wholesale noncompetitive electric service and may authorize AEP-Ohio to recover a portion of those above-market wholesale prices through a retail "stability" charge under R.C. 4928.143(B)(2)(d).¹⁴¹ They also argue the Commission can authorize the deferral of revenue to shift recovery to a period outside the term of the ESP under R.C. 4928.144 even though the phased-in rate or price did not originate under a proceeding authorized by R.C. 4928.141 to 4928.143.¹⁴² AEP-Ohio adds that this Court has already approved the use of

¹⁴⁰ IEU-Ohio Brief at 38-42.

¹⁴¹ Commission Brief at 22; AEP-Ohio Brief at 14.

¹⁴² Commission Brief at 22-23; AEP-Ohio Brief at 12-18.

accounting deferrals for FERC-authorized charges, citing a 2006 Court decision (“*2006 Consumers’ Counsel Case*”).¹⁴³

The rationale offered by the Commission and AEP-Ohio in support of the Capacity Shopping Tax and its collection through nonbypassable riders fails because it is based on a faulty assumption that the Commission can invent and apply a cost-based ratemaking methodology to increase AEP-Ohio’s compensation for Capacity Service.¹⁴⁴ As demonstrated in IEU-Ohio’s briefs in this case and the appeal of the Capacity Case,¹⁴⁵ the Commission did not comply with the requirements of Chapter 4909 when it invented and applied a cost-based ratemaking methodology to increase AEP-Ohio’s compensation for Capacity Service. Even if it had followed the dictacts of Chapter 4909, the Commission would have exceeded its statutory authority because the Commission’s price setting authority under Chapter 4909 has no application to the regulation of retail electric services that have been declared competitive.¹⁴⁶ This is because R.C. 4928.05(A)(1) provides, in part, “On and after the starting date of competitive electric service, a competitive retail electric service supplied by an electric utility ... shall not be subject to supervision and regulation ... by the public utilities commission under Chapters 4901. to 4909., 4933., 4935., and 4963. of the Revised Code” Capacity Service, by definition a generation-related service, has been declared a competitive electric service.¹⁴⁷

¹⁴³ AEP-Ohio Brief at 14, citing *Ohio Consumers’ Counsel v. Pub. Util. Comm’n of Ohio*, 111 Ohio St.3d 384 (2006).

¹⁴⁴ Commission Brief at 22; AEP-Ohio Brief at 14 n.3.

¹⁴⁵ IEU-Ohio Brief at 38-41; *In the Matter of the Commission Review of the Capacity Charges of Ohio Power Company and Columbus Southern Power Company*, Sup. Ct. Case Nos. 2012-2098 & 2013-228, Merit Brief of Appellant/Cross-Appellee Industrial Energy Users-Ohio (July 15, 2013).

¹⁴⁶ R.C. 4928.05(A).

¹⁴⁷ R.C. 4928.03.

Because retail electric generation service has been declared competitive, the Commission has no authority to apply the traditional ratemaking provisions contained in Chapter 4909 to set the price of Capacity Service and certainly has no authority to invent and apply a cost-based ratemaking methodology to increase AEP-Ohio's compensation for Capacity Service, as it did in the Capacity Case.

Further, the Court should reject the Commission's claim that it may authorize the phase-in of the Capacity Shopping Tax under R.C. 4928.143(B)(2)(d) and R.C. 4928.144.¹⁴⁸ As discussed above, the Commission did not have authority to authorize a nonbypassable rider to bill and collect the Capacity Shopping Tax. Further, R.C. 4928.144 allows for the phase-in of a price approved under R.C. 4928.141 to R.C. 4928.143. Since the Commission states it authorized an above-market price for Capacity Service and the accounting changes authorizing the deferral of the Capacity Shopping Tax under provisions of Chapters 4905 and 4909,¹⁴⁹ the Commission had no authority to authorize phase-in the price or rate under R.C. 4928.144.

AEP-Ohio's argument that the Court's decision in *2006 Ohio Consumers' Counsel Case* supports authorization of an accounting deferral also is incorrect. That case addressed whether the Commission could modify an EDU's accounting practices to defer collection of FERC-approved transmission charges in a manner that could result in rate increases after the end of the Market Development Period. The Court rejected the Consumers' Counsel's challenge of the order, noting that the Commission was authorized to modify the amounts collected by an EDU

¹⁴⁸ *Id.* at 23; AEP-Ohio Brief at 13-14.

¹⁴⁹ Capacity Order at 12-13, 23 (Supp. at 245-46, 256). Further, the Commission specifically found that the provisions of R.C. Chapter 4928 did not apply to its determination of the appropriate capacity price. *Id.* at 13 (Supp. at 246).

under the rate caps established in an electric transition plan for charges “authorized by federal law.”¹⁵⁰

In contrast to the order permitting accounting modifications the Court affirmed in the *2006 Consumers’ Counsel Case*, the ESP II Order is not approving accounting modifications for FERC-approved rates. As the Commission makes clear, it claims it acted under state law in authorizing the price and the accounting changes that result in the Capacity Shopping Tax.¹⁵¹ To the extent that AEP-Ohio is looking to state law to authorize the deferral accounting, it is clear that state law does not authorize the Commission to order accounting deferrals for an electric service that has been declared competitive unless it is approved as part of a lawful phase-in under R.C. 4928.144. As discussed above, the Commission does not have that authority.

- E. **Proposition of Law No. V: The ESP II Order is unlawful and unreasonable because it fails to recognize that the rates and charges applicable to non-shopping customers also are providing AEP-Ohio with compensation for Capacity Service, it ignores or disregards the fact that AEP-Ohio has maintained that non-shopping customers are, on average, paying nearly twice the \$188.88/MW-day price, and it fails to establish a mechanism to credit such excess compensation obtained from non-shopping customers against any deferred balance the ESP II Order in combination with the Capacity Order works to create**

The Commission has authorized AEP-Ohio to freeze its base generation rates that AEP-Ohio has stated implies a rate or price of \$355/MW-day even though the Commission determined that the price of Capacity Service is \$188.88/MW-day. In its fifth Proposition of Law, IEU-Ohio identified the unlawful subsidy embedded in base generation rates (the difference between the implied price of \$355/MW-day and \$188.88/MW-day) and recommended that the Court order the Commission to credit the excess compensation obtained from nonshopping customers against the deferred balance created by the Commission’s authorization

¹⁵⁰ *2006 Consumers’ Counsel Case*, 111 Ohio St.3d 384 at ¶ 38.

¹⁵¹ Capacity Order at 23 (Supp. at 256).

of above-market capacity charges.¹⁵² By authorizing a credit, the Court can craft a remedy to mitigate the substantial and unlawful deferred above-market charges the Commission has authorized in this case and the Capacity Case.

In its brief, the Commission seeks to justify the difference in pricing based on its claim that AEP-Ohio provides different services to CRES providers and SSO customers.¹⁵³ AEP-Ohio echoes this argument.¹⁵⁴ Despite the Commission's claim otherwise,¹⁵⁵ the Commission does not provide any citation to the record that demonstrates that what each customer receives is in fact different. Without some evidence to support that claim, those assertions are valueless.¹⁵⁶

Further, AEP-Ohio provided the testimony supporting the comparability of Capacity Service and non-fuel base generation service provided to SSO customers. That testimony established that AEP-Ohio's revenue from its entire connected load at base generation rates would be \$1.102 billion while its revenue at its alleged "cost of capacity" rate of \$355.72/MW-day would be \$1.101 billion.¹⁵⁷ The Commission, however, ultimately determined that the price of Capacity Service was \$188.88/MW-day based on its invented cost-based ratemaking methodology.¹⁵⁸ The Commission then ordered AEP-Ohio to adjust the auction-based portion of the SSO to \$188.88/MW-day as a direct replacement for the non-fuel base generation rate

¹⁵² IEU-Ohio Brief at 42-45.

¹⁵³ Commission Brief at 29; see ESP II Case, Entry on Rehearing at 33 (Appx. at 139).

¹⁵⁴ AEP-Ohio Brief at 24-25.

¹⁵⁵ Commission Brief at 26 (arguing that the "construct" of compensation prevents over-recovery).

¹⁵⁶ *Remand Decision*, 128 Ohio St.3d at 519.

¹⁵⁷ AEP-Ohio Ex. 116 at 9 (Supp. at 33).

¹⁵⁸ Capacity Order at 36 (Supp. at 269).

otherwise embedded in the SSO charges.¹⁵⁹ Thus, the record demonstrated that AEP-Ohio is recovering substantially more than its “cost” through its non-fuel base generation rates, a service that the Commission determined could be directly replaced by Capacity Service in setting SSO prices. Although the record demonstrated the services were comparable, the Commission refused to adjust the balance of non-fuel generation-related charges to produce a lawful result. Accordingly, the Court should direct the Commission to order AEP-Ohio to credit the excess collection against the Capacity Shopping Tax to mitigate its effect on customers.

- F. **Proposition of Law No. VI: The ESP II Order is unlawful and unreasonable because, without authority to do so under R.C. 4928.143, the ESP II Order conditionally approves a transfer of generating assets without making the findings required by R.C. 4928.17 and Rule 4901:1-37-09, OAC, and without netting the above-book market value of AEP-Ohio’s generating assets against the transition revenue which the ESP II Order authorizes AEP-Ohio to collect on a nonbypassable basis during and after the term of the ESP**

In its Proposition of Law VI, IEU-Ohio showed that the Commission unlawfully approved AEP-Ohio’s transfer of generation assets to an unregulated competitive affiliate and the pass through of unlawful and inflated customer-funded subsidies to the affiliate.¹⁶⁰ The Commission responds that it had jurisdiction to authorize the transfer of generation assets in the ESP II Case and that customers have no legal basis to complain about the Commission’s unlawful actions that subsidize the unregulated competitive affiliate.¹⁶¹ Additionally, the Commission argues that it did no damage to customers since it imposed conditions on the

¹⁵⁹ ESP II Case, Entry on Rehearing at 37 (Appx. at 143).

¹⁶⁰ IEU-Ohio Brief at 45-49.

¹⁶¹ Commission Brief at 45-46.

transfer.¹⁶² AEP-Ohio argues that the issues raised by IEU-Ohio should be addressed in the appeal of the Corporate Separation Case and that the pass through is lawful.¹⁶³

As a matter of law, the Commission did not have authority to approve the transfer of generation assets in the case below for two reasons. First, AEP-Ohio's ESP application is governed by R.C. 4928.143 that provides the Commission with authority to approve an ESP; that section does not provide authority to address the transfer of generation assets. Thus, the Commission cannot rely on its authority under R.C. 4928.143 to authorize the transfer, conditionally or otherwise.

Second, AEP-Ohio's election to address the transfer of generation assets and corporate separation plan in the Corporate Separation Case defined the issues that were properly before the Commission in the ESP II Case, and the Commission may not extend its inquiry to matters not put in issue by the applicant and unrelated to the rates that are subject to the application.¹⁶⁴ As the Commission noted in the ESP II Order, AEP-Ohio filed a separate application seeking approval of the transfer of the generation assets and did not move to consolidate that application with its ESP application.¹⁶⁵ Based on AEP-Ohio's reservation, the Commission concluded that approval of the transfer was not before it in the ESP II Case.¹⁶⁶ Yet, the Commission later stated in the Corporate Separation Case that the Commission had already approved divestiture in the

¹⁶² *Id.* at 46-47.

¹⁶³ AEP-Ohio Brief at 28-32.

¹⁶⁴ *Cleveland Elec. Illum. Co. v. Pub. Util. Comm'n of Ohio*, 42 Ohio St.2d 402, 420 (1975).

¹⁶⁵ ESP II Order at 58-59 (Appx. at 81-82); ESP II Case, Ohio Power Company's Modified Electric Security Plan at 3 (Mar. 30, 2012) (Supp. at 3).

¹⁶⁶ ESP II Order at 59 (Appx. at 82).

ESP II Order.¹⁶⁷ Because the Commission approved the transfer of assets in the ESP II Order, it extended the scope of the issues unlawfully.

In addition to stating that it had jurisdiction to approve the transfer, the Commission also attempts to support its decision by arguing that the transfer promotes the public interest.¹⁶⁸ Once again, the Commission has resorted to a policy argument in an attempt to have the Court excuse the Commission's failure to comply with R.C. 4928.143. Policy goals, however, are not a substitute for statutory authority to act.¹⁶⁹

The Court should also reject the Commission's reliance on the Corporate Separation Case to justify its actions in the ESP II Order. For example, the Commission argues that it was not required to compel AEP-Ohio to provide the market and net book-value of the assets in the ESP II case because it properly waived its rule requiring AEP-Ohio to provide that information in the Corporate Separation Case.¹⁷⁰

The Commission's reliance on the Corporate Separation Case is a continuation of the illegal shell game the Commission has used to prevent parties from testing the lawfulness of the terms of the transfer.¹⁷¹ When IEU-Ohio challenged the Commission's terms and conditions of the transfer in this case, the Commission argues that these issues were dealt with in the Corporate Separation Case. When IEU-Ohio sought to pursue issues in the Corporate Separation Case, the Commission waived its hearing requirements, pointing to the record in the ESP II Case.¹⁷² The

¹⁶⁷ Corporate Separation Case, Finding and Order at 11 (Oct. 17, 2012) (Supp. at 697).

¹⁶⁸ Commission Brief at 45.

¹⁶⁹ *Industrial Energy Users-Ohio v. Pub. Util. Comm'n of Ohio*, 117 Ohio St.3d 486, ¶23 (2008).

¹⁷⁰ Commission Brief at 45-46.

¹⁷¹ IEU-Ohio Brief at 46-47.

¹⁷² Corporate Separation Case, Finding and Order at 11-12 (Oct. 17, 2012) (Supp. at 697-98).

Commission's actions were patently unreasonable and illegal because they denied IEU-Ohio due process.¹⁷³

Further, customers are adversely affected by the Commission's shell game because the Commission refuses to address the consequences of the transfer of assets that have a market value exceeding book value.¹⁷⁴ While the Commission argues that customers have no reason to complain because they have no ownership interest in the assets to be transferred,¹⁷⁵ AEP-Ohio customers are paying nonbypassable transition charges that will pass through to the unregulated competitive affiliate, while AEP-Ohio's affiliate also benefits from the above-book market value of the transferred assets. During the Market Development Period, this result would have been unlawful. Under law applicable to establish a proper claim for transition revenue, the Commission would have been required to determine the net transition costs.¹⁷⁶ Although the Commission is authorizing transition revenue or its equivalent, the Commission failed to net the above-book value of the generation assets against the transition revenue. If the Commission is authorized to approve transition revenue (and it is not), it at least should apply the netting principles recognized in Ohio law for transition revenue claims.

Finally, the Court should reject the Appellees' claim that the Commission can authorize the transfer of above-market revenue to the unregulated competitive affiliate. R.C. 4928.17(A)(2) and (3) require a corporate separation plan to contain provisions that prevent an EDU from extending any undue preference or advantage to any affiliate or its own business engaged in the

¹⁷³ *Tongren v. Pub. Util. Comm'n of Ohio*, 85 Ohio St.3d 87 (1998); *Allnet Communications v. Pub. Util. Comm'n of Ohio*, 32 Ohio St.3d 115 (1987).

¹⁷⁴ IEU-Ohio Ex. 121 (Confidential Supplement); Corporate Separation Case, Finding and Order at 11-12 (Oct. 17, 2012) (Supp. at 697-98).

¹⁷⁵ Commission Brief at 46-47.

¹⁷⁶ Transition costs were calculated on a "net" basis that recognized any above-book value. R.C. 4928.39(B).

business of supplying a competitive electric service.¹⁷⁷ Nonetheless, the Commission authorized a pass through that created an unlawful preference and competitive advantage in violation of R.C. 4928.17.

Even if the ESP II Order did not create an unlawful preference or advantage, the affiliate has no claim to transition revenue. As discussed above, AEP-Ohio has no lawful claim to above-market generation-related nonbypassable charges such as the RSR because the charges are prohibited under two provisions of Ohio law.¹⁷⁸ If the unregulated competitive affiliate steps into the shoes of AEP-Ohio as the Appellees argue, the unregulated competitive affiliate has no better claim than AEP-Ohio.

In summary, the Commission acted unlawfully when it conditionally approved the transfer of assets and authorized the pass through of above-market generation-related revenue to the unregulated competitive affiliate in the ESP II Order. Accordingly, the Commission's orders regarding the transfer of the generation assets were unlawful and unreasonable and must be reversed.

G. AEP-Ohio seeks to unlawfully extend its discriminatory and noncomparable pricing for generation-related services in violation of R.C. 4928.141

¹⁷⁷ Commission rules reflect a requirement that cost allocation not provide any subsidies between the affiliate and the EDU. Rule 4901:1-37-08(C), OAC. The subsidy to the affiliate produces a real injury. Although the Commission was aware that at least one CRES provider had offered to serve the SSO load at a lower price than the AEP-Ohio proposed,¹⁷⁷ it authorized the pass through of above-market charges to the affiliate (at the same time stating that it did not have jurisdiction over the underlying contract). ESP II Order at 60 (Appx. at 83). Thus, the preference the Commission approved increases the cost of electric service of customers.

¹⁷⁸ R.C. 4928.02(H) & 4928.38. See *Elyria Foundry Co.*, 114 Ohio St.3d at 316-17. In other proceedings arising out of the ESP II Order, AEP-Ohio has admitted that transfers of generation-related revenue between an affiliate and the EDU are unlawful. *In the Matter of the Application of Ohio Power Company to Establish a Competitive Bidding Process for Procurement of Energy to Support its Standard Service Offer*, Case No. 12-3254-EL-UNC, Ohio Power Company's Reply Brief at 9 (Aug. 30, 2013) (viewed at <http://dis.puc.state.oh.us/TiffToPDF/A1001001A13H30B51515G18787.pdf>).

R.C. 4928.141 requires an EDU to provide an SSO on a comparable and nondiscriminatory basis within its certified territory. In the ESP II Order¹⁷⁹ and Entry on Rehearing,¹⁸⁰ the Commission directed that the “state compensation mechanism” be applied to the SSO energy-only auctions and nonshopping customers beginning January 1, 2015. This order effectively reduced AEP-Ohio’s total compensation for capacity related services supplied for load served by the auction bidders from the implied price of \$355/MW-day that AEP-Ohio identified in its testimony to \$188.88/MW-day, the price for Capacity Service the Commission ordered in the Capacity Case. In AEP-Ohio’s Proposition of Law IV, it alleges that the Commission erred when it extended the “state compensation mechanism to SSO auctions and non-shopping customers.”¹⁸¹ In support of its assignment of error, AEP-Ohio argues that the Commission failed to explain the reduction in the non-fuel base generation charge, that it is constitutionally entitled to the higher compensation, and that the Commission’s order reducing its total compensation will “wreak havoc on the auctions.”¹⁸² AEP-Ohio’s Proposition of Law IV ignores the Commission’s findings and is without legal merit.

AEP-Ohio’s assertion that the Commission failed to explain its decision in the ESP II Order is not correct. The Commission stated that it lowered AEP-Ohio’s recovery to \$188.88/MW-day, in part, because AEP-Ohio offered to take less than the non-fuel base generation rate in its application and, in part, because the Commission found that \$188.88/MW-day “would allow AEP-Ohio to recover its embedded capacity costs without overcharging

¹⁷⁹ ESP II Order at 59 (Appx. at 82).

¹⁸⁰ ESP II Case, Entry on Rehearing at 37 (Appx. at 143).

¹⁸¹ AEP-Ohio Brief at 47.

¹⁸² *Id.* at 49.

customers.”¹⁸³ Thus, it is clear that the Commission explained why it ordered AEP-Ohio to charge the lower rate.

AEP-Ohio’s constitutional claim also is meritless. AEP-Ohio has no claim under the Takings Clause to any more than the market value for the use of its property.¹⁸⁴ The market value of Capacity Service is the RPM-Based Price, which is a fraction of the \$188.88/MW-day price the Commission authorized AEP-Ohio to charge for the load served by successful auction bidders. Thus, AEP-Ohio has no legitimate complaint when it is receiving more than the market value of Capacity Service.

Finally, AEP-Ohio has not demonstrated that it will be prejudiced by the Commission’s order to reduce its total compensation for SSO load served by successful auction bidders. As noted above, the Commission concluded that AEP-Ohio will recover its “cost.” Since it will be recovering its “cost,” AEP-Ohio has not demonstrated prejudice that warrants reversal.¹⁸⁵

H. The Court does not have jurisdiction to address AEP-Ohio’s Proposition of Law No. VII because the Commission’s reservation of issues concerning implementation of the energy-only auctions was not unlawful and was “invited” by AEP-Ohio¹⁸⁶

¹⁸³ ESP II Case, Entry on Rehearing at 37 (Appx. at 143). As discussed above, the Commission’s order further demonstrates that the Court should reverse and remand the Commission’s order refusing to credit amounts above \$188.88/MW-day against the Capacity Shopping Tax. As the Commission indicated, \$188.88/MW-day is sufficient compensation for AEP-Ohio for the provision of non-fuel base generation-related services that are currently effectively priced at \$355/MW-day because of the ESP II Order.

¹⁸⁴ *Market Street R. Co.*, 324 U.S. at 567.

¹⁸⁵ *In re Application of Columbus S. Power Co.*, 134 Ohio St.3d at 400.

¹⁸⁶ The Court may also reject the assignment of error because it was not presented with specificity to the Commission in AEP-Ohio’s Application for Rehearing. *In re Complaint of Cameron Creek Apts. v. Columbia Gas of Ohio, Inc.*, 136 Ohio St.3d 333, 337 (2013). See ESP II Case, Application for Rehearing of Ohio Power Company at 1-2 (Sept. 7, 2012) (AEP-Ohio Appx. at 7-8).

In its Proposition of Law No. VII, AEP-Ohio complains that its right to withdraw from the ESP is impaired because the Commission unlawfully reserved resolution of the design of the energy-only auctions to a separate proceeding. AEP-Ohio's complaint is without merit because the actions of the Commission did not impair AEP-Ohio's unilateral right to withdraw from the ESP. Additionally, the Court should reject the Proposition of Law because AEP-Ohio invited the Commission to make the alleged error.

Initially, AEP-Ohio's Proposition of Law No. VII is without legal merit. Because the Commission's ESP II Order modifies AEP-Ohio's application, AEP-Ohio "may withdraw the application, thereby terminating it, and may file a new standard service offer under [R.C. 4928.143] or a standard service offer under [R.C. 4928.142]."¹⁸⁷ Nothing in the ESP II Order prevented AEP-Ohio from withdrawing its application for the ESP if it had chosen to do so in a timely manner.

Even if the Commission's reservation of issues was unlawful, AEP-Ohio waived the error when it asked the Commission to delay addressing the details of the auction process. In supporting testimony, AEP-Ohio proposed that the design of the auctions be addressed in a separate proceeding.¹⁸⁸ Because AEP-Ohio asked for exactly what it received, it cannot "be permitted to take advantage of an error which [it] invited or induced the [Commission] to make."¹⁸⁹

¹⁸⁷ R.C. 4928.143(C)(2)(a).

¹⁸⁸ AEP-Ohio Ex. 101 at 21(Supp. at 539).

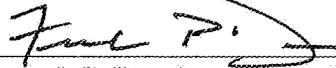
¹⁸⁹ *Lester v. Leuck*, 142 Ohio St. 91 (1943) (syllabus 1); *State v. Abercrombie*, 2002-Ohio-2414 ¶28 (12th Dist. Ct. App. 2002) ("appellant cannot now complain seeking to undo that error and any prejudice it may have caused [itself]").

Accordingly, AEP-Ohio's Proposition of Law No. VII is without legal merit. Its statutory right to withdraw its application is not impaired. Even if its legal right was impaired, it invited the error through its application.

III. CONCLUSION

Because the Commission refuses to bring the ESP II Order into compliance with Ohio law, IEU-Ohio must once again turn to this Court. For the reasons discussed above, the Court should reverse and remand the ESP II Order with the directions requested herein to bring the ESP II Order into compliance with Ohio law.

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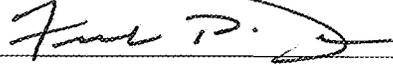
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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing *Third Merit Brief of Appellant Industrial Energy Users-Ohio* was served upon the parties of record this 10th day of December 2013 via electronic transmission, hand-delivery, or ordinary U.S. mail, postage prepaid.



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