IN THE SUPREME COURT OF OHIO

In the Matter of the Application of The Dayton Power and Light Company for Approval of Its Electric Security Plan.	: : :	Supreme Court Case No. 14-1505
In the Matter of the Application of The Dayton Power and Light Company for Approval of Revised Tariffs.	: : :	Appeal from the Public Utilities Commission of Ohio
In the Matter of the Application of The Dayton Power and Light Company for Approval of Certain Accounting Authority.	: : : :	Public Utilities Commission of Ohio Case Nos. 12-426-EL-SSO, 12-427-EL-ATA, 12-428-EL-AAM,
In the Matter of the Application of The Dayton Power and Light Company for Waiver of Certain Commission Rules.	: : :	12-429-EL-WVR, and 12-672-EL-RDR
In the Matter of the Application of The Dayton Power and Light Company to Establish Tariff Riders.	: : :	
Industrial Energy Users-Ohio, Appellant, v. Public Utilities Commission of Ohio, Appellee.	: : : : : : : : :	

FIRST MERIT BRIEF
OF APPELLANT
INDUSTRIAL ENERGY USERS-OHIO

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FIRST MERIT BRIEF OF APPELLANT

INDUSTRIAL ENERGY USERS-OHIO

In the case below, the Public Utilities Commission of Ohio ("Commission") authorized The Dayton Power and Light Company ("DP&L") to bill and collect an annual generation-related non-bypassable charge of $110 million. It further approved an electric security plan ("ESP") that is at least $250 million worse than the alternative market rate offer ("MRO"). In authorizing the electric security plan, including the non-bypassable generation-related Service Stability Rider, the Commission ignored the prohibition on the authorization of generation-related above-market revenue contained in R.C. 4928.38, authorized a term of an electric security plan that does not fit under the permissible categories under R.C. 4928.143(B)(2), and approved an electric security plan that is substantially worse than the market-based alternative in violation of R.C. 4928.143(C)(1). Additionally, the Commission violated the Supremacy Clause of the United Sates Constitution when it authorized DP&L to collect a revenue supplement in excess of the federally-authorized wholesale rates. Because the Commission's decisions on appeal[1] are unlawful and unreasonable, the Court should reverse and remand these decisions to the Commission and direct the Commission to reduce the non-bypassable Service Stability Rider rates to reverse the financial damage caused to customers by the unlawful and unreasonable decisions on appeal.

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[1] These decisions are the Commission's Opinion and Order issued September 4, 2013 ("Opinion and Order"), the Entry *Nunc Pro Tunc* issued September 6, 2013 ("Entry Nunc Pro Tunc"), the Entry on Rehearing issued October 23, 2013 ("Entry on Rehearing"), the Second Entry on Rehearing issued March 19, 2014 ("Second Entry on Rehearing"), the Fourth Entry on Rehearing issued June 4, 2014 ("Fourth Entry on Rehearing"), and the Fifth Entry on Rehearing issued July 23, 2014 ("Fifth Entry on Rehearing") and are collectively referred to herein as the "ESP Orders".

I. STATEMENT OF FACTS

Up until the turn of this century, retail electric generation, transmission, and distribution services were bundled together and were subject to cost-based regulation under the Commission's jurisdiction. However, in 1999, Ohio restructured, through Amended Substitute Senate Bill 3 ("SB 3"), the regulation of retail electric services to bring the dynamic forces of competition to retail electric service. SB 3 unbundled generation, transmission, and distribution services and declared the generation service component competitive. R.C. 4928.03 (Appx. at 152).

SB 3 also provided a brief transition period for electric utilities and customers to prepare for retail electric competition. R.C. 4928.40(A) (Appx. at 176). SB 3 established a market development period that could last up to five years, ending no later than December 31, 2005. *Id.* This transition period provided protections to both customers and the electric utilities. SB 3 protected customers by specifying the total price that each electric utility could charge non-shopping customers during the market development period. R.C. 4928.34(A)(6) (Appx. at 171-172). SB 3 protected the electric utilities during the transition period by providing the electric utilities a one-time opportunity to recover generation-related costs that were projected to be unrecoverable in a competitive market; these costs were known as transition costs or stranded costs.

If an electric utility believed it had generation-related costs that would be stranded due to competition, it was provided a one-time opportunity to request transition revenue as part of its electric transition plan. If such a request was made, the Commission was required to "determine the total allowable amount of the transition costs of the utility to be received as transition revenues." R.C. 4928.39 (Appx. at 175).[2] If the Commission determined that the electric utility had a legitimate claim to transition revenue, it could authorize the collection of transition revenue for a finite period. For certain transition revenue recovery, the period was defined by the market development period that could not extend beyond 2005. R.C. 4928.40 (Appx. at 176-177). For transition costs identified as regulatory assets, the collection period could not extend beyond 2010. *Id.* Following the one-time opportunity to collect transition revenue, an electric utility was "fully on its own in the competitive market." R.C. 4928.38 (Appx. at 174). Amended Substitute Senate Bill 221 ("SB 221"), enacted in 2008, reinforced the prohibition against authorizing additional transition revenue. R.C. 4928.141 (Appx. at 159).

DP&L's claim for transition revenue under its electric transition plan was resolved by way of a settlement approved by the Commission. *See* IEU-Ohio Ex. 14 at 30 (Supp. at 50); OCC Ex. 21 at 6-9 (Supp. at 62-65). Under the Commission-approved settlement, DP&L was authorized to collect approximately $441 million of transition revenue. *Id.*

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[2] Ohio law defined that total amount of transition revenue as:

> ... the just and reasonable transition costs of the utility, which costs the commission finds meet all of the following criteria:
>
> (A) The costs were prudently incurred.
>
> (B) The costs are legitimate, net, verifiable, and directly assignable or allocable to retail electric generation service provided to electric consumers in this state.
>
> (C) The costs are unrecoverable in a competitive market.
>
> (D) The utility would otherwise be entitled an opportunity to recover the costs.
>
> Transition costs under this section shall include the costs of employee assistance under the employee assistance plan included in the utility's approved transition plan under section 4928.33 of the Revised Code, which costs exceed those costs contemplated in labor contracts in effect on the effective date of this section.

R.C. 4928.39 (Appx. at 175).

To prevent an abuse of market power and unfair competitive advantage, SB 3 also prohibited the electric utilities from providing both non-competitive and competitive retail electric services. R.C. 4928.17 (Appx. at 168-169). To accomplish this, the electric utilities were required to separate their generation assets from their distribution and transmission assets. R.C. 4928.17 (Appx. at 168-169). This separation is known as corporate separation and can take two forms. Ohio law requires that each electric utility either transfers its generation assets or transfers its distribution and transmission assets to a separate company; this is known as structural or legal corporate separation. *Id.* For good cause shown, however, the Commission is authorized to permit an electric utility to operate under functional separation requirements "for an interim period" so long as the functional separation complies with "such functional separation requirements as the commission authorizes" and the functional separation "will provide for ongoing compliance with the policy specified in section 4928.02 of the Revised Code." R.C. 4928.17(D) (Appx. at 169). DP&L operates under functional separation requirements.[3]

In 2008, the General Assembly passed SB 221, which somewhat altered the structure put in place in SB 3. SB 221 provided that the standard service offer applicable to customers who had not elected to switch to a competitive supplier must be in one of two forms. R.C. 4928.14 (*repealed and replaced by* SB 221) (Appx. at 157); R.C. 4928.141 to R.C. 4928.144 (Appx. at 159-167); *see also In re Columbus S. Power Co.*, 128 Ohio St.3d 512, 2011-Ohio-1788, ¶ 2-5. Pursuant to SB 221, the standard service offer can either take the form of a market rate offer under R.C. 4928.142 or an electric security plan under R.C. 4928.143.

The market rate offer, as the name suggests, relies on a competitive auction process to establish prices that are blended with existing rates to produce the final market rate offer rate.

[3] In the case below, DP&L was directed to transfer all of its generating assets to achieve structural separation.

R.C. 4928.142 (Appx. at 160-162). If an electric distribution utility has a standard service offer approved that takes the form of a market rate offer, the electric distribution utility is precluded from pursuing an electric security plan for any future standard service offer. *Id.*

An electric security plan allows additional terms and conditions to be included as part of the standard service offer that cannot be included in a market rate offer, but these additional terms and conditions are limited. An electric security plan may only contain terms or conditions as provided under R.C. 4928.143(B)(2). *In re Columbus S. Power Co.*, 128 Ohio St.3d 512, 2011-Ohio-1788, ¶ 32. "[I]f a given provision does not fit within one of the categories listed 'following' (B)(2), it is not authorized by statute." *Id.* Additionally, the electric security plan "including its pricing and all other terms and conditions, including any deferrals and any future recovery of deferrals," must be "more favorable in the aggregate as compared to the expected results that would otherwise apply under section 4928.142 of the Revised Code," the market rate offer option. Thus, under SB 221, a standard service offer is either market-based, in the case of the market rate offer, or more favorable than the market-based option.

DP&L's first standard service offer under SB 221 took the form of an electric security plan and continued until December 31, 2013. In March 2012, DP&L initiated this case and filed an application to establish its second standard service offer under SB 221. DP&L's initial application in the case took the form of a market rate offer; however, DP&L withdrew its market rate offer application on September 7, 2012. On October 5, 2012, DP&L filed an application to establish a standard service offer in the form of an electric security plan. On December 12, 2012, DP&L further modified its application to establish an electric security plan.

The application that DP&L ultimately presented to the Commission in the case below proposed a five-year electric security plan and contained requests for two non-bypassable generation-related riders. The first of these non-bypassable generation-related riders, the Service Stability Rider, was proposed to increase DP&L's generation earnings. See Opinion and Order at 17 (Appx. at 25). Based upon its projections of its total company earnings, which includes its distribution, transmission, and both wholesale and retail generation businesses, DP&L argued that it needed additional revenue to produce what it argued was a reasonable return on its sole shareholder's investment. *See id.* at 17 (Appx. at 25). DP&L argued that a total company return on investment of 7.7 to 10.4 percent was reasonable. Opinion and Order at 22 (Appx. at 30) (*citing* DP&L Ex. 4 at 2); Opinion and Order at 25 (Appx. at 33) (*citing* DP&L Ex. 1A at 11-13). DP&L claimed that three factors were driving its reduced revenue which, in turn, impacted its lower-than-desired projected earnings: "increased switching, declining wholesale prices, and declining capacity prices." Opinion and Order at 17 (Appx. at 25) (*citing* DP&L Ex. 1A at 13, Tr. Vol. 1 at 135-136).[4] It is undisputed that these three factors are generation-related. To achieve a return of between 7.7 to 10.4 percent, DP&L requested authority to collect $687.5 million over five years ($137.5 million annually) through the proposed Service Stability Rider to make up for the generation-related shortfalls related to increased switching, declining wholesale prices, and declining capacity prices.

DP&L also requested that the Commission authorize another generation-related non-bypassable rider, the switching tracker. This rider would have provided DP&L additional revenue above the $687.5 million requested under its Service Stability Rider proposal in the event that customer switching increased in DP&L's service area. Opinion and Order at 28-29

[4] DP&L further admitted during the hearing that earnings of its distribution and transmission businesses were sufficient and would continue to be sufficient into the future. Tr. Vol. I at 117-118 (Supp. at 72-73); Tr. Vol. I at 150 (Supp. at 81). DP&L also acknowledged that if its distribution or transmission earnings were insufficient, there were other mechanisms available to address the earnings shortfall for its regulated lines of business. *Id.*

(Appx. at 36-37). The Commission found that DP&L's request for the switching tracker was being driven by the same three factors driving the request for the Service Stability Rider: increased switching, declining wholesale prices, and declining capacity prices. *Id.* DP&L's request for the switching tracker was also made under the same statutory provision as the Service Stability Rider, R.C. 4928.143(B)(2)(d). *Id.* at 29 (Appx. at 37).

After extensive hearings, the Commission modified and approved DP&L's proposed electric security plan. The Commission modified the term of the electric security plan, shortening the length from five to three years. Opinion and Order at 15 (Appx. at 23).

The Commission also modified and approved DP&L's request for the non-bypassable generation-related Service Stability Rider. The Commission accepted DP&L's total company earnings calculation and made an adjustment to account for certain projected operation and maintenance expense reductions. Opinion and Order at 25 (Appx. at 33). With its adjustment, the Commission concluded that DP&L needed an additional $110 million, annually, in order for DP&L to achieve a total company return on equity in the range of 7 to 11 percent. *Id.* The Commission then authorized DP&L to bill and collect $110 million, annually, through the Service Stability Rider for the period of January 1, 2014 through December 31, 2016. Opinion and Order at 25-26 (Appx. at 33-34) (approving the Service Stability Rider for two years at $110 million/year); Entry Nunc Pro Tunc at 2 (Appx. at 64) (modifying the term of the Service Stability Rider to three years at $110 million/year). The Commission also provided DP&L with the ability to seek a further subsidy through an additional non-bypassable rider, the Service Stability Rider-Extension, of up to $45.8 million over the period of January 2017 through May 2017 if DP&L meets certain conditions and demonstrates the need for a further subsidy. Opinion and Order at 26-28 (Appx. at 34-36); Entry Nunc Pro Tunc at 2 (Appx. at 64) (in the Entry Nunc

Pro Tunc, the Commission reduced the cap on the additional subsidy from $92 million to $45.8 million).

The Commission, however, rejected DP&L's request for a second non-bypassable generation-related rider, the switching tracker. Opinion and Order at 30 (Appx. at 38). The Commission found that the switching tracker "violates the policies of the state of Ohio, is anticompetitive, and would discourage further development of Ohio's retail electric services market." *Id.* The Commission also held that the switching tracker was not related to default service and therefore could not be authorized under R.C. 4928.143(B)(2)(d) because the switching tracker was related to customer switching. *See id.* The Commission continued:

> One of the principal aspects of a market is the opportunity for consumers to shop for a diversity of products offered by a multitude of suppliers. When a customer purchases a product from a new supplier, the previous supplier will necessarily lose that customer's representative market share. DP&L's proposed [switching tracker] would provide DP&L a stream of revenue to directly compensate it for market share lost when a customer switches to a competitive retail electric service provider. The Commission believes that this makes the proposed [switching tracker] anticompetitive because it may discourage customers from shopping for a retail electric supplier.

Id.

In approving an electric security plan that included the Service Stability Rider at a value of $330 million over the three-year term of the electric security plan, the Commission found in the Opinion and Order that the approved electric security plan was quantitatively $250 million worse than a market rate offer. Opinion and Order at 49-50 (Appx. at 57-58). The Commission's estimate, however, does not include the effects of the Commission's Entry Nunc Pro Tunc. In the Entry Nunc Pro Tunc, the Commission added $110 million to the Service Stability Rider and decreased the potential magnitude of the Service Stability Rider-Extension from $92 million to $45.8 million; a net increase of $64 million to the cost of the electric security plan. Entry Nunc Pro Tunc at 2 (Appx. at 64).[5]

Despite finding that the electric security plan was quantitatively worse than a market rate offer, the Commission found that the approved electric security plan satisfied the requirements of R.C. 4928.143(C)(1) because there were qualitative benefits of the electric security plan that rendered the electric security plan more favorable than a market rate offer. Opinion and Order at 50-52 (Appx. at 58-60). In its Opinion and Order, the Commission identified five qualitative benefits. *Id.* On rehearing, the Commission found that there were additional qualitative benefits that supported its conclusion that the electric security plan was more favorable than a market rate offer, but the Commission did not identify these additional qualitative benefits in any of its Entries on Rehearing. Second Entry on Rehearing 28-29 (Appx. at 99-100); Fourth Entry on Rehearing at 6-7 (Appx. at 111-112).

IEU-Ohio (and others) sought rehearing of the Commission's Opinion and Order on grounds that the approved electric security plan was unlawful and unreasonable due to the inclusion of the Service Stability Rider and because the approved electric security plan was not more favorable in the aggregate than a market rate offer. IEU-Ohio's First Application for Rehearing (Appx. at 180-261) (IEU-Ohio also sought rehearing on numerous other grounds, but the other grounds for rehearing are not part of IEU-Ohio's appeal). The Commission denied IEU-Ohio's first Application for Rehearing in the Second Entry on Rehearing. Second Entry on Rehearing (Appx. at 72-105). IEU-Ohio sought rehearing of the Commission's Second Entry on Rehearing, which was denied by the Commission in its Fourth Entry on Rehearing. IEU-Ohio's

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[5] The Commission does not provide any estimate of the effect of extending the auction-based standard service offer for an additional five months; thus, it is unclear what the net effect of the Commission's changes will be on the ESP v. MRO test other than to make the approved electric security plan less favorable.

Second Application for Rehearing (Appx. at 262-284); Fourth Entry on Rehearing (Appx at 106-117). IEU-Ohio timely filed its Notice of Appeal with the Court on August 29, 2014. (Appx. at 1-8).

II. STANDARD OF REVIEW

"R.C 4903.13 provides that a [Commission] order shall be reversed, vacated, or modified by this court … when, upon consideration of the record, the court finds the order to be unlawful or unreasonable." *Constellation NewEnergy, Inc. v. Pub. Util. Comm.*, 104 Ohio St.3d 530, 2004-Ohio-6767, ¶ 50. The Court "has 'complete and independent power of review as to all questions of law' in appeals from the commission." *Elyria Foundry Co. v. Pub. Util. Comm.*, 118 Ohio St.3d 269, 2008-Ohio-2230, ¶ 13 (*quoting Ohio Edison Co. v. Pub. Util. Comm.*, 78 Ohio St.3d 466, 469 (1997)). As to factual determinations, the Court will review the Commission action to determine if the Commission based its decision on the record: "[r]uling on an issue without record support is an abuse of discretion and reversible error." *In re Columbus S. Power Co.*, 128 Ohio St.3d 512, 2011-Ohio-1788, ¶ 29.

III. ARGUMENT

As the facts set forth above demonstrate, the Commission has authorized DP&L to collect generation-related revenue in violation of Ohio and federal law. Ohio law declares the entire generation service component competitive from the point of production to the point of delivery, and prohibits the Commission from providing an electric distribution utility, such as DP&L, with transition revenue or its equivalent. Ohio law also prohibits the Commission from providing an electric distribution utility an unfair competitive advantage or subsidy for its generation business. Ohio law also limits the Commission's price-setting authority over generation services to the standard service offer statutes (R.C. 4928.141 to 4928.144), and relevant here, the Service Stability Rider is not a term or condition that may be authorized as part of an electric security plan. Further, the inclusion of the Service Stability Rider in the electric security plan causes the electric security plan to be less favorable in the aggregate than a market rate offer. Finally, the Commission is preempted under federal law from authorizing the Service Stability Rider.

A. The ESP Orders are unlawful and unreasonable because they authorize the above-market, non-bypassable generation-related Service Stability Rider.

1. *The ESP Orders are unlawful and unreasonable because the Service Stability Rider cannot be approved under R.C. 4928.143(B)(2).*

a. The ESP Orders are unlawful because they authorize a non-bypassable generation-related rider, the Service Stability Rider, which is not included in the list of permissive electric security plan provisions under R.C. 4928.143(B)(2).

In the ESP Orders, the Commission held that it could authorize a non-bypassable generation-related rider, the Service Stability Rider, under R.C. 4928.143(B)(2)(d). Opinion and Order at 21 (Appx. at 29); Second Entry on Rehearing at 3, 7-8 (Appx. at 74, 78-79). Because that Section does not allow for the creation of a non-bypassable generation-related rider, the ESP Orders are unlawful and unreasonable.

Operating as a definitional section, R.C. 4928.143(B) limits the terms of an electric security plan to those specified in the Section. *In re Columbus S. Power Co.*, 128 Ohio St.3d 512, 2011-Ohio-1788, ¶ 32. R.C. 4928.143(B)(2) provides only two instances in which the Commission may authorize a non-bypassable generation-related rider, divisions (b) and (c). Under those two divisions, a non-bypassable charge is available to recover costs associated with generating facilities under construction or constructed after 2009 that meet additional statutory requirements. R.C. 4928.143(B)(2)(d) does not similarly provide that a rider approved under that division may be non-bypassable. (Appx. at 164).

By authorizing non-bypassable riders in only two instances, the General Assembly did not provide the Commission with authority to approve a non-bypassable rider under R.C. 4928.143(B)(2)(d). (Appx. at 164).

> As a general rule of statutory construction, the specific mention of one thing implies the exclusion of another. This principle is especially pertinent where, as in the cases *subjudice,* the statute involved is a definitional provision. Had the General Assembly intended to allow the utilities to recapture other types of expenses through this rate, it would have expanded the definitions. In addition, it is well-settled "that the General Assembly's own construction of its language, as provided by definitions, controls in the application of a statute."

Montgomery County Bd. of Comm'rs v. Pub. Util. Comm., 28 Ohio St.3d 171, 175 (1986) (citations omitted).

Despite the limitations on the Commission's authority to authorize non-bypassable riders, the Commission unlawfully authorized the Service Stability Rider as a non-bypassable rider.

b. The ESP Orders are unlawful and unreasonable because the Commission concluded that the Service Stability Rider can be authorized under R.C. 4928.143(B)(2)(d) even though the record demonstrated that the Service Stability Rider will not have the effect of stabilizing or providing certainty regarding retail electric service.

R.C. 4928.143(B)(2)(d) provides that an electric security plan may include "[t]erms, conditions, or charges relating to limitations on customer shopping for retail electric generation service, bypassability, ... [and] default service ... as would have the effect of stabilizing or providing certainty regarding retail electric service." (Appx. at 164). "Retail electric service" is defined to mean the "supplying or arranging for the supply of electricity to ultimate customers in this state, from the point of generation to the point of consumption." R.C. 4928.01(A)(27) (Appx. at 145). The Service Stability Rider cannot be authorized under R.C. 4928.143(B)(2)(d) because it will not have the effect of stabilizing or providing certainty regarding retail electric service, in either a physical or economic sense.

In the Opinion and Order, the Commission found "that the SSR meets the criteria of Section 4928.143(B)(2)(d), Revised Code, as it is a charge related to default service and bypassability that has the effect of stabilizing and providing certainty regarding retail electric service." Opinion and Order at 22 (Appx. at 30). The Commission agreed "with DP&L that if its financial integrity becomes further compromised, it may not be able to provide stable or certain retail electric service." *Id.* According to the Commission, because DP&L is functionally and not structurally separated, "the financial losses in the generation, transmission, or distribution business of DP&L are financial losses for the entire utility." *Id.* at 23 (Appx. at 31). "Therefore, if one of the businesses suffers financial losses, it may impact the entire utility, adversely affecting its ability to provide stable, reliable, or safe retail electric service." *Id.* The Commission then concluded that because "the SSR will provide stable revenue to DP&L for the purpose of maintaining its financial integrity" the rider satisfies the requirement in R.C. 4928.143(B)(2)(d) that it "have the effect of stabilizing or providing certainty regarding retail electric service." *Id.*; R.C. 4928.143(B)(2)(d) (Appx. at 164); *see also* Second Entry on Rehearing at 7-8 (Appx. at 78-79).

The Service Stability Rider has nothing to do with the physical supply of service; rather, its sole purpose is to provide DP&L additional (and above-market) revenue to help DP&L maintain higher earnings. Because the Service Stability Rider will not have the effect of stabilizing or providing certainty regarding retail electric service, the Commission unlawfully and unreasonably authorized the charge under R.C. 4928.143(B)(2)(d).

As DP&L admitted, the performance and ongoing operation of DP&L's generation business will have no effect on the physical stability and certainty of default service. Tr. Vol. I at 172 (Supp. at 84). DP&L's service reliability is within the control and supervision of PJM

Interconnection, L.L.C. ("PJM"). Because DP&L operates within the PJM system, the reliability of retail generation service is a function of PJM's management practices and reliability assurance responsibilities. *Id.* DP&L witness Jackson conceded that PJM would still dispatch resources under its control to satisfy the needs of DP&L's customers if DP&L did not have any generating facilities or if DP&L's generating facilities did not run. *Id.* Thus, the record confirms that the Service Stability Rider is not necessary and does not have the effect of producing stable or certain retail electric generation service.

The Service Stability Rider is, likewise, not necessary to ensure stable and certain transmission and distribution service. DP&L witness Jackson testified that he believed that DP&L's transmission and distribution businesses received adequate revenue. Tr. Vol. I at 242 (Supp. at 90).

The Service Stability Rider also fails to produce economic stability and certainty in the provision of retail electric service to customers. For customers there is nothing certain or stable, economically, regarding DP&L's electric security plan, and this conclusion holds regardless of whether or not the Service Stability Rider is authorized. The total price that customers are charged for retail electric service under DP&L's electric security plan will vary, unpredictably, throughout the term of the electric security plan. Competitive auctions will be held throughout the term of the electric security plan, and the unknown auction results will be blended with DP&L's existing electric security plan rates to produce one component of the total price charged to customers. *See* Opinion and Order at 15-16 (Appx. at 23-24). The remainder of the price charged to standard service offer customers under the electric security plan is a function of various riders that have been, and will continue to be, updated periodically over the term of the electric security plan. The riders authorized as part of the electric security plan include: the

Alternative Energy Rider, the Transmission Cost Recovery Rider–Bypassable; the Transmission Cost Recovery Rider Non-Bypassable; the Reconciliation Rider; the FUEL Rider; the Storm Damage Recovery Rider; the Competitive Bid True-up Rider; the Service Stability Rider, and the Service Stability Rider-Extended. Opinion and Order, *in passim* (Appx. at 9-62). The only fixed component of the electric security plan is the unlawful Service Stability Rider charge. Accordingly, from an economic standpoint, there is nothing stable or certain about DP&L's electric security plan and the Service Stability Rider does nothing to cure the instability and uncertainty regarding the total electric security plan rate charged to standard service offer customers. The Service Stability Rider only increases the total charge ultimately paid by customers.[6]

The record does not support the unreasonable conclusion that the Service Stability Rider has the effect of stabilizing or providing certainty regarding the provision of retail electric service, in either a physical or economic sense. Accordingly, the Service Stability Rider cannot be authorized under R.C. 4928.143(B)(2)(d).

2. The ESP Orders are unlawful and unreasonable because the Service Stability Rider provides DP&L transition revenue or its equivalent in violation of the prohibitions in R.C. 4928.38 and R.C. 4928.141.

R.C. 4928.38 and 4928.141 prohibit the Commission from authorizing transition revenue or its equivalent. In violation of the statutory prohibition, the Commission has provided DP&L

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[6] In the Opinion and Order, the Commission concluded that the financial losses in one of the lines of business (and generation was the only one DP&L states would be at risk) might adversely impact other lines of business and thereby affect DP&L's ability to provide stable, reliable, or safe retail electric service. Opinion and Order at 21-22 (Appx. at 29-30). Once DP&L divests the generation assets, however, DP&L will be only a distribution and transmission company; the generation assets that are alleged to be causing or will cause DP&L financial distress will be gone. The result will be a company with revenue from transmission and distribution that DP&L admits is adequate. Thus, even if there were some lawful basis for authorizing the Service Stability Rider while DP&L owned the generation assets, that rationale would no longer exist after the divestiture.

with a $330 million ($110 million annually for three years) above-market subsidy related to DP&L's generation-related costs that are unrecoverable in a competitive market.[7]

The Commission found that the $330 million subsidy was "the minimum amount necessary to ensure [DP&L's] financial integrity and provide [DP&L] with the opportunity to achieve a reasonable ROE during the ESP." Opinion and Order at 25 (Appx. at 33). In authorizing the Service Stability Rider in an amount of $110 million/year, the Commission adopted DP&L's calculation of its projected revenue and expenses and made an adjustment to account for DP&L's projected operation and maintenance cost reductions that were not reflected in DP&L's calculation. *Id.* at 25. Although initially authorized for two years, in its Entry Nunc Pro Tunc, the Commission extended the duration of the Service Stability Rider subsidy to three years. *Id.* at 26 (Appx. at 34); Entry Nunc Pro Tunc at 2 (Appx. at 64). The Commission then found that the Service Stability Rider subsidy would produce a return on equity in the range of 7 to 11 percent. *Id.*

Under SB 3, however, an electric distribution utility had a single opportunity to secure transition revenue. Within 90 days of the effective date of SB 3, an electric distribution utility was required to file its transition plan. R.C. 4928.31(A) (Appx. at 170).[8] As part of its transition plan, it could request transition revenue. *Id.* Transition revenue was based on a determination of transition costs. Before authorizing collection of any transition revenue, the Commission had to find 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," "*the costs [were] unrecoverable in a competitive market*" and the electric distribution utility "would

[7] The authorization of transition revenue also violates the terms of a prior Commission-approved settlement, where DP&L agreed to limit its collection of transition revenue. *See* IEU-Ohio Ex 14 (Supp. at 18).

[8] SB 3 became effective on October 5, 1999.

otherwise be entitled an opportunity to recover the costs." R.C. 4928.39 (emphasis added) (Appx. at 175).

If the Commission determined that an electric distribution utility had a legitimate claim to transition revenue, it could authorize the collection of transition revenue for a finite period. For certain transition revenue recovery, the period was defined by the market development period that could not extend beyond 2005. R.C. 4928.40 (Appx. at 176-177). For transition costs identified as regulatory assets, the collection period could not extend beyond 2010. *Id.*

As part of its transition plan, DP&L sought transition revenue. Under a settlement resolving the case, DP&L was authorized to collect approximately $441 million of transition revenue. IEU-Ohio Ex. 14 at 30 (Supp. at 50); OCC Ex. 21 at 6-9 (Supp. at 62-65).

Following the collection of transition revenue authorized under a transition plan, DP&L's generation business was, and is, required to operate fully on its own in the competitive market. R.C. 4928.38 (Appx at 174). The Commission is also prohibited from authorizing any additional transition revenue, or its equivalent. *Id.* R.C. 4928.141, enacted as part of SB 221, precluded any further recovery of transition revenue. (Appx. at 159). Thus, Ohio law bars DP&L from collecting transition revenue.

DP&L and the Commission admit that the factors driving DP&L's request for the Service Stability Rider subsidy are generation-related and two of those relate to wholesale prices established by Federal Energy Regulatory Commission ("FERC")-approved tariffs. These factors are: "increased switching, declining wholesale prices, and declining capacity prices." Opinion and Order at 17 (Appx. at 25); Tr. Vol. I at 111-114, 137 (Supp. at 67-70, 78); Tr. Vol. I at 227 (Supp. at 87). Additionally, the chief financial officer of DP&L admitted during the hearing that its revenue from its other two lines of business, transmission and distribution, were adequate and would remain so. DP&L Ex. 1 at 13 (Supp. at 2); Tr. Vol. I at 118 (Supp. at 73); Tr. Vol. 1 at 150 (Supp. at 81). Thus, the Service Stability Rider is solely focused on providing DP&L additional generation-related revenue that DP&L admits it cannot recover through the market. By definition, the Service Stability Rider collects transition revenue or its equivalent.

Additionally, DP&L witness Chambers also admitted that, from an economic standpoint, the purpose of transition revenue is to compensate a utility when its assets would not be competitive when subjected to market prices. Tr. Vol. II at 536-537 (Supp. at 93-94). Specifically, he agreed that, if DP&L's return on equity deficiency is being driven by lower-than-desired generation revenue (which is DP&L's claim), and the Service Stability Rider is designed to make up the difference, then the Service Stability Rider is equivalent to a transition charge. Tr. Vol. II at 540-542 (Supp. at 96-98). As discussed herein, DP&L and the Commission agree that the Service Stability Rider is driven by DP&L's inability to recover revenue from the market related to its generation business.

In the Opinion and Order, the Commission held that the $330 million Service Stability Rider subsidy did not represent additional transition revenue because DP&L had not requested additional transition revenue or claimed that it did not receive sufficient transition revenue under its electric transition plan ("ETP" or "transition plan"). Opinion and Order at 22 (Appx. at 30). Further, in the Opinion and Order, the Commission found that authorization of the Service Stability Rider was consistent with the Commission's determination in Ohio Power Company's ("AEP-Ohio") electric security plan case. *Id.* The Commission also noted that DP&L remains obligated to provide a standard service offer and that the Service Stability Rider was the minimum amount necessary to maintain its financial integrity to enable DP&L to provide the standard service offer. *Id.* On rehearing, the Commission affirmed its findings and further asserted that the revenue collected through the Service Stability Rider is not transition revenue or its equivalent because "transition charges are cost-based charges" and "the SSR is not a cost-based charge; it was not designed for DP&L to recover specific costs." Second Entry on Rehearing at 6 (Appx. at 77). The Commission's justifications in support of the $330 million Service Stability Rider transition revenue subsidy are meritless.

First, the Commission's claim that this additional above-market generation-related subsidy is not transition revenue or its equivalent because DP&L did not request additional transition revenue or claim that its transition plan did not produce adequate transition revenue is meritless. *See* Opinion and Order at 22 (Appx. at 30). Both "rationales" ignore that the Commission has authorized DP&L to collect above-market transition revenue that is directly attributable to revenue unrecoverable in the market by DP&L's generation business. It is irrelevant that DP&L did not request "transition" revenue when that is exactly the result the Commission approved. Likewise, it is irrelevant that DP&L did not claim its prior recovery was insufficient—DP&L has no current legally enforceable claim to additional transition revenue regardless of what it collected under its transition plan settlement. Additionally, reliance on the AEP-Ohio decision does not justify the illegal authorization in this case. The AEP-Ohio decision also authorizes transition revenue outside the period permitted by R.C. 4928.38 and that illegal authorization is on appeal.

The Commission's reference to DP&L's continuing obligation to offer the standard service offer also does not provide a lawful basis for the Commission to authorize additional transition revenue. Under SB 3, DP&L was obligated to offer a standard service offer to non-shopping customers, and was provided the one-time opportunity to collect transition revenue. Under SB 221, DP&L remains obligated to provide a standard service offer for non-shopping customers, but SB 221 did not alter the prohibition on transition revenue. SB 221 did not repeal the statutes prohibiting the authorization of transition revenue outside the transition plan and which prohibit the authorization of additional transition revenue, and in fact SB 221 explicitly prohibits the Commission from authorizing additional transition revenue. R.C. 4928.141.

Furthermore, DP&L's obligation to provide standard service offer service, *i.e.* its provider of last resort obligation, is unrelated to the Service Stability Rider. DP&L made it clear that it was not seeking compensation for its provider of last resort obligation. Tr. Vol. V at 1357-1359 (Supp. at 103-105). Additionally, had it been seeking compensation for its provider of last resort obligation, DP&L would have had to demonstrate its provider of last resort costs. *In the Matter of the Application of Columbus Southern Power Company for Approval of an Electric Security Plan; an Amendment to its Corporate Separation Plan; and the Sale or Transfer of Certain Generating Assets*, Case Nos. 08-917-EL-SSO, *et al.*, Order on Remand at 22-24 (Oct. 3, 2011) ("Order on Remand");[9] *see also In re Columbus S. Power Co.* 128 Ohio St.3d 512, 2011-Ohio-1788, ¶ 29. DP&L admitted that it does not account for its provider of last resort costs and admitted it had not reviewed its provider of last resort costs or risks since 2005. Tr. Vol. V at 1357-1359 (Supp. at 103-105). Additionally, the Commission has held that customer switching (one of the factors driving the lower projected earnings and DP&L's reason for requesting the Service Stability Rider) is not a cost of satisfying the provider of last resort obligation and providing a standard service offer. Order on Remand at 31-32.[10] Thus, the Commission's reference (without further analysis) to DP&L's obligation to provide a standard service offer is irrelevant to the question of whether the Service Stability Rider provides

[9] Available at:
http://dis.puc.state.oh.us/ViewImage.aspx?CMID=A1001001A11J03B20528I67558.

[10] Available at:
http://dis.puc.state.oh.us/ViewImage.aspx?CMID=A1001001A11J03B20528I67558.

transition revenue or its equivalent, is unsupported by the evidence, and conflicts with precedent regarding what qualifies as a provider of last resort charge.

The Commission's claim that the revenue collected through the Service Stability Rider is not transition revenue because transition revenue relates to specific costs and the Service Stability Rider is not related to any costs is also meritless. The record below demonstrates that DP&L's revenue requirement calculation for the Service Stability Rider is essentially the same cost-based ratemaking methodology found in R.C. Chapter 4909. DP&L's calculation identifies specific costs that are input into its revenue requirement calculation, and the Commission reduced DP&L's revenue requirement calculation for additional cost reductions that DP&L had projected but omitted from its revenue requirement calculation. DP&L Ex. 1 at CLJ-2 (Supp. at 4). Accordingly, the Commission's statement that the Service Stability Rider is unrelated to any specific cost is against the manifest weight of the evidence.

In sum, the Service Stability Rider provides DP&L with unlawful transition revenue prohibited by R.C. 4928.38 and 4928.141.

3. **The ESP Orders authorizing the Service Stability Rider are unlawful and unreasonable because the Service Stability Rider provides DP&L with an anticompetitive subsidy in violation of R.C. 4928.02(H).**

4. **The ESP Orders authorizing the Service Stability Rider are unlawful and unreasonable and violate R.C. 4928.17 because they allow DP&L, an electric distribution utility, to provide an unfair competitive advantage and undue preference to its own competitive generation business and to its affiliate's competitive generation business.**

The Service Stability Rider allows DP&L to use its role as an electric distribution utility to charge its distribution customers and use this revenue to provide an above-market subsidy to DP&L's affiliated generation business. This result is prohibited by R.C. 4928.17, R.C. 4928.02(H), and the Commission's rules and precedent.

R.C. 4928.17 requires that an electric distribution utility separate its generation and other non-regulated businesses from its regulated distribution and transmission businesses. (Appx. at 168-169). The corporate separation requirements embodied in this statute and the Commission's rules require DP&L's generation business to operate independently from its generation and transmission businesses. R.C. 4928.17 (Appx. at 168-169); Rule 4901:1-37-04(A)(1), O.A.C (Appx. at 131). DP&L is also prohibited from "extend[ing] any undue preference or advantage to any affiliate, division, or part of its own business engaged in the business of supplying the competitive retail electric service or nonelectric product or service." R.C. 4928.17(A)(2) (Appx. at 168); Rule 4901:1-37-04(D)(10)(c), O.A.C. (Appx. at 133).

As discussed previously, DP&L operates under functional corporate separation requirements under R.C. 4928.17(C), which requires DP&L to maintain ongoing compliance with the State policies in R.C. 4928.02(H). R.C. 4928.02(H) provides that it is the policy of the State to ensure effective competition in the provision of retail electric service by *avoiding anticompetitive subsidies* flowing from a noncompetitive retail electric service to a competitive retail electric service or a product or service other than retail electric service or vice versa. R.C. 4928.17(C) (Appx. at 168-169); Rules 4901:1-37-04(A)(3) & (D)(6), O.A.C. (Appx. at 131-132). Additionally, R.C. 4928.02(H) prohibits the recovery of any generation-related costs through distribution or transmission rates. (Appx. at 150). Further, R.C. 4928.06 requires the Commission to effectuate the State polices contained in R.C. 4928.02, and the Commission has found that an electric distribution utility's standard service offer must comply with those State policies. (Appx. at 155-156).[11]

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[11] *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Approval of a Market Rate Offer to Conduct a Competitive Bidding Process for Standard Service Offer Electric Generation Supply, Accounting*

The Commission has previously interpreted R.C. 4928.02(H) to prohibit the collection of generation-related costs through a non-bypassable rider. Through an application filed by AEP-Ohio in 2010, AEP-Ohio requested to recover, through a non-bypassable charge, costs related to the closure of Unit 5 at the Sporn generating facility.[12] In its Finding and Order dismissing the application, the Commission concluded that no provision of R.C. 4928.143 authorized a rider to recover the plant closure costs and further held that "[a]pproval of such a charge would effectively allow [AEP-Ohio] to recover competitive, generation-related costs through its noncompetitive, distribution rates, in contravention of [R.C. 4928.02(H)]." *Id.* at 19. The Service Stability Rider similarly collects generation-relation costs through a non-bypassable, *i.e.* distribution, rate in contravention of R.C. 4928.02(H).

The Commission's rules governing corporate separation also prohibit an electric distribution utility, such as DP&L, from providing financial integrity payments to its internal generation business or to an affiliate. Rule 4901:1-37-04(C)(2), O.A.C. (Appx. at 131). The Commission's rules also define DP&L's generation business as an affiliate of DP&L, the electric distribution utility. Rule 4901:1-37-01(A), O.A.C. (Appx. at 129). Thus, the Commission

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Modifications Associated with Reconciliation Mechanism, and Tariffs for Generation Service, Case Nos. 08-936-EL-SSO, *et al.*, Opinion and Order at 13-14 (Nov. 25, 2008), available at: http://dis.puc.state.oh.us/TiffToPDf/A1001001A08K25B35520I16384.pdf; *see also Elyria Foundry v. Public Util. Comm.*, 114 Ohio St.3d 305 (2007); *In the Matter of the Application of The Cincinnati Gas & Electric Company to Modify its Nonresidential Generation Rates to Provide for Market-Based Standard Service Offer Pricing and to Establish an Alternative Competitive-Bid Service Rate Option Subsequent to the Market Development Period*, Case Nos. 03-93-EL-ATA, *et al.*, Order on Remand at 37 (Oct. 24, 2007), available at: http://dis.puc.state.oh.us/TiffToPDf/A1001001A07J24B41421C94009.pdf.

[12] *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 1-2 (Jan. 11, 2012), available at: http://dis.puc.state.oh.us/ViewImage.aspx?CMID=A1001001A12A11B35831F43601.

violated its rules when it authorized DP&L to make financial integrity payments to its generation business.

Thus, the Service Stability Rider violates R.C. 4928.17, R.C. 4928.02(H), and the Commission's rules and precedent.

5. The ESP Orders authorizing the Service Stability Rider are unlawful and unreasonable in violation of R.C. 4903.09 because the Commission failed to address IEU-Ohio's arguments that demonstrated that the ESP Orders violated R.C. 4928.17 by providing DP&L's and its affiliate's competitive generation businesses an unfair competitive advantage and undue preference.

The ESP Orders are unlawful and unreasonable because IEU-Ohio demonstrated that the Service Stability Rider provides DP&L's generation business an unlawful competitive advantage, preference, and subsidy in violation of R.C. 4928.17 and 4928.02(H). The Commission failed to address IEU-Ohio's arguments in its Opinion and Order, and failed to respond to IEU-Ohio's arguments in its Application for Rehearing. Instead, the Commission provided a blanket denial of all assignments of error that it had not specifically addressed in its Second Entry on Rehearing. Second Entry on Rehearing at 2 (Appx. at 73). "In all contested cases heard by the public utilities commission, a complete record of all of the proceedings shall be made, including a transcript of all testimony and of all exhibits, and the commission shall file, with the records of such cases, findings of fact and written opinions setting forth the reasons prompting the decisions arrived at, based upon said findings of fact." R.C. 4903.09 (Appx. at 142). The Commission must also "explain its rationale, respond to contrary positions, and support its decision with appropriate evidence." *See In re Columbus S. Power Co.*, 128 Ohio St.3d 512, 2011-Ohio-1788, ¶ 29-30. Because the ESP Orders failed to address IEU-Ohio's arguments, the Commission unlawfully and unreasonably failed to provide a reasoned explanation as required by R.C. 4903.09 and Court precedent.

6. The ESP Orders authorizing the Service Stability Rider are unlawful and unreasonable because the Commission is preempted from increasing DP&L's total compensation for the provision of wholesale energy and capacity service under the Federal Power Act.

In addition to being barred by Ohio law, the Commission's authorization of the Service Stability Rider is also preempted by federal law. The Federal Power Act provides FERC with exclusive jurisdiction to regulate wholesale sales of electricity. Because the Service Stability Rider provides DP&L additional compensation to the wholesale electricity prices authorized by FERC, a field within the exclusive jurisdiction of FERC, the Commission's authorization of the Service Stability Rider is preempted and void.

Under the Supremacy Clause of the United States Constitution, federal law is "the supreme Law of the Land." U.S. Const. Art. VI, cl. 2. As the supreme law of the land, federal law can nullify or preempt state or local actions. *Anderson v. Sara Lee Corp.*, 508 F.3d 181, 191 (4th Cir. 2007). Preemption may be express or implied. A federal law or regulation may impliedly preempt state law or regulation "where Congress has legislated comprehensively, thus occupying an entire field of regulation." *La. Pub. Serv. Comm'n v. F.C.C.*, 476 U.S. 355, 368 (1986).

The preemptive effect of the Federal Power Act is implied. *Morales v. Trans World Airlines,* 504 U.S. 374, 383 (1992). Under Section 201 of the FPA, Congress placed with FERC jurisdiction over "the sale of electric energy at wholesale in interstate commerce." 16 U.S.C. § 824(b). As a result of Congress's enactment of the Federal Power Act, "Congress has drawn a bright line between state and federal authority in the setting of wholesale rates and in the regulation of agreements that affect wholesale rates. States may not regulate in areas where FERC has properly exercised its jurisdiction to determine just and reasonable wholesale rates or to insure that agreements affecting wholesale rates are reasonable." *Miss. Power and Light Co.*

v. Miss. ex rel. Moore, 487 U.S. 354, 374 (1988). To ensure the lawfulness and reasonableness of wholesale electric energy rates, "the FPA implements a regulatory framework that vests FERC with authority to determine the lawfulness of wholesale energy rates or prices." *PPL Energy Plus, LLC v. Nazarian*, 974 F. Supp. 2d 790, 827-828 (D. Md. 2013). These wholesale rates include the prices for capacity and energy. *Id.*, citing *Miss. Indus. v. FERC*, 808 F.2d 1525, 1541 (D.C. Cir. 1987). Accordingly, "it appears well accepted that Congress intended to use the FPA to give FERC exclusive jurisdiction over setting wholesale electric energy and capacity rates or prices and thus intended this field to be occupied exclusively by federal regulation. Thus, state action that regulates within this field is void under the doctrine of field preemption." *Id.* at 828-829.

Two recent federal court cases, both affirmed on appeal, demonstrate that attempts by states to price wholesale generation-related capacity and energy services are preempted because they invade a field of regulation within the exclusive authority of FERC. In the first decision, a federal district court in Maryland reviewed an order of the Maryland Public Service Commission that increased compensation for the provision of wholesale electric services of an entity that was seeking to construct a generation plant ("Generation Owner"). In the challenged order, the Maryland Commission had directed the incumbent local electric utilities to enter into contracts with the Generation Owner. The contracts would have required the local electric utilities to pay the Generation Owner the difference between what the Generation Owner received for market-based sales of capacity and energy to PJM and a contract price established by the Maryland Commission based on the cost of construction and operation of the plant for 20 years. Any loss or gain that the local electric utilities incurred under the contracts ordered by the Maryland

Commission was to be passed on to Maryland ratepayers by the local electric utilities. *Id.* at 830-833.

The federal district court concluded that the Maryland Commission's order fixed the monetary value of wholesale generation-related capacity and energy services provided by the Generation Owner. *Id.* at 833. As a result, the court held that the Maryland Commission's order was preempted because the Maryland Commission was without authority to establish the price for wholesale energy and capacity sales. *Id.* Based on its determination that FERC has exclusive authority in that field and has fixed the price for wholesale energy and capacity sales in the PJM markets as the market-based rate produced by the auction processes approved by FERC and utilized by PJM, the district court declared the action of the Maryland Commission to be preempted. *Id.* at 840. In the opinion affirming the decision of the district court, the United States Fourth Circuit Court of Appeals agreed that the Maryland Commission was preempted because the field of wholesale electricity prices was exclusively within the jurisdiction of FERC. *PPL Energy Plus, LLC v. Nazarian*, 753 F.3d 467 (4th Cir. 2014).

A federal district court in New Jersey reached the same result, concluding that state legislation that attempted to encourage the construction of new generation plants by guaranteeing a price of capacity to the builder was preempted. In the New Jersey case, the state legislature passed legislation "to provide a transaction structure that would result in new power plants being constructed in the PJM territory that benefit New Jersey." *PPL Energy Plus, LLC v. Hanna,* 977 F. Supp. 2d 372, 393 (D. N.J. 2013). The law authorized the New Jersey Board of Public Utilities to issue a standard offer capacity agreement and directed the state's four electric distribution utilities to enter into contracts with the generators to pay any difference between the wholesale market price (the RPM-Based Price) and the development costs of the generators that the Board approved. *Id.* at 393-394. Like the Maryland federal court, the New Jersey federal district court found that the New Jersey legislation was preempted because the Federal Power Act occupied the field of wholesale electricity sales, including the price at which electricity is sold at wholesale. *Id.* at 406-412. Based on its finding that the state law was preempted, the federal court declared the statute under which the Board had authorized above-market payments to the generator "null and void." *Id.* at 412.

The Third Circuit Court of Appeals affirmed the New Jersey district court's decision holding that "the Federal Power Act, as administered by FERC, preempts and, therefore, invalidates state intrusions into the field" of wholesale electricity pricing. *PPL Energy Plus, LLC v. Solomon*, 766 F.3d 241, 253 (3d Cir. 2014) at 26. The Third Circuit noted that FERC had set the wholesale capacity price in PJM through the RPM auction process. *Id.* at 252. "At the same time," however, the New Jersey law provided certain generators "an additional amount" of compensation in excess of the wholesale market price. *Id.* "Because FERC has exercised control over the field of interstate capacity prices, and because FERC's control is exclusive, New Jersey's efforts to regulate the same subject matter cannot stand." *Id.* at 253.

The preemptive effect of the Federal Power Act similarly precludes the Commission from asserting jurisdiction to authorize the Service Stability Rider. As noted above, DP&L and the Commission claim that DP&L's lower projected returns on equity were being driven by: "increased switching, declining wholesale prices, and declining capacity prices." Opinion and Order at 17 (Appx. at 25). To remedy the reduced wholesale revenue (the latter two factors) that was in part driving DP&L's reduced returns, DP&L proposed the Service Stability Rider. The Commission, through the ESP Orders approving the Service Stability Rider, has increased DP&L's compensation for the provision of wholesale generation-related services.

Based on the well-understood principles of federal preemption, the Commission has no authority to increase DP&L's compensation for wholesale electricity services. FERC's jurisdiction to set the price of wholesale electricity and capacity is exclusive. Because the Commission is preempted from increasing DP&L's compensation for wholesale energy and capacity services above FERC-approved prices, the Commission lacks jurisdiction to authorize the Service Stability Rider.

Accordingly, for the aforementioned reasons, the authorization of the Service Stability Rider was unlawful in violation of Ohio and federal law.

B. The ESP Orders are unlawful and unreasonable because the approved electric security plan, including its pricing and all other terms and conditions, including any deferrals and any future recovery of deferrals, and which is quantitatively at least $250 million worse than a market rate offer, is not more favorable in the aggregate for consumers as compared to the expected results that would otherwise apply under R.C. 4928.142.

The Commission may approve or modify and approve an electric security plan if the electric security plan, including its pricing and all other terms including any deferrals and the collection of those deferrals, is more favorable in the aggregate than a market rate offer (the ESP v. MRO test). R.C. 4928.143(C)(1) (Appx. at 164-165). DP&L has the burden to demonstrate that the electric security plan meets the statutory requirements governing an electric security plan. *Id.* If the electric security plan does not satisfy the ESP v. MRO test, the Commission must reject it or modify it so that the electric security plan as modified satisfies the test. *Id.*

Based on the record in this case, there is no dispute that the approved electric security plan is more costly to customers than a market rate offer. In the Opinion and Order, the Commission correctly concluded that on a quantitative basis, the approved electric security plan as modified was $250 million worse than a market rate offer. Opinion and Order at 49-50 (Appx. at 57-58). The Commission's estimate, however, does not include the effects of the

Commission's Entry Nunc Pro Tunc. In the Entry Nunc Pro Tunc, the Commission added $64 million in non-bypassable charges to the approved electric security plan that make the approved electric security plan even less favorable than a market rate offer. Entry Nunc Pro Tunc at 2 (Appx. at 64).[13]

Once the Commission determined that the approved electric security plan was at least $250 million worse than a market rate offer, the Commission should have rejected it or made additional modifications to bring the approved electric security plan into compliance with the law. Instead, the Commission erred by injecting subjectively valued and unsupported qualitative benefits to offset the substantial amount that the electric security plan failed the test. On rehearing, the Commission concluded that additional but unidentified qualitative factors existed that also supported its finding that the electric security plan as modified and approved was more favorable than a market rate offer. Second Entry on Rehearing at 28 (Appx. at 99). The Commission's reliance on qualitative benefits to justify its conclusion that the electric security plan as modified and approved is more favorable than a market rate offer was unlawful and unreasonable.

1. The ESP Orders are unlawful and unreasonable because they assign subjective value to allegedly qualitative benefits of the approved electric security plan in violation of the requirements of R.C. 4928.143(C)(1) and R.C. 4903.09.

In analyzing whether the approved electric security plan satisfies the ESP v. MRO test, the Commission must engage in reasoned decision making. In a contested case, R.C. 4903.09 requires the Commission to issue "findings of fact and [a] written opinion[] setting forth the

[13] The Commission does not provide any estimate of the effect of extending the auction-based standard service offer for an additional five months; thus, it is unclear what the net effect of the Commission's changes will be on the ESP v. MRO test other than to make the approved electric security plan less favorable.

reasons prompting the decision[] arrived at, based on said findings of fact." In assessing the record the Commission must explain its rationale, respond to contrary positions, and support its decision with appropriate evidence. *In re Columbus S. Power Co.*, 128 Ohio St.3d 512, 2011-Ohio-1788, ¶ 30. "The commission cannot decide cases on subjective belief, wishful thinking, or folk wisdom." *Consumers' Counsel v. Pub. Util. Comm.*, 61 Ohio St.3d 396, 406 (1991) (*quoting Columbus v. Pub. Util. Comm.*, 58 Ohio St.2d 103, 104 (1979) (Brown, J., dissenting)). Thus, R.C. 4903.09 imposes on the Commission a requirement to apply an objective standard to the ESP v. MRO test.

Because the approved electric security plan is substantially less favorable than the market rate offer on a quantitative basis for all customers, in the Opinion Order the Commission assigns some indeterminate, but apparently significant, weight to qualitative benefits attributed to the approved electric security plan. The Commission, however, does not explain in what way it values the five "qualitative benefits" so as to offset the substantial amount that the approved electric security plan fails the ESP v. MRO test.

As demonstrated in more detail below, the Commission's unlawful failure to comply with the requirement to apply the ESP v. MRO test in a reasoned manner supported by the record extends to the Entry Nunc Pro Tunc. In that Entry, the Commission increased the cost of the electric security plan by extending the term of the Service Stability Rider, but does not discuss whether the approved electric security plan, as further modified by the Entry Nunc Pro Tunc, passes the ESP v. MRO test. Clearly, the approved electric security plan does not pass on an objective basis as, directionally, the quantitative amount by which the approved electric security plan is worse than a market rate offer is increased by an additional $64 million by the Entry

Nunc Pro Tunc.[14] Thus, by any reasoned analysis based on the quantitative results of the ESP v. MRO test, the Commission could not approve the electric security plan as modified by the Opinion and Order or as further modified by the Entry Nunc Pro Tunc. Without any further discussion of the effect of the Entry Nunc Pro Tunc on the ESP v. MRO test, the Commission, nonetheless, approved the electric security plan. Thus, it again failed to comply with the requirements of R.C. 4903.09.

R.C. 4903.09 requires more than the "trust me" reasoning contained in the ESP Orders. *In re Columbus S. Power Co.*, 128 Ohio St.3d 512, 2011-Ohio-1788, ¶ 29-30. Without an objective and articulated explanation of how each of the so-called qualitative benefits was weighted, the Commission's subjective qualitative benefits test prevents the parties, the Court, and the public from assessing the validity of the Commission's decisions. As a result, the Commission's conclusion that the approved electric security plan is more favorable in the aggregate than a market rate offer based on subjective and unexplained belief violates the requirements of R.C. 4903.09 that require the Commission to make findings of fact, to base its decisions on those findings, explain its rationale, respond to contrary positions, and support its decision with appropriate evidence.

2. The ESP Orders are unreasonable and violate R.C. 4903.09 because the Commission's finding that there are qualitative benefits of the approved electric security plan is against the manifest weight of the evidence.

The Commission identified five "qualitative benefits" and concluded that those offset the $250 million that the Commission found the approved electric security plan was worse than a

[14] In the quantitative calculation performed by the Commission, the Commission correctly recognized that the full effects of the Service Stability Rider and the Service Stability Rider-Extended must be counted on the electric security plan side of the test. Opinion and Order at 49 (Appx. at 57).

market rate offer. Opinion and Order at 50-52 (Appx. at 58-60). The various so-called qualitative benefits of the approved electric security plan, however, are variously unsupported by the record, rest on faulty factual and legal assumptions, and are largely illusory.

a. There is no benefit from the alleged faster move to a market-based electric security plan.

The Commission asserts that the faster move to a market-based electric security plan is a qualitative benefit that is "consistent with Section 4928.02(A) and (B), Revised Code." *Id.* This "finding" that the faster move to a market-based electric security plan is a qualitative benefit ignores the fact that the Staff's calculation that the Commission relies upon for its ESP v. MRO analysis already incorporates the effects of the use of an auction to set the standard service offer price. Embedded in the Staff's calculation are the same alleged benefits of "accelerating" the use of an auction to set the price of the electric security plan that are contained in DP&L's testimony supporting its rejected version of the ESP v. MRO test.[15] Thus, the "qualitative" benefit of the faster move to a market-based standard service offer is both quantifiable and fully incorporated into the calculation of the ESP v. MRO test. The Commission does not explain what additional benefit is not reflected in the quantification already included in the test. As a result, the record does not support a finding that there is a benefit from the alleged faster move to a market-based electric security plan.

Further, the Opinion and Order assumes that the approved electric security plan will produce a qualitative "benefit" through a quicker transition to market when that outcome is not within the control of the Commission. R.C. 4928.143(C)(2)(a) does not require DP&L to agree

[15] Staff witness Turkenton relied on an exhibit provided by DP&L to test its proposed electric security plan. Staff Ex. 8 at 4 (Supp. at 66). The base case calculations DP&L provided incorporated the results of an auction for a portion of the electric security plan. DP&L Ex. 5 at Ex. RJM-1R (Supp. at 5).

to the terms of the approved electric security plan or to submit a standard service offer that establishes default generation supply prices based on a capacity and energy auction. Under these circumstances, it was unreasonable and unlawful for the Commission to conclude that the approved electric security plan provides a future qualitative benefit greater than its near-term quantitative disadvantage on the unsupported assumption that DP&L will provide an auction-based standard service offer on June 1, 2017.

Additionally, assigning a benefit to a faster move to a competitive bidding process to set the default generation supply price represents fundamental misconception about the statutory outcomes required by Chapter 4928. The General Assembly has declared retail generation service to be a competitive service. R.C. 4928.03 (Appx. at 152). The General Assembly's expressed goal is to encourage customer choice through actions by individual customers having comparable and non-discriminatory access to a diverse group of competitive retail electric service providers. R.C. 4928.02(A) (Appx. at 150). The goal includes a statutory scheme that specifically limits the role of the electric distribution utility to that of a default supplier of competitive services and prohibits an electric distribution utility from being directly engaged in the business of providing competitive services. R.C. 4928.17 (Appx. at 168-169). The standard service offer, whether based on an electric security plan or a market rate offer, contains a default generation supply component for those customers not receiving competitive service from a competitive retail electric service provider. R.C. 4928.14 (Appx. at 158). Under the applicable requirements of an electric security plan or market rate offer, the standard service offer must be either market-tested (in the case of an electric security plan) or market-based (in the case of a market rate offer). The Commission cannot elevate the outcome already required by Ohio law, a market-based standard service offer, to support its finding that the approved electric security plan, which burdens customers with unlawful charges, is more favorable in the aggregate than a market rate offer. By assigning some subjective benefit to the "quicker" move to a competitively bid standard service offer, the Commission unreasonably and unlawfully reverses the priorities clearly expressed in Ohio law.

b. The alleged improvements in service reliability are based on faulty factual assumptions and an illegal charge.

The Commission states that the expensive and unlawful Service Stability Rider will produce adequate and reliable retail electric service, another qualitative benefit. Opinion and Order at 51 (Appx. at 59). Retail electric service encompasses both competitive and non-competitive services. R.C. 4928.01(A)(27) (Appx. at 145).[16] Non-competitive services, including distribution services, remain subject to the Commission's traditional rate regulation. R.C. 4928.05(A) (Appx at 153). DP&L's distribution service reliability is a distribution function for which DP&L is compensated based on traditional cost-based regulation. Opinion and Order at 27 (Appx. at 35).[17] Distribution reliability, therefore, is not a function of the approved electric security plan.

Further, the record does not support the finding that the Service Stability Rider will result in improved generation service reliability. DP&L is presently bidding all of its generation assets into the wholesale market and being compensated at market-based prices. Tr. Vol. I at 172 (Supp. at 84). Other than some general and unsupported claims by DP&L's witness Malinak, there is no support in the record that rejecting the Service Stability Rider subsidy will negatively

[16] R.C. 4928.01(A)(27) defines retail electric service to include "any service involved in supplying or arranging for the supply of electricity to ultimate consumers in this state, from the point of generation to the point of consumption." (Appx. at 145). R.C. 4928.03 declares that retail electric generation service is a competitive service. (Appx. at 152).

[17] The Commission recognized that DP&L's distribution service remains subject to traditional regulation and ordered DP&L to file a distribution rate case as a condition to any approval of an extension of the Service Stability Rider. Opinion and Order at 27 (Appx. at 35).

affect the reliability of the generation supply (or distribution service, or the transmission grid). *See* DP&L Ex. 14 at 17 (Supp. at 6). Thus, the Commission's finding that the Service Stability Rider provides some qualitative benefit of service reliability to customers that offsets at least $250 million is unsupported. Opinion and Order at 51 (Appx. at 59).

Additionally, the Commission has ignored the role of PJM in maintaining system reliability. PJM is responsible for maintaining the real-time reliability of the electric grid in a 13-state region that includes the DP&L service territory. IEU-Ohio Ex. 2 at 7-8 (Supp. at 7-8).[18] Because the reliability of DP&L's service to its customers as it relates to generation and transmission service is no longer within the control of DP&L, the Commission's assumption that there is some qualitative benefit to propping up DP&L's return on equity for its generation assets is inconsistent with the actual operation of the electric grid. *See* Opinion and Order at 51 (Appx. at 59).

Even if authorization of the Service Stability Rider did affect service reliability, the Opinion and Order rests on the fundamentally flawed position that DP&L may cross-subsidize its competitive and non-competitive business segments. The State energy policy (on which the Opinion and Order relies to find that there are qualitative benefits to the approved electric security plan)[19] provides that the Commission is to "[e]nsure effective competition in the provision of retail electric service by avoiding anticompetitive subsidies flowing from a noncompetitive retail electric service to a competitive retail electric service ... *and vice versa*, including by prohibiting the recovery of any generation-related costs through distribution or transmission rates." R.C. 4928.02(H) (emphasis added) (Appx. at 150). Under this provision of

[18] DP&L does not dispute that PJM is responsible for both supply and transmission service reliability. Tr. Vol. I at 172 (Supp. at 84).

[19] Opinion and Order at 50 (Appx. at 58).

the State energy policy, DP&L's generation, transmission, and distribution segments must stand on their own; subsidies between various business segments are unlawful. *See Elyria Foundry Co. v. Pub. Util. Comm.*, 114 Ohio St.3d 305, 315 (2007) (the predecessor of R.C. 4982.02(H) provided that the State policy "prohibits public utilities from using revenues from competitive generation-service components to subsidize the cost of providing noncompetitive distribution service, or vice versa."). If retail electric service reliability were a problem (there has been no demonstration that it is), then the correct solution under Ohio law would be for DP&L to file a distribution rate case, not to saddle customers with an unlawful generation-related non-bypassable charge designed to prop up the earnings of DP&L's generation business. The Commission, however, turns the unlawful and unreasonable subsidization of the Service Stability Rider charge into a supposed "qualitative" benefit of improved service quality. Opinion and Order at 51 (Appx. at 59). The Commission's attempt to treat an illegal cross-subsidy as a qualitative benefit is plainly unlawful.

c. The alleged benefits of separation of the competitive generation business from the noncompetitive lines of business are based on faulty legal and factual assumptions.

As another qualitative benefit, the Commission points to the requirement that DP&L legally separate its generation because it will provide "customers the benefits of market pricing as soon as possible under the circumstances." *Id.* The assumption that customers will somehow benefit from legal corporate separation of generation assets initially suggests the Commission's own confusion regarding the requirements of Ohio law. Ohio law deems the generation business segment of DP&L's business as competitive, and it further requires that the electric distribution utility may no longer engage either directly or through an affiliate in supplying a competitive retail electric service and a non-competitive retail electric service except under an approved corporate separation plan and only to the extent otherwise permitted by law. R.C. 4928.03

(Appx. at 152); R.C. 4928.17(A) (Appx. at 168).[20] If DP&L is in compliance with Ohio law, there should not be any benefit from divestiture that does not already exist.

Moreover, the fact that DP&L currently owns generation resources does not legally or logically prevent DP&L's customers from benefiting from market pricing through auctions to set the standard service offer price. DP&L, like Duke Energy Ohio, Inc. ("Duke"), could offer an auction-based standard service offer today, without resorting to legal separation of electric distribution utility-owned generation assets.[21] It is the Commission's order requiring customers to shore up DP&L's revenue through non-bypassable generation-related charges that is preventing DP&L's shopping and non-shopping customers from realizing the benefits of historically low wholesale generation prices by imposing a non-bypassable generation-related rider. Once again, the Commission has permitted an electric distribution utility to strip away the consumer benefit associated with shopping for the sake of illegal transition revenue or its equivalent. Thus, the claimed benefit from the legal separation of generation assets is illusory.

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[20] R.C. 4928.17(C), permits the Commission to issue an order approving a corporate separation plan that does not comply with the separation legal requirement of subsection (A) for "good cause shown" if the functional separation complies with Commission rules and the policies set out in R.C. 4928.02. Commission rules require that structural and accounting safeguards to "create competitive equality, prevent unfair competitive advantage, prohibit the abuse of market power and effectuate the policy of the state of Ohio embodied in section 4928.02 of the Revised Code." Rule 4901:1-37-02(B), O.A.C. (Appx. at 130).

[21] When Duke's current electric security plan was approved (by way of a settlement) in November 2011, Duke was functionally separated, still owning generation assets. As part of the electric security plan (which is currently in effect), Duke agreed to immediately (two months after a settlement was signed and just over one month after the Commission approved its electric security plan) set its entire standard service offer price through a competitive auction. *In the Matter of the Application of Duke Energy Ohio, Inc. 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.*, Opinion and Order (Nov. 22, 2011), available at: http://dis.puc.state.oh.us/ViewImage.aspx?CMID=A1001001A11K22B02754A96233.

d. There is no demonstration that the alleged benefit of competitive retail enhancements exceeds the costs paid by customers.

The Commission states that the benefits of the competitive retail enhancements it has ordered DP&L to complete will have benefits that exceed their cost of $2.5 million (plus carrying charges). Opinion and Order at 51 (Appx. at 59). If that is the case, then there should be some evidence in the record indicating the quantitative benefit of these enhancements, but there is not.

e. There is no demonstration that the alleged benefit in competitiveness exceeds the costs paid by customers and the alleged benefit is based on a fundamental misunderstanding of the effect of increased electric bills on the ability of customers to compete in the global economy.

In the Opinion and Order, the Commission states that the competitive retail enhancements, billing system modernization, and economic development provisions will improve Ohio's competitiveness in the global market. Opinion and Order at 52 (Appx. at 60). Once again, the Commission fails to point to anything in the record to support this finding. Further, both the competitive retail enhancements and the billing system modernization will be paid for by customers. There is no demonstration that the benefits are in fact any greater than the costs that customers will incur to implement these changes. Moreover, the Commission ignores the effect of the substantial rate increases the Commission has authorized DP&L to bill and collect. As IEU-Ohio pointed out in its testimony, "[i]t is axiomatic that an ESP that results in higher electricity prices for the vast majority of commercial and industrial customers cannot be properly characterized as creating a more favorable business climate." IEU-Ohio Ex. 2 at 36. (Supp. at 17).

f. The Commission failed to make any findings of fact, or even identify, the additional qualitative benefits that the Commission indicated existed in its Second Entry on Rehearing.

In its Application for Rehearing, IEU-Ohio sought rehearing of the Commission's unlawful and unreasonable decision to rely on five nonquantifiable "benefits" to support its finding that the approved electric security plan passed the ESP v. MRO test. IEU-Ohio's First Application for Rehearing at 15-24 (Oct. 4, 2013) (noting the factors listed in the Opinion and Order at 50-52) (Appx. at 201-210). In the Second Entry on Rehearing, the Commission took exception to IEU-Ohio's statement that the Commission relied on five nonquantifiable benefits to find that the quantitative benefits of a market rate offer were outweighed by the nonquantitative benefits of the approved electric security plan, stating, "there are more qualitative benefits of the authorized ESP." Second Entry on Rehearing at 28 (Appx. at 99). It then identifies the same five benefits it listed in the Opinion and Order: advancement of State policies, more rapid implementation of market rates, preservation of reliable and safe service, competitive retail enhancements, and support of economic development. *Id.* Apart from offering a few additional details about the competitive retail enhancements it had already noted as a nonquantifiable benefit in the Opinion and Order, the Commission does not identify the additional nonquantifiable benefits it relies on to support its conclusion that the approved electric security plan was more favorable in the aggregate than a market rate offer.

Because the Commission has not identified the additional nonquantifiable benefits that support its decision, the Commission has violated R.C. 4903.09. As discussed above in Sections II.A.5 and II.B.1, in a contested case, R.C. 4903.09 requires the Commission to issue "findings of fact and [a] written opinion[] setting forth the reasons prompting the decision[] arrived at, based upon said findings of fact." (Appx. at 142). Under this section, the Commission must explain its rationale, respond to contrary positions, and support its decision with appropriate evidence. *In re Columbus S. Power Co.*, 128 Ohio St.3d 512, 2011-Ohio-1788, ¶ 30. The Commission violated these requirements when it claimed that there were additional qualitative benefits of the approved electric security plan, but failed to identify these alleged additional benefits.

IV. RELIEF

As demonstrated above, the Service Stability Rider is an unlawful subsidy that the Commission was without jurisdiction to authorize and could not lawfully authorize as a provision of an electric security plan. Because the Service Stability Rider was not authorized under traditional ratemaking, *i.e.* R.C. Chapter 4909, but rather as a rider under an electric security plan, the prohibition against retroactive ratemaking does not bar a prospective adjustment to the Service Stability Rider rates to return the amounts customers have already paid under the rider, as the Commission recently argued to the Court. *In the Matter of the Application of Duke Energy Ohio, Inc. for an Increase in its Natural Gas Distribution Rates,* S.Ct. Case No. 2014-328, Brief Regarding Bond Requirements Submitted on Behalf of Appellee, the Public Utilities Commission of Ohio at 3 (Aug. 12, 2014). Accordingly, the Court should reverse the Commission ESP Orders, and remand the case to the Commission with directions to the Commission to order DP&L to modify its Service Stability Rider rates to prevent DP&L from collecting a further unlawful subsidy and to correct the unlawful and unreasonable economic harm already done to customers through the imposition of this charge.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing *First Merit Brief of Appellant Industrial Energy Users-Ohio* was served upon the parties of record *via* electronic transmission this 1st day of December 2014.

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