

BEFORE

THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of)
Ohio Power Company to Establish a)
Competitive Bidding Process for) Case No. 12-3254-EL-UNC
Procurement of Energy to Support Its)
Standard Service Offer.)

OPINION AND ORDER

The Public Utilities Commission of Ohio, coming now to consider the above-entitled matter, having reviewed the exhibits introduced into evidence in this matter, and being otherwise fully advised, hereby issues its opinion and order in this case.

APPEARANCES:

Steven T. Nourse, American Electric Power Service Corporation, One Riverside Plaza, 29th Floor, Columbus, Ohio 43215-2373, and Porter, Wright, Morris & Arthur, LLP, by Daniel R. Conway, 41 South High Street, Columbus, Ohio 43215, on behalf of Ohio Power Company.

Calfee, Halter & Griswold, LLP, by James F. Lang and N. Trevor Alexander, 1400 The Calfee Building, 1405 E. Sixth Street, Cleveland, Ohio 44114, and Mark A. Hayden, 76 South Main Street, Akron, Ohio 44308, on behalf of FirstEnergy Solutions Corporation.

Vorys, Sater, Seymour & Pease, LLP, by M. Howard Petricoff, 52 East Gay Street, Columbus, Ohio 43215-1008, on behalf of Exelon Generation Company, Constellation NewEnergy, Inc., and Constellation Energy Commodities Group, Inc.

Boehm, Kurtz & Lowry, by Michael L. Kurtz and Jody Kyler Cohn, 36 East Seventh Street, Suite 1510, Cincinnati, Ohio 45202, on behalf of Ohio Energy Group.

McNees, Wallace & Nurick, LLC, by Matthew R. Pritchard, 21 East State Street, Suite 1700, Columbus, Ohio 43215-4228, on behalf of Industrial Energy Users-Ohio.

Bruce J. Weston, Ohio Consumers' Counsel, Office of the Ohio Consumers' Counsel, by Maureen R. Grady, Assistant Consumers' Counsel, 10 West Broad Street, Columbus, Ohio 43215-3485, on behalf of the residential utility consumers of Ohio Power Company.

Mike DeWine, Attorney General of the State of Ohio, by Stephen Reilly, Assistant Attorney General, 180 East Broad Street, Columbus, Ohio 43215-3793, on behalf of the Staff of the Public Utilities Commission of Ohio.

OPINION:

I. HISTORY OF PROCEEDINGS:

By opinion and order issued August 8, 2012, the Commission modified and approved application for an electric security plan filed by Ohio Power Company (AEP Ohio), including a competitive auction-based Standard Service Offer (SSO) format in *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 No. 11-346-EL-SSO, et al.* (ESP II). In the ESP II opinion and order (ESP II Order), the Commission established a series of competitive energy auctions for AEP Ohio's SSO load, including a 10 percent slice-of-system energy only auction to commence six months after issuance of a final order in the Company's corporate separation proceeding¹, a 60 percent slice-of-system energy only auction for delivery commencing on June 1, 2014, and, finally, a 100 percent slice-of-system energy only auction for delivery commencing on January 1, 2015, and continuing throughout the remainder of the ESP. The Commission also directed AEP Ohio to implement a competitive bid procurement (CBP) process consistent with Section 4928.142, Revised Code, by December 31, 2012, and to establish a stakeholder process prior to filing its CBP.

On January 30, 2013, the Commission issued its Entry on Rehearing in the ESP II proceeding and addressed the merits of the applications for rehearing, including several areas pertaining to the CBP. On March 27, 2013, the Commission issued its Second Entry on Rehearing in the ESP II case.

By correspondence filed in the ESP II case on September 7, 2012, and October 12, 2012, AEP Ohio initiated its stakeholder process and scheduled a stakeholder meeting. AEP Ohio filed its application to establish a CBP process for its SSO on December 21, 2012, in the above captioned case. On January 31, 2013, a procedural schedule was established to assist the Commission in its review of AEP Ohio's proposed CBP process. On February 11, 2013, AEP Ohio filed a supplement to its application.

¹ *In the Matter of the Application of Ohio Power Company for Approval of an Amendment to Its Corporate Separation Plan, Case No. 12-1126-EL-UNC.*

Several parties filed motions to intervene in this proceeding including Ohio Energy Group (OEG); Industrial Energy Users-Ohio (IEU-Ohio); FirstEnergy Solutions Corp. (FES); Exelon Generation Company, LLC and Constellation NewEnergy, Inc. (jointly, Exelon); and Ohio Consumers' Counsel (OCC). By entry issued May 23, 2013, the attorney examiner granted intervention to OEG, IEU-Ohio, FES, Exelon, Constellation, and OCC.

In accordance with the procedural schedule, initial comments were filed by OCC, FES, IEU-Ohio, OEG and Exelon. Reply comments were filed on March 14, 2013, by AEP Ohio, OCC, FES, and Exelon. In light of the issues raised in the initial and reply comments, the attorney examiner scheduled this matter for hearing, which commenced as scheduled on June 24, 2013. Rebuttal testimony was heard on July 15, 2013. The scope of the hearing was limited to matters relating to the auction schedule, auction pricing, and customer retail rates.

II. SUMMARY OF THE APPLICATION:

In its application, AEP Ohio indicates it developed its CBP proposal with input from interested stakeholders on October 25, November 8, November 9, and November 27, 2012. AEP Ohio explains that documents were circulated at each meeting documenting its proposals in order to solicit feedback and input from the participants. Further, AEP Ohio provides that it fully considered all of the issues raised during the stakeholder process as it developed its application.

The application provides details associated with AEP Ohio's energy-only auction procurement. Specifically, it includes bidding rules under the CBP, as well as rules and protocols for participating by associated bidders. In addition, the application contains the master energy supply agreement (MESA) and communicational protocols for the CBP auctions. Further, the application includes AEP Ohio's recommendation to retain the National Economic Research Associates, Inc. d/b/a/ NERA Economic Consulting (NERA) as the auction manager for AEP Ohio's energy auctions.

In its supplemental application, AEP Ohio also introduces its proposals to recover auction related costs and to unbundle its current fuel adjustment clause (FAC). AEP Ohio maintains that the total SSO rate that will be paid by non-shopping customers would include the current base generation rates, a newly established Fixed Cost Rider (FCR) and an Auction Phase-In Rider (Auction Rider). The supplement provides that AEP Ohio will blend the results from the energy auction with the variable energy components that remain from the FAC.

III. DISCUSSION

A. Auction Schedule and Product Term

In its application, AEP Ohio proposes to hold four auctions across three delivery periods. Specifically, the auction schedule consists of a 10 percent slice-of-system energy auction that will commence upon the issuance of final orders in AEP Ohio's ESP II and corporate separation proceedings and continue until May 31, 2015. AEP Ohio proposes to conduct two 25 percent slice-of-system energy auctions, the first to be held in January 2014, and the second to be held in March 2014, for a delivery period beginning June 1, 2014. Finally, a 40 percent slice-of-system energy auction will occur in June 2014, with a delivery period commencing January 1, 2015, and continuing throughout the term of the ESP until May 31, 2015. (AEP Ohio Ex. 1 at 9.)

AEP Ohio maintains that its proposal strikes an appropriate balance between the risk of exposure to market conditions with the risk associated with decreasing bidder interest. Conducting two separate 25 percent slice-of-system energy auctions for the same delivery period, AEP Ohio explains, will average out the variance in market prices during the two auctions. While AEP Ohio states that the lead time prior to the commencement of the June 2014 delivery period allows for two substantial auctions of 25 tranches each to be conducted in January and March of 2014, in its reply brief, AEP Ohio notes that, in light of the extensive litigation of this proceeding, it would be reasonable for the Commission to delay the 10 percent and 60 percent energy auctions, or go straight to the 60 percent energy auction later in 2014. (*Id.* at 9-11; AEP Ohio Reply Br. at 8.)

Although FES originally proposed to conduct one energy auction for the June 1, 2014, delivery period in its initial comments, FES withdrew this position at the evidentiary hearing and supports AEP Ohio's proposal to conduct two 25 percent energy auctions. (FES Comments at 3; Tr. I at 17-18, Tr. II 314-315.)

OCC proposes that the 10 percent energy auction be split into a 10 month product and a 12 month product. In support of its request, OCC argues that having shorter delivery periods will reduce load and price uncertainty, and consequently reduce risk premiums assessed by the auction bidders. OCC believes that procuring a large load at one time is concerning, particularly if the auction results are higher than typical market prices on the scheduled bid day. (OCC Comments at 3-4, Reply Comments at 4.)

Exelon responds that the number of auctions to be held in a CBP should be limited. Specifically, Exelon witness Jonathan Lesser explains that administrative costs increase with the number of auctions held, in turn lowering the expected return for bidders. Dr. Lesser states that OCC's additional auction proposal will not only increase administrative costs by holding more auctions, it will likely reduce bidder participation, and subsequently result in higher bid prices. Similarly, AEP Ohio notes that OCC's proposal may increase costs, because it would require four auctions to procure energy up to the 60 percent threshold, whereas AEP Ohio's proposal requires only three. (Exelon Ex. 1 at 7-9; AEP Ohio Reply Comments at 2-3.)

The Commission finds that AEP Ohio's proposal of four energy auctions is reasonable and should be adopted. AEP Ohio's auction schedule, developed in consultation with NERA, is consistent with our objective of ensuring that customers are able to take advantage of market-based prices prior to the commencement of the 100 percent energy only auction. We are confident that the auction proposal is reasonably designed to maximize bidder participation, while minimizing costs for consumers. We agree with Exelon, AEP Ohio, and FES that the addition of a fifth auction may unnecessarily increase administrative costs and in turn drive prices up by discouraging bidder participation. Accordingly, we decline to adopt OCC's proposal.

The Commission is sensitive to OCC's concerns of consumer rates being determined by a single auction, but we find that AEP Ohio's proposed layering structure of the sixty percent auction mitigates risks that residential customers may face from market conditions. While we are optimistic that all customers will ultimately benefit from market based pricing, we do agree with OCC that the auction timing should be structured in such a way that customers are not only able to benefit from the auction results, but also that customers are protected from the fluidity of market conditions without the Commission interfering with the competitive markets. Therefore, we believe the auction schedule should be amended. Accordingly, the first 10 percent energy auction shall be conducted in February 2014, with delivery to commence April 1, 2014. The first 25 percent energy auction shall be conducted in May 2014, and the subsequent 25 percent energy auction should occur in September 2014, with delivery to commence on November 1, 2014. Finally, the remaining 40 percent energy auction should occur in November 2014, with delivery commencing on January 1, 2015. The product term for all four auctions shall be until May 31, 2015, consistent with the ESP II Order.

The Commission notes that while the February 2014 energy auction is later than anticipated in the ESP II Order, by commencing the auction in February, the Commission is able to ensure there is adequate time for AEP Ohio and NERA to finalize

the auction guidelines in accordance with a final order in this proceeding. Further, the Commission understands that the ESP II Order set forth a June 1, 2014, delivery date for the 60 percent energy auction; however, in light of the complexities of this case that were raised in the stakeholder process, comment cycle, and subsequent hearing, and the fact that the first auction will not commence until February, 2014, we find that amending the delivery date to November 1, 2014, is appropriate. By spreading out the energy auctions and subsequent delivery dates across the calendar year of 2014, we are minimizing any exposure that customers may face from one day of auction results. Therefore, we find that AEP Ohio's revised auction schedule and product term, as modified by this order, are reasonable and should be adopted.

B. Separate Auction Rate Zone Proposal

OEG and OCC contend that, in light of the Commission's decision to maintain separate FAC rates for Ohio Power Company (OP) and Columbus Southern Power Company (CSP) rate zones throughout the term of the ESP II, there should in turn be two separate energy-only auctions for each rate zone. OEG and OCC witness Lane Kollen states that there is a difference of approximately \$6 per megawatt-hour between CSP and OP rate zones, and suggests that in order to ensure OP customers are not exposed to higher energy rates, separate energy auctions should be held. (OCC/OEG Ex. 1 at 22-23; OEG Comments at 7-8.)

Exelon believes that OEG and OCC's arguments are speculative, and points out that the addition of more auctions during the ESP II time frame may increase administrative costs and potentially increase auction prices. AEP Ohio adds that there is no reason to separate the procurement of energy for the two rate zones when the power would all be delivered to a single zone and have no real price difference. Further, AEP Ohio notes that the two rate zones continue to exist post-merger only for the purpose of gradually unifying the legacy rates. (Exelon Ex. 1 at 7, Comments at 4; AEP Ohio Comments at 5.)

The Commission finds that OEG and OCC's recommendation to hold two separate energy auctions for OP and CSP rate zones is unnecessary in light of the fact that energy procured from each auction will be delivered to a single zone. We see no reason to increase the risk of auction results being higher as a result of the increased administrative costs associated with conducting twice as many auctions. Accordingly, we decline to adopt OEG and OCC's proposal for separate auctions by rate zone.

C. Auction Manager Discretion

In its application, AEP Ohio explains that its independent auction manager should be permitted to reduce the tranche target as needed. Specifically, AEP Ohio witness Chantale LaCasse provides that the auction manager would only reduce the tranche target to ensure that there is a competitive bidding environment that would drive the price down to a point that it is consistent with market conditions. (AEP Ohio Ex. 1 at 6-7.)

In its initial comments, FES raised concerns that a fluctuating tranche size will cause confusion and make the CBP less attractive to potential bidders. However, at the evidentiary hearing, FES and AEP Ohio stipulated that the auction manager should maintain the discretion to modify the tranche size in the event there is a significant load reduction in the future, after first consulting with Staff. The stipulated testimony also provides that AEP Ohio will not have a role in adjusting or establishing a new tranche size. In addition, the exhibit reflects that any changes in tranche size would be provided to bidders at least eight days in advance of the date set forth within AEP Ohio's application. (Tr. I at 16; FES Ex. 1.)

The Commission finds that, in light of the clarifications established at the evidentiary hearing, AEP Ohio's application provision that provides discretion for the auction manager to adjust the tranche size, are reasonable and should be adopted. Accordingly, we find that, consistent with the record in this proceeding, the tranche size should be adjusted only if there is a significant load reduction and an adjustment is necessary to attract bidder interest. If the auction manager seeks to adjust the tranche size, Staff must be consulted prior to any changes, and AEP Ohio should not have a role in the decision to adjust any tranche sizes. Finally, any adjustment to tranche sizes should be provided to bidders in accordance with Exhibit A of AEP Ohio's CBP application.

D. Pre-Auction Process

In its application, AEP Ohio explains there are two parts to the CBP application process. The first part calls for interested parties to apply to become qualified bidders. The second part requires each qualified bidder to: make certifications; provide an indicative offer; and post a pre-bid security prior to becoming a registered bidder. (AEP Ohio Application at 8.)

1. Pre-Bid Security

In its initial comments, FES explains that while AEP Ohio's CBP provides that there should be sufficient security in the form of a letter of credit in order to participate in the first energy auction, under AEP Ohio's proposal, cash would not be accepted as pre-bid security, despite the fact that it could later be accepted from winning bidders. Noting that cash is less expensive than a letter of credit, and less burdensome, FES recommends that cash be an acceptable form of pre-bid security. (FES Comments at 3-4.)

In its reply comments, AEP Ohio offers to modify the CBP rules to reflect that cash may be used as pre-bid security. (AEP Ohio Reply Comments at 6.) Accordingly, as we agree that this is a reasonable amendment, the Commission finds that the application should be modified to include cash as an acceptable form of pre-bid security.

2. MESA

In its application, AEP Ohio's proposed MESA provides for an independent credit threshold (ICT) cap of \$3,000,000 for a BB+/Ba1/BB+ rating, \$1,500,000 for a BB/Ba2/BB rating, and \$0 for a BB-/Ba3/BB- and below rating.

FES argues that the caps will limit supplier participation, and suggests that the caps be eliminated or, at least, increased to \$30,000,000 for a BB+/Ba1/BB+ rating, \$20,000,000 for a BB/Ba2/BB rating, and \$5,000,000 for a BB-/Ba3/BB- rating. (AEP Ohio App. at Ex. B, p. 19; FES Comments at 4-5.)

AEP Ohio responds that its proposal is reasonably designed to limit the amount of credit accepted below investment grade. According to AEP Ohio, its proposed ICT caps would help to reduce any risk associated with supplier default, which would otherwise be placed upon all retail customers. AEP Ohio adds that its proposal is identical to Duke Energy Ohio's proposal, which was approved by the Commission and endorsed by FES. (AEP Ohio Reply Comments at 6-7.)

Additionally, Exelon notes that, under the proposed MESA, a true-up based on estimated demand shares would occur for winning bidders; however, there would be no reconciliation based on actual load data unless the actual load data is 20 percent greater than or less than the load estimate. Therefore, Exelon recommends that there be a reconciliation based on actual, rather than estimated, load, which is the case with all of Exelon's contracts for default service load. Exelon points out that it uses actual data to

formulate its bids and relies on actual data in managing its winning bids. (Exelon Comments at 2-3.)

In its reply comments, AEP Ohio indicates that it can accommodate Exelon's recommendation from an operational standpoint, and agrees to modify the MESA to provide for settlement based on a true-up to actual load data. AEP Ohio notes that it accepts Exelon's proposed modifications to certain definitions, which are necessary to settle based on actual load. (AEP Ohio Reply Comments at 7.)

The Commission agrees that the MESA should be modified to provide for settlement based on a true-up to actual load data. However, we find that FES's proposal to revise the ICT caps should be denied. We are confident that AEP Ohio's proposed caps are reasonably designed to reduce the risk of supplier default and are consistent with the caps implemented by Duke Energy Ohio. Further, the proposed ICT caps benefit retail customers by limiting risks associated with supplier default. Accordingly, we find that AEP Ohio's ICT Caps are reasonable and should be adopted.

E. Retail Rates

AEP Ohio's application provides that customer SSO rates will consist of three components: base generation rates; energy costs, including auction related costs; and other fixed costs associated with the FAC. During the delivery period for the 10 percent energy auction and the 60 percent energy auction, AEP Ohio proposes to continue to charge current base generation rates, and, upon commencement of the 100 percent energy auction delivery period, the base generation rates will be adjusted to incorporate capacity costs of \$188.88/Megawatt-day (MW-day). (Supplement at 3-6.)

AEP Ohio explains that in order to blend its energy auction clearing prices into the SSO rates, it is necessary to unbundle the FAC. Specifically, AEP Ohio proposes to unbundle the FAC rates into an energy variable component and a fixed cost component. AEP Ohio provides that the first component would contain energy and variable costs, including energy costs, auction purchases, and auction costs, and would become the Auction Rider. The remainder of the FAC, AEP Ohio notes, which consists of non-energy fixed costs that are not otherwise comparable to elements of the auction, would become the FCR. AEP Ohio proposes to blend the auction results with the variable energy portion of the FAC in the Auction Rider, and maintain its current base generation rates until January 1, 2015. (Supplement at 3-6.)

1. Blending Auction Results

FES contends that AEP Ohio's retail price proposal is inconsistent with the Commission's ESP II Order. FES witness Sharon Noewer provides that despite the Commission clearly rejecting AEP Ohio's request to freeze base generation rates throughout the term of the ESP, AEP Ohio's proposal erroneously freezes the base generation rates for its SSO customers until January 1, 2015. Further, Ms. Noewer points out that AEP Ohio's failure to blend auction results into the base generation rates precludes AEP Ohio's customers from receiving potential benefits of market based pricing. (FES Ex. 7 at 6.)

In addition, FES maintains that the supplemental application ignores the Commission's order that non-shopping customers should have access to capacity pricing of \$188.88 per MW-day (state compensation mechanism). FES asserts that not only does the failure to incorporate the state compensation mechanism into non-shopping customer rates prevent customers from seeing any benefit of the state compensation mechanism, it also makes no sense to combine the load from the energy-only auctions with capacity priced at \$314 per MW-day. (FES Ex. at 8, Tr. I at 92, FES Reply Comments at 5-6.)

In light of the Commission's ESP II Order and Entry on Rehearing, FES believes that AEP Ohio's current base generation rates should be frozen until the 10 percent energy-only auction, and then blended with increasing percentages as the auctions commence. Specifically, FES proposes that for the first 10 percent energy auction, AEP Ohio should blend its SSO rate to include 90 percent base generation rates and 10 percent energy auction results. FES adds that 10 percent of the capacity should be priced in accordance with the state compensation mechanism. FES witness Noewer estimates that AEP Ohio's non-shopping customers would pay \$179.5 million more under AEP Ohio's proposal than they would under FES's blending proposal. (FES Ex. 18, Tr. at 370-371.)

Similarly, Exelon contends that AEP Ohio's proposal is inconsistent with the Commission's ESP II Order and the subsequent Entry on Rehearing. Exelon witness Lesser argues that AEP Ohio has been inconsistent in presenting its base generation rates, pointing out that in this proceeding the base generation rates represent capacity only, while AEP Ohio's previous position in the ESP II case was that the base generation rates included capacity costs, energy, and ancillary services. Exelon urges the Commission to affirm its previous rejection of AEP Ohio's request to freeze base generation rates through the term of the ESP in order to allow customers to take

advantage of potential savings as a result of the energy-only auctions. (Exelon Ex. 1 at 16-17; Tr. I at 273.)

Likewise, OEG and OCC point out that AEP Ohio's rate proposal does not accurately represent the Commission's ESP II Order, and request that the Commission affirm its previous ruling in the ESP II case. OEG and OCC add that FES's proposal is sound and may save customers a significant amount of money. In addition, OEG and OCC propose that, if the Commission adopts FES's blending provisions, it should clarify that the energy and demand costs resulting from AEP Ohio's energy auctions will be allocated in the same manner that FirstEnergy allocates its action costs. (OEG/OCC Reply Br. at 2-3.)

AEP Ohio argues that its proposal does not contradict the Commission's ESP II Order, but rather, FES's blending provisions are inconsistent with the Commission's order. In response to FES's arguments, AEP Ohio opines that FES witness Noewer ignores the narrow scope of the Entry on Rehearing, and stresses that the Commission adopted frozen base generation rates throughout the entire ESP, except for the final five months. In addition, AEP Ohio states that FES's interpretation is inappropriate and could cause AEP Ohio substantial financial harm. Further, AEP Ohio alleges that, in calculating the Retail Stability Rider (RSR), the Commission relied upon the current base generation rate without any blending of the auction prices. AEP Ohio provides that the combination of the Entry on Rehearing and the ESP II Order support its arguments that the Commission only intended to unfreeze base generation rates for the final five months of the ESP. (AEP Ohio Ex. 2 at 5-7, AEP Ohio Ex. 6; Surreply Comments at 2-3.)

Contradicting Exelon witness Lesser's testimony, AEP Ohio witness David Roush explains that there is no reasonable basis to conclude that the base generation rates reflect energy costs. Mr. Roush points out that adopting the blending proposal raised by parties in this proceeding would unfairly take ESP revenues from AEP Ohio in order to allow for customer rate decreases. Regarding the state compensation mechanism, AEP Ohio provides that, in order to adjust the base generation rates to reflect the state compensation mechanism price on January 1, 2015, AEP Ohio proposes to reduce the base generation rates for all customers by 40 percent. Mr. Roush states that this reduction was computed by applying the state compensation mechanism towards AEP Ohio's load information that was filed in the ESP II proceeding. In support of this approach, AEP Ohio offers that the reduction maintains the existing cost relationships between AEP Ohio's customers while allowing for a transition towards market based pricing. (AEP Ohio Ex. 2 at 6-7.)

The Commission finds that AEP Ohio's auction rate proposal is inconsistent with the Commission's ESP II Order and the subsequent Entry on Rehearing. In the ESP II case, AEP Ohio initially proposed to freeze base generation rates until all rates were established through a CBP process, and the Commission determined that AEP Ohio's proposed base generation rates were reasonable and should be approved. (ESP II Order at 15.) On rehearing, AEP Ohio requested, in light of the Commission's decision to accelerate the CBP, that base generation rates remain frozen throughout the ESP term, including the delivery period from January 2015 through May 2015, following the 100 percent energy only auction. Specifically, in its application for rehearing, AEP Ohio argued that "it would be unreasonable to adjust SSO base generation rates as part of conducting the 2015 energy auction given the other changes to the early auctions as well as the decision to reject RSR revenue decoupling." AEP Ohio, therefore, proposed that base generation rates remain frozen throughout the entire term of the ESP and that energy auction costs be flowed through the FAC. (AEP Ohio ESP II Application for Rehearing at 7.)

In the ESP II Entry on Rehearing, the Commission denied AEP Ohio's assignment of error, finding:

...AEP-Ohio's request to continue to freeze base generation rates through the auction process is inappropriate and should be rejected. The entire crux of the [ESP II] Order was the value in providing customers with the opportunity to take advantage of market-based prices and the importance of establishing a competitive electric marketplace. AEP-Ohio's proposal is completely inconsistent with the Commission's mission and would preclude AEP-Ohio customers from realizing any potential savings that may result from its expanded energy auctions. This is precisely the reason why the Commission expanded and accelerated the CBP in the first place. Further, we find AEP-Ohio's fear of adverse financial impacts is unfounded, as the RSR will in part ensure AEP-Ohio has sufficient funds to efficiently maintain its operations. Therefore, we find AEP-Ohio's application for rehearing should be denied.

(ESP II Entry on Rehearing at 36-37.)

Also in its application for rehearing in the ESP II proceeding, AEP Ohio requested that the Commission clarify that the state compensation mechanism was inapplicable to the energy only auctions. AEP Ohio couched its request in terms of the final five months of the ESP. Specifically, AEP Ohio noted that its ESP II application "contained a compromise offer...to provide capacity to winning auction suppliers for the January 2015 auction at \$255/MW-day." (AEP Ohio ESP II Application for Rehearing at 16.) The Commission not only denied AEP Ohio's application for rehearing that requested clarification that the state compensation mechanism did not apply to the energy auctions in the ESP II case, but the Commission also addressed AEP Ohio's proposed compromise, finding:

...AEP-Ohio's application for rehearing should be denied. In its modified ESP application, AEP-Ohio originally offered to provide capacity for the January 1, 2015 energy auction at \$255 per MW-day. In light of the Commission's decision in the Capacity Case, which determined \$188.88 per MW-day would allow AEP-Ohio to recover its embedded capacity costs without overcharging customers, it would be unreasonable for us to permit AEP-Ohio to recover an amount higher than its cost of service. Further, we disagree with AEP-Ohio's assertion that the Commission should not rely on the Capacity Case in determining the cost of capacity for non-shopping customers beginning January 1, 2015, because, as previously stated, the Commission was able to determine that...\$188.88 per MW-day establishes a just and reasonable rate for capacity. Therefore, consistent with our [ESP II] Order, the use of \$188.88 per MW-day allows for AEP-Ohio to be adequately compensated and ensures ratepayers will not face excessive charges over AEP-Ohio's actual costs.

(ESP II Entry on Rehearing at 37.)

Despite the Commission expressly finding that AEP Ohio could not continue to freeze base generation rates throughout the entire auction process, and that the state compensation mechanism does determine the cost of capacity for SSO customers once the auctions commence, AEP Ohio curiously proposed frozen base generation rates with no adjustment to reflect the results of the auctions, and failed to incorporate the

state compensation mechanism of \$188.88/MW-day. We note that, in the ESP II case and again in this matter, AEP Ohio actually raised the fact that a disproportionate customer rate impact could occur when class rates are set by auction, in apparent recognition of the fact that auction results were to be included as a part of the base generation rate design established by the ESP II Order. (ESP II Order at 15-16.) Regardless of the timeframe for which AEP Ohio sought clarification in its assignments of error in the ESP II Order, nothing within the Commission's conclusion limited it to the final five months of the ESP. Even if, *arguendo*, our rejection of AEP Ohio's assignments of error were in any way unclear², we note that AEP Ohio did not file an additional application for rehearing on this matter in the ESP II proceeding nor did AEP Ohio seek clarification on any part of the Entry on Rehearing.

Therefore, consistent with our holding in the ESP II Order and the Entry on Rehearing, we find that FES's blending proposals appropriately reflect our decision, and should be adopted. AEP Ohio's current, frozen base generation rates should be adjusted to account for the results of the slice-of-system energy only auctions. Further, as the winners of the energy only auctions will receive capacity from AEP Ohio, winning auction bidders should pay for capacity at the rate of \$188.88/MW-day, in accordance with the ESP II case and the Case No. 10-2929-EL-UNC (Capacity Case). For the first 10 percent energy auction, AEP Ohio should blend its SSO rate to reflect 90 percent base generation rates, 10 percent energy auction results, and 10 percent capacity priced in accordance with the state compensation mechanism. For the 60 percent energy auction, the SSO rates should reflect 40 percent base generation rates, 60 percent energy auction results, and 60 percent capacity priced in accordance with the state compensation mechanism. For the final five months of the ESP II, the SSO rate should reflect 100 percent energy auction results and 100 percent capacity priced at the state compensation mechanism. In addition we note that the SSO rate should also contain AEP Ohio's FAC, which is discussed below.

Finally, we find AEP Ohio's arguments that the blending of base generation rates with energy auction results will cause AEP Ohio serious financial harm to be unpersuasive. As indicated in the Entry on Rehearing, AEP Ohio will continue to receive the RSR throughout the remainder of the ESP II. Further, as a result of the extensive litigation in this matter delaying the energy only auction schedule, we see no basis in AEP Ohio's claims. Accordingly, AEP Ohio should modify its CBP application to incorporate the blending provisions set forth herein.

² We note that the opposition of AEP Ohio's auction rate proposal by OCC, OEG, Exelon, and FES on the basis that it was inconsistent with our ESP II Order and the Entry on Rehearing, confirms that our directives were unmistakably clear.

2. FAC Proposal

IEU-Ohio urges the Commission to deny AEP Ohio's request to bifurcate its FAC into the FCR and Auction Rider. In support of its position, IEU-Ohio explains that AEP Ohio is already recovering its fixed costs through the state compensation mechanism of \$188.88/MW-day. IEU-Ohio notes that the fixed costs AEP-Ohio seeks to include in the FCR relate to purchased power costs from the Ohio Valley Electric Corporation (OVEC) and Lawrenceburg, both of which are included in Federal Energy Regulatory Commission (FERC) Account 555 that is currently being recovered through AEP Ohio's FAC. However, IEU-Ohio states that the fixed costs in FERC Account 555 were also included in the calculation of the state compensation mechanism, thus allowing AEP Ohio to double recover the costs associated with the Lawrenceburg and OVEC power purchases. (Tr. at 98-102.)

FES adds that not only did AEP Ohio witness Roush acknowledge that AEP Ohio's proposed FCR costs appear to be included in the state compensation mechanism, but also that every item proposed to be included in the FCR consist of capacity related charges that are included in FERC Account 555. Exelon opines that AEP Ohio has not and cannot justify double recovery of the same purchased power costs. (FES Ex. 2; Exelon Br. at 3-4.)

Further, in its initial comments, FES argues that AEP Ohio is not entitled to receive the FCR after January 1, 2015. OEG adds that the Commission should only approve AEP Ohio's proposal to unbundle the FAC if the Commission also requires that the starting price for the energy auctions for each rate zone consist of the energy component of the FAC rate that customers would otherwise pay. OCC supports the comments of FES and OEG regarding the unbundling of the FAC. (FES Comments at 5-6; OEG Comments at 8-10; OCC Reply Comments at 3.)

AEP Ohio contends that IEU-Ohio, OEG and OCC, and FES make the flawed assumption that FAC demand charges are reflected in AEP Ohio's base generation rates, despite the fact that AEP Ohio witness Roush confirmed that base generation rates are not cost based. Furthermore, AEP Ohio provides that consistent with Section 4928.143(B)(2)(a), Revised Code, it was able to implement a FAC that provides for the automatic recovery of the costs of purchased power. AEP Ohio explains that the FCR, as proposed, does not amount to double recovery any more than the previous FACs that have been in place throughout the term of AEP Ohio's first two ESPs have doubled recovered such costs. (AEP Ohio Ex. 2 at 3, AEP Ohio Reply Br. at 5-6.)

The Commission finds that AEP Ohio's proposal to unbundle the FAC, including its request for authority to establish the FCR and Auction Rider, should be adopted. We agree with AEP Ohio that, in light of the fact that the CBP in this matter pertains to energy-only auctions, as a practical standpoint it makes sense to divide the FAC, with one section to capture all energy and variable components and the other to retain all non-energy fixed costs. Accordingly, we find that AEP Ohio shall be entitled to collect all of its costs related to conducting the energy auctions, as outlined in the order, through the newly established Auction Rider. Regarding the FCR, while we are approving AEP Ohio's request to establish a new, bypassable rider, we wish to point out that the non-energy costs to be collected through the FCR pertain to previous purchased power contractual commitments that AEP Ohio has made to fulfill its obligation to provide a SSO to all non-shopping customers.

Although several parties object to the bifurcation of the FAC, no party advanced any persuasive arguments against the proposal itself. Rather, the majority of the dissent was directed towards the allegations of AEP Ohio double recovering certain capacity revenues. Turning to these allegations, we find that this proceeding is not the appropriate forum to address these issues. Therefore, we find that AEP Ohio's proposal to establish an Auction Rider and FCR is reasonable and should be adopted.

F. Auction Pricing

Throughout the comment process and during the evidentiary hearing, several parties advocated for the establishment of an auction reserve price in order to insulate customers from uncertainty that may occur with the auction results. Also, an alternative proposal for a crediting mechanism was raised at the evidentiary hearing.

1. Reserve Price

OEG, OCC, and IEU-Ohio propose the establishment of a reserve price for the energy auctions to be set at the current SSO FAC rates. OEG and OCC witness Lane Kollen provides that under AEP Ohio's CBP proposal, SSO customers will be denied the competitive benefits of capacity being priced at market rates, and may pay energy costs that exceed its current FAC rates. Mr. Kollen notes that, while this issue will be substantially mitigated under AEP Ohio's proposal beginning in January 2015 when AEP Ohio proposes to incorporate the state compensation mechanism, customers may still be harmed unless a FAC energy rate ceiling is established. OEG and OCC believe that by capping the energy only auctions at the FAC rate, customer rates will not exceed the rates they would have otherwise paid had the auction not occurred. Similarly, in its initial comments, OCC proposes that the Commission be given greater

discretion to reject winning price offers that are not consistent with current market prices that result in SSO customers paying more than they would have otherwise paid under current FAC prices. (Joint Ex. 1 at 9-12; OCC Reply Comments at 2-3; OEG Comments at 3-7; OCC Initial Comments at 4.)

IEU-Ohio maintains that, unless the CBP is conducted with a reserve price that is equal to AEP-Ohio's forecasted FAC rates, it is likely that the CBP auction will clear at a price higher than the current FAC, causing SSO customer rates to increase. IEU-Ohio explains that the reserve price is consistent with the Commission's intent that energy-only auctions be beneficial to customers. (IEU-Ohio Ex. 8 at 9; IEU-Ohio Comments at 1-3.)

AEP Ohio disagrees that the results of an auction should be accepted or rejected based on their relationship to legacy SSO rates. According to AEP Ohio, the current FAC rates have no bearing on whether an auction produces a competitive clearing price. AEP Ohio notes that the Commission has already rejected the notion that the benefits of market pricing depend upon the temporary relation to legacy rates. AEP Ohio concludes that the Commission should again reject this position, as it does not constitute true market pricing. (AEP Ohio Ex. 1 at 4-9; AEP Ohio Reply Comments at 3-5, citing ESP II Order at 39.)

Likewise, FES argues that the proposals of IEU-Ohio and OEG and OCC to cap the starting price would impose false and arbitrary restrictions on a competitive auction and should thus be rejected. FES believes that auction results should reflect market prices at the time of the auction without regard to AEP Ohio's prior non-market based rates. Further, FES posits that a starting price cap would prevent suppliers, with the exception of AEP Ohio, from participating in the auctions. FES argues that an artificial cap may actually have the effect of increasing costs to customers. In her testimony, FES witness Noewer explains that FES's blending proposals that are consistent with the Commission's ESP II Order and Entry on Rehearing will adequately address IEU-Ohio's and OCC and OEG's concerns about customer rate increases. (FES Ex. 1 at 16-19; FES Reply Comments at 2-4.)

Similarly, Exelon argues that the FAC should not be used to establish an opening bid price. Exelon witness Lesser stresses that imposing a reserve price will actually cause long-term harm, explaining that a reserve price cap may lead to an increase in the auction clearing price. Specifically, Dr. Lesser states that a reserve price cap will dramatically shift the supply curve as potential suppliers may offer smaller quantities or drop out of the auction altogether. Dr. Lesser acknowledges that consumers may benefit in the event the auction price exceeds the FAC, but points out that in, the long

run, the price cap would cause a chilling effect in the retail market and lead to regulatory uncertainty. (Exelon Ex. 1 at 10-16; Exelon Reply Comments at 1-2.)

The Commission finds that the requests to establish a reserve price should be rejected. As the Commission has previously stated, we will not interfere with the competitive market and, therefore, find it inappropriate to establish a starting price, opening bid price cap, or mechanism to reject auction results (ESP II Entry on Rehearing at 35). We find that, in order to create an attractive auction that will facilitate maximum bidder participation, the Commission should avoid unnecessarily implementing mechanisms that may ultimately limit bidder participation and subsequently harm customers from the benefits associated with a competitive market. In addition, we note that the application provides reasonable safeguards for the Commission to ensure that the energy auctions are conducted in a manner that is not only consistent with the CBP but also in a manner that provides regulatory certainty and attracts auction participants.

While we understand parties concerns about the auction rates being higher than what SSO customers currently pay, our affirmation of the ESP II Order and Entry on Rehearing serves the purpose of both ensuring that SSO customers will be able to benefit from market based prices without having a chilling effect on the competitive market. As OEG and OCC witness Kollen testified, blending base generation rates and energy auction results, along with the inclusion of the state compensation mechanism price of \$188.88 per MW-day, would address concerns raised by OCC and OEG (Tr. I at 243-244). Regardless of what the auction prices are, customers will still maintain the ability to shop for offers in the competitive marketplace. Further, we are confident that our effort to provide consumer education throughout the State on current electric choice options will lead to customers making electric choices that best serve their individualized needs.

2. Crediting Mechanism

Exelon witness Lesser proposes a crediting mechanism that will address concerns raised over higher auction prices by reducing AEP Ohio's regulatory asset that was previously approved in the Capacity Case. Dr. Lesser explains that if the auction clearing price rises above the FAC price, then AEP Ohio would reduce the deferral amount by an amount equal to the difference between the auction clearing price and the FAC, times the auction load served by auction suppliers. Exelon believes that this approach balances customer interests by ensuring they still benefit from a fully competitive marketplace, and does not penalize AEP Ohio if the auction prices are above the FAC. Exelon reasons that AEP Ohio will be able to sell additional energy that would have otherwise been sold to its SSO customers. (Exelon Ex. 1 at 21-24.)

AEP Ohio responds that the proposal inappropriately requires a comparison of the auction clearing price to the FAC, as the variable portion of the FAC price is retrospective and the energy auction price is prospective. AEP Ohio explains that, once 100 percent of its SSO load is auctioned off, there will no longer be any variable FAC costs in order to draw the necessary comparison under Exelon's proposal. In addition, AEP Ohio asserts that the proposal makes an unsupported assumption that AEP Ohio will be able to sell off all of its freed up resources. OEG and OCC also oppose Exelon's recommended crediting mechanism, noting that the ESP II Order provides no basis for establishing the mechanism. (AEP Ohio Ex. 7 at 2; OEG and OCC Reply Br. at 5-6.)

The Commission finds that Exelon's proposed crediting mechanism should be rejected. As several parties point out, there was no foundation established in either the Capacity Case or the ESP II Order to establish a mechanism that would draw from deferral related costs. Further, we find that by upholding our decision in the ESP II proceeding which blends SSO customers' base generation rates with energy auction results and the state compensation mechanism price for capacity, the result intended by the mechanism is already accomplished. Accordingly, we decline to adopt the proposed crediting mechanism.

G. Auction Cost Recovery

AEP Ohio proposes to collect prudently-incurred costs associated with the energy auctions. Specifically, AEP Ohio seeks to recover costs associated with auction manager and consultant fees, incidental expenses acquired from conducting the stakeholder process, costs associated with energy supply contracts as a result of the energy auctions, and incremental expenses from conducting the auctions. (Supplement Application at 2-3.)

In its comments, OCC argues that the Commission should direct AEP Ohio to identify and justify the costs it seeks to recover from conducting the energy auctions. Specifically, OCC suggests that AEP Ohio articulate which costs are included in its energy supply contract costs, how these costs arise from conducting energy auctions, and the basis for charging costs to SSO customers instead of CBP suppliers. Further, OCC objects to AEP Ohio's proposal to recover balancing charges from SSO customers, arguing that the MESA should require that the CBP supplier bear all costs associated with real-time balancing. (OCC Comments at 2-3.)

AEP Ohio responds that it is impossible to identify all costs to be recovered before auctions have been conducted, and adds that no other EDU has been required to

do so prior to conducting an auction. AEP Ohio notes that it still provides cost estimates, and is only seeking recovery of costs that are prudently incurred. In response to OCC's concerns about balancing charges, AEP Ohio points out that such costs are a cost of participating in the PJM market and there is nothing new or controversial for retail customers to bear the balancing charges. (AEP Ohio Reply Comments at 9-10.)

The Commission finds that AEP Ohio's auction cost recovery proposal is reasonable and should be adopted. OCC provides no justification to depart from Commission precedent which allows for an EDU to recover prudently incurred auction costs. (See *In re FirstEnergy*, Case No. 12-1230-EL-SSO (July 18, 2012); *In re Duke-Energy Ohio*, Case No. 11-3549-EL-SSO (November 22, 2011); *In re Dayton Power and Light*, Case No. 12-426-EL-SSO (September 4, 2013). Further, we disagree that AEP Ohio has not justified recovery of its auction related costs, as AEP Ohio's supplemental application contains an estimate of its auction related costs. Therefore, we find AEP Ohio's proposal to recover auction related costs is reasonable and should be approved.

IV. Conclusion

Upon review of the record in this matter, including AEP Ohio's application and supplemental application, as well as the initial, reply, and surreply comments of the parties, the Commission finds that AEP Ohio's application, as supplemented, should be approved, as modified herein. We note that our evaluation of AEP Ohio's application and supplement reflect the consideration of the comment cycle, and evidentiary hearing, which has resulted in a CBP, that, as modified, reflects reasonable auction procedures that are consistent with the auctions conducted by other EDUs in Ohio.

The Commission notes, however, that we reserve the right to review and modify any feature of the CBP process as the Commission deems necessary from our continuing oversight of the process, including any reports on the auctions provided to the Commission by the independent auction manager, AEP Ohio, Staff, or any consultant retained by the Commission. Although AEP Ohio's application addresses four specific situations in which the Commission may reject the results of an auction, we note that this provision does not circumscribe the Commission's authority to oversee the CBP process. With respect to auction results, the Commission emphasizes again that we will not interfere with the competitive market or establish a mechanism to reject auction results. Accordingly, we find AEP Ohio's application and its supplement, as modified, should be approved.

FINDINGS OF FACT AND CONCLUSIONS OF LAW:

- (1) AEP Ohio is a public utility as defined in Section 4905.02, Revised Code, and is subject to the jurisdiction of this Commission.
- (2) On August 8, 2012, the Commission approved AEP Ohio's ESP in the ESP II proceeding and established a series of competitive energy auctions for AEP Ohio's SSO load.
- (3) By correspondence filed in the ESP II case on September 7, 2012, and October 12, 2012, AEP Ohio initiated its stakeholder process and scheduled a stakeholder meeting, respectively.
- (4) On December 21, 2012, AEP Ohio filed its application in the above-captioned case to establish a CBP process for its SSO.
- (5) On January 30, 2013, the Commission issued its Entry on Rehearing in the ESP II case.
- (6) By entry issued on January 31, 2013, a procedural schedule was established to assist the Commission in its review of AEP Ohio's proposed CBP process. AEP Ohio was directed to amend or supplement its application no later than February 11, 2013.
- (7) On February 11, 2013, AEP Ohio filed a supplement to its CBP application.
- (8) Initial comments were filed on March 4, 2013, by OCC, FES, IEU-Ohio, and OEG, and by Exelon on March 8, 2013.
- (9) Timely reply comments were filed on March 14, 2013, by AEP Ohio, OCC, FES, and Exelon.
- (10) Surreply comments were filed on March 20, 2013, by AEP Ohio.
- (11) By entry issued May 23, 2013, OEG, IEU-Ohio, FES, Exelon, and OCC were granted intervention in this proceeding.

- (12) The evidentiary hearing commenced on June 24, 2013.
- (13) Rebuttal testimony was heard on July 15, 2013.
- (14) Initial briefs were filed on August 16, 2013, by OEG and OCC, AEP Ohio, IEU-Ohio, FES, and Exelon.
- (15) Reply briefs were submitted by Exelon, OEG and OCC, FES, AEP Ohio, and IEU-Ohio on August 30, 2013.
- (16) AEP Ohio's CBP application, as supplemented, and modified consistent with this opinion and order, is reasonable and should be adopted.

It is, therefore,

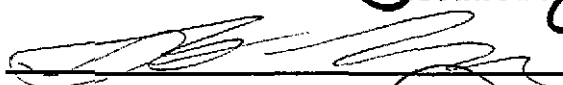
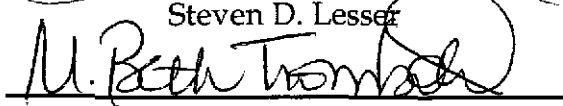
ORDERED, That AEP Ohio's application, as supplemented, be approved and modified consistent with this opinion and order. It is, further,

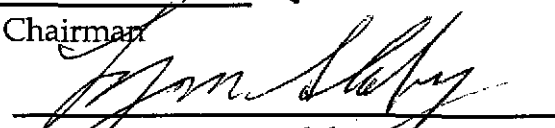

ORDERED, That AEP Ohio shall file proposed compliance tariffs consistent with this opinion and order, and subject to review and approval by the Commission. It is, further,

ORDERED, That a copy of this opinion and order be served upon all parties of record.

THE PUBLIC UTILITIES COMMISSION OF OHIO

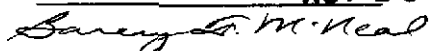

 Todd A. Spitchler, Chairman


 Steven D. Lesser

 M. Beth Trombold


 Lynn Slaby

 Asim Z. Haque

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Entered in the Journal **NOV 13 2013**


 Barcy F. McNeal
 Secretary

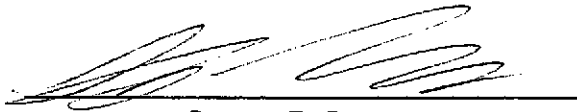
BEFORE

THE PUBLIC UTILITIES COMMISSION OF OHIO

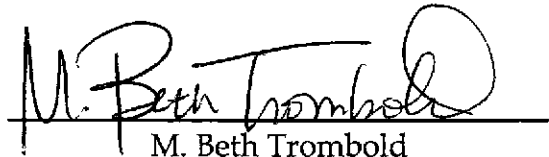
In the Matter of the Application of)
Ohio Power Company to Establish a)
Competitive Bidding Process for) Case No. 12-3254-EL-UNC
Procurement of Energy to Support Its)
Standard Service Offer.)

CONCURRING OPINION OF
COMMISSIONERS STEVEN D. LESSER AND M. BETH TROMBOLD

Although we do concur with the majority in the opinion and order; we have misgivings concerning AEP Ohio's proposal to unbundle the FAC. We would note that in the ESP II proceeding, AEP Ohio proposed to flow all energy procurement costs through the FAC. We believe that AEP Ohio's original proposal was a reasonable approach that avoided the complex task of dividing costs into a fixed non-energy component and variable energy component. Nonetheless, we agree with the conclusion reached by the majority, as there is no meaningful evidence in the record that could serve as an alternative to AEP Ohio's proposal to unbundle the FAC. In addition, although we are troubled by the allegations of AEP Ohio double recovering certain capacity related costs, we are confident that AEP Ohio's subsequent FAC proceedings, where the auditor should be directed to investigate these claims, provides an appropriate forum to examine these issues.



Steven D. Lesser

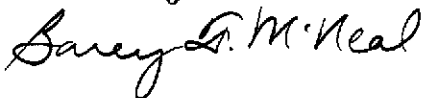


M. Beth Trombold

JJT/sc

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NOV 13 2013



Barcy F. McNeal
Secretary