

Individual Electric Utilities' Rate History and Rate Plans¹

February 2010

Dayton Power & Light (“DP&L”)

A. Rate Stabilization Plan (“RSP”)

On October 28, 2002, DP&L filed an Application before the Public Utilities Commission of Ohio (“PUCO” or “Commission”) to extend the end date of its market development period (“MDP”) from December 31, 2003 (the date agreed upon in its Electric Transition Plan² [“ETP”]) proceeding to the statutorily established date of December 31, 2005. DP&L’s Application recognized that development of the wholesale market was taking longer than expected at the time Ohio’s restructuring legislation, Substitute Senate Bill 3 (“SB 3”), was enacted.

During the course of the proceeding, interested stakeholders developed the rate stabilization plan (“RSP”) concept and, on September 2, 2003, the PUCO approved a contested Stipulation and Recommendation³ (“Stipulation”) that extended DP&L’s MDP through the end of 2005 and created an RSP having a term ending December 31, 2008. The RSP approved by the PUCO: continued generation rates as of January 1, 2004 subject to a potential 11% increase (designated as the rate stabilization surcharge or “RSS”) upon PUCO approval of costs associated with increases in fuel, environmental and tax laws, security, and changes required by administrative agencies; continued frozen distribution rates subject to changes permitted by the ETP Order; permitted DP&L to incorporate changes to its transmission rates approved by the Federal Energy Regulatory Commission (“FERC”); and, created a Voluntary Enrollment Procedure (“VEP”) Program to facilitate customers’ evaluation of competitive suppliers.⁴ In

¹ Author’s Note – Information on the status of any PUCO case identified herein can be obtained *via* the PUCO’s website using the menu item for the PUCO’s Docketing Information System (“DIS”) at <http://www.dis.puc.state.oh.us> by inserting the case number in the “Case Lookup” box.

² *In the Matter of the Application of The Dayton Power and Light Company for Approval of its Electric Transition Plan Pursuant to Section 4928.31, Revised Code and for the Opportunity to Receive Transition Revenues as Authorized Under Sections 4928.31 to 4928.40, Revised Code*, PUCO Case Nos. 99-1687-EL-ETP, *et al.*, Opinion and Order at 30 (September 21, 2000).

³ *In the Matter of the Continuation of the Rate Freeze and Extension of the Market Development Period for The Dayton Power and Light Company*, PUCO Case Nos. 02-2779-EL-ATA, *et al.*, Opinion and Order (September 2, 2003), Entry on Rehearing (October 22, 2003), upheld in *Constellation NewEnergy, Inc. v. Pub. Util. Comm.*, 104 Ohio St.3d 530, 2004-Ohio-6767.

⁴ *In the Matter of the Continuation of the Rate Freeze and Extension of the Market Development Period for The Dayton Power and Light Company*, PUCO Case Nos. 02-2779-EL-ATA, *et al.*, Opinion and Order

approving the settlement, the PUCO held that if market prices fell during the RSP, the PUCO could terminate the RSP and allow generation rates to be set by the prescribed competitive methods in Section 4928.14, Revised Code.⁵ Finally, the PUCO encouraged other electric distribution utilities (“EDUs”) to consider RSPs if competitive electric markets had not fully developed in their service territory by the end of the MDP.⁶

B. Rate Stabilization Surcharge

On March 1, 2005, DP&L announced that it intended to file an application to establish an RSS Rider and a distribution rate increase to recover costs associated with expenses for fuel, security, and environmental regulations, among others.⁷ The PUCO’s Order in DP&L’s RSP case limited DP&L to an RSS increase of 11% of its generation rate as of January 1, 2004, and DP&L requested the maximum 11% increase. A Staff Report of Investigation found that DP&L’s actual cost increases were in excess of the 11% cap.⁸

On November 3, 2005, several parties filed a Stipulation and Recommendation (“RSS Stipulation”) that recommended that the PUCO allow DP&L to increase its generation rates, subject to the 11% cap, and also extend the RSP through the end of 2010.⁹ In exchange for the extended predictability and rate stability through 2010, the RSS Stipulation recommended that the PUCO approve an Environmental Investment Rider (“EIR”) with annual increases of 5.4% commencing January 1, 2007, applied to rates in effect on January 1, 2004, and extending through 2010. As proposed, the EIR was

(September 2, 2003). The Stipulation was filed on May 28, 2003, by DP&L, the Office of the Ohio Consumers’ Counsel (“OCC”), Staff of the PUCO (“Staff”), Industrial Energy Users-Ohio (“IEU-Ohio”), Ohio Partners for Affordable Energy (“OPAE”), and Community Action Partnership of the Greater Dayton Area (“CAP”). In each of the three years of the VEP program, suppliers were provided an opportunity to submit supply proposals to serve customers in DP&L’s service area as part of an annual request for proposal (“RFP”) process. However, no suppliers submitted a proposal during the three-year period. *See, generally, In the Matter of the Commission’s Selection of Generation Providers for the Dayton Power and Light Company’s Voluntary Enrollment Procedure*, PUCO Case No. 05-302-EL-UNC.

⁵ Additionally, while the proposed Stipulation stated that non-residential shopping credits would be phased in over two-years, the PUCO held that an immediate, more substantial increase in the shopping credits in 2004 was more likely to encourage diversity and competition in the electric market and, thus, the PUCO modified the settlement so that the credits in 2004 equaled the shopping credits proposed for 2005. *In the Matter of the Continuation of the Rate Freeze and Extension of the Market Development Period for The Dayton Power and Light Company*, PUCO Case Nos. 02-2779-EL-ATA, *et al.*, Opinion and Order at 25 (September 2, 2003).

⁶ *Id.* at 29.

⁷ *In the Matter of the Application of The Dayton Power and Light Company for the Creation of a Rate Stabilization Surcharge Rider and Distribution Rate Increase*, PUCO Case No. 05-276-EL-AIR, Notice of Intent to File an Application to Increase Rates for Electric Service (March 1, 2005) (hereinafter, “*DP&L RSS Proceeding*”).

⁸ *DP&L RSS Proceeding*, Staff Report at 3 (August 26, 2005).

⁹ *DP&L RSS Proceeding*, Stipulation and Recommendation at 4-6 (November 3, 2005). The RSS Stipulation was filed by DP&L, IEU-Ohio, Honda of America Manufacturing, Inc. (“Honda”) and Cargill, Inc. (“Cargill”) and was not opposed by Staff.

avoidable by shopping customers in 2009 and 2010. The PUCO approved the RSS Stipulation, with modifications, on December 28, 2005.¹⁰

OCC appealed the RSS Order to the Ohio Supreme Court.¹¹ While the appeal to the Ohio Supreme Court was pending, the PUCO approved DP&L's Application to implement and set the EIR, which increased generation rates 5.4% on top of the 11% RSS increase.¹²

On September 5, 2007, the Ohio Supreme Court affirmed the PUCO's decision in the case except in one area.¹³ The Ohio Supreme Court ruled that the PUCO erred by allowing DP&L to include generation-related RSS charges in the rate schedules for distribution service and directed the PUCO to, on remand; remove the RSS charges from DP&L's distribution rate schedules.¹⁴ The Ohio Supreme Court also stated that, in light of the multiple RSP appeals, the PUCO might do well to share "...its evaluations and reports on the effectiveness of competition with the legislature ... so that it can continue to evaluate the need for further legislative action."¹⁵ In response to the Ohio Supreme Court's decision, DP&L filed an Application at the PUCO to move its RSS Rider to the generation portion of its tariffs, which the PUCO approved on April 30, 2008.¹⁶

C. Storm Cost Recovery Riders

On September 2, 2005, DP&L filed a request for approval of a Storm Cost Recovery Rider to recover expenses and capital costs incurred in restoring service after major storms that occurred in December 2004 and January 2005.¹⁷ DP&L sought to recover

¹⁰ *DP&L RSS Proceeding*, Opinion and Order (December 28, 2005), Entry on Rehearing (February 22, 2006), appealed in *The Office of the Ohio Consumers' Counsel v. The Public Utilities Commission of Ohio*, Supreme Court Case No. 2006-0788. The PUCO modified the RSS Stipulation by making the EIR avoidable from 2007 through 2010 instead of just 2009 and 2010. *DP&L RSS Proceeding*, Opinion and Order at 9 (December 28, 2005).

¹¹ *The Office of the Ohio Consumers' Counsel v. The Public Utilities Commission of Ohio*, Supreme Court Case No. 2006-0788, Notice of Appeal (April 21, 2006).

¹² *In the Matter of the Application of The Dayton Power & Light Company for Approval of Tariff Changes Associated with Implementation of an Environmental Investment Rider*, PUCO Case No. 06-1093-EL-ATA, Finding and Order (November 1, 2006).

¹³ *Ohio Consumers' Counsel v. Pub. Util. Comm.*, 114 Ohio St.3d 340, 2007-Ohio-4276.

¹⁴ *Id.* at ¶26.

¹⁵ *Id.* at ¶41.

¹⁶ *In the Matter of the Application of The Dayton Power & Light Company for Relocation of the Rate Stabilization Surcharge*, PUCO Case No. 07-1252-EL-ATA, Finding and Order (April 30, 2008).

¹⁷ *In the Matter of the Application of The Dayton Power and Light Company for Approval of Tariff Changes Associated with a Request to Implement a Storm Cost Recovery Rider*, PUCO Case No. 05 1090 EL ATA, Application (September 2, 2005) (hereinafter, "*DP&L Storm Cost Rider Proceeding*").

\$8.6 million over a two-year period through a 2.3% adder to distribution charges.¹⁸ The PUCO approved DP&L's Application¹⁹ and denied OCC's Application for Rehearing since OCC signed both DP&L's ETP and RSP Stipulations, which allowed DP&L to recover storm damage expenses through a tariff approval proceeding rather than an application for an increase in rates.²⁰ DP&L withdrew and discontinued its Storm Cost Recovery Rider as of July 24, 2008 inasmuch as DP&L expected its storm costs to be fully recovered as of that date.²¹

Similarly, DP&L filed an Application for accounting authority to defer (with carrying costs) as a regulatory asset a portion of its operations and maintenance ("O&M") expenses related to storm damage from Hurricane Ike in September 2008.²² Specifically, DP&L requested authority to defer O&M expenses associated with Hurricane Ike and other storms experienced in 2008 that exceed the three-year average service restoration O&M expenses associated with major storms. DP&L noted that both its ETP and RSP permit it to recover storm restoration costs. DP&L did not give an indication of when it would file an application for permission to actually collect the deferred costs or the total amount it would ask to collect related to storm damage expenses. The PUCO approved DP&L's Application on January 14, 2009.

D. PJM Interconnection ("PJM") Cost Deferrals/Transmission Cost Recovery Rider ("TCRR")

On December 21, 2007, DP&L filed an Application for accounting authority to defer PJM transmission enhancement charges ("TEC") assessed to all PJM customers for the cost of planned transmission facilities or upgrades in the PJM territory of 500 kilovolts ("kV") or greater.²³ On August 20, 2008, the PUCO approved DP&L's Application and

¹⁸ DP&L cited provisions in the ETP and RSP Stipulations allowing for recovery of storm damage as its authority for an exception to the otherwise applicable distribution rate freeze. *Id.* at Exhibit C-1.

¹⁹ *DP&L Storm Cost Rider Proceeding*, Finding and Order at 5 (July 12, 2006). The PUCO noted that DP&L sought recovery of costs over and above the costs normally incurred to repair storm damage and that DP&L limited recovery to only those costs related to severe weather in 2004 and 2005. Commissioners Mason and Jones dissented, stating that they believed DP&L was entitled to recovery of some storm damage costs, but that DP&L had not justified recovery of the entire \$8.6 million for storm damages inasmuch as it did not demonstrate what portion of the \$8.6 million could have been avoided had DP&L not cut its line clearance expenditures in half (as compared to expenditures from 1996 through 1998) during the time that the storm damage occurred.

²⁰ *DP&L Storm Cost Rider Proceeding*, Entry on Rehearing at 4-5 (August 30, 2006).

²¹ *DP&L Storm Cost Rider Proceeding*, Tariff Filing (July 25, 2008).

²² *In the Matter of the Application of The Dayton Power and Light Company for Authority to Modify its Accounting Procedure for Certain Storm-Related Restoration Costs*, PUCO Case No. 08-1332-EL-AAM, Application (December 26, 2008).

²³ *In the Matter of the Application of The Dayton Power and Light Company for Authority to Modify its Accounting Procedures*, Case No. 07-1287-EL-AAM, Application (December 21, 2007).

required DP&L to file an Application no later than June 1, 2009 to begin collecting the deferred TECs.²⁴

On November 7, 2008, DP&L filed an Application requesting accounting authority to defer all transmission and transmission-related costs in excess of those costs recovered in its retail rates.²⁵ DP&L asserted that Amended Substitute Senate Bill 221 (“SB 221”) and the PUCO’s rules permit the recovery of a broader range of costs than that authorized in the August 2008 TEC Order. DP&L indicated that it would file an application to begin collecting all of these costs (i.e., TECs as well as all other transmission and transmission-related costs) by the June 1, 2009 date set forth in the August 2008 TEC Order. Upon approval of its Application to recover the deferrals, DP&L said it would withdraw its retail transmission and ancillary service rates and include those costs in its TCRR. The PUCO approved DP&L’s Application on February 19, 2009.

On March 27, 2009 DP&L filed an Application for approval of a TCRR and the recovery of transmission costs and other regional transmission operator (“RTO”)-related costs through the TCRR, including those authorized for deferral in Case Nos. 07-1287-EL-AAM and 08-1209-EL-AAM.²⁶ DP&L requested authority to recover approximately \$96 million through its TCRR.²⁷ Over the objections of IEU-Ohio, the PUCO approved DP&L’s Application on May 27, 2009. On rehearing, the Commission partially reversed its prior decision and agreed with IEU-Ohio that generation-related reliability pricing model (“RPM”) costs are not recoverable through the TCRR inasmuch as RPM costs are not transmission or transmission-related costs.²⁸ However, the Commission also noted that the Stipulation in DP&L’s electric security plan (“ESP”) proceeding (see Subsection E below) may permit DP&L to recover RPM costs through a separate rider inasmuch as such costs are RTO-related costs not recovered through the TCRR.

Equipped with the Commission’s observation that RPM costs may be recoverable through a separate rider, on September 23, 2009 DP&L filed a Notice of Filing proposing to adjust its TCRR rates in accordance with the PUCO’s Finding and Order and Entry on Rehearing (*i.e.* minus RPM costs) and proposing to recover its RPM costs through a separate rider. On November 18, 2009 the PUCO issued a Second Finding and Order denying an IEU-Ohio Motion to Strike DP&L’s Notice of Filing, rejecting

²⁴ *In the Matter of the Application of The Dayton Power and Light Company for Authority to Modify its Accounting Procedures*, Case No. 07-1287-EL-AAM, Finding and Order (August 20, 2008).

²⁵ *In the Matter of the Application of The Dayton Power and Light Company for Authority to Modify its Accounting Procedures*, Case No. 08-1209-EL-AAM, Application (November 7, 2008).

²⁶ *In the Matter of the Application of The Dayton Power and Light Company for Approval of its Transmission Cost Recovery Rider*, Case No. 09-256-EL-UNC, Application at 3 (March 27, 2009). (hereinafter, “*DP&L TCRR Proceeding*”).

²⁷ *DP&L TCRR Proceeding*, DP&L’s Notice of Filing Revised Schedules and Workpapers at Schedule B-1 (May 15, 2009).

²⁸ *DP&L TCRR Proceeding*, Entry on Rehearing (September 9, 2009).

IEU-Ohio's arguments that DP&L could only recover RPM costs through a separate ESP case or that DP&L is already recovering its RPM costs through its current generation rates.²⁹ The Second Finding and Order also approved DP&L's revised TCRR and new RPM riders.

E. Electric Security Plan

Unlike the other EDUs, DP&L's RSP was scheduled to end on December 31, 2010 rather than on December 31, 2008. But the Ohio enacted new legislation (Amended Senate Bill 221 or "SB 221") in 2008 that altered both the process and means by which the price of default generation supply must be established by the PUCO. As a result of this difference between DP&L and the other EDUs, SB 221 contains specific ESP-related provisions to address DP&L's somewhat unique condition. More specifically, SB 221 permitted DP&L's then existing RSP to remain in effect for the balance of its term subject to DP&L's ability to file an ESP during such term.

DP&L filed its ESP proposal on October 10, 2008.³⁰ Consistent with SB 221, DP&L proposed to continue its current RSP, but make some adjustments related to providing standard service offer ("SSO") service.³¹ DP&L also requested authority to recover costs related to complying with the new alternative energy portfolio standards ("AEPS") and energy efficiency/peak demand reduction ("EE/PDR") benchmarks.

A Stipulation was filed with the PUCO on February 24, 2009 for the purpose of resolving the issues in DP&L's ESP case and it was approved in its entirety by the Commission on June 24, 2009.³² Among other things, the approved Stipulation extended DP&L's RSP through December 31, 2012 and permitted DP&L to implement an avoidable fuel recovery rider to recover fuel and purchased power costs.³³ The Stipulation permitted the current RSS charge to continue as an unavoidable surcharge through 2012, except that customers served under a governmental aggregation program may avoid DP&L's RSS so long as those customers agree to return to DP&L's provider of last resort ("POLR") service at market-based rates rather than tariffed rates.³⁴ DP&L's distribution

²⁹ *DP&L TCRR Proceeding*, Second Finding and Order (November 18, 2009).

³⁰ *In the Matter of the Application of The Dayton Power and Light Company for Approval of its Electric Security Plan*, PUCO Case Nos. 08-1094-EL-SSO, *et al.*, Application (October 10, 2008). (hereinafter, "*DP&L ESP Proceeding*").

³¹ See Section 4928.141(A), Revised Code.

³² *DP&L ESP Proceeding*, Opinion and Order (June 24, 2009).

³³ In accordance with the Stipulation, DP&L filed and the Commission approved the creation of DP&L's fuel rider on December 16, 2009. *In the Matter of the Application of The Dayton Power and Light Company to Establish a Fuel Rider*, Case No. 09-1012-EL-FAC, Finding and Order (December 16, 2009). The initial fuel rider rate is \$0.0197 per kilowatt hour ("kWh").

³⁴ The only party to oppose any portion of the Stipulation was Cargill. Cargill argued that all shopping customers should be able to avoid the RSC (i.e. the RSS charge described above in Subsection B) in 2011 and 2012 if they agree to return to POLR service at market-based rates rather than tariffed rates. {C29886:4 }

base rates were frozen through December 31, 2012 subject to DP&L's right to seek emergency rate relief. DP&L may also apply to the Commission to recover the costs of complying with changes in tax or regulatory laws or regulation which take effect after the date of the Stipulation as well as for the cost of storm damage. Additionally, the Stipulation allows DP&L to apply to the Commission for approval of separate riders to recover: the cost of complying with new environmental legislation or regulations related to climate change or carbon-related emissions or storage; environmental costs required to keep the Hutchings Generating Station in operation and available to customers to the extent such costs are cost effective; TCRR costs; and RTO costs not recovered in the TCRR. The Stipulation further dictates that the significantly excessive earnings test ("SEET") created by SB 221 will not apply to DP&L for the years 2009 through 2011.

Further, the PUCO-approved Stipulation requires DP&L to present to the Commission independent business cases for its advanced metering infrastructure ("AMI") and Smart Grid plans, thereby delaying implementation of DP&L's infrastructure investment rider ("IIR") until further approved by the Commission.³⁵ DP&L will also implement an energy efficiency rider to recover the costs associated with complying with the EE/PDR requirements established in SB 221³⁶ as well as an avoidable alternative energy rider ("AER") to recover the costs of complying with the AEPS contained in SB 221. Finally, the approved Stipulation requires DP&L to establish a collaborative process to address energy efficiency and demand response programs.

Duke Energy-Ohio, Inc. ("DE-Ohio"), formerly Cincinnati Gas & Electric Company ("CG&E")³⁷

A. Rate Stabilization Plan

On January 10, 2003, DE-Ohio filed an Application with the PUCO³⁸ for approval of an SSO pricing formula, which had to be established before it could accelerate the end of

The Commission denied Cargill's request to amend the Stipulation. *DP&L ESP Proceeding*, Opinion and Order at 10 (June 24, 2009).

³⁵ DP&L submitted its independent business cases for its AMI and Smart Grid plans on August 4, 2009. Initial and Reply Comments were submitted to the Commission on December 15, 2009 and January 8, 2010 respectively. The PUCO has not yet issued an order regarding the AMI and Smart Grid independent business cases. Of note, the PUCO Staff has recommended that the PUCO not approve the revised AMI and Smart Grid plans. *DP&L ESP Proceeding*, Comments of the Staff of the Public Utilities Commission of Ohio at 8, 15 (December 15, 2009).

³⁶ DP&L filed an Application with the PUCO requesting a determination that its EE/PDR programs approved in its ESP proceeding satisfied the requirement in Rule 4901:1-39-04, O.A.C., that each EDU file a three-year EE/PDR program portfolio plan for PUCO approval. *In the Matter of the Application of The Dayton Power and Light Company for a Finding that DP&L has Satisfied Program Portfolio Filing Requirements*, PUCO Case No. 09-1986-EL-EEC, Application (December 23, 2009).

³⁷ CG&E became Duke Energy-Ohio or DE-Ohio after a merger with Deer Holding Corporation, a subsidiary of Duke Energy Corporation ("Duke"). While many of the proceedings referenced herein were filed prior to the merger, CG&E is referred to as DE-Ohio in all case references because of the merger.

its MDP for non-residential customers ahead of the statutory MDP end date of December 31, 2005. DE-Ohio also made three additional filings seeking accounting authorizations associated with higher levels of transmission and distribution costs that DE-Ohio claimed were not reflected in its then-current rates.³⁹ In December 2003, the PUCO consolidated the DE-Ohio cases, directed DE-Ohio to file an alternative RSP, and set a hearing schedule to consider the consolidated proceeding. On January 26, 2004, in response to the PUCO's invitation to file an RSP, DE-Ohio filed another application seeking approval of SSO prices.⁴⁰

On May 19, 2004, several parties filed a Stipulation to resolve the issues raised in DE-Ohio's consolidated SSO-related proceedings. On September 29, 2004⁴¹ the PUCO issued an Opinion and Order that operated to substantially modify the plan proposed in the Stipulation. Among other things, the PUCO's Order included: a requirement that it approve changes in rates for certain cost components; more avoidability of certain charges by shopping customers; and full corporate separation by DE-Ohio if it failed to accept the PUCO's Order.⁴² DE-Ohio filed an Application for Rehearing on October 29,

³⁸ *In the Matter of the Application of The Cincinnati Gas & Electric Company to Modify Its Non-Residential Generation Rates to Provide for Market-Based Standard Service Offer Pricing and to Establish an Alternative Competitively-Bid Service Rate Option Subsequent to the Market Development Period*, PUCO Case No. 03-93-EL-ATA, Application (January 10, 2003) (hereinafter, "*DE-Ohio RSP Proceeding*"). OCC, IEU-Ohio, OPAC, and AK Steel Corp. ("AK Steel") filed motions requesting that the PUCO dismiss DE-Ohio's Application because, among other things, the Application was filed prior to the PUCO completing its SSO rules. The PUCO denied the Motions to Dismiss, but set a procedural schedule including a hearing to address issues raised by the motions about DE-Ohio's Application.

³⁹ See *In the Matter of the Application of The Cincinnati Gas & Electric Company for Authority to Modify Current Accounting Procedures for Certain Costs Associated with the Midwest Independent Transmission System Operator*, PUCO Case No. 03-2079-EL-AAM, Application (October 8, 2003), as well as *In the Matter of the Application of The Cincinnati Gas & Electric Company for Authority to Modify Current Accounting Procedures for Capital Investment in its Electric Transmission and Distribution System and to Establish a Capital Investment Reliability Rider to be Effective after the Market Development Period*, PUCO Case Nos. 03-2080-EL-ATA and 03-2081-EL-AAM, Application (October 8, 2003).

⁴⁰ *DE-Ohio RSP Proceeding*, The Cincinnati Gas & Electric Company's Filing in Response to the Request of the Public Utilities Commission of Ohio to File a Rate Stabilization Plan (January 26, 2004).

⁴¹ *DE-Ohio RSP Proceeding*, Opinion and Order (September 29, 2004).

⁴² Specifically, the PUCO modified the annually adjusted component ("AAC") (see Section B.III. below for further discussion of the AAC) by stripping a provision that provided for automatic annual increases of 6% (with additional 8% increases permitted upon PUCO approval), and instead removed the cap on PUCO approved increases. For 2005, the PUCO approved an AAC charge of \$53,757,267, but made it 100% avoidable for shopping customers. Further, while DE-Ohio would be allowed to seek, no more often than annually, unrestricted changes in the AAC charge that are applied as part of shopping customers' avoidable costs, the PUCO directed DE-Ohio to file quarterly reports detailing all fuel and economy purchased power ("EPP") costs. The PUCO also increased the percentage of nonresidential shopping customers that could avoid the rate RSC from 25% to 50%. The PUCO denied the extension of regulatory transition charge ("RTC") collection from residential consumers beyond 2008 and stated that, while it could not require the extension of the residential discount past 2005, the discount must continue through December 31, 2005. Further, the PUCO determined that the SSO rate under the Stipulation amounted to a "market-based" rate and approved provisions allowing the PUCO to order a competitive bidding process ("CBP") to test the ongoing reasonableness of the RSP under certain circumstances, but did not mandate that DE-Ohio conduct a CBP as requested by some parties. DE-Ohio was not required

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2004 requesting that the PUCO adopt the original Stipulation without modification or a new alternative proposal included in its Application for Rehearing.⁴³ On November 23, 2004, the PUCO issued an Entry on Rehearing generally adopting DE-Ohio's alternative plan with yet more modifications.⁴⁴

OCC appealed the PUCO's RSP determinations for DE-Ohio to the Ohio Supreme Court.⁴⁵ OCC's appeal was mainly focused on its general campaign to promote the use of an auction process to set default generation supply prices and to require electric utilities to divest their generating assets (campaign objectives that are difficult to reconcile with OCC's consumer-focused mission). The Ohio Supreme Court subsequently issued a decision that affirmed in part and reversed in part the PUCO's decision.⁴⁶

The Ohio Supreme Court rejected OCC's claims that the PUCO failed to adhere to the procedural steps required before approving an increase in rates and accepted the PUCO's finding that the SSO price set forth in the RSP was a "market-based" offer (unlike the Ohio Supreme Court's holdings in the FirstEnergy Corporation and American Electric Power RSPs). However, the Ohio Supreme Court held that the PUCO failed to show, in sufficient detail, the facts in the record upon which the Commission's Entry on Rehearing was based and the reasoning followed by the PUCO in reaching its

to divest its generation assets during the RSP. The PUCO also kept the Stipulation provision allowing DE-Ohio to defer for future recovery certain distribution costs incurred for non-residential customers between July 1, 2004 and December 31, 2005. *Id.*

⁴³ *DE-Ohio RSP Proceeding*, DE-Ohio Application for Rehearing (October 29, 2004).

⁴⁴ *DE-Ohio RSP Proceeding*, Entry on Rehearing (November 23, 2004). The PUCO's modifications required further evaluations of the reasonableness of the FPP component of the price to compare, the system reliability tracker ("SRT"), and the AAC; required DE-Ohio to annually file an application by September 1 to establish the FPP, SRT, and AAC levels for the following year (except for the AAC for 2005 and 2006 which were otherwise established in the alternative plan); and set baselines for the includable costs of the SRT, AAC and FPP. Additionally, DE-Ohio's alternative plan was changed to provide that: the level of avoidability of future SRTs was to be determined in a proceeding commenced by DE-Ohio within 60 days of the implementation of Midwest Independent Transmission System Operator ("MISO") Day 2 or July 1, 2005, whichever was earlier; the costs of environmental compliance, security and tax law changes in the AAC were to be based on changes in costs since 2000; the amounts recoverable for fuel, economy purchased power and emission allowances in the FPP were those in excess of amounts authorized in DE-Ohio's last electric fuel component ("EFC") proceeding; customers had a 60-day notice period to establish eligibility to avoid the RSC and the AAC; the cost of SSO for non-residential customers that return to DE-Ohio from a CRES provider would be based on the highest hourly cost of power that DE-Ohio incurred for that hour; and, for 2005, the RSC, AAC, and SRT could be avoided by current, non-residential shopping customers.

⁴⁵ The PUCO's final decisions are directly appealable to the Ohio Supreme Court, Ohio's highest court. See Sections 4903.10 through 4903.13, Ohio Revised Code.

⁴⁶ In order to ensure that its Notices of Appeal of the PUCO's approval of DE-Ohio's RSP were timely, OCC filed two Notices of Appeal with the Court – on March 18, 2005, and May 23, 2005. *Consumers' Counsel v. Pub. Util. Comm.*, Court Case Nos. 2005-0518 and 2005-0946. The Court granted a Joint Motion to consolidate the appeals on October 5, 2005 and held oral arguments on the consolidated cases on April 25, 2006. The Court issued its decision on November 22, 2006. *Ohio Consumers' Counsel v. Pub. Util. Comm.*, 111 Ohio St.3d 300, 2006-Ohio-5789.

conclusion. Additionally, while the Ohio Supreme Court affirmed its previous holding that “side agreements” are irrelevant to the PUCO’s consideration of the second and third prongs of the PUCO’s test for settlements, it held that the PUCO erred in denying discovery of “side agreements” requested by OCC inasmuch as they may be relevant to the first prong of the PUCO’s test – whether the settlement was the product of serious bargaining among capable, knowledgeable parties. However, the Ohio Supreme Court left open to the PUCO’s discretion whether or not the side agreements would be admissible. The Ohio Supreme Court remanded the case to the PUCO with directions to: compel disclosure of the requested “side agreements”; thoroughly explain its conclusion that the modifications on rehearing are reasonable; and identify the evidence it considered to support its findings.⁴⁷

On November 29, 2006, the PUCO ordered a hearing to be held in the remanded RSP proceeding to obtain record evidence to sufficiently explain its rationale, as directed by the Ohio Supreme Court.⁴⁸ The PUCO later clarified that the remanded hearing would be limited to testimony and evidence regarding the modifications made in the Entry on Rehearing and side agreements to the extent that they may have impacted the seriousness of the bargaining that led to the May 19, 2004 Stipulation that was rejected by the first Opinion and Order.⁴⁹ In the meantime, DE-Ohio sought to extend its then-current AAC charges into 2007 and to implement the 2007 SRT subject to a reconciling true-up. On December 20, 2006, the PUCO issued an Entry that permitted DE-Ohio to largely retain its then-current rates subject to such reconciliation as the PUCO might determine necessary when it resolved pending issues.⁵⁰

On February 1, 2007, the Attorney Examiner issued an Entry establishing two separate procedural paths to address the Ohio Supreme Court’s rulings and to set DE-Ohio’s RSP-related rider rates. A hearing to consider the Ohio Supreme Court’s evidentiary rulings (“Phase I”) commenced in March 2007 and a hearing regarding adjustments to DE-Ohio’s individual riders (“Phase II”) occurred in April 2007.

On October 24, 2007, the PUCO issued its Order on Remand on the Phase I issues.⁵¹ The PUCO’s Order on Remand made it clear that the PUCO rejected the May 19, 2004 Stipulation. It also approved an RSP consisting of generation and POLR components which, as a general proposition, tracked the charges then contained within DE-Ohio’s

⁴⁷ *Id.* at ¶¶36, 94.

⁴⁸ *DE-Ohio RSP Remand Proceeding*, Entry at 3 (November 29, 2006). The “*DE-Ohio RSP Proceeding*” citation will change to “*DE-Ohio RSP Remand Proceeding*” to denote the PUCO’s post-remand proceedings.

⁴⁹ *DE-Ohio RSP Remand Proceeding*, Entry (January 3, 2007).

⁵⁰ *DE-Ohio RSP Remand Proceeding*, Entry (December 20, 2006). Thus, the PUCO, for the interim, allowed DE-Ohio to continue its AAC into 2007 at the level as of December 2006, permitted DE-Ohio to continue its quarterly adjustment of the FPP, allowed the IMF to be adjusted in 2007 as previously approved, and let the SRT expire at the end of 2006.

⁵¹ *DE-Ohio RSP Remand Proceeding*, Order on Remand (October 24, 2007).

RSP.⁵² Further, the Order on Remand amended DE-Ohio's corporate separation plan to require DE-Ohio to retain its generating assets during the RSP and also required DE-Ohio to file tariffs that implemented the PUCO's Order on Remand.

The PUCO also considered certain side agreements entered into before the PUCO issued its initial Opinion and Order (on September 29, 2004) to determine whether the May 19, 2004 Stipulation (now rejected by the PUCO) was the product of serious bargaining among capable and knowledgeable parties. The PUCO found that the side agreements provided reason to question whether serious bargaining did occur in conjunction with the May 19, 2004 Stipulation. Because the side agreements contained trade secret and other customer-specific information (including account numbers), the PUCO also wrestled with issues related to how much of the side agreements should be placed in the public portion of the record in the case. After extensive litigation about which materials and to what extent those materials should be protected from public disclosure, the PUCO ultimately issued an Entry ordering the public disclosure of much of the information it previously protected inasmuch as that information was publicly made available through a Cincinnati newspaper as part of the records of a wrongful termination lawsuit in the Hamilton County Court of Common Pleas.⁵³

Among other things, the Order on Remand further found that: (1) terminating the previously established RTC and the 5% residential discount at the end of 2008 would encourage the development of competition; (2) the generation price approved was market-based and complied with Ohio law; and, (3) Ohio law afforded the PUCO flexibility in approving methods for determining market-based rates for SSO.⁵⁴

With specific regard to the PUCO's legal authority to establish a "market-based" price for competitive services (including generation supply) available from an EDU to customers not served by a competitive retail electric supply ("CRES") provider, the PUCO's Order on Remand interpreted then-current Ohio law to provide the PUCO with considerable flexibility and discretion on how to establish a "market-based" price. The PUCO explained, "a market-based standard service offer price is not the same as a deregulated price. ... Thus, while a standard service offer price need not reflect the sum

⁵² *Id.* at 29-37. The PUCO authorized the collection of the following generation charges, all of which were avoidable by shopping customers: a tracker analogous to the currently existing FPP Rider, which would parallel the FPP costs previously approved in a recent FPP case; a generation charge equal to 100% of DE-Ohio's unbundled generation rates; and a mechanism (similar to the AAC) to collect the incremental costs associated with homeland security, environmental compliance, and taxes. Regarding POLR charges, the Order on Remand approved charges to maintain a reserve margin (using the methodology of the SRT currently in place) as well as an unavoidable risk recovery rider in order to compensate DE-Ohio for the pricing risk of providing POLR service. However, the PUCO made both POLR charges avoidable for non-residential customers who agreed to remain off of DE-Ohio's RSP through 2008.

⁵³ *DE-Ohio RSP Remand Proceeding*, Second Entry on Rehearing (October 1, 2008). Practically speaking, the PUCO's ruling suggested that confidential information is not subject to its protection if the information finds its way into a newspaper regardless of how or why the newspaper came to obtain the information.

⁵⁴ *DE-Ohio RSP Remand Proceeding*, Order on Remand at 36-41 (October 24, 2007).

of specific cost components, the result must produce reasonably priced retail electric service, avoid anticompetitive subsidies flowing from noncompetitive to competitive services, be consistent with protecting consumers from market deficiencies and market power, and meet other statutory requirements.”⁵⁵ This legal interpretation was somewhat in conflict with PUCO determinations made previously in other cases. But it was consistent with the contemporaneous recommendations made to the PUCO by consumer groups, including IEU-Ohio.

Several Applications for Rehearing were filed and the PUCO denied all of them, except to make changes requested by DE-Ohio and IEU-Ohio.⁵⁶ The DE-Ohio Application for Rehearing was granted in order to clarify the applicability of DE-Ohio riders during certain shopping situations as well as to take under further advisement the PUCO’s edict that DE-Ohio not transfer any of its generating assets to an exempt wholesale generator (“EWG”). IEU-Ohio’s Application for Rehearing was granted in order to extend protective treatment of certain customer information (including account numbers) for five years instead of 18 months.

Both DE-Ohio and OCC filed appeals of the PUCO’s Order on Remand.⁵⁷ The Ohio Supreme Court granted DE-Ohio’s request to withdraw its appeal on April 2, 2008. Briefing of this case proceeded through the summer of 2008 and oral arguments were held on November 18, 2008. On February 19, 2009, the Court affirmed the PUCO’s decisions related to the trade secret challenges and found that issues related to RSP prices/charges were moot because there was no effective remedy to the problems cited by OCC and OPAE - the RSP had expired so there was no prospective relief the PUCO could provide and Court precedent does not permit retroactive refunds.⁵⁸ As to the trade secrets issue, the Court held that the PUCO’s decision to protect certain categories of information from public disclosure was reasonable and the information met the test in Ohio law for protecting the information. The Court also acknowledged the weakness and the "volatility and competitiveness" of the electric industry and asserted that exposing a competitor’s business strategies and pricing points would likely have a negative impact on that electric provider’s viability. Justice Pfeiffer dissented on the grounds that he believed the pricing provisions in the side agreements are not trade secrets and that the PUCO should have released that information.

The PUCO’s decision as to Phase II of the RSP Remand proceeding, the rider adjustment phase, is discussed in the sections below that relate to DE-Ohio’s individual riders.

⁵⁵ *Id.* at 37.

⁵⁶ *DE-Ohio RSP Remand Proceeding*, Entry on Rehearing (December 19, 2007).

⁵⁷ *Office of the Ohio Consumers’ Counsel v. Public Utilities Commission of Ohio*, Court Case No. 2008-0367.

⁵⁸ *Ohio Consumers’ Counsel v. Pub. Util. Comm.*, 121 Ohio St.3d 362, 2009-Ohio-604.

B. Proceedings Related to Riders Established in DE-Ohio's RSP

I. System Reliability Tracker

The SRT was established in DE-Ohio's RSP to compensate DE-Ohio for the costs of purchasing power to provide reliable POLR service, including an adequate reserve margin. On December 3, 2004, DE-Ohio filed an Application to modify the SRT in accordance with the PUCO's Entry on Rehearing in the RSP proceeding.⁵⁹ On February 9, 2005, the PUCO approved the SRT charges for 2005 and reaffirmed its requirement that DE-Ohio file an application by September 1 of each year to establish the SRT for the following calendar year (hereinafter, "SRT Order").⁶⁰

On March 11, 2005, OCC filed an Application for Rehearing contesting the PUCO's SRT Order and arguing that: (1) the SRT was a rate increase and, thus, a hearing was required prior to approval; (2) the SRT violated Section 4928.14(A), Revised Code, which requires an SSO to be market-based; and, (3) DE-Ohio failed to demonstrate that the SRT was necessary because it did not show that the costs of its POLR obligation increased since the MDP. The PUCO denied OCC's Application for Rehearing on April 6, 2005. The SRT charges for 2006 were established by a Stipulation that all parties either signed or did not oppose, which was approved by the PUCO on November 22, 2005.⁶¹

As a result of the RSP Remand proceeding, the PUCO allowed the SRT to expire in 2006 and initially did not authorize an SRT charge for 2007.⁶² However, a Stipulation and Recommendation ("Phase II Stipulation") approved by the PUCO addressed outstanding issues regarding DE-Ohio's Rider adjustments, including the 2007 SRT. In particular, the Phase II Stipulation adopted many of the recommendations made by the management/performance ("m/p") auditor that related to the SRT, allowed DE-Ohio to recover its 2007 planning reserve purchases by year's end (with quarterly reconciliation filings), and permitted DE-Ohio to recover capacity purchases made from former Duke

⁵⁹ *In the Matter of the Application of The Cincinnati Gas & Electric Company to Modify its System Reliability Tracker Component of its Market-Based Standard Service Offer*, PUCO Case No. 04-1820-EL-ATA, Application (December 3, 2004). DE-Ohio stated that its filing was not an acceptance of the PUCO's revision to DE-Ohio's alternative plan, but that it expected to proceed with implementing the plan, pursuant to the PUCO's Entry on Rehearing. *Id.* at 4.

⁶⁰ *In the Matter of the Application of The Cincinnati Gas & Electric Company to Modify its System Reliability Tracker Component of its Market-Based Standard Service Offer*, PUCO Case No. 04-1820-EL-ATA, Finding and Order at 4 (February 9, 2005).

⁶¹ *In the Matter of the Application of The Cincinnati Gas & Electric Company to Adjust and Set its System Reliability Tracker Market Price*, PUCO Case No. 05-724-EL-UNC, Stipulation and Recommendation at 5-6 (October 27, 2005). The Stipulation provided, among other things, that: non-residential customers may avoid the SRT upon certain conditions but the SRT was unavoidable for residential customers; DE-Ohio must maintain a 15% planning reserve margin; the 2006 SRT would be adjusted and reconciled quarterly; and, SRT costs would be allocated among certain classes of customers.

⁶² *DE-Ohio RSP Remand Proceeding*, Entry at 5-6 (December 20, 2006).

Energy North America (“DENA”) assets under certain conditions.⁶³ Regarding the DENA assets, the PUCO highlighted its belief that the “market for capacity is not mature,” but approved the methodology for determining a market price for purchases from DENA assets in light of the different mechanisms available for setting a market price and the fact that DE-Ohio would likely be unable to obtain timely PUCO approval of a DENA purchase in an emergency circumstance.⁶⁴ OCC and OPAE filed Applications for Rehearing of the PUCO’s Order; the PUCO denied the Applications for Rehearing in their entirety.

On September 4, 2007, DE-Ohio filed its Application for approval of the SRT charge for 2008.⁶⁵ The PUCO’s Attorney Examiner set a joint hearing to consider the 2008 SRT and AAC Applications, as well as the PUCO’s review of DE-Ohio’s July 1, 2006 through June 30, 2007 FPP and SRT costs. A Stipulation (“SRT/FPP Cost Review Stipulation”) proposing to resolve contested issues regarding DE-Ohio’s 2008 SRT and FPP charges was filed at the PUCO on December 13, 2007.⁶⁶ With regards to the SRT, the SRT/FPP Cost Review Stipulation permitted DE-Ohio to implement the 2008 SRT as initially filed with the PUCO, allowing DE-Ohio to recover \$16.8 million in planning reserve capacity purchases as well as \$11.3 million related to prior years’ under-recovery of SRT Rider purchases. Also, the PUCO required DE-Ohio to continue making quarterly filings to reconcile the SRT. Initial and Reply briefs were filed on January 8, 2008 and January 15, 2008, respectively, and the Commission adopted the SRT/FPP Stipulation in its entirety on February 27, 2008.⁶⁷

In January 2009, the PUCO selected an auditor to undertake a review of DE-Ohio’s SRT and FPP for the July 1, 2007 through December 31, 2008 time period. An unopposed Stipulation resolving issues identified in the audit was submitted on August 28, 2009 and the PUCO approved the Stipulation on September 30, 2009. The

⁶³ *In the Matter of the Application of The Cincinnati Gas & Electric Company to Adjust and Set its System Reliability Tracker Market Price*, PUCO Case Nos. 05-724-EL-UNC, *et al.*, Opinion and Order at 11-12, 16-21 (November 20, 2007). The market pricing methodology for capacity from the DENA assets is: (1) the midpoint of broker quotes received, or (2) the average price of third-party purchases transacted, or (3) an alternative agreed to by DE-Ohio and Staff.

⁶⁴ *Id.* at 20-21.

⁶⁵ *In the Matter of the Application of Duke Energy Ohio, Inc., to Establish its 2008 System Reliability Tracker of its Market-Based Standard Service Offer*, PUCO Case No. 07-975-EL-UNC, Application (September 4, 2007). The PUCO, in connection with DE-Ohio’s annual SRT filings, also procured audits of DE-Ohio’s previous four quarters’ SRT and FPP charges in order to allow the PUCO to make the appropriate adjustments to the SRT and FPP charges. See *In the Matter of the Commission’s Review and Adjustment of the Fuel and Purchased Power and the System Reliability Tracker Components of Duke Energy Ohio, Inc., and Related Matters*, PUCO Case No. 07-723-EL-UNC, Entry (July 25, 2007).

⁶⁶ *In the Matter of the Application of Duke Energy Ohio, Inc. to Adjust and Set its 2008 System Reliability Tracker*, PUCO Case Nos. 07-975-EL-UNC, *et al.*, Stipulation and Recommendation (December 13, 2007).

⁶⁷ *In the Matter of the Commission’s Review and Adjustment of the Fuel and Purchased Power and the System Reliability Tracker Components of Duke Energy Ohio, Inc., and Related Matters*, PUCO Case Nos. 07-723-EL-UNC, *et al.*, Opinion and Order (February 27, 2008).

Stipulation largely dealt with operational issues related to DE-Ohio's generation assets, including DE-Ohio's coal contracts, DE-Ohio's coal supply management, and the development of better internal asset management policies.⁶⁸

In March 2008, OCC and OPAE filed appeals with the Ohio Supreme Court contesting the PUCO's approval of the Phase II Stipulation.⁶⁹ Briefing of this case proceeded through the summer of 2008 and oral arguments were held on November 18, 2008. As noted above, on February 19, 2009, the Court found that issues related to RSP prices/charges were moot because there was no effective remedy to the problems cited by OCC and OPAE - the RSP had expired so there was no prospective relief the PUCO could provide and Court precedent does not permit retroactive refunds.⁷⁰

On November 18, 2009, the Commission instructed its Staff to issue an RFP for a consultant to audit DE-Ohio's SRT Rider and on January 7, 2010 the Commission chose the consultant to perform the auditing work of DE-Ohio's SRT and FPP Riders for calendar year 2009 rates.⁷¹ The auditor is expected to complete its work in May 2010.

II. Fuel and Economy Purchased Power

The FPP Rider consists of fuel and purchased power expenses, a reconciliation adjustment, a system loss adjustment, emission allowances, and environmental reagents. As required by DE-Ohio's RSP case, on a quarterly basis DE-Ohio files the proposed FPP rate for the following quarter. Additionally, a backward-looking audit is conducted annually to verify the reasonableness of the FPP.

As required by its approved RSP, DE-Ohio filed a renewed Application for recovery of FPP costs on June 1, 2005.⁷² After an audit conducted by Energy Ventures Associates, Inc. ("EVA") of the FPP costs incurred from January 1, 2005 through June 30, 2005, DE-Ohio and Staff filed a Stipulation ("FPP Stipulation") on January 18, 2006 resolving the issues identified by EVA and the parties to this case. The FPP Stipulation delineated how DE-Ohio must report its coal contracts going forward; directed DE-Ohio to develop a methodology for allocating fuel costs or fuel contracts to an affiliate following the transfer of its generating units; provided that DE-Ohio shall not allocate

⁶⁸ *In the Matter of the Application of Duke Energy Ohio, Inc., to Establish its Fuel and Economy Purchased Power Component of its Market-Based Standard Service Offer for the Period of July 1, 2007, through December 31, 2008*, Opinion and Order (September 30, 2009).

⁶⁹ *Office of the Ohio Consumers' Counsel v. Public Utilities Commission of Ohio*, Court Case No. 2008-0466.

⁷⁰ *Ohio Consumers' Counsel v. Pub. Util. Comm.*, 121 Ohio St.3d 362, 2009-Ohio-604.

⁷¹ *In the Matter of the Application of Duke Energy Ohio, Inc., to Establish its Fuel and Economy Purchased Power Component of its Market-Based Standard Service Offer for 2009*, PUCO Case Nos. 09-974-EL-FAC, *et al.*, Entry (January 7, 2010).

⁷² *In the Matter of the Application of The Cincinnati Gas & Electric Company to Modify its Fuel and Economy Purchased Power Component of its Market-Based Standard Service Offer*, PUCO Case Nos. 05-806-EL-UNC, *et al.*, Application at 3-4 (June 1, 2005).

any part of its December 31, 2004 sulfur dioxide (“SO₂”) emission allowance (“EA”) bank to FPP customers; and made certain allocations for Environmental Protection Agency (“EPA”)-allotted zero-cost SO₂ EAs.⁷³ On February 6, 2006, the PUCO issued an Opinion and Order approving the Stipulation in its entirety.⁷⁴

DE-Ohio filed its Application for approval of the 2006 FPP component of its SSO on September 1, 2006, pursuant to the RSP Entry on Rehearing.⁷⁵ EVA and Larkin & Associates (“Larkin”) filed their m/p audit of the fuel procurement activities recovered by the FPP Rider (for the previous four quarters, from July 1, 2005 through June 30, 2006) on October 12, 2006. EVA and Larkin recommended, among other things, that DE-Ohio cease its “active management” of its fuel procurement and adopt traditional utility procurement strategies, and also suggested that DE-Ohio should not be permitted to purchase reserve capacity from its DENA assets. This FPP approval proceeding was put on hold by the November 29, 2006 Attorney Examiner Entry addressing the Ohio Supreme Court’s remand of the RSP to the PUCO. A subsequent PUCO Entry addressing the RSP remand allowed DE-Ohio to continue adjusting the FPP quarterly in 2007, but did not address or approve the July 1, 2005 through June 30, 2006 FPP charges.

The PUCO, in approving the Phase II Stipulation, resolved outstanding issues regarding the FPP. The Phase II Stipulation: provided customers an FPP credit, as a result of the settlement of coal contracts; moved the recovery of congestion costs to DE-Ohio’s FPP; and allowed DE-Ohio to continue its active management of its coal, EA, and purchased power portfolio.⁷⁶ The PUCO also gave its blessing to a Phase II Stipulation provision requiring DE-Ohio to commence talks to discuss the terms and conditions under which DE-Ohio could actively manage its coal, EA, and purchased power portfolio, including addressing the m/p auditor’s recommendation that DE-Ohio procure fuel and EAs beyond the end of the RSP period (December 31, 2008).

On September 4, 2007, DE-Ohio filed its Application for approval of the FPP charge for 2008.⁷⁷ As discussed in the SRT section, a Stipulation was filed proposing to resolve

⁷³ *In the Matter of the Application of The Cincinnati Gas & Electric Company to Modify its Fuel and Economy Purchased Power Component of its Market-Based Standard Service Offer*, PUCO Case No. 05-806-EL-UNC, Stipulation and Recommendation (January 18, 2006).

⁷⁴ *In the Matter of the Application of The Cincinnati Gas & Electric Company to Modify its Fuel and Economy Purchased Power Component of its Market-Based Standard Service Offer*, PUCO Case No. 05-806-EL-UNC, Opinion and Order (February 6, 2006).

⁷⁵ *In the Matter of the Application of The Cincinnati Gas & Electric Company to Modify its Fuel and Economy Purchased Power Component of its Market-Based Standard Service Offer*, PUCO Case Nos. 05-725-EL-UNC, *et al.*, Application (September 1, 2006).

⁷⁶ *In the Matter of the Application of The Cincinnati Gas & Electric Company to Adjust and Set its System Reliability Tracker Market Price*, PUCO Case Nos. 05-724-EL-UNC, *et al.*, Opinion and Order at 13-16 (November 20, 2007).

⁷⁷ *In the Matter of the Application of Duke Energy Ohio, Inc. to Establish its Fuel, Economy Purchased Power Component of its Market-Based Standard Service Offer for the Period of July 1, 2007 through December 31, 2008*, Case No. 07-974-EL-UNC, Application (September 4, 2007).

issues related to DE-Ohio's SRT and FPP for the July 1, 2006 through June 30, 2007 time period.⁷⁸ The SRT/FPP Cost Review Stipulation required DE-Ohio to take certain steps with regards to its fuel procurement active management program, temporarily foreclosed the possibility of a disallowance of costs due to an outage at DE-Ohio's Zimmer plant, and required DE-Ohio to make certain changes with regards to the operations of its coal plants. Finally, the SRT/FPP Cost Review Stipulation committed DE-Ohio to make a true-up filing in the first quarter of 2009 for the SRT and FPP Riders as well as for AAC Rider reagents costs. As noted above, Initial and Reply Briefs were filed on January 8, 2008 and January 15, 2008, respectively, and the Commission adopted the Stipulation in its entirety on February 27, 2008.

As also noted above, OCC and OPAE filed appeals with the Ohio Supreme Court contesting the PUCO's approval of the Phase II Stipulation in March 2008.⁷⁹ Briefing of this case proceeded through the summer of 2008 and oral arguments were held on November 18, 2008. Again, as discussed above, on February 19, 2009, the Court affirmed the PUCO's decision and found that issues related to RSP prices/charges were moot because there was no effective remedy to the problems cited by OCC and OPAE.

III. Annually Adjusted Component

The AAC was created in DE-Ohio's RSP and compensates DE-Ohio for actual expenses related to increases in the cost of environmental compliance, security, and taxes above December 31, 2000 levels. The initial AAC Rider for calendar years 2005 and 2006 was set by the PUCO in its RSP Entry on Rehearing. DE-Ohio filed its first update to its AAC Rider on September 5, 2006 in order to set AAC levels for 2007 bills.⁸⁰ A hearing on the update was continued indefinitely as a result of the RSP remand proceeding and the AAC charge was continued into 2007 at 2006 levels.⁸¹ However, pursuant to the Phase II Stipulation, the PUCO permitted DE-Ohio to: adjust

⁷⁸ *In the Matter of the Application of Duke Energy Ohio, Inc. to Adjust and Set its 2008 System Reliability Tracker*, PUCO Case Nos. 07-975-EL-UNC, *et al.*, Stipulation and Recommendation (December 13, 2007). As noted above, the PUCO also approved a Stipulation regarding the FPP Rider for the July 1, 2007 through December 31, 2008 period. See *In the Matter of the Application of Duke Energy Ohio, Inc., to Establish its Fuel and Economy Purchased Power Component of its Market-Based Standard Service Offer for the Period of July 1, 2007, through December 31, 2008*, Opinion and Order (September 30, 2009).

⁷⁹ *Office of the Ohio Consumers' Counsel v. Public Utilities Commission of Ohio*, Court Case No. 2008-0466.

⁸⁰ *In the Matter of The Application of Duke Energy Ohio, Inc. to Adjust and Set the Annually Adjusted Component of its Market Based Standard Service Offer ("MBSSO")*, PUCO Case No. 06-1085-EL-UNC, Application (September 5, 2006).

⁸¹ *DE-Ohio RSP Remand Proceeding*, Entry at 4-5 (December 20, 2006).

its AAC to collect \$74 million;⁸² collect an AAC true-up to January 1, 2007; and recoup construction work in progress (“CWIP”) costs through the AAC.⁸³

On September 4, 2007, DE-Ohio filed its Application for approval of its 2008 AAC Rider.⁸⁴ A hearing on the 2008 AAC Application was held on December 13-14, 2007 and briefs were filed on December 21, 2007. On January 16, 2008, the PUCO approved DE-Ohio’s Application, permitting DE-Ohio to collect 2008 AAC charges of approximately \$111 million.⁸⁵

On August 28, 2008, DE-Ohio filed an Application to modify its AAC, effective December 1, 2008 and the PUCO approved DE-Ohio’s Application on November 25, 2008.⁸⁶ The PUCO also reserved the right to reconsider its AAC approval if it made a material modification to the Stipulation filed in DE-Ohio’s ESP (see above) that resulted in provisions related to the AAC being ineffective.⁸⁷

DE-Ohio filed an Application to update its AAC on September 1, 2009 and an unopposed Stipulation was filed on November 19, 2009. The Commission approved the stipulated AAC adjustment on December 16, 2009, which included a \$156.7 million revenue requirement for Rider AAC.⁸⁸

IV. RSP Extension

On August 2, 2006, DE-Ohio filed a proposal to modify its MBSSO, beginning January 1, 2009, and continuing for an indefinite time.⁸⁹ DE-Ohio withdrew its

⁸² *DE-Ohio RSP Remand Proceeding*, Phase II Stipulation at Attachment 2 (page 1 of 8) (April 4, 2007).

⁸³ *In the Matter of the Application of The Cincinnati Gas & Electric Company to Adjust and Set its System Reliability Tracker Market Price*, PUCO Case Nos. 05-724-EL-UNC, *et al.*, Opinion and Order at 11, 21-24 (November 20, 2007).

⁸⁴ *In the Matter of the Application of Duke Energy Ohio, Inc., to Adjust and Set the 2008 Annually Adjusted Component of its Market-Based Standard Service Offer*, PUCO Case No. 07-973-EL-UNC, Application (September 4, 2007).

⁸⁵ *In the Matter of the Application of Duke Energy Ohio, Inc., to Adjust and Set the 2008 Annually Adjusted Component of its Market-Based Standard Service Offer*, PUCO Case No. 07-973-EL-UNC, Opinion and Order (January 16, 2008). The PUCO re-emphasized that the stage of completion of CWIP should not be a bar to DE-Ohio earning a return on CWIP, and also denied OCC’s request that the PUCO require an m/p audit of DE-Ohio’s AAC Rider.

⁸⁶ *In the Matter of the Application of Duke Energy Ohio, Inc., to Adjust and Set the Annually Adjusted Component of its Market-Based Standard Service Offer*, PUCO Case No. 08-1025-EL-UNC, Finding and Order (November 25, 2008).

⁸⁷ *Id.* at 4.

⁸⁸ *In the Matter of the Application of Duke Energy Ohio, Inc., to Adjust and Set the Annually Adjusted Component of its Market-Based Standard Service Offer*, PUCO Case No. 09-770-EL-RDR, Finding and Order (December 16, 2009).

⁸⁹ *In the Matter of the Application of Duke Energy Ohio to Modify its Market-Based Standard Service Offer*, PUCO Case No. 06-986-EL-UNC, Application (August 2, 2006).

Application on November 30, 2007, citing the likely affect of pending energy restructuring legislation on Ohio law as the reason for its withdrawal.⁹⁰

V. Transmission Cost Recovery Rider

At the same time that DE-Ohio was establishing and implementing the various riders approved in the RSP, it also filed an Application to levy a TCR Rider (which was also created and approved in the RSP proceeding) to recover costs associated with taking transmission service from the MISO.⁹¹ The PUCO approved most aspects of the Application as submitted. However, the PUCO rejected DE-Ohio's proposal to recover "other incremental costs" (i.e., internal costs) that were not specifically addressed in DE-Ohio's RSP.⁹² Additionally, the PUCO mandated that FERC-ordered reductions in DE-Ohio's transmission rate should flow back through the TCR Rider and required semi-annual filings to modify and true-up the TCR Rider.

In accordance with the PUCO's Finding and Order approving the TCR Rider, DE-Ohio submitted proposed TCR Rider rates in May 2006 for billing cycles beginning June 2006. On June 14, 2006, the PUCO suspended the TCR Rider update and ordered DE-Ohio's then-current TCR Rider rates to remain in effect (subject to true-up) until Staff completed its review of costs included in the TCR Rider.⁹³ DE-Ohio submitted its semi-annual amendment to its TCR Rider (for rates effective on December 1, 2006) on October 15, 2006 and subsequently modified the filing on November 3, 2006. Staff filed its report on DE-Ohio's TCR Rider on November 16, 2006, finding that the costs included in the proposed rider for December 2006 through May 2007 were appropriately included and also proposed that, on a biennial basis, DE-Ohio should provide a detailed report of each of the costs Staff identified as within DE-Ohio's control and a description of all actions taken by DE-Ohio to minimize these costs. Staff also recommended that it should be authorized to audit the costs included in the TCR Rider to determine if DE-Ohio had minimized controllable costs.⁹⁴ On November 28, 2006, the PUCO accepted DE-Ohio's proposed TCR Rider for December 2006 through May 2007 and also adopted Staff's recommendation regarding the biennial review of DE-Ohio's TCR Rider.⁹⁵ A subsequent Staff review concluded that DE-Ohio properly included and calculated the controllable RTO-related costs/credits in its TCR Rider rates.⁹⁶ Pursuant to its RSP, DE-Ohio's TCR Rider rates

⁹⁰ *In the Matter of the Application of Duke Energy Ohio to Modify its Market-Based Standard Service Offer*, PUCO Case No. 06-986-EL-UNC, Notice of Withdrawal (November 30, 2007).

⁹¹ *In the Matter of the Transmission Rates Contained in the Rate Schedules of The Cincinnati Gas & Electric Company and Related Matters*, PUCO Case Nos. 05-727-EL-UNC, et al., Application at 2 (June 3, 2005) (hereinafter, "*DE-Ohio TCR Rider Proceeding*").

⁹² *DE-Ohio TCR Rider Proceeding*, Finding and Order at 7 (October 5, 2005).

⁹³ *DE-Ohio TCR Rider Proceeding*, Entry at 3 (June 14, 2006).

⁹⁴ *DE-Ohio TCR Rider Proceeding*, Staff Report at 1-2 (November 16, 2006).

⁹⁵ *DE-Ohio TCR Rider Proceeding*, Entry (November 28, 2006).

⁹⁶ *DE-Ohio TCR Rider Proceeding*, Staff's Biennial Review of Controllable RTO Costs for Duke Energy-Ohio (November 27, 2007).

since May 2007 have been adjusted semi-annually. Finally, in May 2008, the PUCO adopted suggestions contained within Staff's biennial review of controllable costs in DE-Ohio's TCR Rider. These suggestions included requiring DE-Ohio to: (1) continue to monitor and report on its load deviations between day-ahead and real-time; (2) collect data on all events that result in generation deviations and an allocation of revenue sufficiency guarantee costs; and, (3) collect data on all events that result in generation deviations and allocation of uninstructed deviation charges.⁹⁷

On July 17, 2009 (as updated on July 31, 2009), DE-Ohio filed an Application to adjust its TCR Rider and for a waiver of the Commission's rules in order to recover MISO costs for net congestion and losses, including net revenue received from financial transmission rights and auction revenue rights, through DE-Ohio's FPP Rider instead of through its TCR Rider.⁹⁸ After Staff filed a report recommending approval of DE-Ohio's proposal to reduce its TCR Rider by approximately \$24.4 million, the Commission approved the TCRR update as well as DE-Ohio's waiver request on September 23, 2009.⁹⁹

C. Electric Security Plan

On July 31, 2008 (the date that SB 221 became effective), DE-Ohio filed its proposed ESP¹⁰⁰ and on October 27, 2008 a Stipulation ("DE-Ohio ESP Stipulation") was filed resolving most of the issues in the case.¹⁰¹ Although the Stipulation resolved most issues, it left open for litigation the issue of bypassability of charges and shopping credits for residential governmental aggregation customers.¹⁰² Additionally, IEU-Ohio opposed the Stipulation on the grounds that it contained illegal restrictions on the opportunity for mercantile customers to seek and obtain an exemption (permitted by SB 221) from DE-Ohio charges associated with meeting the energy efficiency and peak demand reduction requirements contained within SB 221.

On December 17, 2008, the PUCO modified and approved the Stipulation.¹⁰³ Under the terms of the modified Stipulation, base generation rates increased approximately 2% in 2009, and a similar level of increase was set in place for establishing the 2010 and 2011 default service prices for non-residential customers. Similar increases apply to residential customers in 2009 and 2010 (but not 2011). Additionally, the PUCO

⁹⁷ DE-Ohio TCR Rider Proceeding, Entry at 3 (May 28, 2008).

⁹⁸ *In the Matter of the Application of Duke Energy Ohio to Update its Transmission Cost Recovery Rider*, PUCO Case No. 09-601-EL-UNC, Application (July 17, 2009).

⁹⁹ *In the Matter of the Application of Duke Energy Ohio to Update its Transmission Cost Recovery Rider*, PUCO Case No. 09-601-EL-UNC, Finding and Order (September 23, 2009).

¹⁰⁰ *In the Matter of the Application of Duke Energy Ohio for Approval of an Electric Security Plan*, Case Nos. 08-920-EL-SSO, et al., Application (July 31, 2008) (hereinafter cited as *DE-Ohio ESP Proceeding*).

¹⁰¹ *DE-Ohio ESP Proceeding*, Stipulation and Recommendation (October 27, 2008).

¹⁰² *DE-Ohio ESP Proceeding*, Stipulation and Recommendation at 32, FN 11 (October 27, 2008).

¹⁰³ *DE-Ohio ESP Proceeding*, Opinion and Order (December 17, 2008).

approved numerous riders that are subject to periodic adjustments, up or down, to recover additional generation,¹⁰⁴ transmission, ancillary service and distribution-related costs. Because DE-Ohio also had a distribution rate case pending before the PUCO, DE-Ohio's distribution rates were not recognized or addressed in the Stipulation.¹⁰⁵

The PUCO modified the Stipulation to allow residential customers participating in a governmental aggregation program to avoid paying DE-Ohio's SRT Rider, which is otherwise non-bypassable, if they elect to participate in a governmental aggregation program, but upon such election those customers will return during the term of the ESP to a "market-based" price for default generation supply instead of ESP-stabilized rates.¹⁰⁶ Additionally, the PUCO accepted IEU-Ohio's primary argument that the provision of the Stipulation preventing any "mercantile customer"¹⁰⁷ with demand of 3 megawatts ("MW") or less from seeking or obtaining an exemption from the rider recovering energy efficiency and peak demand reduction benchmarks compliance costs¹⁰⁸ was illegal and modified the Stipulation accordingly.¹⁰⁹

OCC and the Ohio Chapter of the Sierra Club jointly filed an Application for Rehearing while the Ohio Environmental Council ("OEC") also filed an Application for Rehearing. The PUCO denied the Applications for Rehearing on February 11, 2009. OCC appealed the Commission's decision on April 13, 2009, contesting the Commission's refusal to permit customers in residential aggregation programs who commit to returning at a market price (instead of the SSO price) to also avoid paying DE-Ohio's capacity dedication rider ("SRA-CD").¹¹⁰ This case has been fully briefed on appeal to the Ohio

¹⁰⁴ Many of the generation-related riders are the same as or recover similar costs as the riders contained within DE-Ohio's RSP.

¹⁰⁵ On December 15, 2008, DE-Ohio filed a letter indicating that implementation of the Stipulation would effectuate a total bill rate decrease of approximately 3.8% for residential customers, 4.4% for commercial customers, and 5.0% for industrial customers. The decrease is a result of an adjustment (reduction) in DE-Ohio's Rider to recover its fuel and purchased power costs.

¹⁰⁶ *DE-Ohio ESP Proceeding*, Opinion and Order at 26-28 (December 17, 2008). Rider SRT compensates DE-Ohio for the purchase of capacity to maintain service to switched customers.

¹⁰⁷ A "mercantile customer" is any non-residential customer that "consumes more than seven hundred thousand kilowatt hours per year or is part of a national account involving multiple facilities in one or more states." Section 4928.01(A)(19), Ohio Revised Code.

¹⁰⁸ DE-Ohio's program to meet the energy efficiency and peak demand reduction mandates is called Save-a-Watt. On December 29, 2009, DE-Ohio filed an Application essentially re-filing an updated Save-a-Watt program as its required three-year EE/PDR program portfolio plan under Rule 4901:1-39-04, Ohio Administrative Code. *In the Matter of the Report of Duke Energy Ohio, Inc., Concerning its Energy Efficiency and Peak Demand Reduction Programs and Portfolio Planning*, PUCO Case No. 09-1999-EL-POR, Programs Portfolio (December 29, 2010).

¹⁰⁹ *DE-Ohio ESP Proceeding*, Opinion and Order at 36-37 (December 17, 2008).

¹¹⁰ *Ohio Consumers' Counsel v. Pub. Util. Comm.*, Ohio Supreme Court Case No. 2009-0669, Notice of Appeal (April 13, 2009). Rider SRA-CD compensates DE-Ohio for providing customers with a first call on its capacity, foregoing the opportunity to sell capacity that is currently dedicated to its standard service offer, permitting customers to switch to competitive suppliers, and assuming the risk associated with maintaining a reasonably stable price during the ESP period. *DE-Ohio ESP Proceeding*, Opinion and Order at 27 (December 17, 2008).

Supreme Court and is awaiting the setting of a date for oral argument. Additionally, on Wednesday, January 20, 2010, the Ohio Supreme Court, citing Section 4928.20(J), Revised Code, asked the Parties in the appeal to file memoranda addressing three questions: (1) Are there any legislative authorities that formed or are forming governmental aggregation that are providing electric aggregation service in DE-Ohio's geographic service area?; (2) If the answer to question one is yes, has any such legislative authority elected not to receive standby service?; and (3) Should this cause be dismissed for failure to present a justifiable cause or controversy?¹¹¹ The memoranda are due by February 19, 2010 and replies are permitted if filed by March 8, 2010.

D. Distribution Rate Increases

DE-Ohio filed an Application to increase its distribution rates and to change its accounting procedures on February 17, 2005.¹¹² On December 6, 2005, an unopposed Stipulation and Recommendation ("Distribution Rate Case Stipulation") was filed that was subsequently adopted by the PUCO in its entirety on December 21, 2005.¹¹³ Among other things, the adopted Distribution Rate Case Stipulation authorized DE-Ohio to increase distribution rates by \$51.5 million (which resulted in an average 4.4% increase in most residential customer's bills). DE-Ohio was also required, among other things, to: (1) withdraw its request for a capital investment reliability rider and refrain from making a capital investment reliability rider request until 2007; (2) withdraw its proposed modification to its line extension policy; continue to fund its weatherization and energy assistance programs until 2009; and, (3) implement a non-residential demand side management ("DSM") tracker.¹¹⁴

In June 2008, DE-Ohio filed another Application with the PUCO to increase its distribution rates.¹¹⁵ On July 8, 2009, the Commission approved an unopposed Stipulation which permits DE-Ohio to increase its distribution revenues by \$55.3 million

¹¹¹ The questions that the Court has asked the parties to address suggest that the Court is concerned that the parties that have filed this appeal are asking the Court to rule on abstract or hypothetical questions. Generally, courts will not use their authority to resolve contested cases until and unless there is a real controversy.

¹¹² *In the Matter of the Application of The Cincinnati Gas & Electric Company for an Increase in Electric Distribution Rates*, PUCO Case Nos. 05-59-EL-AIR, *et al.*, Application (February 17, 2005).

¹¹³ *In the Matter of the Application of The Cincinnati Gas & Electric Company for an Increase in Electric Distribution Rates*, PUCO Case Nos. 05-59-EL-AIR, *et al.*, Opinion and Order at 7 (December 21, 2005).

¹¹⁴ *Id.* at 4-8. In 2007, the PUCO also approved a DE-Ohio Application to implement electric and natural gas DSM programs for residential, commercial, and industrial customers as well as a research DSM program. *In the Matter of the Application for Recovery of Costs, Lost Margin, and Performance Incentive Associated with the Implementation of Electric Residential Demand Side Management Programs by The Cincinnati Gas & Electric Company*, PUCO Case Nos. 06-91-EL-UNC, *et al.*, Finding and Order (July 11, 2007).

¹¹⁵ *In the Matter of the Application of Duke Energy Ohio for an Increase in Electric Distribution Rates*, Case Nos. 08-709-EL-AIR, *et al.*, Application (June 25, 2008) (hereinafter cited as *DE-Ohio 2008 Distribution Rate Case*).

annually.¹¹⁶ The PUCO-approved Stipulation also sets new depreciation rates for DE-Ohio, establishes pole attachment rates, initiates a mechanism by which DE-Ohio may recoup storm damage costs related to Hurricane Ike,¹¹⁷ and resolves issues related to DE-Ohio's rider governing back-up delivery point capacity.¹¹⁸

FirstEnergy (Ohio Edison ["OE"], Cleveland Electric Illuminating ["CEI"], and Toledo Edison ["TE"])

A. Rate Stabilization Plan

On October 21, 2003, FirstEnergy filed an Application with the PUCO for approval of a CBP (sometimes referred to as an auction process) to establish "market-based" rates effective January 1, 2006, or, in the alternative, to adopt an RSP for the period beginning January 1, 2006 through December 31, 2008.¹¹⁹ On February 11, 2004, an evidentiary hearing began and several parties submitted a partial Stipulation ("RSP Stipulation").¹²⁰

On June 9, 2004, the PUCO issued its Opinion and Order adopting the RSP Stipulation with the following significant modifications: the PUCO limited adjustments to generation charges during the RSP to cost increases related to material changes in tax regulations or laws; the PUCO denied FirstEnergy's proposed adjustment to the annual increases in shopping credits for 2005 and limited the shopping credit values to those in the ETP Stipulation but used the 2005 shopping credit level, separated by class, as the avoided cost cap for the RSP; the PUCO limited distribution rate increases, consistent with those in the ETP Stipulation; the PUCO held that \$10 million of additional funding for energy efficiency programs should be divided equally between energy efficiency programs and economic development activities; the PUCO scheduled a meeting of the parties to determine the best approach to bill shopping customers for retail transmission, net congestion, and ancillary services once the MDP ends, and directed FirstEnergy to meet with Staff to recalculate new sales target levels for recovery of RTCs; and, the PUCO directed FirstEnergy to submit a pricing plan for POLR prices for returning customers, as well as its methodology for the supply of market support generation

¹¹⁶ *DE-Ohio 2008 Distribution Rate Case*, Opinion and Order at 8 (July 8, 2009).

¹¹⁷ During the rate case DE-Ohio filed a Motion for accounting authority to create a regulatory asset for storm restoration costs related to Hurricane Ike. The accounting authority requested by DE-Ohio was approved by the PUCO on January 14, 2009.

¹¹⁸ *Id.* at 9-10.

¹¹⁹ *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company and the Toledo Edison Company for Authority to Continue and Modify Certain Regulatory Accounting Practices and Procedures, for Tariff Approvals and to Establish Rates and Other Charges Including Regulatory Transition Charges Following the Market Development Period*, PUCO Case No. 03-2144-EL-ATA, Application (October 21, 2003) (hereinafter, "*FirstEnergy RSP Proceeding*").

¹²⁰ *FirstEnergy RSP Proceeding*, Stipulation and Recommendation (February 11, 2004). The Stipulation was signed by FirstEnergy, Ohio Energy Group ("OEG"), Ohio Hospital Association ("OHA"), Ohio Partners for Affordable Energy ("OPAE"), Cargill, and IEU-Ohio.

("MSG"), within 90 days of the PUCO's Order. Additionally, the PUCO directed FirstEnergy to conduct a CBP, as modified by the PUCO, which encompassed FirstEnergy's total load (including certain special contracts) to cover its risk of providing POLR service for the entire 2006-2008 period. On August 4, 2004, the PUCO issued an Entry on Rehearing that gave FirstEnergy the ability to file an application to adjust generation charges during 2006-2008, required FirstEnergy to supply MSG to maintain minimum levels of shopping, made transmission and ancillary charges avoidable by shopping customers, and changed the 2005 shopping credit cap from a rate class basis to a rate schedule basis. On September 29, 2004, the PUCO issued a Second Entry on Rehearing that clarified that the deadline for calculating the MSG requirements should be the latter of December 31, 2004, or 45 days after the PUCO ruled on the CBP results and OPAE and other low-income agencies could receive funding for low-income energy efficiency projects from the \$5 million reallocated by the PUCO.

Pursuant to the PUCO's finding that a CBP should be conducted to determine whether the RSP generation charges would exceed market prices as such prices were determined through a CBP, on September 1, 2004, FirstEnergy designed its proposed CBP based on a New Jersey basic generation service ("BGS") supply procurement model.¹²¹ FirstEnergy also employed National Economic Research Associates Inc. ("NERA") as the independent auction manager as required by the PUCO's Order.

The CBP was conducted on December 8, 2004, by NERA, and was also observed by Charles River Associates, a consultant employed by the Staff to review and provide oversight of the auction. On December 9, 2004, NERA, Charles River Associates, and the Staff filed reports and recommendations to the PUCO. On the same day, the PUCO responded by issuing its Finding and Order that held that the final auction price of 5.45¢/kWh should be rejected inasmuch as the probability modeling determined that there was a 100% probability that the closing bid price was higher than the adjusted RSP price even before taking into account other factors that would have a downward influence on the adjusted RSP price.¹²²

Pursuant to another PUCO mandate, on July 22, 2005, FirstEnergy submitted its plan for a second CBP for 2007, which essentially mirrored the original CBP.¹²³ On September 28, 2005, the PUCO issued an Entry in which it, among other things, deferred the CBP until the end of March 2006 due to FirstEnergy's rate certainty plan ("RCP") filing (discussed below) as well as disruptions in energy supplies and pricing

¹²¹ *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company and The Toledo Edison Company for Approval of a Competitive Bid Process to Bid Out Their Retail Electric Load*, PUCO Case No. 04-1371-EL-ATA, Application at 2 (September 1, 2004).

¹²² *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company and The Toledo Edison Company for Approval of a Competitive Bid Process to Bid Out Their Retail Electric Load*, PUCO Case No. 04-1371-EL-ATA, Finding and Order at 3-4 (December 9, 2004).

¹²³ *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Approval of a Competitive Bidding Process for Retail Electric Load*, PUCO Case No. 05-936-EL-ATA, Application (July 22, 2005) (hereinafter, "*FirstEnergy 2005 CBP Proceeding*").

caused by Hurricane Katrina.¹²⁴ On January 25, 2006, the PUCO issued an Entry setting the starting price for the auction at 5.1¢/kWh, which it indicated was the upper bound of the PUCO's evaluation range.¹²⁵ On February 23, 2006, NERA informed the PUCO that insufficient supplier interest had been expressed in participating in the CBP process to warrant moving forward with the CBP process (no potential bidding party submitted an application to participate by the deadline). Accordingly, the PUCO closed the docket on September 6, 2006.¹²⁶

OCC and the Cities of Maumee, Northwood, Oregon, Perrysburg, Sylvania, Toledo, the Village of Holland and the Board of County Commissioners of Lucas County (collectively, the "Cities") appealed the PUCO's FirstEnergy RSP Order to the Ohio Supreme Court.¹²⁷ On May 3, 2006, the Ohio Supreme Court upheld the PUCO's approval of most aspects of FirstEnergy's RSP but remanded the case to the PUCO asserting that it failed to comply with a statutory requirement that gave customers an alternative means of securing generation supply. The statutory alternative required the PUCO to give customers the option to elect to receive service at prices established through competitive bids or other means providing similar opportunities.¹²⁸

The PUCO responded to the Ohio Supreme Court's ruling by opening a docket to conduct a CBP and FirstEnergy filed a CBP plan on September 29, 2006.¹²⁹ Interested parties filed Initial and Reply Comments regarding FirstEnergy's proposed CBP and a Stipulation and Recommendation ("CBP Stipulation") was ultimately submitted for the PUCO's consideration. The CBP Stipulation recommended that the PUCO permit FirstEnergy to move forward with the CBP that it originally proposed (including agreed-upon modifications), but also required FirstEnergy to offer a green product tariff allowing customers to voluntarily choose to purchase generation supply produced from "renewable sources" by buying renewable energy credits ("REC").¹³⁰ Participating

¹²⁴ *FirstEnergy 2005 CBP Proceeding*, Entry at 2 (September 28, 2005).

¹²⁵ *FirstEnergy 2005 CBP Proceeding*, Entry at 9 (January 25, 2006).

¹²⁶ *FirstEnergy 2005 CBP Proceeding*, Entry at 3 (September 6, 2006).

¹²⁷ See *The Office of the Consumers' Counsel v. The Public Utilities Commission of Ohio*, Court Case No. 2004-1993; affirmed in part and reversed in part by *Consumers' Counsel v. Pub. Util. Comm.*, 109 Ohio St.3d 328, 2006-Ohio-2110. The Court granted an OCC Motion to Consolidate two other appeals with the 2004-1993 appeal, joining *City of Maumee*, *City of Northwood*, *City of Oregon*, *City of Perrysburg*, *City of Sylvania*, *City of Toledo*, *Village of Holland*, *Board of County Commissioners of Lucas County v. The Public Utilities Commission of Ohio*, Court Case No. 2005-0118 and *The Office of the Ohio Consumers' Counsel v. The Public Utilities Commission of Ohio*, Court Case No. 2005-0766, July 5, 2005, *Case Announcements*, 2005-Ohio-3437.

¹²⁸ *Ohio Consumers' Counsel v. Pub. Util. Comm.*, 109 Ohio St.3d 328, 2006-Ohio-2110, at ¶19.

¹²⁹ *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company, and the Toledo Edison Company for Authority to Establish a Competitive Bid Process to Supply Market-Based Generation*, PUCO Case No. 06-1112-EL-UNC, Application (September 29, 2006) (hereinafter "*FirstEnergy 2006 CBP Proceeding*").

¹³⁰ *FirstEnergy 2006 CBP Proceeding*, Stipulation and Recommendation at 3 (May 29, 2007). FirstEnergy, Staff, and OCC signed the Stipulation.

customers were required to purchase a minimum of two 100 kWh blocks per month, up to a maximum of fifty 100 kWh blocks per month. The CBP Stipulation also recommended that the PUCO permit FirstEnergy to create a regulatory asset or liability for recovery or refund in its next distribution rate case if the amounts collected from customers under the program were less than or more than the amounts incurred by FirstEnergy for payments to winning bidders for RECs and allow FirstEnergy to recover the administrative costs of running the program. The PUCO approved the CBP Stipulation in its entirety on August 15, 2007.¹³¹ FirstEnergy subsequently filed tariffs indicating that the REC for each 100 kWh block could be purchased for 50¢/month.

B. Rate Certainty Plan

On May 27, 2005, FirstEnergy filed an application for approval of a generation charge adjustment factor (“GCAF”) Rider (“GCAF Application”), pursuant to its RSP, in which it sought to recover the estimated amount of fuel cost increases over the 2002 base year during 2006.¹³² Additionally, on September 9, 2005, FirstEnergy filed a series of applications that collectively represented FirstEnergy’s RCP proposal (hereinafter, “RCP Application”).¹³³ Along with its RCP Application, FirstEnergy filed a Stipulation signed by multiple parties supporting the proposed RCP. The proposed RCP created a fuel cost recovery mechanism and set forth a recovery methodology for new regulatory assets, and also focused on certain other accounting modifications. FirstEnergy also incorporated the previously filed GCAF Application into the proposed RCP Stipulation and addressed rising fuel costs, variability in rates, and the manner in which the FirstEnergy companies would mitigate the impacts of increased fuel costs on customers’ bills.¹³⁴ The RCP Stipulation provided that base distribution rates would not increase for OE and TE customers until January 1, 2009 and would remain frozen for CEI customers until May 1, 2009, with the exception that the FirstEnergy companies were permitted to apply for increases related to incremental taxes or in the event of an emergency. The FirstEnergy RCP Stipulation also reduced deferred shopping incentive

¹³¹ *FirstEnergy 2006 CBP Proceeding*, Order on Remand (August 15, 2007). On a separate but related note, the PUCO also gave certain customers an alternative method to receive market-based generation service from FirstEnergy in 2008, approving a FirstEnergy application to extend its experimental market-based tariff (“MBT”) until the end of 2008. *In the Matter of the Application of The Cleveland Electric Illuminating Company for Extension of the Existing Experimental Market-Based Tariff*, PUCO Case Nos. 07-227-EL-ATA, *et al.*, Finding and Order (November 28, 2007). The MBT afforded qualifying general service customers the opportunity to subject a limited percentage of their usage to hourly, market-based pricing. *Id.* at 1.

¹³² *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Approval of a Generation Charge Adjustment Rider*, PUCO Case No. 05-704-EL-ATA, Application (May 27, 2005).

¹³³ *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Authority to Modify Certain Accounting Practices and for Tariff Approvals*, PUCO Case Nos. 05-1125-EL-ATA, *et al.*, Application (September 9, 2005) (hereinafter, “*FirstEnergy RCP Proceeding*”).

¹³⁴ *Id.* at 3. FirstEnergy also filed, and the PUCO approved, a Motion to Consolidate the GCAF case with the RCP Application inasmuch as approval of the RCP would render the GCAF Application moot.

balances for each of the FirstEnergy companies and proposed that the companies' increased fuel costs of up to \$75 million, \$77 million, and \$79 million in 2006, 2007, and 2008, respectively, would be recovered from all OE and TE distribution and transmission customers through a fuel recovery mechanism ("FRM"). FirstEnergy proposed that fuel costs above the set amounts recovered through the FRM would be deferred for recovery in a future FirstEnergy distribution rate case.

The PUCO modified and approved the proposed RCP Stipulation on January 4, 2006. The Stipulation was modified to require the PUCO's consultant in the next CBP auction (March 2006) to impute the anticipated fuel cost deferral into FirstEnergy's "price to beat" (the reference price used to evaluate the results of the CBP), thereby increasing the price to beat and providing a more level playing field for the CBP. Additionally, the PUCO altered the Stipulation to require FirstEnergy to demonstrate to Staff, on a monthly basis, actual fuel cost increases so that Staff could verify the proper amount of fuel costs to be deferred (capitalized as a regulatory asset) and also mandated that the deferred distribution expenses yield necessary improvements in a shorter time frame than usual to compensate for the special accounting treatment given to such expenditures.¹³⁵

On January 10, 2006, FirstEnergy filed a Motion for Clarification, seeking to further refine the review process of the distribution deferrals, as mandated in the PUCO's Opinion and Order.¹³⁶ In particular, FirstEnergy sought permission to record deferrals prior to the annual staff review and clarification of the types of costs and the related amounts allowed to be deferred. On January 25, 2006, the PUCO issued an Entry on Rehearing that allowed FirstEnergy to book fuel and distribution deferrals on a monthly basis (after January 1, 2006) instead of waiting until after the Staff's annual review of the deferrals, revised the categories of costs that may be subject to deferral to parallel the categories recommended in the Stipulation, and changed the methodology by which the PUCO would limit the expenses deferred to the amount in excess of the expense levels included in the current rates.¹³⁷

Elyria Foundry and WPS Energy Services ("WPS") appealed the PUCO's approval of FirstEnergy's RCP to the Ohio Supreme Court after the PUCO denied their Applications for Rehearing.¹³⁸ Oral arguments were held on February 27, 2007. In August 2007, the Ohio Supreme Court affirmed in part and reversed in part the PUCO's approval of the RCP.¹³⁹ The Ohio Supreme Court upheld all aspects of the RCP except one, finding that the PUCO violated Ohio's state policy to avoid anti-competitive subsidies when it

¹³⁵ *FirstEnergy RCP Proceeding*, Opinion and Order (January 4, 2006).

¹³⁶ *FirstEnergy RCP Proceeding*, Motion for Clarification of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company (January 10, 2006).

¹³⁷ *FirstEnergy RCP Proceeding*, Entry on Rehearing (January 25, 2006).

¹³⁸ *Elyria Foundry Company v. The Public Utilities Commission of Ohio*, Ohio Supreme Court Case No. 2006-0830; affirmed in part and reversed in part by *Elyria Foundry Co. v Pub. Util. Comm.*, 114 Ohio St.3d 305, 2007-Ohio-4164.

¹³⁹ *Elyria Foundry Co. v Pub. Util. Comm.*, 114 Ohio St.3d 305, 2007-Ohio-4164.

permitted FirstEnergy to defer generation-related fuel costs for collection from all customers (including shopping customers) through distribution rates.¹⁴⁰

In response to the Ohio Supreme Court's decision, FirstEnergy filed an Application on Remand at the PUCO to recover the fuel costs addressed by the Ohio Supreme Court.¹⁴¹ FirstEnergy's Application proposed two separate riders, one to recover the fuel costs deferred since the inception of the fuel deferral (called the Deferred Fuel Rider ["DFR"]) under the RCP until September 30, 2007 and a second rider (called the "Fuel Rider" ["FR"]) to recover ongoing fuel costs from September 30, 2007 through December 31, 2008.¹⁴² FirstEnergy's Application requested recovery of both the deferred and ongoing fuel charges (beginning in October 2007 and running through the first quarter of 2009), as well as permission to recover the fuel costs on a kWh basis.¹⁴³

On January 9, 2008, the PUCO denied in part and granted in part FirstEnergy's Application.¹⁴⁴ The PUCO denied FirstEnergy's request to collect the fuel costs deferred during 2006-2007 in calendar year 2008, ruling that collecting these fuel costs (plus carrying costs) in a single year would be unreasonable as it would cause rates to rise substantially. Instead, the PUCO directed FirstEnergy to file within 30 days a separate application with an alternative recovery mechanism to collect the 2006-2007 deferred fuel costs and carrying costs. However, the PUCO did approve FirstEnergy's request to recover ongoing fuel costs (those incurred beginning on January 1, 2008), reasoning that it is in consumers' best interests to pay the charges now rather than defer the costs and incur carrying charges on those costs for future recovery. The PUCO also noted the FR will be adjusted and reconciled quarterly and further ordered an audit of the FR at the end of 2008 to ensure that the fuel costs were just and reasonable as well as to reconcile the fuel costs. FirstEnergy was ordered to make quarterly submissions, at least 30 days before the start of each quarter, so that Staff could review FirstEnergy's proposed FR charge for the upcoming quarter.

¹⁴⁰ *Id.* at ¶¶57-58. The Court subsequently denied FirstEnergy's Motion for Reconsideration of its decision. *November 21, 2007 Case Announcements*, 2007-Ohio-6140.

¹⁴¹ *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Authority to Modify Certain Accounting Practices and for Tariff Approvals*, PUCO Case Nos. 07-1003-EL-ATA, *et al.*, Application (September 10, 2007).

¹⁴² *Id.* at 5.

¹⁴³ FirstEnergy's proposed timeframe for collection of the fuel costs (17 months) was significant inasmuch as FirstEnergy proposed in its distribution rate case to spread the recovery of the fuel costs over a 25-year period. See *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Authority to Increase Rates for Distribution Service, Modify Certain Accounting Practices and for Tariff Approval*, PUCO Case Nos. 07-551-EL-AIR, *et al.*, Application (June 7, 2007).

¹⁴⁴ *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Authority to Modify Certain Accounting Practices and for Tariff Approvals*, PUCO Case Nos. 07-1003-EL-ATA, *et al.*, Finding and Order (January 9, 2008).

As ordered by the PUCO, on February 8, 2008 FirstEnergy filed an Application proposing an alternative mechanism to recover the 2006-2007 fuel costs.¹⁴⁵ FirstEnergy proposed to recover the applicable fuel cost deferrals beginning with the first billing cycle in June 2008, but no later than the first billing cycle in January 2009, through a separate generation rider for each of its operating companies based on an annual revenue requirement associated with each of the operating companies' deferred fuel cost, including carrying charges and an annual amortization expense based upon a recovery period set by the Commission. FirstEnergy left open the time period for recovery to the Commission's discretion (although it suggested that the recovery period be established between 5 and 25 years) and proposed that the approved charges allow the operating companies to also fully recover the deferred fuel costs, all associated carrying charges, applicable uncollectible expense and Commercial Activity Tax ("CAT") expense. FirstEnergy also suggested that if the Commission rejected its proposal that FirstEnergy be permitted to collect the projected balance over the time period between June 2008 and the last billing period in December 2008.

On June 4, 2008, Staff filed a Staff Report regarding FirstEnergy's deferred fuel costs, recommending recovery of \$197 million rather than FirstEnergy's requested \$207 million, but Staff did not take into account carrying costs and CAT implications. The hearing in this proceeding was ultimately continued (without a firm hearing date) in light of the resources needed to focus on FirstEnergy's ESP and market rate option ("MRO") proceedings (see Section D).¹⁴⁶

C. 2007 Auction Proceeding

On July 10, 2007, FirstEnergy filed an Application to set its SSO generation price, beginning January 1, 2009, through an auction process.¹⁴⁷ FirstEnergy proposed two alternatives, suggesting the solicitation of bids to serve customers on either a load class or "slice-of-system" basis. FirstEnergy also advocated for a descending clock auction and the procurement of generation over multiple solicitations throughout the year, with prices being blended to arrive at a single price in order to smooth out potentially volatile market prices. FirstEnergy proposed limiting suppliers to providing a maximum of 75% of the SSO supply and further suggested that the auction plan include PUCO authority to phase-in rates for residential customers in order to limit price increases to no more than 15% per year (including changes in distribution charges resulting from the pending

¹⁴⁵ *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Authority to Modify Certain Accounting Practices and for Tariff Approvals*, PUCO Case Nos. 08-124-EL-ATA, et al., Application (February 8, 2008).

¹⁴⁶ *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Authority to Modify Certain Accounting Practices and for Tariff Approvals*, PUCO Case Nos. 08-124-EL-ATA, et al., at 1 (August 25, 2008).

¹⁴⁷ *In the Matter of the Application of the Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Approval of a Competitive Bidding Process for Standard Service Offer Electric Generation Supply, Accounting Modifications Associated with Reconciliation Mechanism and Phase in, and Tariffs for Generation Service*, PUCO Case Nos. 07-796-EL-ATA, et al., Application (July 10, 2007) (hereinafter, "*FirstEnergy Auction Proceeding*").

distribution rate case). Additionally, FirstEnergy included a reconciliation mechanism to adjust generation pricing to retail customers to ensure that billed amounts do not exceed the costs FirstEnergy incurs and to ensure that FirstEnergy collects adequate amounts to pay SSO suppliers in full for SSO generation service. FirstEnergy also: proffered a generation service rate design and tariffs based solely on kWh charges instead of the demand charges and declining block structure included in FirstEnergy's current tariffs; incorporated demand response and conservation components into its proposal; and continued its "green power" program.

After a technical conference, the PUCO requested stakeholders file both Initial and Reply Comments, with its Staff's comments filed in between the due dates for the Initial and Reply Comments. In the Initial Comments, various parties: criticized the pricing implications of an auction; questioned the existence of an effectively competitive market; lamented the market power held by FES, FirstEnergy's unregulated affiliate; and favored the "load class" approach for allocating the results of a CBP and establishing SSO generation-related prices. Marketers and AEP were supportive of FirstEnergy's proposal, with AEP urging the PUCO to conduct a statewide auction. The PUCO's Staff then filed comments expressing the view that a competitive market had not yet developed and urged the PUCO to reject FirstEnergy's filing.¹⁴⁸ Reply commenters then focused on whether a competitive market existed and whether an auction could produce reasonable prices. It is worth noting that during the period of time that these issues were being considered by the PUCO, the legislative process that ultimately produced SB 221 in 2008 was gaining traction. Accordingly, the advocacy of stakeholders in the PUCO venue was affected by the positioning that was part of the legislative process. On August 1, 2008, after SB 221 became effective, FirstEnergy filed a Motion to Withdraw its Application and close this proceeding inasmuch as SB 221 removed the PUCO's authority to approve FirstEnergy's Application.

D. Electric Security Plan and Market Rate Option Cases

I. FirstEnergy's Initial ESP and MRO Applications

On July 31, 2008 (the effective date of SB 221), FirstEnergy simultaneously filed an ESP and an MRO for the PUCO's consideration in order to establish its new SSO pursuant to SB 221. FirstEnergy proposed an ESP with a three-year term from 2009 through 2011, indicating that if the Commission so chose, it could terminate the final year of the ESP.¹⁴⁹ FirstEnergy also filed an MRO that would serve as the default

¹⁴⁸ *FirstEnergy Auction Proceeding*, Staff Comments on the FirstEnergy Companies' Proposed Competitive Bidding Process (September 21, 2007). Among other things, Staff cited the failure of wholesale markets to discipline prices to reasonable levels, pointing to the dramatic price increases caused by market-based rates in Maryland and Illinois, and further noted its belief that FirstEnergy's customers would be "plagued by dramatic price increases such as those that have resulted in states where competitive procurements relying on wholesale markets have been used" if the PUCO were to approve FirstEnergy's auction proposal. *Id.* at 7.

¹⁴⁹ *In the Matter of the Application of the Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Authority to Establish a Standard Service Offer Pursuant* {C29886:4 }

option should the PUCO modify or deny its ESP or if FirstEnergy did not accept changes made by the PUCO to its ESP.¹⁵⁰ Finally, within the ESP, FirstEnergy proposed a four-month short-term ESP that required PUCO approval by November 14, 2008 to become effective on January 1, 2009 through April 31, 2009 in order to provide the PUCO with additional time to review the ESP or work through a CBP as part of FirstEnergy's MRO. FirstEnergy's short-term ESP was the byproduct of a rather common recognition that the Commission was not likely to satisfy the statutory requirement requiring the PUCO to issue orders in response to these applications within a specified amount of time.

FirstEnergy's ESP defined the SSO price during the three-year period and also included provisions for transmission service, economic development, alternative energy resources and energy efficiency. The proposed ESP would have also resolved the pending distribution rate case and the deferred fuel cost recovery case, among other features. FirstEnergy proposed an increase in base SSO rates each year, as well as additional increases that were to be collected through rider mechanisms.

FirstEnergy's MRO included a proposal for an initial bid process in which one-third of the total SSO load of all three companies would be bid out for the period from January 1, 2009 through May 31, 2010; one-third of the total SSO load for all three companies for the period from the January 1, 2009 through May 31, 2011 would be bid out; and one-third of the total SSO load for all three companies for the period from January 1, 2009 through May 31, 2012 would be put out for bid. After the initial CBP, in each calendar year starting in 2009, FirstEnergy would hold two CBPs, in October and January, to obtain one-third of the power requirements of all three companies' POLR load for a three-year period. FirstEnergy proposed this approach to smooth out the pricing effects of potentially volatile market prices. The CBP proposal utilized a "slice-of-system" approach (bidders will bid on tranches of total SSO customer load) and also featured a reconciliation mechanism.

On November 25, 2008, the PUCO issued an Order denying FirstEnergy's MRO Application.¹⁵¹ The PUCO determined that FirstEnergy did not prove that it had met the requirements contained within SB 221 to proceed to a CBP to serve its load. FirstEnergy filed an Application for Rehearing of the PUCO's Opinion and Order on December 22, 2008 and parties to the case filed Memoranda Contra FirstEnergy's Application for Rehearing on January 2, 2009. The PUCO granted FirstEnergy's Application for Rehearing to further consider the matters raised by FirstEnergy. But, the

to Section 4928.143, Revised Code, in the Form of an Electric Security Plan, PUCO Case No. 08-935-EL-SSO, Application (July 31, 2008), (hereinafter "FE ESP Proceeding").

¹⁵⁰ *In the Matter of the Application of the 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 Modifications Associated with Reconciliation Mechanism, and Tariff for Generation Service*, PUCO Case No. 08-936-EL-SSO, Application (July 31, 2008), (hereinafter "FE MRO Proceeding").

¹⁵¹ *FE MRO Proceeding*, Opinion and Order (November 25, 2008).

statutory decisional clock that the PUCO was obligated to follow had expired setting the stage for the chaos that followed.¹⁵²

On December 19, 2008, the PUCO issued its Opinion and Order in the FirstEnergy ESP Proceeding, significantly modifying FirstEnergy's proposed ESP.¹⁵³ On December 22, 2008, FirstEnergy exercised its statutorily-granted right and filed a letter at the PUCO withdrawing and terminating its ESP. On that same day, FirstEnergy also made a tariff filing to continue, in most cases,¹⁵⁴ its current rates until an ESP or MRO is authorized and in place. Additionally, FirstEnergy announced that it would issue an RFP to serve its SSO customers from January 5, 2009 through March 31, 2009.

After permitting a very brief comment opportunity for intervenors and a reply comment opportunity for FirstEnergy on FirstEnergy's proposal to continue its current rate plan, the PUCO issued an Order on January 7, 2008 to continue FirstEnergy's rate plan pursuant to Section 4928.143, Revised Code.¹⁵⁵ The PUCO determined that, except for CEI,¹⁵⁶ FirstEnergy's RTC charges should end as of December 31, 2008 inasmuch as there was a specific end date of December 31, 2008 established in the most recent rate plan and the full RTC amounts have been collected. The Commission also eliminated the FRM and the RTC Offset Rider ("RTCO") for all three companies. The Commission found that FirstEnergy could continue its RSC and shopping credits inasmuch as there was no specific end date established other than the point at which the rate plan itself ended. The PUCO also permitted FirstEnergy to continue its fuel rider for the limited purpose of collecting the remaining 2008 actual fuel costs. Finally, the PUCO explained that, pursuant to Section 4928.143, Revised Code, FirstEnergy could apply for fuel cost recovery. The PUCO required FirstEnergy to file its compliance tariffs by Monday, January 12, 2009.

On January 9, 2009, FirstEnergy filed an Application for Rehearing and a Motion to Stay the PUCO's January 7, 2009 Order continuing its current rate plan. The Attorney Examiner granted FirstEnergy's request to delay filing its compliance tariffs. However, on January 14, 2009, the PUCO issued a subsequent order that, in light of the PUCO approving a rider to recover FirstEnergy's purchased power costs (see below), required FirstEnergy to file tariffs consistent with its January 7, 2009 Order.

¹⁵² The resulting chaos was most profound in the case of FirstEnergy's interruptible or non-firm customers.

¹⁵³ *FE ESP Proceeding*, Opinion and Order (December 19, 2008).

¹⁵⁴ On or about December 22, 2008 FirstEnergy began notifying customers with interruptible service components that there would be significant changes to the protocols used by FirstEnergy to call interruptions as well as the pricing of buy-through service. FirstEnergy implemented these changes on or about January 1, 2009 over the protests of affected customers.

¹⁵⁵ *FE ESP Proceeding*, Finding and Order (January 7, 2009). After receiving comments regarding whether Section 4928.143 or Section 4928.141, Revised Code, applied in this circumstance, the PUCO determined that Section 4928.143, Revised Code, controlled for purposes of continuing FirstEnergy's current rate plan.

¹⁵⁶ The RTC charges for CEI will continue because they are not slated to expire until December 31, 2010.

As noted above, in the midst of its PUCO proceedings, FirstEnergy also announced that it had conducted a successful RFP for generation supply from January 5, 2009 through March 31, 2009.¹⁵⁷ The auction price settled at a price “consistent with” 6.98¢ per kWh. FirstEnergy subsequently filed an Application at the PUCO for approval of Rider FUEL to recover its purchased power costs.¹⁵⁸ The Rider FUEL applied a retail surcharge to all SSO retail electric customers (beginning January 1, 2009) for the difference in all costs incurred by FirstEnergy to purchase power for SSO customers and the unbundled generation revenue received for each of the customer classes (as set out in the current rate plan). FirstEnergy proposed to update the charge, the reconciliation, and the forecasted costs and revenues on a quarterly basis.

The PUCO approved FirstEnergy’s Rider FUEL Application on January 14, 2009. The PUCO directed FirstEnergy to make a filing by February 2, 2009 that included testimony and provided information sufficient for the PUCO to conduct a prudence review of the costs incurred and to determine whether the recovery of such costs was necessary to avoid a confiscatory result. The Commission noted that the PUCO was approving the request to comply with its Constitutional requirements¹⁵⁹ and the PUCO would examine whether the costs were prudent at a later date. Finally, the PUCO permitted CEI to defer its Rider FUEL costs for future recovery.¹⁶⁰ FirstEnergy filed its Rider FUEL tariff schedules on January 16, 2009.

On January 23, 2009, FirstEnergy filed a motion for an extension of time to file its testimony and a suspension of the requirement that FirstEnergy make any filing with respect to the "confiscatory result" issue pending resolution of this issue on rehearing. FirstEnergy also requested a procedural schedule that recognized the rebuttable presumption of management prudence in utility decisions, contending that it should not be required to file evidence that its purchased power costs were prudent unless and until the PUCO first determines that the evidence presented by intervenors and Staff overcomes the presumption of prudence. FirstEnergy’s motion was granted in part and denied in part. The Attorney Examiner required FirstEnergy to file on February 2, 2009 information such as the final post-RFP report and other information that was available to

¹⁵⁷ See http://www.firstenergycorp.com/NewsReleases/Ohio_RFP_Release.pdf (last accessed on January 16, 2009). FirstEnergy purchased power from the MISO spot market to supply customers from January 1, 2009 through January 4, 2009.

¹⁵⁸ *In the Matter of the Application of the Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Approval of Rider FUEL and Related Accounting Authority*, PUCO Case Nos. 09-21-EL-ATA,, *et al.*, Application (January 9, 2009).

¹⁵⁹ The prices that FirstEnergy paid for the wholesale supply purchased to meet the needs of its SSO or non-shopping customers were and are subject to the regulatory jurisdiction of the FERC. Under a doctrine known as the “filed rate doctrine” and by the force of the Supremacy Clause of the United States Constitution, a state regulator may not block retail recovery of wholesale prices that FERC has determined to be “just and reasonable”. Notwithstanding these legal concepts, a state regulatory may disallow recovery in cases where the state regulator finds that the costs were imprudently incurred (where a lower cost option was available, for example).

¹⁶⁰ CEI is the only operating company whose RTC charge continued past December 31, 2008.

bidders, but permitted FirstEnergy an extension of time to file testimony and supporting evidence pertaining to prudency issues until the PUCO orders otherwise. As required by the Attorney Examiner, FirstEnergy timely filed the final post-RFP report on February 2, 2009.

II. Electric Security Plan Settlement

On January 29, 2009, the PUCO issued an Entry directing its Staff to develop a proposal to establish an ESP for FirstEnergy and circulate the proposal among the parties in the ESP case.¹⁶¹ The Entry also requested FirstEnergy and others to seriously consider Staff's proposal and asked FirstEnergy to reconsider its decision to withdraw its ESP. The Entry ordered Staff to conduct a conference with the parties in the ESP case on February 5, 2009, to discuss Staff's proposal and the possibility of an agreement on that proposal. After extensive settlement discussions, on February 19, 2009, FirstEnergy filed an Amended Application in its ESP Case and a Stipulation signed by many of the intervening parties. On February 26, 2009 a Supplemental Stipulation was filed that contained refinements to the original Stipulation (largely dealing with governmental aggregation) that was joined by additional signatory parties. The Stipulation, as supplemented, was not opposed by the non-signatory Parties in the ESP case.

The as-supplemented Stipulation contained an interim term ESP that resolved issues related to the procurement of power to serve FirstEnergy's retail SSO customers from April 1, 2009 through May 31, 2009, as well as a long term ESP for the SSO from June 1, 2009 through May 31, 2011 period. The stipulating parties recommended that the PUCO act by March 4, 2009 on the limited term ESP and recommended that the Commission act, by March 25, 2009, on the remaining long-term ESP provisions of the Stipulation.

The PUCO approved the portion of the Stipulation regarding the limited term ESP on March 4, 2009.¹⁶² The limited term ESP provided that, for the April 1, 2009 through May 31, 2009 period, FirstEnergy would obtain from FES the necessary energy, capacity, and resource adequacy requirements to serve FirstEnergy's retail SSO load and the load for special contracts at the rate of \$66.68 per megawatt hour ("MWh"). The \$66.68 per MWh wholesale rate was adjusted for distribution line losses and the interim term ESP specified that FirstEnergy would recover MISO charges for the SSO load and special contract load through FirstEnergy's transmission rider. The Stipulation also requested the PUCO find that the procurement process used to acquire power from January through March 2009 period was not imprudent and the stipulating parties agreed that they would not challenge the recovery or amount of supply costs for the January through March 2009 period.

¹⁶¹ *FE ESP Proceeding*, Entry (January 29, 2009).

¹⁶² *FE ESP Proceeding*, Second Finding and Order (March 4, 2009).

The Stipulation also permitted FirstEnergy to continue deferring purchased power costs for CEI for the April through May 2009 period and set the interest rate on the deferrals. Additionally, the Stipulation addressed issues related to interruptions and buy through arrangements for interruptible customers for the period prior to June 1, 2009 and required the withdrawal of (as well as the future filing of) Complaint cases pending at the PUCO related to FirstEnergy's buy through policy if the PUCO approved the Stipulation. Finally, the Stipulation also called for the PUCO to find that all special contracts terminate on the dates specified in the RCP Stipulation approved in the FirstEnergy RCP Case as well as set a generation price of \$0.05 per kWh for April 2009 and May 2009 for domestic automaker facilities that use more than 50 million kWhs annually.

On March 25, 2009 the PUCO approved the remaining provisions of the Stipulation regarding FirstEnergy's SSO generation price for the June 1, 2009 through May 31, 2009 period.¹⁶³ Under the approved Stipulation, retail generation rates for June 1, 2009 through May 31, 2011 were determined by a descending-clock format CBP and FirstEnergy procured, on a slice of system basis, 100 percent of the aggregate wholesale "full requirements" SSO supply. The Stipulation also explicitly indicated bidding would be for a single two-year product and there would not be a load cap for bidders (*i.e.* FES may participate without limitation).¹⁶⁴ The Stipulation also contemplated a possible phase-in of generation prices resulting from the CBP in an amount not to exceed, in the aggregate for all three companies, \$300 million in 2009, \$500 million in 2010, and \$200 million in 2011, provided FirstEnergy had the ability to finance the additional funds. As it turned out, the phase-in was not needed because of the results of the CBP process that followed. The Stipulation also prohibited minimum stay provisions for residential and small commercial non-aggregation customers, eliminated RSC charges effective June 1, 2009, explicitly noted that all generation rates for the Stipulated ESP period are avoidable, and prohibited shopping credit caps

The Stipulation also blessed FirstEnergy's modified Economic Load Response Program Rider ("Rider ELR") and Optional Load Response Program Rider ("Rider OLR"), discounted rates for certain qualifying schools, and required that any revenue shortfall resulting from the application of a \$1.95 per kW interruptible credit in Rider ELR and Rider OLR will be recovered as part of an unavoidable Demand Side Management and Energy Efficiency Rider ("Rider DSE"). Further, the Stipulation established a Generation Service Uncollectible Rider, instituted a distribution rate freeze until December 31, 2011 (subject to the SEET and certain other factors), and approved a

¹⁶³ FE ESP Proceeding, Second Opinion and Order (March 25, 2009).

¹⁶⁴ Two separate concurring opinions as well as one opinion concurring and dissenting were filed by the Commissioners. All of the separate opinions addressed whether a cap should be placed on the amount of load that a single supplier may bid on and acquire through the CBP. Chairman Schriber and Commissioner Fergus joined an opinion that concluded that it is unknown whether a load cap is beneficial. Commissioners Centolella and Lemmie joined an opinion that expressed a preference for a 65% bid cap. Commissioner Roberto filed a dissenting opinion, dissenting on the grounds that a bid cap of 50% should be imposed by the Commission.

Delivery Service Improvement Rider (“Rider DSI”) for April 1, 2009 through December 31, 2011 for the purpose of improving the overall performance of the distribution system, including reliability of the distribution systems.

The Stipulation further provided for the creation of riders to recover distribution uncollectible expenses, deferred distribution costs, deferred transmission costs, demand side management and energy efficiency program costs, and percentage of income payment plan (“PIPP”) uncollectible costs. FirstEnergy also wrote off 50% of CEI’s extended RTC balance (approximately \$215 million) with the remaining RTC balance recoverable, with any additional amounts collected through the RTC used to reduce the purchased power deferral that arose for CEI for the January 1, 2009 through May 31, 2009 period (the period for the chaos that took place after the PUCO modified FirstEnergy’s ESP -- after the statutory clock had run -- and FirstEnergy exercised its statutory right to reject the PUCO’s as-modified ESP).

Additionally, the Stipulation noted that there would be no company-funded energy efficiency and AMI programs as part of the Stipulation, but obligated FirstEnergy to develop a proposal to pursue federal funds available under the American Recovery and Reinvestment Act that may be available for Smart Grid investment.¹⁶⁵ The Stipulation further required FirstEnergy to develop an EE/PDR program for the period 2009 through 2011, including conducting a market study to identify EE/PDR opportunities. The costs associated with the EE/PDR program were made subject to recovery through the Rider DSE. Customers that committed their demand-response or other customer-sited capabilities for integration into FirstEnergy’s program were also given the opportunity to be exempted, with Commission approval, from FirstEnergy’s portfolio compliance cost recovery mechanism.

Further, FirstEnergy committed to contribute \$25 million to support economic development and job retention. The Stipulation also created a Reasonable Arrangements Rider and a Delta Revenue Recovery rider to recover delta revenues¹⁶⁶ associated with reasonable arrangements approved by the Commission with a separate unavoidable rider for existing CEI reasonable arrangements that continued past December 31, 2008.

¹⁶⁵ FE filed its proposed AMI/Smart Grid proposal on November 18, 2009. *In the Matter of the Application of the Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Approval of Ohio Site Deployment of the Smart Grid Modernization Initiative and Timely Recovery of Associated Costs*, PUCO Case Nos. 09-1820-EL-ATA, *et al.*, Application (November 18, 2009). FirstEnergy proposed to recover approximately \$36 million in AMI/Smart Grid costs from Ohio jurisdictional customers inasmuch as the other half of the AMI/Smart Grid costs associated with the planned Ohio site deployment were covered by a federal stimulus funds grant. IEU-Ohio objected to the volumetric rate design of the proposed rider to recover these costs and PUCO Staff suggested a fixed, per customer charge to recover FirstEnergy’s AMI/Smart Grid initiative costs. Initial and Reply Comments were filed in the case in January 2009. The PUCO has not yet issued an order in this case.

¹⁶⁶ Delta Revenues are defined by the PUCO as “the deviation resulting from the difference in rate levels between the otherwise applicable rate schedule and the result of any reasonable arrangement approved by the commission.” Rule 4901:1-38-01(C), O.A.C.

III. Auction to Set June 1, 2009 through May 31, 2011 Standard Service Offer Generation Price

The descending clock auction required by the Supplemental Stipulation was conducted on May 13, 2009 and May 14, 2009.¹⁶⁷ The CBP produced a final wholesale auction load-weighted average price of \$61.50 per MWh for FirstEnergy customers for the June 1, 2009 through May 31, 2011 period. The PUCO accepted the results of the CBP on May 14, 2009.

IV. Accelerated Recovery of Deferred Distribution Costs Due to Auction Results

On July 27, 2009, FirstEnergy filed two separate applications (one for non-residential customers and another for residential customers) requesting permission to recover deferred distribution costs (RCP distribution deferrals, line extension deferrals, and transition tax deferrals) from customers more rapidly than that authorized in its distribution rate case.¹⁶⁸ FirstEnergy reasoned that the lower than expected generation price stemming from the auction in its ESP case created an opportunity to collect these deferrals now instead of over a longer period of time, thus generating savings of approximately \$142 million for non-residential customers and \$178 million for residential customers in carrying costs on deferred balances that otherwise would accrue if collected over the original time frames established in the distribution rate case. FE's Application proposed to recover these deferred balances over the 18 winter months between September 2009 and May 2011 (the rider would be zero during June, July, and August of 2010) instead of over 25 years for the RCP distribution deferrals and five years for the line extension and transition tax deferrals. FirstEnergy proposed to update the rider three times between September 2009 and May 2011. Finally, FirstEnergy explained that the recovery period for CEI customers would be the same as OE and TE customers, but that the rider charge would be set at a higher level from January 2011 through May 2011 as compared to the September 2009 through December 2010 period to coincide with the termination of RTC charges for CEI customers. On July 28, 2009, FirstEnergy filed a letter indicating that a coalition of consumer and environmental groups (including the OCC) called the Ohio Consumer and Environmental Advocates ("OCEA") supported FirstEnergy's request and that they had agreed to terms of the Fuel Fund Grant ("FFG") Program contemplated by the Supplemental Stipulation approved by the Commission in the ESP Proceeding.¹⁶⁹ Specifically, FirstEnergy agreed to make an additional \$2.5 million available to the FFG Program, which provides electric bill assistance to eligible residential customers, and not seek recovery of such amount from customers. The Commission approved FirstEnergy's Application on August 19, 2009.

¹⁶⁷ *FirstEnergy ESP Proceeding*, Finding and Order (May 14, 2009).

¹⁶⁸ *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Approval of a Residential Distribution Deferral Rider*, PUCO Case Nos. 09-641-EL-ATA, *et al.*, Application (July 27, 2009).

¹⁶⁹ Specifically, OCEA agreed to support the Application pertaining to residential customers and to not oppose the Application pertaining to non-residential customers.

V. Market Rate Option Application to Set Standard Service Offer Generation Price beginning June 1, 2011

On October 20, 2009, FirstEnergy filed an Application pursuant to Sections 4928.141 and 4928.142, Revised Code, and Rule 4901:1-35, O.A.C., for approval from the PUCO of an MRO plan to secure SSO generation supply when the current ESP expires on May 31, 2009. Approval of the MRO Application would permit FirstEnergy to conduct a CBP, outside of the context of an ESP, to obtain generation supply for SSO service beginning on June 1, 2011. An evidentiary hearing was held in December 2009 and parties filed Initial and Reply Briefs on January 8, 2010 and January 15, 2010, respectively.

While the PUCO has a clear statutory obligation to issue a decision on an MRO application within a time period that ends ninety days after the application filing date¹⁷⁰, the Commission has not done so in this case. FirstEnergy's latest MRO Application is awaiting Commission action as of the date of this report.

E. Energy Efficiency and Peak Demand Reduction Portfolio Plans

On December 15, 2009, FE filed a three-year EE/PDR program portfolio plan for PUCO approval in accordance with Rule 4901:1-39-04, O.A.C. FE's proposed plan, if approved as proposed, would collect costs (through Rider DSE) of \$76.5 million in 2010, \$65.3 million in 2011, and \$72.6 million in 2012 associated with meeting the EE/PDR benchmarks.¹⁷¹ A procedural schedule was issued in this proceeding on January 14, 2010 which establishes several due dates for testimony and other items and sets the hearing in this case to begin on March 2, 2010.

F. Recovery of Regional Transmission Organization Costs

Pursuant to its RSP, FirstEnergy filed an Application with the PUCO to change its tariffs to incorporate transmission and ancillary service-related costs under MISO's Open Access Transmission Tariff and Transmission Energy Market Tariff ("MISO Tariffs") and for permission to modify accounting procedures.¹⁷² Multiple parties submitted a

¹⁷⁰ Section 4928.142, Revised Code. An EDU that receives the PUCO's approval to establish the default generation supply price through the MRO option is not permitted thereafter to use the ESP option.

¹⁷¹ *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Approval of Their Energy Efficiency and Peak Demand Reduction Program Portfolio Plans for 2010 through 2012 and Associated Cost Recovery Mechanism*, PUCO Case Nos. 09-1947-EL-POR, *et al.*, Program Portfolio and Initial Benchmark Report at 3 (December 15, 2009).

¹⁷² *In the Matter of the Application of the Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Approval of a Rider for the Collection of RTO Costs and Transmission and Ancillary Service Costs and for Authority to Modify Their Accounting Procedures*, PUCO Case No. 04-1932-EL-ATA, Application (December 30, 2004).

Stipulation and Recommendation (“RTO Cost Stipulation”)¹⁷³ to the PUCO that recommended, among other things, that the PUCO permit FirstEnergy to recover – on a dollar-for-dollar basis – the MISO Tariff charges through a cost recovery mechanism in effect from January 1, 2006 through December 31, 2008 and authorize FirstEnergy to remove these costs from base rates and include them in a TCR. The PUCO approved the Stipulation without any material alterations on August 31, 2005.

However, OCC filed a motion to reject the RTO cost recovery tariffs FirstEnergy filed on November 1, 2005, claiming that FirstEnergy included costs not approved in the PUCO’s Opinion and Order. In a December 21, 2005 Finding and Order, the PUCO denied OCC’s motion and accepted the filed tariffs. OCC appealed the PUCO’s decision to the Ohio Supreme Court. OCC subsequently withdrew its appeal on December 14, 2006.¹⁷⁴

On April 27, 2006, FirstEnergy filed an Application with revised transmission and ancillary service (“TAS”) riders, to be effective July 1, 2006. On February 1, 2007, FirstEnergy filed a Stipulation signed by OCC and OPAE that: urged the PUCO to approve FirstEnergy’s April 27, 2006 filing; recognized that MISO charges associated with revenue sufficiency guarantees (“RSG”) are the type of charges that may be collected through the transmission and ancillary service riders; resolved concerns (through the funding and implementation of DSM programs) regarding the effectiveness and implementation of the RCP Stipulation agreed to by the PUCO; asked the PUCO to open a new docket to consider transmission and ancillary service rider issues in the future; and required OCC to not participate in the Elyria Foundry appeal of FirstEnergy’s RCP plan.¹⁷⁵ The PUCO approved the Stipulation in its entirety and also ordered a biennial review (per Staff’s request) of the transmission and ancillary services riders to determine if FirstEnergy’s management and operating processes are minimizing controllable transmission and ancillary services costs.¹⁷⁶

¹⁷³ *In the Matter of the Application of the Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Approval of a Rider for the Collection of RTO Costs and Transmission and Ancillary Service Costs and for Authority to Modify Their Accounting Procedures*, PUCO Case No. 04-1932-EL-ATA, Stipulation and Recommendation (July 22, 2005). The signatory parties to the Stipulation included FirstEnergy, IEU-Ohio, OCC, OPAE, and PUCO Staff. Dominion Retail signed the Stipulation as a non-opposing party.

¹⁷⁴ *See The Office of Ohio Consumers’ Counsel v. The Public Utilities Commission of Ohio*, Court Case No. 2006-0600. *December 19, 2006 Case Announcements*, 2006-Ohio-6709. In a related appeal by OCC regarding recovery of RTO costs, the Court upheld the PUCO’s decision allowing FirstEnergy and DP&L to defer collection of RTO charges until after the MDP ends. *See Ohio Consumers’ Counsel v. Pub. Util. Comm.*, 111 Ohio St.3d 384, 2006-Ohio-5853.

¹⁷⁵ *In the Matter of the Application of the Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Approval of a Rider for the Collection of RTO Costs and Transmission and Ancillary Service Costs and for Authority to Modify Their Accounting Procedures*, PUCO Case Nos. 04-1932-EL-ATA and 07-128-EL-ATA, Finding and Order at 3-6 (February 14, 2007).

¹⁷⁶ *Id.* at 8.

On June 2, 2008, Staff filed its biennial review on controllable RTO costs included in FirstEnergy's TAS.¹⁷⁷ Staff generally found that FirstEnergy should be authorized to include the presented costs/credits in its transmission rider update and recommended that FirstEnergy continue to monitor and provide updates on net congestion costs/revenues, net transmission losses, revenue sufficiency guarantee costs, and revenue neutrality uplift charges. Staff also made some specific recommendations: (1) FirstEnergy should provide updated details on issues identified by the PUCO's Staff with each of its update filings, including a discussion of any actions taken by FirstEnergy or MISO to minimize these costs; and, (2) FirstEnergy should provide a breakdown of revenue neutrality uplift ("RNU") costs it proposes to include in the rider with each rider update filing so that the amount of RNU related to RSG can be determined.

On October 17, 2008, FirstEnergy filed proposed revisions to its transmission rates, for recovery beginning January 1, 2009, or the effective date on which distribution rates approved in its distribution rate case (see below) become effective.¹⁷⁸ FirstEnergy proposed to decrease its transmission rates currently in effect, with average decreases of 10% for OE, 17% for CEI, and 6% for TE. FirstEnergy explained the decreased rates resulted mainly from lower projected costs in 2009, as well as a net over-collection for 2008 cost recoveries made through September 2008. The PUCO approved FirstEnergy's Application on December 19, 2008, but extended FirstEnergy's current transmission and ancillary services tariffs until the distribution rate design and tariff structure was determined in FirstEnergy's pending distribution rate case, at which time the rider would become effective. The PUCO also modified the Application to incorporate recommended changes from Staff as well.

On October 16, 2009, FirstEnergy filed an Application to revise its TAS Rider pursuant to Section 4928.05(A)(2), Revised Code, and Chapter 4901:1-36, O.A.C.¹⁷⁹ FirstEnergy filed an amended Application on December 3, 2009, revising its request to credit all customers, on an unavoidable basis, an over-collection of \$68.9 million. The PUCO approved FirstEnergy's Application on December 16, 2009 and required FirstEnergy to

¹⁷⁷ *In the Matter of the Application of the Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Approval of a Rider for the Collection of RTO Costs and Transmission and Ancillary Service Costs and for Authority to Modify Their Accounting Procedures*, PUCO Case Nos. 04-1932-EL-ATA and 07-128-EL-ATA, Staff's Biennial Review of Controllable RTO Costs (June 2, 2008).

¹⁷⁸ *In the Matter of the Application of the Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Approval of a Transmission Cost Recovery Rider*, PUCO Case Nos. 08-1172-EL-ATA, *et al.*, Application (October 17, 2008).

¹⁷⁹ *In the Matter of the Application of the Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company to Revise its Transmission and Ancillary Services Rider*, PUCO Case No. 09-968-EL-ATA, Application (October 16, 2009).

provide PUCO Staff with ongoing monthly cost and revenue data in order to ensure that the proposed TAS rates are terminated, if necessary, prior to December 31, 2010.¹⁸⁰

G. Distribution Rate Case

On June 7, 2007, FirstEnergy filed an Application for permission to increase its distribution rates.¹⁸¹ A partial Stipulation was submitted by multiple parties settling revenue distribution and non-residential rate design issues, but the remainder of the case was litigated. On January 21, 2009, the PUCO issued an Opinion and Order modifying and approving FirstEnergy's application.¹⁸² The PUCO authorized a rate of return of 8.48% for each of FirstEnergy's operating companies, which resulted in a revenue increase of \$69.9 million for OE, \$29.2 million for CEI, and \$38.5 million for TE.

The PUCO modified the partial settlement to require FirstEnergy to provide a discount to schools through a rider. The PUCO also ordered FirstEnergy to continue existing DSM programs at current program levels and to increase funding for the Community Connections Program to \$5 million per year. Additionally, the PUCO approved the tariff consolidation proposed by FirstEnergy that combines all of the existing distribution service schedules into a total of eight distribution service rate schedules. Two riders designed to mitigate the drastic impact that the rate schedule consolidation will have on some customers on certain rate schedules was also approved.¹⁸³

The PUCO rejected OCC's recommendation for a separate proceeding to investigate FirstEnergy's service quality and reliability. Further, the PUCO declined to adopt FirstEnergy's proposal to continue its up-front payment concept for line extensions, noting that a rulemaking is pending on this topic. However, FirstEnergy must include all line extension expenditures in rate base until new line extension rules become effective. Finally, the PUCO established and set at zero a rider related to AMI and Modern Grid projects, but directed FirstEnergy to conduct a study on AMI and Modern Grid deployment options.

Commissioners Roberto and Centolella filed a Concurring and Dissenting Opinion, concurring with the entire Order but objecting to the baseline from which a deferral

¹⁸⁰ *In the Matter of the Application of the Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company to Revise its Transmission and Ancillary Services Rider*, PUCO Case No. 09-968-EL-ATA, Finding and Order (December 16, 2009).

¹⁸¹ *See In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Authority to Increase Rates for Distribution Service, Modify Certain Accounting Practices and for Tariff Approval*, PUCO Case Nos. 07-551-EL-AIR, *et al.*, Application (June 7, 2007) (hereinafter, "*FirstEnergy Distribution Rate Case*").

¹⁸² *FirstEnergy Distribution Rate Case*, Opinion and Order (December 21, 2007). This was the first distribution rate increase for OE since 1990 and the first distribution rate increase for TE and CEI since 1996.

¹⁸³ The riders are called the Residential Distribution Credit Rider ("Rider RDC") and the Business Distribution Credit Rider ("Rider BDC").

amount (stemming from the RCP case) related to certain distribution expenses was calculated. Chairman Schriber filed a Concurring Opinion supporting the Commission's decision on the chosen baseline.

AEP (Ohio Power [“OP”] and Columbus Southern Power [“CSP”])

A. Rate Stabilization Plan

AEP filed its proposed RSP on February 9, 2004¹⁸⁴ and on January 26, 2005; the PUCO approved AEP's RSP, despite it being the only RSP that did not include a settlement supported by a majority of the parties and did not include a market-based SSO or a CBP even to test AEP's proposed SSO.¹⁸⁵ The PUCO approved AEP's requested 3% and 7% automatic annual increases in generation prices for the years 2006, 2007, and 2008 for CSP and OP, respectively, and the additional annual generation rate increases, capped at 4% above the 3% and 7% automatic increases.¹⁸⁶ The PUCO indicated that the rate increases would be avoidable by shopping customers but ignored the fact that practically no shopping had occurred in AEP's service territory and that all parties agreed that the market was a “no show.”¹⁸⁷ The PUCO also approved AEP's proposal to freeze distribution rates through 2008 at the level in effect on December 31, 2005, subject to adjustment for: emergencies; changes in transmission/distribution allocations under FERC's seven-factor test; and, increased distribution expenses due to changes in environmental requirements, security, taxes, O&M requirements imposed by federal or state legislative and regulatory bodies, and major storm damage restoration.¹⁸⁸

¹⁸⁴ *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of a Post-Market Development Period Rate Stabilization Plan*, PUCO Case No. 04-169-EL-UNC, Application (February 9, 2004).

¹⁸⁵ *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of a Post-Market Development Period Rate Stabilization Plan*, PUCO Case No. 04-169-EL-UNC, Opinion and Order (January 26, 2005).

¹⁸⁶ *Id.* at 18, 21. The additional generation increases subject to the 4% annual cap are for increased expenditures for complying with changes in laws, rules or regulations related to environmental requirements, taxes, and security; or for customer load switches that materially jeopardize AEP's ability to recover the anticipated generation revenues.

¹⁸⁷ *Id.* at 18.

¹⁸⁸ *Id.* at 22-23. The PUCO concluded without explanation that a distribution rate case before 2008 would run counter to its ultimate goals of rate and financial stability. Additionally, the PUCO denied AEP's request to defer RTO administrative charges and CWIP for recovery after the RSP, but then directed AEP to recover those same amounts through a non-bypassable POLR Rider applicable to all distribution customers. The PUCO approved requested deferrals for consumer education, choice implementation, transition plan and RSP filing costs. The PUCO authorized AEP to adjust transmission charges to reflect FERC-approved rates and charges during the RSP, including RTO administrative charges, amortization of RTO start-up costs, and recovery of lost transmission revenues, but changed the requested expedited PUCO approval process for the pass-through from 30-days to 60-days. The PUCO approved AEP's proposal to not charge the regulatory asset charge rider to the first 20% of OP residential customer load that switches, until January 1, 2008. The PUCO directed AEP to use \$14 million in unused shopping incentives for the benefit of CSP and OP low-income customers and economic development during the RSP. Finally, the PUCO also encouraged AEP to move forward with a plan to construct an integrated

On March 23, 2005, the PUCO denied all Applications for Rehearing.¹⁸⁹ On April 29, 2005, OCC filed an appeal to the Ohio Supreme Court.¹⁹⁰ Consistent with its remand of FirstEnergy's RSP, the Ohio Supreme Court remanded the case to the PUCO with instructions for the PUCO to conduct a CBP.¹⁹¹ The Ohio Supreme Court's decision also explicitly permitted OCC to bring another appeal on any of the other assignments of error that the Ohio Supreme Court did not address.

In response to the Ohio Supreme Court's remand, the PUCO required AEP to file a proposal for a CBP, which AEP submitted to the PUCO on September 22, 2006.¹⁹² After a technical conference to discuss AEP's proposal, interested parties filed Initial and Reply Comments regarding AEP's proposed CBP. A Stipulation and Recommendation ("AEP CBP Stipulation") was submitted for the PUCO's consideration.¹⁹³ The AEP CBP Stipulation proposed a voluntary Green Pricing Option through which customers would pay an additional rider (on top of the standard service rates and riders) in return for AEP procuring power from renewable sources by buying RECs at prices determined through a competitive bid. Participating customers were required to purchase a minimum of two 100 kWh blocks per month, up to a maximum of fifty 100 kWh blocks per month.¹⁹⁴ The AEP CBP Stipulation also permitted AEP to create a regulatory asset or liability, to the extent that the amounts collected from customers do not match the payments to winning bidders, for recovery or refund in its next distribution rate case. AEP was also allowed

gasification combined-cycle ("IGCC") generating facility in Ohio and noted that it was exploring regulatory mechanisms by which utilities might recover the costs of new IGCC facilities.

¹⁸⁹ Applications for Rehearing were filed by OCC; OEG; IEU-Ohio; the Ohio Gas Marketers Group ("OGMG") in conjunction with PSEG Energy Resources & Trade, LLC and Constellation Energy Commodities Group, Inc.; and the Low Income Associates ("LIA") (consisting of the Appalachian People's Action Coalition ["APAC"]), Lima/Allen Council on Community Affairs, OPAE, and WSOS Community Action.

¹⁹⁰ *The Office of the Ohio Consumers' Counsel v. The Public Utilities Commission of Ohio*, Court Case No. 2005-0767, Notice of Appeal (April 29, 2005); reversed in *Ohio Consumers' Counsel v. Pub. Util. Comm.*, 109 Ohio St.3d 511, 2006-Ohio-3054.

¹⁹¹ *Ohio Consumers' Counsel v. Pub. Util. Comm.*, 109 Ohio St.3d 511, 2006-Ohio-3054, at ¶1.

¹⁹² *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of Their Plan to Provide Additional Options for Customer Participation in the Electric Market*, PUCO Case No. 06-1153-EL-UNC, Columbus Southern Power Company's and Ohio Power Company's Plan to Provide Additional Options for Customer Participation in the Electric Market (September 22, 2006).

¹⁹³ *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of Their Plan to Provide Additional Options for Customer Participation in the Electric Market*, PUCO Case No. 06-1153-EL-UNC, Stipulation and Recommendation (March 23, 2007).

¹⁹⁴ The cost of each block is 70¢ per 100 kWh block. *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of Their Plan to Provide Additional Options for Customer Participation in the Electric Market*, PUCO Case No. 06-1153-EL-UNC, Tariff Filing (August 27, 2007).

to recover the administrative costs of running the program. The PUCO approved the CBP Stipulation in its entirety on May 2, 2007.¹⁹⁵

B. Discretionary Generation Increase Applications Permitted by Rate Stabilization Plan

I. 2007 Increase

As permitted by its RSP, on January 23, 2007, AEP filed for PUCO approval of a discretionary increase in its generation rates, asking for \$24.5 million from CSP customers and \$8.2 million from OP customers.¹⁹⁶ AEP proposed to collect the monies through a Generation Cost Recovery Rider (“GCRR”) from May 2007 through December 2007 in order to recover costs associated with environmental compliance, generation-related Sarbanes-Oxley (“SOX”) requirements, and compliance with North American Reliability Corporation (“NERC”) security requirements for generating units. Pursuant to the RSP, and after PUCO’s rejection of requests to delay implementation, the proposed discretionary generation increase went into effect in May 2007 on an interim basis and subject to true-up.

On October 3, 2007, the PUCO issued its Opinion and Order approving AEP’s Application for a discretionary generation increase, subject to the PUCO’s modifications.¹⁹⁷ The PUCO authorized AEP to recover \$19.9 million and \$3.9 million from CSP and OP customers, respectively, including carrying costs for expenditures incurred through February 2007 on environmental compliance costs. The PUCO found that discretionary generation increases would only be permitted for expenses: (1) incurred (*not projected*) at the time of the discretionary generation increase application; (2) that represent an increase in expenditures in excess of the baseline approved in AEP’s RSP; and (3) that have been the result of AEP complying with changes in laws, rules, or regulations since the RSP. Additionally, the approved amounts were reduced to reflect the applicability of a federal tax statute that affects AEP’s taxable income as well as to factor in AEP’s off-system sales. In accordance with its decision to only allow recovery for costs actually incurred, the PUCO denied AEP’s request to recover amounts anticipated for compliance with SOX as well as O&M costs for NERC Critical Infrastructure Protection security requirements. AEP was permitted to recover the carrying costs through the end of December 2008 (spreading out the payments over an extra year) and directed to apply the GCRR as a percentage increase to base generation rates before the application of any other riders. In light of the PUCO’s modifications, AEP was directed to review the interim GCRRs and file

¹⁹⁵ *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of Their Plan to Provide Additional Options for Customer Participation in the Electric Market*, PUCO Case No. 06-1153-EL-UNC, Order on Remand (May 2, 2007).

¹⁹⁶ *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of an Additional Generation Service Rate Increase Pursuant to Their Post-Market Development Period Rate Stabilization Plans*, PUCO Case No. 07-63-EL-UNC, Application (January 23, 2007) (hereinafter “2007 Discretionary Generation Increase Proceeding”).

¹⁹⁷ *2007 Discretionary Generation Increase Proceeding*, Opinion and Order (October 3, 2007).
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revised tariffs within 30 days that take into account the PUCO's decision. Further, the PUCO clarified that AEP could apply for discretionary generation increases of no greater than an average of 4% per year, which may include a carryover from one-year to the next, and that AEP was not limited to a 4% ceiling in each filing. Finally, the PUCO ordered AEP to utilize the revised revenue requirements to recalculate whether the revised revenue requirements were below the average 4% cap and to file an updated calculation to allow the PUCO to determine whether the revenue requirements were below the average 4% cap.

On November 2, 2007, AEP filed its updated revenue calculation and revised tariffs. Based on this filing, CSP customers were to be charged a GCRR of 1.1% (applied to base generation rates) through December 2008; OP customers would not pay a GCRR in 2008 and also received a one-time credit (for December 2007 only) of 1.18%. Subsequently, the PUCO denied the Applications for Rehearing of AEP and OCC and clarified that it expected AEP to maintain detailed and accurate records to substantiate the monthly generation levels at each facility. The PUCO's Entry on Rehearing further mandated that AEP document the emission credits needed per generation facility by emission control regulation as well as the number of emission credits generated, transferred, and/or purchased by or on behalf of CSP or OP by facility.¹⁹⁸

II. 2008 Increase

Additionally, on October 24, 2007, AEP filed another discretionary generation increase application to recover expenditures incurred in 2008 related to changes in environmental requirements and to factor in increased costs resulting from PJM implementation (on June 1, 2007) of a marginal loss method for reflecting transmission losses.¹⁹⁹ AEP proposed recovery of \$35.2 million and \$11.9 million from CSP and OP customers in 2008, respectively, and also introduced a monthly adjustment mechanism in order to collect its actual, incurred costs on a timely basis.²⁰⁰ The resulting rider rates proposed for 2008 were 3.74% of base generation rates for CSP and 1.16% of base generation rates for OP. The CSP Rider Rate would be in addition to the increases approved in the 2007 Discretionary Generation Increase Proceeding.²⁰¹

On January 18, 2008, an unopposed Stipulation was submitted by multiple parties and was approved subsequently by the PUCO.²⁰² The Stipulation: (1) moved recovery of \$78 million in net locational marginal pricing losses to AEP's TCRR, subject to a true-up

¹⁹⁸ *2007 Discretionary Generation Increase Proceeding*, Entry on Rehearing (November 28, 2007).

¹⁹⁹ *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of an Additional Generation Service Rate Increase Pursuant to Their Post-Market Development Period Rate Stabilization Plans*, PUCO Case No. 07-1132-EL-UNC, Application (October 24, 2007) (hereinafter "2008 Discretionary Generation Increase Proceeding").

²⁰⁰ *2008 Discretionary Generation Increase Proceeding*, Direct Testimony of David M. Roush (October 24, 2007).

²⁰¹ *Id.* at Exhibit 2, page 1 of 4.

²⁰² *2008 Discretionary Generation Increase Proceeding*, Opinion and Order (January 30, 2008).

in 2009; (2) credited to customers \$18 million associated with net congestion costs, subject to a true-up in 2009; (3) included the net cost of marginal line losses towards the cap in generation increases that AEP is permitted to request under its RSP; (4) reduced by \$10 million the amount of costs (as compared to AEP's request) that AEP may recover through its GCRR; and (5) forbade AEP from making any filings for permission to collect additional monies related to specified environmental mandates.²⁰³

On February 27, 2008, Ormet filed an Application for Rehearing of the PUCO's decision to adopt the Stipulation. Ormet claimed that the PUCO erred in permitting approximately \$78 million in generation-related locational marginal pricing losses to be recovered through AEP's TCRR instead of its GCRR. Ormet complained that any transmission losses attributable to Ormet are recovered as part of its generation contract with AEP and therefore recovery of these costs from Ormet through the TCRR results in a double recovery from Ormet. Ormet explained that it does not pay the GCRR, but pays the TCRR, and shifting recovery of the locational marginal pricing losses to the TCRR amounted in an increase of \$4 million to its electric bills for 2008.

Ormet and AEP submitted a Supplemental Agreement on August 20, 2008 for the PUCO's approval in which Ormet agreed to withdraw its Application for Rehearing so long as the Commission approved the proposed modification of Ormet's special contract to reduce Ormet's deposit obligation from 130% of its anticipated monthly bill to a flat \$7 million. On August 27, 2008, the PUCO approved the Supplemental Agreement and reiterated its adoption of the Stipulation in this case without modification.

C. Electric Security Plan

On July 31, 2008, AEP filed its ESP Application at the PUCO to establish its SSO price pursuant to Section 4928.141, Revised Code.²⁰⁴ AEP proposed an ESP with a three-year term from 2009 through 2011, indicating that it would not pursue the MRO option available under SB 221. AEP's ESP Application defined the pricing applicable to SSO customers during the three-year period and included provisions for distribution service, economic development, alternative energy resources and AEP's compliance with energy efficiency, corporate separation, and government aggregation requirements. After a fully litigated proceeding, the Commission issued its Opinion and Order on March 18, 2009, nearly three months beyond the statutory timeframe that Ohio law required the PUCO to issue its Opinion and Order.²⁰⁵ The Commission modified and approved AEP's ESP in several regards and found that the modified ESP met the statutory test for approval of the ESP (*i.e.* the ESP was "more favorable in the aggregate" as compared to the expected results of an MRO).

²⁰³ *Id.* at 10-11.

²⁰⁴ *In the Matter of the Application of Columbus Southern Power Company for Approval of its Electric Security Plan; an Amendment to its Corporate Separation Plan; and the Sale or Transfer of Certain Generating Assets*, PUCO Case Nos. 08-917-EL-SSO, *et al.*, Application (July 31, 2008) (hereinafter, "AEP ESP Proceeding").

²⁰⁵ R.C. 4928.143 requires the PUCO to issue an order within 150 days of the filing of an initial ESP application by an EDU. The PUCO's Opinion and Order was issued 80-days after the statutory deadline.

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From a structural standpoint, the PUCO utilized the framework of AEP's ESP Application, which AEP-proposed as a 15% total bill cap with deferrals of authorized revenues that exceed the bill caps. More specifically, the PUCO's decision appeared to limit annual increases to total bills to 7% for CSP and 8% for OP in 2009, 6% for CSP and 7% for OP in 2010, and 6% for CSP and 8% for OP in 2011. However, when the Commission got around to revealing the "fine print", the actual total bill increases that the PUCO set in motion were much higher than the above-mentioned bill caps. Also, the PUCO did not actually limit the amount that customers will ultimately pay, but rather delayed the payment for a later time. The amounts the PUCO would otherwise permit AEP to collect but for the limited bill caps are, in accordance with the PUCO's decision, deferred for future collection through a non-bypassable charge that will fall on customers during the period 2012 through 2018. The PUCO also authorized AEP to inflate the deferred amount to reflect a hypothetical carrying cost calculated, in part, as though the deferred balance was being financed by AEP's equity investors.

As indicated above, the PUCO's so-called total bill caps did not actually limit the increases customers see on their total bill. For example, the PUCO's bill caps were diluted by the PUCO exempting AEP's rider to recover its EE/PDR benchmark compliance costs, AEP's TCRR, and any rate increase authorized in a distribution rate case.²⁰⁶ Finally, while the PUCO did not accept AEP's proposal to implement a one-time rider to retroactively recover any increase in rates to make AEP whole (back to January 1, 2009) because the Commission missed its statutory deadline to issue a decision on AEP's proposed ESP, the PUCO in effect granted AEP's request by permitting AEP to collect 12 months worth of ESP-approved revenue over the remaining nine months of 2009.

The PUCO also approved an FAC for AEP and modified AEP's FAC request to limit the FAC mechanism to the term of the ESP. The PUCO noted also that the costs to comply with alternative energy portfolio requirements must be bypassable and separately accounted for from fuel. Finally, the PUCO adopted Staff's recommendation to use 2007 actual fuel cost data, escalated by 3% for CSP and 7% for OP, as a reasonable proxy for 2008 fuel costs to serve as the FAC baseline instead of actual 2008 fuel costs (as recommended by IEU-Ohio and others).²⁰⁷

²⁰⁶ *AEP-Ohio ESP Proceeding*, Entry on Rehearing at 9, 31 (July 23, 2009).

²⁰⁷ The recommendation to use the 2008 actual costs was designed to make sure that the FAC baseline value was not too low and the non-FAC rate set too high. Determination of the FAC baseline was critical inasmuch as FAC costs are the last costs recovered from customers under the revenue increase limitations imposed by the Commission and therefore those FAC costs that exceed the limitations and that are deferred will be collected (with interest) from all customers as part of the unavoidable surcharge pursuant to R.C. 4928.144. Setting the baseline too low means that it will appear that fuel costs increased more than they actually did, making the FAC adjustment greater than if the 2008 actual fuel costs had been used, and thereby possibly pushing too much money associated with the FAC into the deferral bucket that will be recovered through the unavoidable surcharge.

Additionally, the PUCO granted AEP revenue increases for non-FAC costs, including for carrying costs that AEP would incur post-January 1, 2009 on environmental investments that it made between 2001 and 2008. The PUCO rejected AEP's request for automatic non-FAC increases that AEP contended would reflect the capitalized investments it intended to make in 2009, 2010, and 2011. Although the PUCO disallowed any recovery of automatic non-FAC increases, the PUCO found that AEP could request, through an annual filing, recovery of additional carrying costs for anticipated environmental investments made during the ESP period after the investments have been made.²⁰⁸

The PUCO also modified and approved AEP's requested automatic distribution rate increases for an enhanced service reliability plan ("ESRP") and a GridSMART plan. The PUCO denied all of the distribution service-related requests in AEP's proposed ESP, except for (1) the implementation of a GridSMART rider to recover a limited GridSmart program to deploy advanced metering infrastructure and distribution automation in CSP's service territory and (2) the recovery of incremental costs associated with an enhanced vegetation management program to improve service reliability.

Further, the PUCO's Opinion and Order denied AEP's request to include specific language in its tariffs to ban customers from participating in PJM's demand response programs, other than through AEP. The PUCO reasoned that it did not have sufficient information on this matter and, thus, it should be deferred and addressed in a separate proceeding. However, on rehearing, the PUCO partially granted AEP's request and prohibited customers served by reasonable arrangements from participating in PJM's demand response programs.²⁰⁹ The PUCO's confusing decisions related to the ability of customers to participate in the PJM demand response programs have benefited electric generators interested in using the PJM market structure to bias the operation of the market in favor of higher prices. Despite suggestions by the PUCO that it would move forward with a process to make effective use of the demand response programs available from RTOs such as PJM, the PUCO has not taken further action. The practical effect of the dithering on this issue is to favor the interests of electric generators and capacity-long utilities like AEP.

Additionally, AEP's proposed ESP included a non-bypassable POLR rider (a generation-related item) as part of AEP's distribution rates, based on AEP's estimated cost of its POLR risk determined by using the Black-Scholes options pricing model. Despite strenuous objections from virtually every intervenor and the fact that there was virtually no customers shopping in AEP's territory, the PUCO held that AEP does have POLR risk associated with customers migrating from its system that is equal to 90% of

²⁰⁸ AEP-Ohio made its first request to recover carrying costs on environmental investments made during the ESP period on February 8, 2010. See *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company to Establish Environmental Investment Carrying Cost Riders*, PUCO Case No. 10-155-EL-RDR, Application (February 8, 2010).

²⁰⁹ *AEP ESP Proceeding*, Entry on Rehearing at 40-41 (July 23, 2009).

the POLR costs that AEP requested. The PUCO granted AEP the authority to collect an *annual* POLR revenue authorization of \$97.4 million for CSP and \$54.8 million for OP. The POLR charge is bypassable; however it is bypassable only by shopping customers that agree to come back to AEP at market-based prices. Since the PUCO could only approve AEP's ESP based on a finding that the ESP was better in the aggregate than the MRO, the likely opportunity for customers to obtain a better price by shopping was quite slim (and particularly so in the case of Ohio Power customers) when the PUCO authorized AEP to begin charging the POLR charge.

The PUCO also denied AEP's request for authority to sell or transfer: two recently-acquired generating facilities (Waterford Energy Center and Darby Electric Generating Station); AEP's entitlement in certain generating facilities of the Ohio Valley Electric Corporation ("OVEC"); and its ownership in the Lawrenceburg Generation Station. The PUCO held that AEP's requests were premature and AEP should file a separate application when it wishes to sell or transfer the generation facilities. However, the PUCO held that AEP may obtain recovery for Ohio customers' jurisdictional share of any costs associated therewith, through the non-FAC portion of the generation rate, and indicated that AEP should modify its ESP accordingly. In its first Entry on Rehearing, the PUCO partially modified its Opinion and Order to remove cost recovery for expenses related to the Waterford and Darby generating assets.²¹⁰

IEU-Ohio and CSP filed additional Applications for Rehearing from the PUCO's July 23, 2009 Entry on Rehearing. IEU-Ohio challenged the PUCO's decision to prohibit customers served by reasonable arrangements from participating in PJM demand response programs and averred that it was illegal to permit AEP to accept the benefits (higher rates) permitted by the ESP while simultaneously holding out its legal right to withdraw and terminate its ESP. CSP's Application for Rehearing objected to the Commission not permitting CSP to recover its costs associated with the Darby Electric Generation Station and the Waterford Energy Center while also prohibiting CSP from selling or transferring the generation assets. The PUCO denied IEU-Ohio's and CSP's Applications for Rehearing on November 4, 2009.

IEU-Ohio and OCC took appeals to the Ohio Supreme Court from the PUCO's Orders in November 2009.²¹¹ Additionally, CSP took its own appeal related solely to the PUCO's denial of its request to transfer generation assets. The appeals are in the briefing stage at the Ohio Supreme Court.

²¹⁰ *Id.* at 35-36.

²¹¹ IEU-Ohio also filed a Complaint for a Writ of Prohibition at the Ohio Supreme Court arguing that the PUCO lost jurisdiction over AEP's ESP Application when it failed to issue an order within the 150-day timeframe required by Section 4928.143(C)(1), Revised Code. *Indus. Energy Users-Ohio v. Pub. Util. Comm.*, Ohio Supreme Court Case No. 2009-1907. The Court granted AEP and PUCO Motions to Dismiss IEU-Ohio's Complaint for a Writ of Prohibition on January 27, 2010. See *01/27/2010 Case Announcements*, 2010-Ohio-188.

D. 2010 Increases Authorized by AEP's Approved Electric Security Plan

As noted above, the ESP approved by the PUCO permits maximum rate increases in 2010 of 6% for CSP customers and 7% for OP customers. On December 1, 2009, AEP filed a request in Case Nos. 09-872-EL-FAC and 09-873-EL-FAC to increase their FAC rates to “reflect the percent increases permitted by the Commission in the ESP cases.”²¹² AEP also specifically noted that its FAC increase filing includes the FAC-related deferrals associated with the interim reasonable arrangement approved for Ormet for the January 2009 through September 2009 time period. Additionally, in conjunction with its request to increase its FAC rates, AEP filed a separate Application to decrease certain non-FAC riders in order to stay within the maximum rate increase limitations set forth in the approved ESP. However, the non-FAC Application was not actually a rate decrease inasmuch as it was merely collecting the same revenues over 12 months instead of cramming the revenue collection into 9 months as AEP was permitted to do in 2009.²¹³

On November 13, 2009, AEP filed an Application in Case No. 09-1094-EL-FAC for permission to recover delta revenue related to a Commission-approved interim reasonable arrangement with Ormet. As noted above, AEP had already included its requested delta revenue recovery related to the Ormet interim reasonable arrangement in its 2010 FAC revenue request. The delta revenue associated with the Ormet interim reasonable arrangement relate to the period of January 1, 2009 through September 17, 2009, and include carrying costs proposed by AEP.²¹⁴ On November 13, 2009, AEP also filed an Application in Case No. 09-1095-EL-UNC to recover through its EDR Rider actual and predicted 2009 delta revenue associated with the long-term unique arrangement approved for Ormet and with the unique arrangement approved for Eramet Marietta, Inc. (“Eramet”).²¹⁵ AEP also proposed to recover its 2010 estimated delta revenue associated with the Ormet and Eramet unique arrangements.

On December 10, 2009, the PUCO's Staff issued a review and recommendation in Case Nos. 09-872-EL-FAC, 09-873-EL-FAC, and 09-1906-EL-ATA. Staff found that the rates proposed by AEP provide for increases no greater than those authorized by the Commission and recommended that the Applications be approved and the proposed rates be effective on a bills rendered basis beginning with the first billing cycle of 2010.

²¹² *In the Matter of the Fuel Adjustment Clauses for Columbus Southern Power Company and Ohio Power Company*, Case Nos. 08-972-EL-FAC, *et al.*, Tariff Filing (December 1, 2009).

²¹³ *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company to Modify Their Standard Service Offer Rates*, Case No. 09-1906-EL-ATA, Application (December 3, 2009).

²¹⁴ *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company to Recover Commission-Authorized Deferrals Through Each Company's Fuel Adjustment Clause*, Case No. 09-1094-EL-FAC, Application at 3-5 (November 13, 2009).

²¹⁵ *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company to Adjust Their Economic Development Cost Recovery Rider Rates*, Case No. 09-1095-EL-UNC, Application at 6 (November 13, 2009).

And, on January 7, 2010, the PUCO approved AEP's request to adjust its FAC and non-FAC rates. The PUCO also approved AEP's request to adjust Rider EDR. Over the objections of IEU-Ohio, the PUCO found that Rider EDR is excluded from the maximum revenue increase limitations and therefore the increase from Rider EDR is added on top of the maximum rate increase limitations approved in the FAC/non-FAC proceedings. IEU-Ohio as well as AEP filed Applications for Rehearing in February 2010 in these cases and the Applications for Rehearing are still pending at the PUCO.

E. Energy Efficiency and Peak Demand Reduction Portfolio Plans

On November 12, 2009, AEP filed a three-year EE/PDR Program Portfolio Plan for PUCO approval in accordance with Rule 4901:1-39-04, O.A.C. AEP also simultaneously filed a Stipulation with many consumer and environmental organizations as signatory Parties. Under AEP's proposed Application and Stipulation, AEP would recover from customers estimated expenditures of \$161.9 million over a three-year period to comply with the EE/PDR benchmarks, as well as additional amounts related to allowances for shared savings, incentives, and lost distribution revenues.²¹⁶ IEU-Ohio did not sign the Stipulation and filed comments objecting to, among other things, the excessive rate impacts of the EE/PDR Program portfolio, excessive administrative costs for the portfolio programs, and AEP's failure to take advantage of lower cost compliance options.²¹⁷ A procedural schedule was issued in this proceeding on January 21, 2010 which establishes several due dates for testimony and other documents and sets the hearing in this case to begin on February 25, 2010.

F. Storm Cost Recovery Rider

On March 10, 2006, AEP filed a request for approval of a Storm Cost Recovery Rider to recover expenses and capital costs incurred in restoring service after major storms that occurred in December 2004 and January 2005.²¹⁸ AEP sought to recover \$23.7 million over a 12-month period (or a shorter time if the full costs are recovered sooner) through a 3.8% adder to CSP customers' distribution charges and a 3.6% adder to OP customers' distribution charges. The PUCO approved AEP's Application, noting that

²¹⁶ *The Matter of the Application of Columbus Southern Power Company for Approval of its Program Portfolio Plan and Request for Expedited Consideration*, PUCO Case Nos. 09-1089-EL-POR, *et al.*, Application at 3 (November 12, 2009).

²¹⁷ *The Matter of the Application of Columbus Southern Power Company for Approval of its Program Portfolio Plan and Request for Expedited Consideration*, PUCO Case Nos. 09-1089-EL-POR, *et al.*, Initial Objections and Recommendations of The Industrial Energy Users-Ohio (December 11, 2009).

²¹⁸ *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company to Implement Storm Related Service Restoration Cost Recovery Riders*, PUCO Case No. 06-412-EL-UNC, Application (March 10, 2006).

AEP sought recovery of costs over and above the costs normally incurred to repair storm damage, based upon a three-year average from 2003 through 2005.²¹⁹

On December 15, 2008, AEP filed an Application for accounting authority to defer as regulatory assets the portion of its O&M expenses related to storm damage from Hurricane Ike in September 2008.²²⁰ AEP explained that the total O&M expenses it proposed to defer was the amount by which the total O&M expenses associated with Hurricane Ike exceeded the three-year average service restoration O&M expenses associated with major storms. AEP noted that it was not requesting authority to commence recovery of these expenses, but if the PUCO determined that such deferrals (with carrying costs) do not present the optimal method for AEP recovering these costs, then AEP requested permission to recover the O&M expenses over a 12-month period beginning with the first billing cycle in February 2009. On December 19, 2008, the PUCO modified and approved AEP's Application.²²¹ The PUCO modified AEP's Application to remove the equity component from carrying costs, setting the interest rate at the same rate approved in AEP's most recent TCRR case. The PUCO also stressed that the reasonableness of the deferred amounts and the recovery thereof will be addressed in a future Commission proceeding.

G. Integrated Gasification Combined Cycle Facility

On March 18, 2005, AEP filed an Application for authority to recover costs of at least one 600 MW IGCC facility in Meigs County, Ohio through a three-phase recovery scheme.²²² Phase I, originally estimated to cost \$18 million, would allow AEP to recover expenditures made up until the time an Engineering, Procurement, and Construction ("EPC") contract is executed through a temporary (12-month) generation rate surcharge to the SSO. Phase II would allow AEP to recover a carrying charge on costs of constructing the facility via the SSO rate, beginning with the first billing cycle of 2007 through the last billing cycle before the IGCC plant is in commercial operation. Also as

²¹⁹ *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company to Implement Storm Related Service Restoration Cost Recovery Riders*, PUCO Case No. 06-412-EL-UNC, Finding and Order (August 9, 2006).

²²⁰ *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Authority to Modify Their Accounting Procedure for Certain Storm Related Service Restoration Costs*, PUCO Case No. 08-1301-EL-AAM, Application (December 15, 2008).

²²¹ *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Authority to Modify Their Accounting Procedure for Certain Storm Related Service Restoration Costs*, PUCO Case No. 08-1301-EL-AAM, Finding and Order (December 19, 2008).

²²² *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Authority to Recover Costs Associated with the Construction and Ultimate Operation of an Integrated Gasification Combined Cycle Electric Generating Facility* (hereinafter, "IGCC Proceeding"), PUCO Case No. 05-376-EL-UNC, Application (March 18, 2005). AEP also applied for Ohio Power Siting Board ("OPSB") approval of the IGCC Project, which the OPSB approved (with conditions) on April 23, 2007. *In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for a Certificate of Environmental Compatibility and Public Need for the Great Bend IGCC Project in Meigs County, Ohio*, PUCO Case No. 06-30-EL-BGN, Opinion, Order, and Certificate (April 23, 2007).

part of Phase II, AEP requested accounting authority to defer the carrying costs and asked to amortize those costs during the 12 months of 2007. Phase III would allow AEP to recoup the costs incurred to build the facility, operating costs, and a return on investment for the useful life of the IGCC facility.²²³ AEP's proposal was contested by all stakeholder sectors and the PUCO's Staff indicated that the quality of information available precluded anything more than moving forward with Phase I of AEP's proposal.²²⁴ Nonetheless, the PUCO authorized AEP to recover approximately \$24 million associated with Phase I of its proposal over a 12-month period through a "bypassable" surcharge.²²⁵ The PUCO justified its allowance of Phase I costs by classifying AEP's IGCC proposal as potentially providing ancillary services necessary to support the distribution function, which is noncompetitive and subject to PUCO regulation, as opposed to providing a competitive generation service.²²⁶ The PUCO put on hold AEP's proposal to recover the Phase II and Phase III costs until some future proceeding. The PUCO denied all of the Applications for Rehearing as well as an AEP Motion for Clarification requesting recovery assurance of non-Phase I expenditures.²²⁷ In addition to denying the Applications for Rehearing, the PUCO ordered AEP to refund all Phase I charges collected for expenditures associated with items that may be utilized in projects at other sites if AEP has not commenced a continuous course of construction of the proposed facility within 5 years of the date of the Entry.²²⁸

IEU-Ohio filed a Complaint for Writ of Prohibition at the Ohio Supreme Court that sought to stay the PUCO's allowance of the Phase I costs or make them subject to refund if found unlawful by the Ohio Supreme Court and to bar the PUCO from further entertaining any increase in rates for a hypothetical IGCC generating plant unless it did so in accordance with Ohio law.²²⁹ The Ohio Supreme Court, by a 4-3 vote, granted a Motion to Dismiss the Complaint for Writ of Prohibition on October 4, 2006.²³⁰ Additionally, four parties, including IEU-Ohio, filed appeals to the Ohio Supreme Court and oral arguments were held on October 9, 2007.²³¹

On March 13, 2008, the Ohio Supreme Court overturned the PUCO's Order allowing AEP to recover the IGCC Project's Phase I costs.²³² The Ohio Supreme Court ruled

²²³ *IGCC Proceeding*, Application at 11 (March 18, 2005).

²²⁴ *IGCC Proceeding*, Post Hearing Brief of PUCO Staff at 18-19 (September 20, 2005).

²²⁵ *IGCC Proceeding*, Opinion and Order at 11 (April 10, 2006).

²²⁶ *Id.* at 17.

²²⁷ *IGCC Proceeding*, Entry on Rehearing (June 28, 2006).

²²⁸ *Id.* at 16-17.

²²⁹ *State of Ohio ex rel. Industrial Energy Users-Ohio v. The Public Utilities Commission of Ohio, et al.*, Case No. 2006-1257, Writ of Prohibition (June 29, 2006).

²³⁰ *October 4, 2006 Case Announcements*, 2006-Ohio-5803.

²³¹ *Industrial Energy Users-Ohio v. The Public Utilities Commission of Ohio*, Court Case No. 2006-1594. Appeals were filed by IEU-Ohio on August 23, 2006 and by OEG, OP&E, and FES on August 25, 2006.

²³² *Indus. Energy Users-Ohio v. Pub. Util. Comm.*, 117 Ohio St.3d 486, 2008-Ohio-990.

that the evidence assembled by the PUCO did not support the PUCO's ruling that the IGCC unit would provide distribution/ancillary services. However, the Ohio Supreme Court remanded this issue to the PUCO to see if the PUCO could develop a record to support the view that all or part of the IGCC unit might provide distribution/ancillary service. The Ohio Supreme Court's decision also noted that under traditional regulation as defined by Ohio law, the cost of a utility facility is not eligible for recovery unless the facility is at least 75% complete and suggested that the PUCO needed to address this requirement in the case of the IGCC unit since construction of the facility had not even started.²³³ The Ohio Supreme Court declined to reach the question of whether a refund of the approximately \$24 million in Phase I costs was warranted.

On September 17, 2008, OCC filed a request to refund the \$24 million and on January 9, 2009, the Attorney Examiner in this proceeding issued an Entry directing AEP to "provide a detailed statement outlining the status of the construction of the IGCC facility, including whether AEP-Ohio is engaged in a continuous course of construction on the IGCC facility" by February 7, 2009.²³⁴ On February 6, 2009, AEP filed the update required by the Attorney Examiner. AEP stated that it had not commenced construction of the IGCC facility. AEP explained that it believed there are still some barriers in Ohio law to construction of new base load generation in Ohio, despite the efforts contained in SB 221 to address advanced energy resources. AEP also observed that a variety of changes (i.e. environmental legislation, changes in Ohio law, changes in AEP generating capacity) may occur and could result in a continuous course of construction by June 2011. AEP further stated that it continued to believe there are substantial reasons for pursuing the construction of an IGCC facility and that such a facility, with appropriate rate recovery provisions, would be good for Ohio's economy, AEP's customers, and AEP.

In September 2009, IEU-Ohio filed a Motion asking the Commission to require AEP to refund IGCC-related revenues collected from customers or to show cause why an immediate refund should not be required. IEU-Ohio provided the Commission with an integrated resource plan filed by an AEP affiliate, Appalachian Power Company ("APCo"), at the Virginia State Corporation Commission that contained information pertaining to the entire eastern segment (which includes Ohio) of AEP's parent company. The Virginia integrated resource plan stated that AEP had no plans to initiate construction of any IGCC plant prior to June 28, 2011. The PUCO has not done anything to respond to the Ohio Supreme Court's remand or respond to IEU-Ohio's or OCC's Motion for Refunds.

²³³ Prices for distribution/ancillary services are established based on traditional, cost-based ratemaking that continues to apply to regulated services such as distribution/ancillary services.

²³⁴ *IGCC Proceeding*, Attorney Examiner Entry (January 8, 2009).

H. Ormet Primary Aluminum Corporation and Ormet Aluminum Mill Products Corporation (collectively “Ormet”) Proceedings

In 1996, the PUCO approved a Joint Application of OP and South Central Power Company (“SCP”), a municipal electric cooperative that is, in large part, not subject to PUCO regulation, for a reallocation of territory so that Ormet would be served by SCP and any other supplier as necessary.²³⁵ The reallocation was to take effect on December 31, 1999, two-years after an agreement between OP and Ormet entered into in 1966 was set to expire. In the interim period, however, Ormet and OP received approval of an Interim Agreement from the PUCO whereby OP would serve Ormet from November 30, 1997 through December 31, 1999.²³⁶ Thus, Ormet was permitted to source generation from the market at favorable prices prior to all other customers.

On August 25, 2005 Ormet filed a complaint against SCP and OP, requesting among other things, that the PUCO either transfer SCP's rights to furnish electric service to Ormet to OP or reallocate the certified electric service territories of SCP and OP so that Ormet is part of OP's certified electric service territory, and order OP to serve Ormet pursuant to its GS-4 tariff rate schedule.²³⁷ In other words, Ormet sought to reverse the service area assignment and obtain OP's tariffed rates and charges applicable to similarly situated customers at a time when the market rates were no longer favorable. After the PUCO determined that SCP did not provide or propose to provide physically adequate service to Ormet, the parties submitted a Stipulation that the PUCO adopted on November 8, 2006.²³⁸ The Stipulation reallocated SCP's and OP's service territory such that Ormet's facility would be served by OP, provided that OP would serve Ormet's peak demand of approximately 520 MW, and required Ormet to prepay its estimated monthly bill.²³⁹ Further, the Stipulation included a mechanism for pricing the service Ormet would pay OP, which directed Ormet to pay \$43 per MWh for generation service.

²³⁵ See *In the Matter of the Application of the Joint Petition of Ohio Power Company and South Central Power Company for Reallocation of Territory*, Case No. 96-1000-EL-PEB, Finding and Order (November 14, 1996).

²³⁶ See *In the Matter of the Application of The Ohio Power Company for Approval of a Special Contract Arrangement with Ormet Primary Aluminum Corporation*, Case No. 96-999-EL-AEC, Finding and Order (November 14, 1996).

²³⁷ *In the Matter of the Complaint of Ormet Primary Aluminum Corporation and Ormet Aluminum Mill Products Corporation v. South Central Power Company and Ohio Power Company*, PUCO Case No. 05-1057-EL-CSS, Petition to Transfer Rights to Furnish Electric Service and/or Reallocate Certified Electric Service Territories; Complaint for Inadequate Service; Complaint for Unjust, Unreasonable and Discriminatory Proposed Rates (August 25, 2005).

²³⁸ SCP appealed to the Court the PUCO's decision declaring that SCP was not providing or did not propose to provide physically adequate service to Ormet. *South Central Power Company v. The Public Utilities Commission of Ohio*, Court Case No. 2006-1866, Notice of Appeal (October 6, 2006). That appeal was stayed pursuant to the Court granting the Parties' Joint Motion for a Stay of the proceeding and later dismissed at the request of the Parties when a settlement was reached. *December 15, 2006 Case Announcements*, 2006-Ohio-6602.

²³⁹ *In the Matter of the Complaint of Ormet Primary Aluminum Corporation and Ormet Aluminum Mill Products Corporation v. South Central Power Company and Ohio Power Company*, PUCO Case No 05-1057-EL-CSS, Stipulation and Recommendation at 6 (October 20, 2006).

If the market price of electricity exceeded \$43 per MWh, AEP would be compensated for the differential between the market rate and the \$43 per MWh charge by amortizing its Ohio Franchise Tax phase-out regulatory liability (which totals approximately \$57 million). Further, in the event that the amortization of the Ohio Franchise Tax phase-out regulatory liability would not fully compensate AEP for the price differential, AEP would be permitted to recover any remaining portion under the provision in its RSP allowing an additional 4% increase in its generation rates.²⁴⁰ Finally, the Stipulation required AEP to make a filing prior to the start of 2007 to set a market rate for generation service to Ormet's facility for 2007 and required AEP to do the same for Ormet's 2008 generation service.²⁴¹

The PUCO issued a Supplemental Opinion and Order on November 8, 2006 adopting the Stipulation in its entirety.²⁴² As required by the Supplemental Opinion and Order, AEP made a filing indicating the 2007 market price for generation service to Ormet's facility would be \$47.69 per MWh,²⁴³ which the PUCO approved on June 27, 2007.²⁴⁴ Additionally, AEP filed for approval of the 2008 Ormet generation rate on December 27, 2007, quoting a market rate of \$53.03 per MWh.²⁴⁵

On December 29, 2008, AEP and Ormet filed a Joint Application for accounting authority related to serving Ormet as well as approval of an interim reasonable arrangement with Ormet.²⁴⁶ The Joint Application represented that Ormet could not continue to pay its current \$43 per MWh rate for generation service without breaching certain covenants in its bank agreement that would threaten its continued operation. The Joint Application proposed to provide generation service to Ormet on an interim basis (until the effective date of tariffs implementing AEP's ESP and a new agreement is reached with Ormet) at the otherwise applicable tariff-based price (in this case one-half of Ormet's load would pay OP's GS-4 rate and the other half would pay CSP's GS-4

²⁴⁰ *Id.* at 10.

²⁴¹ *Id.* at 9-10.

²⁴² *In the Matter of the Complaint of Ormet Primary Aluminum Corporation and Ormet Aluminum Mill Products Corporation v. South Central Power Company and Ohio Power Company*, PUCO Case No. 05-1057-EL-CSS, Supplemental Opinion and Order (November 8, 2006).

²⁴³ *Columbus Southern Power Company's and Ohio Power Company's Application to Set the 2007 Generation Market Price for Ormet's Hannibal Facilities*, PUCO Case No. 06-1504-EL-UNC, Columbus Southern Power Company's and Ohio Power Company's Ormet-Related 2007 Generation Market Price Submission at 1 (December 26, 2006).

²⁴⁴ *Columbus Southern Power Company's and Ohio Power Company's Application to Set the 2007 Generation Market Price for Ormet's Hannibal Facilities*, PUCO Case No. 06-1504-EL-UNC, Finding and Order at 2-3 (June 27, 2007).

²⁴⁵ *Columbus Southern Power Company's and Ohio Power Company's Application to Set the 2008 Generation Market Price for Ormet's Hannibal Facilities*, PUCO Case No. 07-1317-EL-UNC, Application at 1 (December 27, 2007). The PUCO approved the 2008 Market Price on December 10, 2008.

²⁴⁶ *In the Matter of the Joint Application of Columbus Southern Power Company and Ohio Power Company for Authority to Modify Their Accounting Procedure*, Case Nos. 08-1338-EL-AAM, *et al.*, Joint Application (December 29, 2008).

rate) instead of the \$43 per MWh that Ormet currently pays. The difference between the price paid by Ormet and the 2008 market price would continue to be amortized against the Ohio Franchise Tax phase-out regulatory liability. However, once the regulatory liability is gone (which AEP estimated would occur by the end of 2008), AEP requested accounting authority to defer that differential and to recover that differential from its remaining retail customers through the FAC that AEP proposed in its ESP. The PUCO approved the Joint Application on January 7, 2009. OCC filed an Application for Rehearing on February 6, 2009 and the PUCO has not yet ruled on the Application for Rehearing.

On February 17, 2009, Ormet made a unilateral Application at the PUCO for approval of a long-term reasonable arrangement governing service for 2009 through 2018. On July 15, 2009 the PUCO modified and approved Ormet's Application, largely keeping the suggested structure for the reasonable arrangement.²⁴⁷ For calendar year 2009, the PUCO directed AEP to bill Ormet at a rate which, for all of 2009, averages \$38 per MWh for periods when Ormet operates six potlines, \$35 per MWh for periods when Ormet curtails production to 4.6 potlines, and \$34 per MWh when Ormet curtails production to 4 potlines. This pricing was contingent upon Ormet maintaining 900 employees at its facility through 2009.

For the years 2010 and 2011, the PUCO approved a modified form of the index pricing tied to the price of aluminum on the London Metals Exchange ("LME"). Each year Ormet will file at the PUCO a target LME price which represents the selling price for aluminum at which Ormet will be able to pay AEP's weighted tariff rates and still have adequate cash flow to sustain operations and pay required legacy costs. The index rate is the power price Ormet would be able to pay based upon then-current LME prices for aluminum while maintaining adequate cash flow to sustain operations and pay required legacy costs. When the LME price for aluminum is less than the target price, Ormet will pay the index price for power. When the LME price for aluminum is greater than the target price by not more than \$300 per ton, Ormet will pay 102% of the AEP weighted tariff rate. When the LME price for aluminum is greater than the target price by more than \$300 per ton, Ormet will pay 105% of the AEP weighted tariff rate.

For the years 2012 through 2018, the formula rate will be adjusted. Each year Ormet will still file an index rate and target price as described above. However, when the LME price for aluminum is greater than the target price by not more than \$300 per ton, Ormet will pay 104% of the AEP weighted tariff rate. When the LME price for aluminum is greater than the target price by more than \$300 per ton, Ormet will pay 108% of the AEP weighted tariff rate. Any revenues in excess of AEP's tariff rate paid by Ormet will be treated as delta revenue credits, first against any deferred balances, with any remaining credit recognized in AEP's Economic Development Rider (*i.e.* Rider EDR).

²⁴⁷ *In the Matter of the Application of Ormet Primary Aluminum Corporation for Approval of a Unique Arrangement with Ohio Power Company and Columbus Southern Power Company*, PUCO Case No. 09-119-EL-AEC, Opinion and Order (July 15, 2009).
{C29886:4 }

In addition to the formula pricing the PUCO approved for the years 2010 through 2018, the PUCO also imposed a maximum discount Ormet may receive in any calendar year, which it subjects to further reduction due to changes in employment and other factors. For calendar years 2010 and 2011, the maximum annual discount that Ormet may receive is \$60 million.

The PUCO also established a cap on the maximum amount of annual delta revenues that other customers will be required to pay of \$54 million per year. AEP was authorized to defer the potential difference of up to \$6 million per year as a regulatory asset, with carrying costs. AEP will be permitted to recover the deferred costs after the end of the term of the reasonable arrangement with Ormet.

For the remaining years of the agreement after 2011, the PUCO directs that the maximum discount to Ormet be reduced to \$54 million in 2012; and by an additional \$10 million each year thereafter for the remaining years of the agreement. The PUCO also provided for a carryover of any unused discount that may result from fluctuations in the LME price for aluminum. For example, in 2012, if Ormet only received a discount of \$50 million, then in any subsequent year it would be allowed to carry over the unused \$4 million discount to increase a discount in a subsequent year.

In the years 2010 through 2018, any discounts to Ormet are contingent upon maintaining employment levels at the facility at or above 650 full time employees. The PUCO directed that the discount will be reduced each month by \$10 million for every 50 employees below 650 employees that Ormet employed in the previous month.

The PUCO also found that under terms of the arrangement AEP will be the exclusive supplier to Ormet and that there is no shopping risk. Therefore, compensating AEP for POLR charges would be paying AEP for a service it is not providing. The Order directed AEP to credit any POLR revenues it receives from Ormet to its Rider EDR to reduce the impact of the reasonable arrangement on other customers.

Additionally, the PUCO approved the proposal to treat Ormet under AEP's standard credit terms. Further, the Opinion and Order imposed an independent termination provision based upon Ormet's claim that aluminum prices will recover. If Ormet does not begin to reduce deferred delta revenues through the payment of above-tariff rates by April 1, 2012, the PUCO retained the option to immediately terminate the agreement.

Several Parties filed Applications for Rehearing and the PUCO granted in part and denied in part the Applications for Rehearing.²⁴⁸ The PUCO generally denied the Applications for Rehearing, but granted in part AEP's Application for Rehearing, reaffirming its finding that there is no risk that Ormet will be permitted to shop for competitive generation and therefore AEP is not entitled to recovery of POLR charges

²⁴⁸ *In the Matter of the Application of Ormet Primary Aluminum Corporation for Approval of a Unique Arrangement with Ohio Power Company and Columbus Southern Power Company*, PUCO Case No. 09-119-EL-AEC, Entry on Rehearing (September 15, 2009).

from Ormet, but clarified that the POLR charge is only known and relevant for the duration (through 2011) of AEP's approved ESP. The PUCO's Entry on Rehearing also granted in part the Joint Application for Rehearing of OCC and OEG to clarify that the rate discount provided to Ormet has no impact whatsoever on the amount of credit to be applied to Rider EDR and that Rider EDR should be credited the full amount of the POLR component of the tariff rate which would otherwise apply to Ormet on a MWh basis.

I. Enhanced Service Distribution Reliability Plan

On January 31, 2006, AEP filed a report ("Final Report") pursuant to a previously PUCO-approved stipulation that required AEP to make specific quantified improvements to its distribution service quality for the years 2003 through 2005 ("Distribution Quality Stipulation").²⁴⁹ AEP's Final Report indicated that, while AEP had made the specified improvements, the recommended levels for distribution quality in other areas did not meet the required standards.²⁵⁰ On April 17, 2006, in accordance with a PUCO directive, Staff filed an investigative report regarding AEP's distribution service reliability which found that there was a degradation in performance over the period 2001 to 2005 and that "the Companies' performance continues to deteriorate over time."²⁵¹ After reviewing AEP's response to Staff's report and recommendations, the PUCO directed AEP to earmark \$10 million to be dedicated toward future measures addressing service and reliability concerns and prohibited AEP from recovering any of that money from AEP ratepayers.²⁵²

In conjunction with AEP's filing of the Final Report, AEP filed a self-complaint with the PUCO in which it reiterated the results of the Final Report and stated that existing distribution rates (the same rates that AEP asked to be frozen as part of its RSP)²⁵³ could not support the continued increased expenditures that AEP made during the previous two-years.²⁵⁴ The PUCO permitted AEP to use the self-complaint mechanism

²⁴⁹ *In the Matter of a Settlement Agreement Between the Staff of the Public Utilities Commission of Ohio and Columbus Southern Power Company and Ohio Power Company*, PUCO Case No. 03-2570-EL-UNC, Columbus Southern Power Company's and Ohio Power Company's Final Report (January 31, 2006).

²⁵⁰ *Id.* at 11 (Attachment 1).

²⁵¹ *In the Matter of the Commission Consideration of a Settlement Agreement Between the Staff of the Public Utilities Commission of Ohio, Columbus Southern Power Company, and Ohio Power Company*, PUCO Case Nos. 03-2570-EL-UNC, *et al.*, Correction to Commission Ordered Investigative Report Submitted by the Staff of the Public Utilities Commission of Ohio at 2 (April 18, 2006).

²⁵² *In the Matter of a Settlement Agreement Between the Staff of the Public Utilities Commission of Ohio and Columbus Southern Power Company and Ohio Power Company*, PUCO Case No. 03-2570-EL-UNC, Finding and Order at 6 (July 26, 2006).

²⁵³ AEP asked the PUCO to continue a freeze of its distribution rates as part of its RSP Proposal. This aspect of AEP's proposal was opposed by the PUCO's Staff as well as IEU-Ohio. IEU-Ohio supported the Staff's position that AEP's distribution rates should be evaluated in the event AEP sought to increase generation prices above the automatic increase levels (3% for CSP and 7% for OP).

²⁵⁴ *In the Matter of the Self-Complaint of Columbus Southern Power Company and Ohio Power Company Concerning the Implementation of Programs to Enhance Their Currently Reasonable Level of Distribution* {C29886:4 }

to deal with issues related to improving its service reliability and ordered AEP to submit a proposed reliability plan with supporting testimony by October 6, 2006.²⁵⁵ As ordered, AEP filed its plan with the PUCO in which it proposed to initiate several programs to maintain its distribution system, including asset management and reliability, vegetation management, distribution station reliability, and the use of advancements in technology, on the condition that it be permitted to recover approximately \$640 million for the costs of implementing the plan.²⁵⁶

On April 18, 2007, multiple parties to this proceeding submitted a Joint Motion to Withdraw AEP's Self-Complaint.²⁵⁷ The signatory parties cited their inability to agree on the critical legal and factual issues in the case or on a cost recovery component for AEP's plan. Additionally, the signatory parties asked the PUCO to order AEP to direct \$10 million, which had previously been earmarked for service and reliability improvements, towards additional vegetation management efforts in a manner consistent with AEP's plan. The signatory parties also requested a PUCO directive for Staff and AEP to determine the circuits to be addressed with the additional monies. On May 16, 2007, the PUCO granted the Joint Motion to Withdraw, as well as the requests contained within it.²⁵⁸ Additionally, the PUCO further required AEP to cooperate with Staff;²⁵⁹ prohibited AEP from recovering any of the \$10 million from ratepayers; and ordered that, beginning in July 2007, any remaining balance will accrue interest at a rate of 1% per month and the accrued interest must be spent on the incremental vegetation management plan.

Service Reliability, PUCO Case No. 06-222-EL-SLF, Self-Complaint (January 31, 2006) (hereinafter, "*AEP Self-Complaint Proceeding*").

²⁵⁵ *AEP Self-Complaint Proceeding*, Entry at 2-3 (July 26, 2006).

²⁵⁶ *AEP Self-Complaint Proceeding*; Enhanced Distribution Service Reliability Plan (October 6, 2006). Over a 5-year period, AEP estimated that it would spend a total of \$637.4 million in incremental O&M and capital costs, with \$234.1 million for O&M and \$403.3 million in capital, and asked to recover those costs through a new rider called the Reliability Cost Recovery Rider ("RCRR"). Initially, the RCRR would be set based on data for the period of July 1, 2007 through December 31, 2008, and would be effective until new base distribution rates were established through a rate case. *AEP Self-Complaint Proceeding*, Testimony of David Roush at 3 (October 6, 2006). The requested RCRR rates, which would be applied to all customers' base distribution charges, represented an increase over current distribution rates of 8.54% for OP and 5.35% for CSP. *Id.* at 7.

²⁵⁷ *AEP Self-Complaint Proceeding*, Joint Motion to Withdraw Self Complaint (April 18, 2007).

²⁵⁸ *AEP Self-Complaint Proceeding*, Entry (May 16, 2007).

²⁵⁹ The PUCO required AEP to: provide Staff a copy of its policies and communications for its tree trimming or tree removal plan; report to Staff on the service quality of the chosen circuits for two-years after a circuit is cleared; report on a quarterly basis AEP's tree trimming progress, including expenditures; audit at least 10% of the work performed pursuant to the incremental vegetation management plan; comply with national standards for tree trimming and removal; track expenditures in a manner which assists Staff's ability to audit the incremental vegetation management plan expenditures and; ensure the incremental vegetation management plan is work above and beyond the PUCO's vegetation management requirements and is not included in AEP's budgets or plans. *Id.* at 3-4.

J. Power Acquisition Rider (“PAR”) Proceeding

In 2005, after extensive litigation with Monongahela Power (“Mon Power”) over its refusal to propose an RSP, the PUCO ordered Mon Power and CSP to enter into negotiations for CSP to acquire Mon Power’s Ohio territory. CSP and Mon Power came to an agreement about CSP’s purchase of Mon Power’s service territory and the PUCO modified and approved their agreement.²⁶⁰ Among other things, the PUCO authorized CSP to collect through the PAR mechanism the shortfall between its power acquisition costs to serve the former Mon Power load and the revenues produced by CSP’s service to the former Mon Power customers at CSP’s rates.²⁶¹ The PUCO also set the initial PAR rate based upon CSP’s purchase (from Mon Power) of its power requirements to serve the former Mon Power customers from January 1, 2006 through May 31, 2007.

For the remainder of the RSP period (June 1, 2007 through December 31, 2008), CSP was authorized to conduct an RFP for the generation to serve the former Mon Power load and to use the PAR mechanism to recoup the difference between the RFP price and CSP’s generation price. After conducting the RFP, CSP filed an Application (and a subsequent correction) requesting a PAR increase based on the average awarded bid price of \$55.88/MWh as well as a true-up of CSP’s under-recovery of the PAR during the initial 17-month period.²⁶² On June 27, 2007, the PUCO approved AEP’s Application, the \$69.1 million PAR revenue requirement for the June 1, 2007 through December 31, 2008 time period, and an allocation of PAR costs using a uniform percentage of generation revenue allocation rather than a per kWh allocation.²⁶³

K. Transmission Cost Recovery Rider

In September 2005, AEP filed an Application to adjust (through a proposed TCRR) its transmission charges to reflect rate changes approved by FERC.²⁶⁴ AEP proposed to use the TCRR to recover costs it incurred to join an RTO as well as suggested that the TCRR be annually trued-up. AEP proposed to implement this process by filing an application by November 1 of each year to become effective the following year. The

²⁶⁰ *In the Matter of the Transfer of Monongahela Power Company’s Certified Territory in Ohio to the Columbus Southern Power Company*, PUCO Case No. 05-765-EL-UNC, Opinion and Order (November 9, 2005).

²⁶¹ *Id.* at 17-18.

²⁶² *In the Matter of the Application of Columbus Southern Power Company to Adjust its Power Acquisition Rider Pursuant to its Post-Market Development Period Rate Stabilization Plan*, PUCO Case No. 07-333-EL-UNC, Application (March 28, 2007) (hereinafter “AEP PAR Proceeding”). See also *AEP PAR Proceeding*, Correction to Application (March 30, 2007).

²⁶³ *AEP PAR Proceeding*, Opinion and Order (June 27, 2007).

²⁶⁴ *In the Matter of the Application of The Columbus Southern Power Company and Ohio Power Company to Adjust the Transmission Components of the Companies’ Standard Service Tariffs to Reflect the Applicable FERC-Approved Charges or Rates Related to Open Access Transmission, Net Congestion, and Ancillary Services*, PUCO Case No. 05-1194-EL-UNC, Finding and Order (December 14, 2005). AEP was granted authority to file applications to adjust its respective transmission charges in its RSP proceeding. *Id.* at 1.

PUCO approved AEP's original TCRR Application, with some modifications, and also ordered Staff to review the costs included in the TCRR prior to the next filing and to update and true-up the rider. The PUCO specifically directed Staff to ensure controllable costs were minimized.²⁶⁵

In February 2006, AEP filed an Application requesting, among other things, permission to adjust the transmission components of its unbundled rates to reflect changes approved by FERC and to combine the transmission component of each operating company's standard service tariff with its previously-approved TCRR.²⁶⁶ The PUCO approved AEP's Application, making adjustments to preclude recovery of certain ancillary service costs and to reconcile AEP's net RTO formation costs.²⁶⁷ Additionally, the PUCO ordered: Staff to complete a biannual audit to determine if AEP's management and operating processes minimize controllable transmission service costs; AEP to provide a detailed report of the identified controllable costs, including all actions taken to minimize those costs; and Staff, with each update filing, to audit all costs included in the TCRR to verify the accuracy of the charges and to ensure they relate only to the provision of service to native load customers.

On October 26, 2006, AEP filed a TCRR Update Application, asking to reduce the TCRR by 30% and 25% for OP and CSP customers, respectively.²⁶⁸ Staff completed its audit of AEP's TCRR and recommended approval of AEP's requested TCRR reduction. Additionally, pursuant to the TCRR review process established in other dockets, Staff conducted its biannual audit of AEP's TCRR to ensure that the appropriate costs were included and that AEP was minimizing controllable transmission costs. The PUCO concurred with Staff's findings and concluded that AEP fairly determined and reasonably incurred its transmission costs during calendar year 2006 and that AEP's practices and policies minimized controllable RTO costs during that same time period.²⁶⁹

²⁶⁵ *Id.* at 5.

²⁶⁶ *In the Matter of the Application of The Columbus Southern Power Company and Ohio Power Company to Adjust the Transmission Component of Each Company's Standard Service Tariff to Combine That Component with its Transmission Cost Recovery Rider*, PUCO Case No. 06-273-EL-UNC, Application (February 3, 2006).

²⁶⁷ *In the Matter of the Application of The Columbus Southern Power Company and Ohio Power Company to Adjust the Transmission Component of Each Company's Standard Service Tariff to Combine That Component with its Transmission Cost Recovery Rider*, PUCO Case No. 06-273-EL-UNC, Finding and Order (May 26, 2006).

²⁶⁸ *In the Matter of the Application of The Columbus Southern Power Company and Ohio Power Company to Adjust Each Company's Transmission Cost Recovery Rider*, PUCO Case No. 06-1294-EL-UNC, Application (October 26, 2006).

²⁶⁹ *In the Matter of the Application of The Columbus Southern Power Company and Ohio Power Company to Adjust Each Company's Transmission Cost Recovery Rider*, PUCO Case Nos. 06-1294-EL-UNC, *et al.*, Entry at 9 (July 25, 2007). The PUCO also left open for the audit in AEP's next TCRR filing an OCC concern that AEP double-recovered approximately \$200,000 in transmission costs in the TCRR that are also recovered in the PAR.

On November 8, 2007, AEP filed its TCRR update for 2008, asking for TCRR increases of 58% and 61% for OP and CSP customers, respectively.²⁷⁰ The PUCO approved AEP's Application on December 19, 2007, thereby permitting AEP to collect \$159 million in transmission costs from OP customers and \$145 million from CSP customers.²⁷¹ Additionally, as previously noted and pursuant to the settlement in AEP's 2008 Discretionary Generation Increase Proceeding, net locational marginal pricing losses will also be recovered through the TCRR.

On October 31, 2008, AEP proposed its annual update to its TCRR rates for 2009, to be effective on a bills-rendered basis beginning on December 30, 2008.²⁷² AEP requested an increase of \$12.6 million for OP, which would produce an average increase in transmission rates of 7%, and an overall decrease of approximately \$5.1 million for CSP, which would result in an average decrease in transmission rates of 3%. Additionally, the TCRR proposal included AEP's proposed increases in its FERC rate case (starting on March 1, 2009.). On December 17, 2008, the PUCO modified and approved AEP's Application.²⁷³ Specifically, the PUCO modified AEP's Application to lower AEP's carrying cost rate. The PUCO also explained that any over-recovery caused by a removal of the credit against the cost of marginal losses from the TCRR would be trued-up in AEP's next TCRR application.²⁷⁴

On April 16, 2009, AEP filed an Application to adjust its TCRR for the July 2009 through June 2010 time period.²⁷⁵ The proposed TCRR rates (after an update filed by AEP) reflected a proposed revenue reduction of \$6.4 million from the current TCRR for CSP for a total revenue authorization of \$168.8 million and proposed a \$5.1 million revenue reduction from the current TCRR for OP for a total revenue authorization of

²⁷⁰ *In the Matter of the Application of The Columbus Southern Power Company and Ohio Power Company to Update Each Company's Transmission Cost Recovery Rider*, PUCO Case No. 07-1156-EL-UNC, Application (November 8, 2007).

²⁷¹ *In the Matter of the Application of The Columbus Southern Power Company and Ohio Power Company to Update Each Company's Transmission Cost Recovery Rider*, PUCO Case No. 07-1156-EL-UNC, Finding and Order (December 19, 2007).

²⁷² *In the Matter of the Application of The Columbus Southern Power Company and Ohio Power Company to Update Each Company's Transmission Cost Recovery Rider*, PUCO Case No. 08-1202-EL-UNC, Application (October 31, 2008).

²⁷³ *In the Matter of the Application of The Columbus Southern Power Company and Ohio Power Company to Update Each Company's Transmission Cost Recovery Rider*, PUCO Case No. 08-1202-EL-UNC, Finding and Order (December 17, 2008).

²⁷⁴ A Staff Report regarding AEP's TCRR Application pointed out that AEP proposed to remove the credit against the cost of marginal losses from the TCRR because it proposed a fuel adjustment clause as part of its ESP, but Staff noted that if the ESP (including a FAC) is not in place by January 1, 2009, then an over-recovery in the TCRR would occur.

²⁷⁵ *In the matter of the application of Columbus Southern Power Company and Ohio Power Company to Update Each Company's Transmission Cost Recovery Rider*, PUCO Case No. 09-339-EL-UNC, Application (April 16, 2009).

approximately \$200 million.²⁷⁶ The PUCO approved AEP's TCRR adjustment on June 24, 2009.

²⁷⁶ *In the matter of the application of Columbus Southern Power Company and Ohio Power Company to Update Each Company's Transmission Cost Recovery Rider*, PUCO Case No. 09-339-EL-UNC, Staff Report (June 9, 2009).
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