

BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Columbus)
Southern Power Company and Ohio Power) Case No. 04- 169 -EL-UNC
Company for Approval of a Post Market)
Development Period Rate Stabilization Plan.)

COLUMBUS SOUTHERN POWER COMPANY'S
AND OHIO POWER COMPANY'S
APPLICATION FOR APPROVAL OF A
POST MARKET DEVELOPMENT PERIOD
RATE STABILIZATION PLAN

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INTRODUCTION

Columbus Southern Power Company (CSP) and Ohio Power Company (OP), collectively referred to as the "Companies," each of which is an electric light company and a public utility as those terms are defined in §§ 4905.05 and 4905.03(A)(4), Ohio Rev. Code, submit this application for approval of a post-Market Development Period (MDP) Rate Stabilization Plan.

By this filing, the Companies strive to strike a balance among several worthy but different policies. The Rate Stabilization Plan presented by the Companies harmonizes these policies in a manner which promotes each of them.

These policies include:

1. Providing rate stability and certainty for customers;
2. Facilitation of a competitive market for the generation component of electric utility services;
3. Preservation of low cost electric generating capacity in Ohio, with improved environmental performance, which is critically important to the vitality of Ohio's economy;

4. Recovery of the costs of complying with environmental requirements, thereby providing a degree of stability and certainty for the Companies;
5. Providing a levelized path to a competitive generation market which would be preferable to uncertain price fluctuations at the conclusion of the MDP. The uncertainty is particularly relevant for residential customers since the temporary discount reduction applied to residential generation rates, which Am.Sub. S.B. No. 3 (S.B.3) guaranteed for a two and a half year period, will expire.

When S.B.3 was enacted in 1999, the Ohio General Assembly set out a detailed path to be followed by the electric companies, customers, alternative providers of generation service, and the Commission. A key component of that path was the MDP. It was anticipated that by the end of the MDP, which by statute would end no later than December 31, 2005, a competitive market structure would be in place which would function in a manner that would provide rate stability, rather than the uncertainty that exists today.¹ Therefore, S.B.3 provides that at the end of the MDP generation rates for customers who did not switch to an alternative supplier would be market-based. As with many aspects of S.B.3, how those market-based rates would be implemented is subject, to some extent, to the Commission's discretion.

As the Companies, their customers, Competitive Retail Electric Service (CRES) providers, and the Commission approach the end of the MDP, increasing concern is focusing on the potential impact of an unguided "flashcut" to market-based generation charges on January 1, 2006.

Moreover, as required by statute, the Commission is nearing completion of rules that would be used to implement the post-MDP Market Based Standard Service Offer (MBSSO)

¹ Stability, however, should not be mistaken for rate reductions or for rates frozen at current levels. This is particularly true for customers of electric utilities, such as the Companies, whose generation costs, and therefore its rates, are among the lowest in the state.

and Competitive Bidding Process (CBP). (See Case No. 01-2164-EL-ORD). The Commission's proposed rules would require the filing of an application for a MBSSO and a CBP by July 1, 2004. In its December 17, 2003 Entry, however, the Commission observed that electric utilities and other interested parties could submit a stipulation that varies from criteria set forth in the proposed rules.

Therefore, the Companies submit this Rate Stabilization Plan which will, with Commission approval, substitute during the Rate Stabilization Period (January 1, 2006 through December 31, 2008) for the Companies' MBSSO without the need for a CBP. The Companies' Plan harmonizes the policies discussed above in a manner which promotes each of the policies. If despite that, this proceeding does not result in the Commission adopting the Plan as the Companies' MBSSO, the Companies would need to submit, in accordance with the Commission's proposed rules, an application to implement MBSSO and/or CBP beginning January 1, 2006.

As described in greater detail below, the Plan provides for increases in 2006, 2007 and 2008 in the rates customers pay for generation service. These increases would provide incremental revenue needed by the Companies as they embark on a program of dramatic levels of environmental investment associated with their current low-cost generation facilities. These environmental-related activities will be undertaken in a manner that minimizes expenditures and which will result in an improved environment. Further they will help maintain adequate, reasonable cost generating supplies for consumers and the wholesale market place, and thereby contribute to the State's obviously worthy policy of maintaining a strong economy.

The Plan also provides that the Companies could recover through additional filings certain other expenditures, including those incurred to enhance security measures taken to protect the Companies' generation facilities. When S.B.3 was enacted, no one could have foreseen the need for the security-related expenditures the Companies continue to make to

safeguard these resources against attack. It is beyond debate that these expenditures to safeguard the Companies' generating resources are of utmost importance not only to Ohio's economy, but to the health and welfare of persons living in and beyond the Companies' service territories.

The Plan sets a cap on annual increases for generation rates for each of the Companies. While the Companies hereby reserve the right to make a filing under Ohio's emergency rate statute, customers will have certainty instead of the unknown results inherent with a MBSSO/CBP regimen. These capped increases will provide the first increases in CSP's and OP's rates since 1994 and 1995, respectively. Moreover, these annual increases affect only the generation portion of customers' total bills. Consequently, the percentage increases proposed by the Companies for the generation portion of electric service result in a much lower percentage increase on a total bill basis for all residential customers and most non-residential customers.

Even with the Companies' proposed increases, their generation charges and total charges will compare favorably to Ohio's other electric utility companies. Moreover, if customers believe that prices available in the market are more favorable than the Companies' rates they will remain free to switch to a CRES provider.

These increases will produce a greater opportunity for CRES providers to successfully market competitive generation to the Companies' customers. It is the Companies' expectation that by the end of the Rate Stabilization Period the opportunity for the development of a competitive market for the generation component of electric utility service in the Companies' service territories will have been enhanced.

Finally, the Companies' Plan addresses the existing temporary discount residential customers receive on their rates for generation service. The General Assembly recognized that the discount could create a barrier to the development of a competitive market for generation service. Therefore, it balanced the desire to assure that residential customers

would receive some benefit from S.B.3 with the desire to develop a competitive market. Pursuant to §4928.40(C), Ohio Rev. Code, the Commission can terminate the temporary discount if it finds that the discount is "unduly discouraging market entry" by CRES providers. Termination of the discount could not have occurred prior to the midpoint of the MDP, i.e., June 30, 2003. This plan provides the Commission the opportunity to remove the discount prior to the end of the MDP in order to stimulate the move to a more competitive market and to create a more gradual cost change for residential customers.

In the context of going to market based generation rates at the end of the MDP, as provided in §4928.14(A) and (B), Ohio Rev. Code, the Companies previously agreed not to ask the Commission to terminate the temporary discount prior to the end of the MDP. For the purpose of developing an alternative Rate Stabilization Plan, the Companies have lowered the residential customers' three annual increases as if the temporary generation discount would terminate June 30, 2004, a year beyond its statutorily guaranteed duration. Then their generation rates will increase 1.6% for CSP customers and 5.7% for OP customers at the start of 2006, 2007 and 2008.

If the Commission decides to retain the temporary discount in effect through the end of the MDP, then the residential customers' annual increases would be at the same level as the non-residential customers' increases. CSP's and OP's residential customers' generation rates will increase by 8.42% and 12.63%, respectively, at the start of 2006 (due to the compounding of the statutorily mandated elimination of the temporary 5% discount and the first of the Companies' annual increases), and 3% and 7%, respectively, at the start of 2007 and 2008. Therefore, the Companies believe that their alternative proposal provides a more levelized transition for residential customers.

While there are other important features to the Companies' Plan, those features that are discussed above form the foundation for a Plan designed to provide generation rate stability and certainty, encourage competition in the market for generation services, enable

the Companies to preserve low-cost generating facilities that will keep market prices lower than they otherwise would be and provide a more levelized path toward market based rates for customers.

Finally, under the Plan, the Companies' customers will continue to have the right to switch to a CRES provider for generation service. Those customers who do not switch, however, will be assured that the Companies will have sufficient low cost generation resources to provide that service, provided the Plan is approved by the Commission.

The Companies recognize that the rules adopted in Case No. 01-2164-EL-ORD could soon become effective and filings under those rules could be required by the middle of the year. Therefore, the Companies hope that the Commission will expedite its consideration of this application so as to avoid the potential confusion and waste of resources associated with two proceedings heading in different directions. To that end, the Companies request that the Commission promptly schedule a technical conference, which would provide an opportunity for interested parties to seek clarification from the Companies on any matters raised by this application, and establish an expedited procedural schedule.

The Companies support the Commission for its encouraging Ohio's electric utility companies to propose rate stabilization plans which would be implemented at the conclusion of the MDP. The Companies' Plan is our effort to respond to that encouragement in a manner which benefits all stakeholders. We believe the Plan is fair and reasonable for both our customers and the Companies. Therefore, the Companies request that the Commission approve the Plan.

THE PLAN

1. Distribution Service: Except for each Company's Universal Service Fund Rider, Energy Efficiency Fund Rider, other tariff provisions authorizing cost-based charges,

and cost recovery specifically provided for by the Ohio Revised Code, such as the recovery of right-of-way charges, CSP's and OP's distribution electric rates and charges as unbundled in Case Nos. 99-1729-EL-ETP and 99-1730-EL-ETP, respectively, and which are in effect on December 31, 2005, will remain the same through December 31, 2008. However, those distribution rates and charges can be adjusted, through a filing with the Commission, during the Rate Stabilization Period (RSP): a) in the event of an emergency under §4909.16, Ohio Rev. Code; or b) as a result of increased distribution-related expenses associated with complying with changes in laws, rules or regulations related to environmental requirements; security; taxes; operation and maintenance associated with new requirements imposed on the Companies by federal or state legislative or regulatory bodies after January 31, 2004; and major storm damage service restoration.

Further, these distribution rates will be adjusted to recover, in the manner described in Section 6 below, regulatory assets to be recorded in 2004 and 2005 plus carrying costs thereon, for deferred RTO administrative charges, adjusted for net congestion costs, imposed on the Companies commencing with their integration into the PJM RTO; and deferred equity carrying costs on capital expenditures plus a full carrying cost in 2004 and 2005 on in-service capital expenditures since January 1, 2002 to comply with regulatory requirements. The distribution rates also can be adjusted to reflect changes in the allocation of transmission/distribution facilities under FERC's seven-factor test, which adjustment will be made in a proceeding initiated by one or both Companies to address only this adjustment.

2. Fixed Generation Service Rate Increases: For CSP and OP, the generation rates, both demand and energy, as applicable, in its standard service tariff for all non-residential customer classes will be increased over the previous year's rates by 3% per year and 7% per year, respectively, for each of the years 2006, 2007 and 2008. The Companies offer as an alternative to these increases for CSP and OP residential customers that instead the Commission can authorize termination of the temporary 5% generation discount on June

30, 2004. The CSP and OP generation rates in their standard service tariff for residential customer classes then will be increased over the previous year's charges by 1.6% per year and 5.7% per year, respectively, for each of the years 2006, 2007 and 2008. These increases result in much lower percentage increases on a total bill basis for all residential customers and most non-residential customers. Each of these increases for non-residential and residential customers will be effective with the first billing cycle in each of those years the increases are in effect.

While discussing this alternative, the Companies are mindful that their residential customers might have anticipated that the 5% generation temporary discount would be in place until December 31, 2005. The Companies believe, however, that such an expectation could only be warranted in the context of a shift to the MBSSO/CBP found in §4928.14, Ohio Rev. Code.

As discussed above, one of the policies which this application promotes is rate stability and certainty throughout the RSP. By terminating the 5% temporary discount on June 30, 2004, the three-step percentage increases for residential customer classes, which will begin a year and a half later, can be reduced from those proposed for all other customer classes.

If the Commission determines that the 5% temporary discount should remain in effect until December 31, 2005, then residential customers will experience a larger increase on January 1, 2006 -- the statutory elimination of the temporary 5% discount plus the first of three annual increases of 3% for CSP customers and 7% for OP customers. Therefore, the Companies believe the more streamlined path from the currently frozen discounted rates for generation service provides greater stability for residential customers and should be approved.

3. Limits on Additional Generation Service Rate Increases: During the RSP, the Companies may further adjust the generation rates and related riders of the standard service

tariff, beyond those specified in Section 2 of the Plan, for increased expenditures (whether capitalized or expensed) incurred either directly, or indirectly through an affiliated pooling arrangement, for complying with changes in laws, rules or regulations related to environmental requirements, security, taxes and any new generation-related regulatory requirement imposed by statute, rule, regulation or administrative or court order. Such an adjustment also can be made if customer load switches to service from a CRES provider such that the loss of that load materially jeopardizes either or both Companies' ability to recover the increased revenues reasonably anticipated pursuant to Section 2 and this section.

Before OP or CSP may implement any increase beyond the increases specified in Section 2 above, each Company shall apply to the Commission for such an increase. After a hearing and a showing that such expenditures were reasonably incurred, the Commission shall approve the increase. If the Commission has not issued a final order concerning such a filing within 90 days of the Company's filing, the proposed increase will become effective on an interim basis and will remain in effect until such time as the Commission's final order is implemented. The Commission's final order shall provide for a reconciliation of the increase authorized in the final order as compared to the interim increase that had been in effect.

In no case shall the combination of any increases from this Section and that of Section 2, above, for either CSP or OP be greater than an average of 7% per year or 11% per year, respectively, for the years 2006, 2007 and 2008, not including the effects of the expiration of the temporary residential discount.

4. RTO Cost Recovery: CSP and OP each may choose to adjust the transmission components of their standard service tariffs to reflect the applicable FERC-approved charges or rates related to open access transmission, net congestion and ancillary services. Such charges include those imposed on the Companies directly or costs imposed on the Companies indirectly through a FERC-approved regional transmission organization

(RTO), including, but not limited to, RTO administrative charges imposed, amortization of RTO start-up costs, and/or surcharges for recovery of lost transmission revenues. However, in all cases, the transmission components of the standard service tariffs may be adjusted pursuant to this Section only if the adjustment is attributable to the applicable Company, affiliated company or RTO Open Access tariff filed at the FERC or is imposed by the RTO. Any adjustment to the transmission component of the standard service tariffs will become effective thirty days after a filing is made for such an adjustment unless the Commission delays the effective date of the adjustment. No such delay will be for a period greater than sixty days after the Company's filing. At the conclusion of sixty days after the filing, the adjustment will be effective unless it has been rejected by the Commission for good cause. RTO administrative charges, adjusted for net congestion costs, imposed on the Companies commencing with their integration into the PJM RTO through December 31, 2005 will be deferred, as described in Section 6, below, along with related carrying charges based on the weighted average cost of capital, and included in recovery adjustments that the Companies make under Section 1, above.

5. Recovery of Regulatory Assets: The Companies will continue to recover through their standard service and open access distribution tariffs the amortization of the generation-related transition regulatory assets under the rates contained in Attachment 1 of the May 8, 2000 Stipulation and Recommendation filed and approved in Case Nos. 99-1729-EL-ETP and 99-1730-EL-ETP and as reflected in the Companies' Regulatory Asset Charge Riders. Pursuant to that Stipulation and Recommendation, the Companies will continue to defer expenditures incurred for Customer Education, Customer Choice Implementation and Transition Plan Filings through December 31, 2005, plus a carrying charge at the weighted average cost of capital, which expenditures exceed the first \$20 million incurred by each Company, for such activities. Customer Education, Customer Choice Implementation and Transition Plan Filing Costs, incurred after December 31, 2005 and all Rate Stabilization

Plan Filing Costs will be deferred as a distribution regulatory asset until recovered, along with carrying charges at the weighted average cost of capital, in future distribution rates, through distribution riders to the Companies' applicable tariffs. Determination of the costs to be recovered, including the carrying charge, will be subject to review by the Commission.

6. Accounting Authority: The Companies request authorization to record regulatory assets in accordance with Statement of Financial Accounting Standards No. 71, Accounting For The Effects Of Certain Types Of Regulation, on the regulated business for the following two items included in this application: (1) the deferral on the regulated business of RTO administrative charges, adjusted for net congestion costs, imposed on the Companies commencing with the Companies' integration into PJM through December 31, 2005 and included in PJM RTO billings as described in Section 4 above and a carrying cost thereon until recovered; and (2) the deferral, in 2004 and 2005, on the Companies' regulated business of a current year supplemental equity carrying charge on the Companies' construction expenditures beginning January 1, 2002 in Account 107, Construction Work In Progress, and a full carrying charge on in-service capital expenditures included in Account 101 Plant In-Service beginning January 1, 2002 and carrying costs thereon for the construction and installation of equipment to comply with requirements imposed by statute, rule, regulation or administrative or court order inclusive of environmental, security and other requirements.

The RTO regulatory deferral will be recorded on the books of the regulated business commencing with the Companies' integration into PJM and amortized over a three-year period commensurate with its recovery beginning in January 2006, through a non-bypassable distribution rider. During the three-year recovery period the Companies will defer a carrying cost on the unrecovered balance of the deferred RTO costs at the full weighted average cost of capital rate until the deferred RTO costs and related deferred carrying costs are fully recovered.

The carrying cost regulatory asset deferral applicable to required capital expenditures beginning January 1, 2002 will be recorded on the books of the regulated business commencing on January 1, 2004 and amortized over a three-year period commensurate with recovery beginning in January 2006 through a non-bypassable distribution rider. The equity carrying cost regulatory asset deferral will supplement the capitalization in Account 107 of a debt-related carrying charge under the FASB's Statement of Financial Accounting Standards (SFAS) No. 34, Capitalization of Interest Cost, in order to provide for an equity return during construction. The accrual of a supplemental equity carrying cost distribution regulatory asset in 2004 and 2005 will be computed by applying the excess of the full weighted average cost of capital rate (with the equity component being the rate in each Companies' last rate filing) over the SFAS 34, interest only capitalization rate to all required construction expenditures beginning January 1, 2002 in Account 107. The carrying cost on the in-service amount of such capital expenditures will be computed at the full weighted average cost of capital, with the equity component being the rate in each Companies last rate filing. A carrying cost will be deferred on the unrecovered balance of the regulatory asset and will continue after the distribution rider becomes effective and until the regulatory asset is fully recovered in order to provide for a carrying cost at the full weighted average cost of capital rate described above on the unrecovered balance. This will provide the Companies with a current equity return in 2004 and 2005 on required capital expenditures not in service and a full current year return on such expenditures after they go in service and carrying costs thereon until the regulatory asset is fully recovered. The Companies are not requesting this deferral to be retroactive to recapture lost carrying costs for periods prior to January 1, 2004.

7. Shopping Incentives: Through the Market Development Period and the Rate Stabilization Period, CSP will make available to the first 25% of residential class load that switches to a CRES provider a shopping incentive of 2.5 mills/kWh. Therefore, any unused portion of the shopping incentive as measured at December 31, 2005 will not be credited by

CSP to its Regulatory Asset Charge recovery. As a result, upon approval of this Plan, CSP will reverse to income any unused shopping credit previously used to reduce the transition regulatory asset balance and cease offsetting unused shopping credits against the transition regulatory asset. There will be no additional shopping incentive for any CSP customers during the Rate Stabilization Period.

As agreed to in the May 8, 2000 Stipulation and Recommendation, for the period of January 1, 2006 through December 31, 2007, the first 20% of OP residential customer load that was on OP's standard service tariff as of December 31, 2005 which switches to a CRES provider will not be charged the Regulatory Asset Charge Rider during that 2006-2007 two-year period. Customer load which remains on the Companies' standard service tariff under § 4928.14(A) or (B), Ohio Rev. Code, does not count as being load which switches to a provider. There will be no shopping incentive for any OP customers during the Rate Stabilization Period.

8. Future Proceedings: The Companies believe that by the end of the Rate Stabilization Period, the competitive market for electric generation service will more closely resemble what the Ohio General Assembly envisioned, when it enacted S.B.3, as being in place by the end of the MDP. However, there are no assurances that such a market will exist by the end of the RSP. Therefore, it is recommended that the Commission conduct a proceeding to determine the manner in which electric generation service should be provided to the Companies' customers after the conclusion of the Plan. The Commission should consider various options ranging from a "flash cut" completion of the transition to competition, to returning to traditional cost-of-service regulation. It is further recommended that the Commission complete and report the results of this proceeding to the Ohio General Assembly no later than December 31, 2005 so that sufficient time will be available for the consideration and enactment of any legislation which might be needed. The report would

include recommendations to the General Assembly. Before making such recommendations, the Commission should provide an opportunity for input by all interested parties.

9. Functional Separation: Each Company will continue to be functionally separated.

10. Participation in Competitive Bidding Processes: The Companies, either individually or together, will be permitted to submit bids in response to any other electric utility companies' competitive bidding process which ultimately becomes effective under rules promulgated pursuant to §4928.14, Ohio Rev. Code.

11. Minimum Stay: During the Rate Stabilization Period, residential and small commercial (GS-1) customers returning to either Company's standard service tariffs must remain on that Company's standard service tariff through April 15 of the following year if that customer took generation service from the Company at any time during the period from May 16 to September 15. During the Rate Stabilization Period, a 12-month minimum stay is required for large commercial and industrial customers returning to service under the Companies' standard service tariff.

12. Effect of Plan: Unless changed by this Plan, the Stipulation and Recommendation in Case Nos. 99-1729-EL-ETP and 99-1730-EL-ETP and the Companies' filed standard service and open access distribution tariff provisions will not be changed.

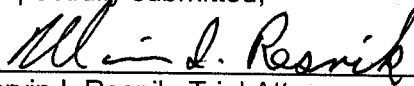
CONCLUSION

Consistent with proposed §4901:1-35-04, Ohio Admin. Code, the Companies are providing notice of this filing to each party in their Electric Transition Plan cases and to all Commission-certified CRES providers, except those that are governmental aggregators in cities and villages not served by either Company. Further, the Companies will make available a copy of this application on their website and at the Companies' main offices.

The Companies invite interested stakeholders to join in support of this Plan. The Companies' Plan advances the public interest by offering rate stability and certainty and by encouraging the further development of a competitive market for generation service in the Companies' service territories. Further, the Companies' Plan, if approved by the Commission, will help maintain an adequate supply of generating capacity for the future at reasonable price levels which move toward the prices of a competitive market during the Rate Stabilization Period.

Therefore, the Companies urge the Commission to approve the Companies' Plan as filed.

Respectfully submitted,



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