FILE

Office of the Ohio Consumers' Counsel
Janine L. Migden-Ostrander
Consumers' Counsel
Your Residential Utility Advocate

April 13, 2007

Ms. Renee Jenkins, Director
Public Utilities Commission of Ohio
Docketing Division
180 East Broad Street, 13th Floor
Columbus, Ohio 43215-3793

Re: OCC's Initial Post-Hearing Brief, Case Nos. 03-93-EL-ATA, et al.

Dear Ms. Jenkins:

Attached please find three "Confidential" copies of OCC's Initial Post-Hearing Brief in the above captioned Consolidated Cases. Pursuant to an oral Motion for Protective Treatment of Confidential Materials, which the Attorney Examiners' granted at hearing on March 21, 2007, parties were formally instructed to file the confidential versions of their briefs under seal.[1] Consistent with the Attorney Examiner's ruling on this matter, please file all copies of OCC's "Confidential" Initial Post-Hearing Brief under seal.

In addition, please find copies of OCC's redacted (public version) Initial Post-Remand Brief – Phase I, which should be docketed for public access.

Very truly yours,

Jeffrey L. Small
OCC Trial Attorney

Cc: Persons on electronic service list

[1] Tr. Vol. III at 176-177 (March 21, 2007).

FILE

76

BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

Consolidated Duke Energy Ohio, Inc. Rate Stabilization Plan Remand and Rider Adjustment Cases.	)	Case Nos. 03-93-EL-ATA
	)	03-2079-EL-AAM
	)	03-2080-EL-ATA
	)	03-2081-EL-AAM
	)	05-724-EL-UNC
	)	05-725-EL-UNC
	)	06-1068-EL-UNC
	)	06-1069-EL-UNC
	)	06-1085-EL-UNC

PUBLIC VERSION

INITIAL POST-REMAND BRIEF, HEARING PHASE I, BY THE OFFICE OF THE OHIO CONSUMERS' COUNSEL

Janine L. Migden-Ostrander
Consumers' Counsel

Jeffrey L. Small, Trial Attorney
Ann M. Hotz
Larry S. Sauer
Assistant Consumers' Counsel

Office Of The Ohio Consumers' Counsel
10 West Broad Street, Suite 1800
Columbus, Ohio 43215-3485
Telephone: 614-466-8574
Fax: 614-466-9475
E-mail: small@occ.state.oh.us
hotz@occ.state.oh.us
sauer@occ.state.oh.us

Dated: April 13, 2007

TABLE OF CONTENTS

TABLE OF CONTENTS cont'd

Page

TABLE OF CONTENTS cont'd

Page

BEFORE
THE *PUBLIC UTILITIES COMMISSION OF OHIO*

Consolidated Duke Energy Ohio, Inc. Rate Stabilization Plan Remand and Rider Adjustment Cases.	)	Case Nos. 03-93-EL-ATA
	)	03-2079-EL-AAM
	)	03-2080-EL-ATA
	)	03-2081-EL-AAM
	)	05-724-EL-UNC
	)	05-725-EL-UNC
	)	06-1068-EL-UNC
	)	06-1069-EL-UNC
	)	06-1085-EL-UNC

PUBLIC VERSION

INITIAL POST-REMAND BRIEF, HEARING PHASE I, BY THE OFFICE OF THE OHIO CONSUMERS' COUNSEL

I. PREFATORY COMMENTS

These cases, on remand from the Supreme Court of Ohio, are important for their determination of, among other matters, the manner in which generation rates will be set for 600,000 residential utility customers and tens of thousands of other customers for the 2007-2008 period. The Public Utilities Commission of Ohio ("PUCO," or "Commission") has important decisions to make about the future of electric choice in areas served by Duke Energy Ohio, Inc. ("Duke Energy Ohio" or the "Company," including its predecessor company, "CG&E") and the rates residential customers and Ohio businesses will pay for generation service. The General Assembly intended that the Commission would approve reasonable standard service offer rates as well as provide a real opportunity for customers to have competitive options to the generation rates

provided by Duke Energy Ohio. The record supports the need for the Commission to take corrective actions that support reasonable prices and the development of the competitive market.

The issues presented in these cases require the Commission to make determinations on matters of law and policy. Serious problems exist in Duke Energy Ohio's proposals. In the absence of a competitive framework to protect customers, Duke Energy Ohio has submitted proposals to increase its standard service rates for generation service. Ohio law and sound policy require the Commission to modify Duke Energy Ohio's proposals for pricing the standard service offer rates that the Company proposes to charge its customers.

II. INTRODUCTION

A. Remand from the Supreme Court of Ohio

The duration of some of the cases captioned above -- the first of which began in January 2003 -- is partly the result of an appeal and remand by the Supreme Court of Ohio ("Court").[1] The matters addressed by the Court that necessitated the remand have been extensively discussed in pleadings regarding the appropriate scope for the hearings that followed the remand.[2] The Court stated that the "portion of the commission's first rehearing entry approving CG&E's [now Duke Energy Ohio's] alternative proposal is devoid of evidentiary support."[3] The Court also stated that the "commission abused its

---

[1] *Ohio Consumers' Counsel v. Pub. Util. Comm.*, 111 Ohio St.3d 300, 2006-Ohio-5789 (*"Consumers' Counsel 2006"*).

[2] See, e.g., Duke Energy Ohio's Motion for Clarification (December 13, 2006) and the OCC's Memorandum Contra Motion for Clarification (December 20, 2006).

[3] *Consumers' Counsel 2006* at ¶28.

discretion in barring discovery of side agreements."[4] The Office of the Ohio Consumers' Counsel ("OCC") presented extensive evidence regarding the missing support for Duke Energy Ohio's standard service offer rate proposals as well as the problems caused by side agreements that the Company entered into with the intent of removing opposition to the its proposals that affected many other customers. The Commission should act upon this evidence and modify its previous entries.

The OCC's appeal of that portion of the case that concluded in 2004 (hereinafter, "*Post-MDP Service Case*") challenged the Commission's authority to determine standard service offer rates for generation service without relying upon actual markets to set rates.[5] The Court, however, deferred to the Commission's determinations regarding the establishment and modification of rates,[6] a matter that the Commission stressed by stating that "the governing statute allows for flexibility in the determination of such [market-based standard service offer] charges . . . ."[7] The decision regarding the Commission's subject matter authority to approve and impose generation rates upon customers also decided the Commission's subject matter authority regarding these same rates without the

[4] Id. at ¶94.

[5] OCC Notice of Appeal, Propositions of Law 1 and 2 (March 18, 2005 in Appeal 05-518; May 23, 2005 in Appeal 05-946).

[6] *Consumers' Counsel 2006* at ¶44 and ¶56.

[7] Entry on Rehearing at 18, ¶20 (November 23, 2004).

requirement that Duke Energy Ohio provide generation service at "voluntary" rates.[8] The determination of rates that customers *must pay* in these recent proceedings ("*Post-MDP Remand* Case"[9]) is the same subject matter as the rates that Duke Energy Ohio *must charge* for its standard service offer. The result in *Consumers' Counsel 2006* does not rely upon Duke Energy Ohio being a volunteer under its statutory obligation to "offer . . . all competitive retail electric services necessary to maintain essential electric service to consumers" and "file[ ] [such offer] with the public utilities commission under section 4909.18 of the Revised Code."[10]

The Commission should exercise its discretion and flexibility and require Duke Energy Ohio to provide new standard service offer rates based upon the evidence presented during the hearings on remand.[11]

B. Burden of Proof

The burden of proof regarding the applications submitted in these cases rests upon Duke Energy Ohio. The posture of these cases -- in which various proposals for rate

[8] Duke Energy Ohio previously stated its intention to charge customers according to its proposal submitted to the Commission on January 10, 2003, but asked the Commission to "acknowledge these statutory rights." Duke Energy Ohio Application for Rehearing at 30 (October 29, 2004). The Company has never fully explained the extent of its claimed right to action independent of that approved by the Commission, which includes more recent statements after the remand. Duke Energy President Meyer was asked at the recent hearing whether the Company would not comply with the Commission's order on remand regarding standard service pricing. She responded that "the company may seek rehearing and provide alternatives." Tr. Vol. I at 45-46 (2007).

[9] For notational convenience, the portions of the case before and after the Court's deliberations are cited separately. However, a single record exists. Exhibit references to the proceedings after remand from the Court, the *Post-MDP Remand Case*, contain the word "Remand" to distinguish them from the earlier exhibits.

[10] R.C. 4928.14(A).

[11] For example, the record evidence supports the suspicion of the Supreme Court of Ohio that "the infrastructure-maintenance fund [charge] may be some type of surcharge and not a cost component." *Consumers' Counsel 2006* at ¶30.

changes for components of standard service offers for 2007-2008 have been linked by consolidation with the remand of the underlying Case No. 03-93-EL-ATA, et. -- does not alter the burden of proof.

The OCC does not bear any burden of proof in these cases. In a hearing regarding a proposal that does not involve an increase in rates, R.C. 4909.18 provides that "the burden of proof to show that the proposals in the application are just and reasonable shall be upon the public utility." In a hearing regarding a proposal that does involve an increase in rates, R.C. 4909.19 provides that, "[a]t any hearing involving rates or charges sought to be increased, the burden of proof to show that the increased rates or charges are just and reasonable shall be on the public utility." In the following sections, the OCC will explain how Duke Energy Ohio has failed to prove that its post-MDP pricing proposals should be adopted without alteration by the Commission.

C. The OCC Framework

The OCC will address and amplify the general concern, stated by the Commission in its Entry on Rehearing in the *Post-MDP Service Case*, regarding the reasonableness of alleged cost components upon which Duke Energy Ohio's standard service offer rates were built. The Commission previously stated: "It is not in the public interest to cede this review. Nor would it foster any rate certainty to allow all decisions of this nature [regarding rate components] to be free from Commission review of reasonableness."[12] The Commission should carefully consider the components devised by Duke Energy Ohio to ensure, pursuant to Ohio policy stated in R.C. 4928.02(A), "the availability . . . of

[12] Entry on Rehearing at 10 (November 23, 2004).

adequate, reliable, safe, efficient, nondiscriminatory, and reasonably priced retail electric service."[13]

The OCC also emphasizes the major theme that echoes from R.C. 4928.02(B)-(H), whereby it is Ohio policy to support competition and competitive options for customers regarding retail electric service. This theme provides the backdrop for the third of the Commission's goals for "rate stabilization plans" -- "further development of competitive markets."[14] Switching statistics since the time of the hearings in 2004 in the *Post-MDP Service Case* show that the competitive market is in retreat, and the evidence in this case demonstrates how Duke Energy Ohio has orchestrated such an event as part of its settlement of the *Post-MDP Service Case*. Duke has acted in contravention of the policy of the State of Ohio and Commission's goal that rate stabilization plans encourage the competitive market. Barriers to competition should be removed.

The concurring opinion by Chairman Schriber to the original Order in the *Post-MDP Service Case* connects with both of the above-stated themes (i.e. reasonable prices and competitive options) as well as with Ohio policy stated in R.C. 4928.02(I) regarding the "state's effectiveness in the global economy."

> [W]e [i.e. the commissioners] have advocated opening up more possibilities for more customers with regard to the magnitude of Cinergy's generation that might be "avoided". Furthermore, we do not believe that shopping should be deterred by the prospect of paying for costs associated exclusively with Cinergy's generation. These might include the costs of reserves, the costs of environment compliance, and security.[15]

---

[13] R.C. 4928.02(A).

[14] See, e.g., Order at 15 (September 29, 2004). The Supreme Court of Ohio recently stated that it has "recognized the commission's duty and authority to enforce the competition-encouraging statutory scheme of S.B. 3 . . . ." *Consumers' Counsel 2006* at ¶44.

[15] Order, Concurring Opinion of Chairman Alan R. Schriber at 2 (September 29, 2004).

While the Chairman's statement was not directed towards the situation confronted by residential customers, the bypassability of standard service offer charges should be examined afresh as the result of the recently concluded hearing. Those standard service offer charges should be made bypassable for all customers of Duke Energy Ohio.

D. The Documents Related to the Company's Side Deals Should be Available to the Public.

The Attorney Examiners announced at the beginning of the hearing on March 19, 2007 that a decision on whether information accumulated by the OCC should be made public will be decided along with the merits of these cases. The OCC has asked that the documents that are attached to the testimony of OCC Witness Beth Hixon be available for public inspection,[16] consistent with R.C. 149.43, 4901.12 and 4905.07 as well as Ohio Adm. Code 4901-1-24(D).[17] Ms. Hixon's testimony, as further explained in this Initial Post-Remand Brief, reveals the fallacy that agreements between affiliates of Duke Energy Ohio and parties or members of parties (referred to collectively by Ms. Hixon as "Customer Parties"[18]) to these cases are competitive supply arrangements and explains that they are settlement agreements connected with these cases.

The evidence presented at hearing exposes the intricate, behind-the-scenes dealings of the Duke-affiliated companies by which they gained the support of selected customers for their post-MDP pricing proposals and have held that support through the

[16] OCC Memorandum Contra Motions for Protective Orders at 11-12 (March 13, 2007).

[17] Id. at 9.

[18] OCC Remand Ex. 2(A) at 4 (Hixon).

proceedings on remand. The OCC presents its case through documents, but also through the words of employees and past employees of the Duke-affiliated companies. As an example, [redacted][19] [redacted][20]

The issue, therefore, is one of revealing the totality of the settlement reached between the Duke-affiliated companies (at the time, the Cinergy-affiliated companies) in the *Post-MDP Service Case* as well as revealing the continuing effect of the overall settlement on the *Post-MDP Remand Case*. The public should have access to the information.

[19] [redacted]

[20] [redacted]

III. PROCEDURAL HISTORY OF THE CASES

On January 10, 2003, the Company filed an application ("January 2003 Application"[21]) containing proposals to provide a market-based standard service offer and to establish an alternative competitive bidding process for the period after the market development period for non-residential customers.[22] Numerous parties and the Commission's staff ("Staff") filed comments on the Company's proposals in March and April 2003.

On December 9, 2003, the Commission issued an entry that stated:

> As the competitive retail market for electric generation has not fully developed in the CG&E [now Duke Energy Ohio] territory, the Commission finds it advisable that CG&E file a rate stabilization plan as part of these proceedings, for the Commission's consideration.[23]

The Entry also set a procedural schedule.

On January 26, 2004, the Company filed another application ("January 2004 Application"). The January 2004 Application proposed that the Commission approve either the approach contained in the January 2003 Application (the "competitive market option," or "CMO") or a substitute plan ("ERRSP Plan") for pricing generation service that the Company submitted for approval in response to the Commission's request on December 9, 2003.[24]

---

[21] The January 2003 Application initiated Case No. 03-93-EL-ATA.

[22] January 2003 Application at 1.

[23] Entry at 5 (December 9, 2003).

[24] January 2004 Application at 8.

On March 22, 2004, the OCC moved to continue these cases until after the Staff prepared a report on its investigation. Among other matters, the OCC was concerned that discovery responses from Duke Energy Ohio stated that explanations of its applications would be forthcoming only in pre-filed testimony. An entry was issued on April 7, 2004 that extended the procedural schedule a few weeks and set these cases for hearing on May 17, 2004 and did not provide for a Staff report of investigation. Duke Energy Ohio submitted pre-filed testimony on April 15, 2004 in which it described its "revised ERRSP." The PUCO Staff filed testimony on April 22, 2004 and intervening parties, including the OCC, filed testimony on May 6, 2004.

The hearing was delayed in connection with the filing of a stipulation in these cases that described another plan of service ("Stipulation Plan" as described in the "Stipulation" filed on May 19, 2004[25]). Duke Energy Ohio, Staff, Dominion Retail, Green Mountain Energy, FirstEnergy Solutions, and other parties (including several large customers and membership organizations made up of large customers) executed the Stipulation. The Ohio Marketers Group ("OMG," consisting of MidAmerican Energy, Strategic Energy, Constellation Power Source, Constellation NewEnergy and WPS Energy Services), PSEG Energy Resources, the National Energy Marketers Association, the OCC and the Ohio Manufacturers Association representing broad customer groups,[26] and OPAE did not execute the Stipulation.

[25] The Stipulation was later submitted and admitted as Joint Ex. 1.

[26] The Ohio Manufacturers Association stated in its Motion to Intervene that it is "the only statewide association exclusively serving manufacturers. It has more than 2,400 Ohio manufacturing companies as members." OMA Motion to Intervene at 2 (March 5, 2004).

The parties who did not execute the Stipulation were permitted a very short period during which they could inquire into the Stipulation by means of discovery. The OCC sought copies of all side-agreements between Duke Energy Ohio and other parties in these cases, and the Company refused to provide copies of such agreements. The first witness appeared at hearing on May 20, 2004 (based on pre-filed testimony not related to the Stipulation). The OCC began the hearing on May 20, 2004 with an oral Motion to Compel Discovery of side agreements. The Motion to Compel Discovery was denied. [27]

Duke Energy Ohio filed supplemental testimony on May 20, 2004 in support of the Stipulation, and Staff Witness Cahaan submitted supporting testimony on May 24, 2004. The OCC and OMG submitted testimony in opposition to the Stipulation on May 26, 2004. The hearing resumed on May 26, 2004 (after two days in recess) for the testimony of witnesses for Duke Energy Ohio, the OCC, the OMG, and one witness for the Staff.

The Commission's Order in the *Post-MDP Service Case* was issued on September 29, 2004, which approved the May 19, 2004 Stipulation with some conditions. Several parties, including Duke Energy Ohio and the OCC, filed applications for rehearing on October 29, 2004. The Company asked the PUCO to either i) approve its original CMO proposal; ii) approve the Stipulation, or iii) approve a new rate plan ("New Proposal") that was proposed for the first time in the Company's Application for Rehearing.

In a November 23, 2004 Entry on Rehearing, the PUCO adopted (in principal part) the New Proposal. The Commission ordered the Company to submit filings with the Commission before Duke Energy Ohio could place certain of the rate increases in the New Proposal into effect.

---

[27] Tr. Vol. II at 8, line 4 though 15 (2004).

The OCC initiated its appeal on May 23, 2005. The Supreme Court of Ohio issued its opinion on November 22, 2006. The Court held that the PUCO erred by failing to properly support modifications to post-MDP rates in the PUCO's November Entry on Rehearing and erred by failing to compel the disclosure of side agreements,[28] and remanded the case for additional consideration by the Commission.

On November 29, 2006, the Attorney Examiner issued an Entry in the above-captioned cases that provided for a "hearing . . . to obtain the record evidence required by the court," and ordered that a prehearing conference be held on December 14, 2006.[29] The above-captioned cases were consolidated (i.e. constituting the *Post-MDP Remand Case*). A procedural Entry was issued on February 1, 2007 that, among other matters, set a cut-off date for discovery and a hearing date for March 19, 2007.

On February 2, 2007, the *Post-MDP Remand Case* was set for hearing in two phases, the first of which would address the framework for post-MDP rates and the second of which would address various matters regarding the level of rates. The hearing on the first phase was conducted in three days, beginning on March 19, 2007. A briefing schedule was set at the conclusion of the first phase of the hearings.[30]

---

[28] *Ohio Consumers' Counsel v. Public Util. Comm.*, 111 Ohio St.3d 300, 2006-Ohio-5789 at ¶95 ("*Consumers' Counsel 2006*").

[29] Entry 3, ¶(7) (November 29, 2006).

[30] The second phase of the hearings began on April. 10, 2007. The substance of the second phase will be addressed in a subsequent brief.

IV. ARGUMENT

A. The Pricing of the Post-MDP Standard Service Offer Lacks a Reasonable Basis, and Results in Unreasonably Priced Retail Electric Service for Customers.

1. Overview

Duke Energy Ohio's current standard service offer generation rates are neither firmly based on accounting costs, as they would be under traditional electric utility ratemaking, nor are they based on prices determined in actual markets.[31] Rather, the standard service offers are composed of a variety of components having different bases. Some components are based on dated historical accounting costs, others are based on accounting costs of services currently acquired by Duke in the market place, and yet others are poorly-defined, partly duplicative and quantitatively uncertain estimates of costs or risks allegedly borne by Duke Energy Ohio.[32] As stated by OCC Witness Talbot, "[t]his confusion allows the Company's proposals to avoid thorough scrutiny."[33]

The Commission should only approve standard service offer rates that, in the absence of true market pricing, move to rates whose bases can be checked and monitored by the PUCO rather than being based on Duke Energy Ohio's desires. The objective should be to approve a good proxy for market-based rates based upon measurable and verifiable costs.[34] Duke Energy Ohio pays lip service to this principle, and offered the speculations and oscillating presentations by Duke Energy Ohio Witness Rose both in

[31] OCC Remand Ex. 1 at 3-4, 6 (Talbot).

[32] Id. at 4-6.

[33] Id. at 55.

[34] Id. at 6. OCC Witness Talbot testified that rate components should "meet[ ] the double standard of reflecting measurable accounting costs and verifiable costs." Id. at 47.

2004 and in the 2007 hearing as the measure of the market.[35] The Commission's best alternative -- and the direction that the Commission seems to have begun in the *Post-MDP Service Case*[36] -- is to devise better defined and more tightly constructed cost-based rates that would provide a reasonable proxy for market-based rates.

Considering the limited amount of time (about twenty months) covered by the current proceeding regarding standard service offer rates, it may be more practical for the Commission to tighten-up the cost basis of the current standard service offer than to institute a process that depends more fully on observed market prices.[37] In making this observation, the OCC is in no way presaging its recommendations for the period beginning in 2009, when different considerations may apply. With a longer period upon which to formulate and implement a post-MDP pricing plan, more options exist for determining prices for Duke Energy Ohio's standard service offer generation service.[38]

2. The Commission should focus on the capacity charges in Duke Energy Ohio's standard service offer rates.

a. The standard service offer charges related to capacity are duplicative and not based upon measurable and verifiable costs.

The Commission should consider the reasonableness of Duke Energy Ohio's standard service offer rates with regard to the relationship between the components

[35] See the later discussion regarding the unreliability and variability of the CMO pricing presented by Company Witness Rose.

[36] OCC Remand Ex. 1 at 6 and 70 (Talbot).

[37] During the hearing, OCC Witness Talbot discussed the immediate-term tightening of the cost basis for the 2007-2008 period, as well as how the Commission's options expand for a later time period. Tr. Vol. III at 56-57 (2007) (Talbot).

[38] Id.

proposed by the Company. As stated by OCC Witness Talbot, "[t]here should be no overlap or duplication of items and the components should work together to achieve standard service offer rates that provide for reasonably priced service and meet the three standards of rate stability for customers, financial stability for the company, and encouragement of competition."[39] The plan proposed by Duke Energy Ohio in its Application for Rehearing provides for duplicative capacity charges, and therefore does not provide for reasonably priced generation service for the Company's customers.

The duplication of capacity charges is exhibited by qualitative responses to the OCC's inquiries regarding the support for capacity-related charges in the Company's standard service offer rates. The Company states that "[l]ittle g and the IMF [i.e. the Infrastructure Maintenance Fund] represent compensation for the Company's *existing* capacity."[40] The Company also states that "[t]he RSC is the Company charge for providing a stable market price over a prolonged period of time."[41] OCC Witness Talbot concluded that "the basis for the IMF charge seems to be similar, if not identical, to that of the RSC charge."[42] Mr. Talbot stated that "[t]here appears to be over-charging for existing capacity to the extent that little g and the RSC and the IMF are all recovering the

[39] OCC Remand Ex. 1 at 17 (Talbot).

[40] Id., NHT Attachment 6 (quoted and analyzed in OCC Remand Ex. 1 at 42) (emphasis added) (Talbot).

[41] Id., NHT Attachment 12 (quoted and analyzed in OCC Remand Ex. 1 at 53) (Talbot).

[42] OCC Remand Ex. 1 at 38 (Talbot).

costs or risks of existing capacity"[43] and that "[t]here is no assurance that these charges are not duplicative."[44]

OCC Witness Talbot shared his insights regarding the proper compensation for capacity. He noted the Company's response that the percentage of energy not used by standard service offer customers from capacity supposedly "committed" to these customers, and paid for by these customers, was "approximately 11%" in 2006.[45] There was no credit back to standard service offer customers for this period.[46] Some sharing of the costs for the capacity would be required before Duke Energy Ohio's standard service offer components could be considered cost-based (i.e. on Company's costs). The Commission previously stated that it was "convinced that CG&E may be recovering some percentage of these costs through off-system sales" when it permitted only a portion of AAC charges from the Stipulation to be charged to standard service offer customers."[47] Another basic problem with capacity costs is plainly stated by OCC Witness Talbot: "There is no justification for the IMF on the record."[48] A sound system of basing standard service offer rates on measurable and verifiable costs would provide credits to customers for sales to customers not on the Company's standard service offer rates and would eliminate the IMF charge.

---

[43] Id. at 42.

[44] Id.

[45] Id. at 43 (citing NHT Attachment 4, a response to OCC Interrogatory RI 140(k)).

[46] Id. at 43.

[47] Order at 3 (September 29, 2004).

[48] OCC Remand Ex. 1 at 48 (Talbot).

Revenues for the use of capacity that is paid for by standard service offer customers should be netted against the cost of that capacity, and the IMF charge should be eliminated.

b. The System Reliability Tracker is the sole successor to the Reserve Margin portion of the Annually Adjusted Component in the Stipulation Plan.

In assessing Duke Energy Ohio's standard service offer pricing components, the prize for vagueness, ambiguity, and duplication of charges surely must go to the IMF charge that has no basis or support from the testimony regarding the Stipulation Plan or any other testimony.[49] According to Duke Energy Ohio, the IMF's ancestry is clear -- it is one of two successor charges to the Reserve Margin portion in the original "annually adjusted component" charge in the earlier Stipulation Plan that was the subject of the Commission's hearing in May 2004.[50] The claim conflicts with the Company's response to the OCC's discovery (previously cited) that the IMF, together with "little g" compensate the Company for existing capacity.[51] The ancestry claimed by Duke Energy Ohio for the IMF is incorrect: the sole successor to the charge for the Reserve Margin under the Stipulation Plan is the System Reliability Tracker ("SRT").

The purported basis of the Company's argument in support of its New Proposal is shown in Attachment JPS-SS1 to the testimony of Company Witness Steffen.[52] The

---

[49] Id. at 48.

[50] Company Remand Ex. 3 at 26 ("The IMF was previously embedded in the reserve margin component of the Stipulated AAC price of $52,898,560.) (Steffen).

[51] OCC Remand Ex. 1, NHT Attachment 6 (quoted and analyzed in OCC Remand Ex. 1 at 42) (Talbot).

[52] Company Remand Ex. 3, Attachment JPS-SS1 (Steffen).

lower arrow in that one-page attachment asserts a connection between the Reserve Margin component ($52,898,560) from the Stipulation Plan to the SRT ($15,000,000) and IMF ($30,080,000). Since the SRT and IMF charges together amount to $45,080,000, according to Witness Steffen's Attachment JPS-SS1, an amount less than the $52,898,560 from the Stipulation Plan, Witness Steffen argues that there is no evidentiary problem regarding the basis of the SRT and IMF charges.[53] According to Company Witness Steffen: "Attachments JPS-2 through JPS-7 included in my Direct Testimony and included as Attachments to the Stipulation presented the supporting pricing calculations."[54]

This Company's argument is disingenuous. Important to the correct understanding of the charges contained in the Stipulation Plan and the New Proposal is the fact that the Reserve Margin component that resulted from the Stipulation was itself an estimate that turned out to be many times the amount actually needed to provide for a reserve margin. The addition of the IMF charge by the New Proposal to the original reserve margin estimate would far exceed the $52,898,560 Reserve Margin estimate that was contained in the Steffen testimony prefiled on April 15, 2004 and subsequently used to support the Stipulation Plan.[55]

[53] Company Remand Ex. 3 at 26-27 (Steffen). Company Witness Steffen concluded that the "evidence of record from the May Hearing fully supported the Stipulation and consequently the Alternative [i.e. New] Proposal." Id. at 30.

[54] Company Remand Ex. 3 at 20 (Steffen).

[55] Company Ex. 11, Attachment JPS-7 (Steffen).

The support for the Reserve Margin figures, as described in Mr. Steffen's Attachment JPS-7 from the *Post-MDP Service Case*,[56] is deceptively simple. The Reserve Margin calculation was obtained by multiplying 826.54 megawatts (826,540 kilowatts), which was 17 percent of the Company's projected peak megawatts for 2005, by $64 per kilowatt-year, which was the annualized cost of a new peaking unit using Electric Power Research Institute Technical Assessment Guide (EPRI-TAG) estimates.[57] The obvious flaw in this calculation is that the Midwest ISO/ ECAR/ ReliabilityFirst region had (and still has) excess capacity over and above the 17 percent required reserve margin.[58] Company testimony in 2004 confirmed this fact.[59] Not surprisingly, this excess capacity resulted in market prices for capacity that were far below the cost of building *new* generating capacity that provided the underlying basis for the Company's calculations. Thus, when the Company substituted the costs of acquiring *existing* capacity in the regional generation market -- as reflected in the SRT that was based upon estimated costs of acquiring capacity for the year ahead -- the charge dropped by 72 percent from $52,898,560 to $15,000,000 as shown in Company Witness Steffen's Attachment JPS-SS1.[60] Even this much-reduced estimate proved to be an over-estimate,

[56] Id.; see also Joint Ex. 1, Attachment JPS-7.

[57] Company Ex. 11, Attachment JPS-7 (Steffen) (reviewed by OCC Witness Talbot, OCC Remand Ex. 1 at 32).

[58] OCC Ex. 1 at 56-57 and Tr. Vol. II at 66-67 (2007) (Talbot) ("adequate capacity or more than adequate"). The 17 percent required reserve margin was subsequently reduced to 15 percent. OCC Remand Ex. 1 at 31 (Talbot).

[59] Company Ex. 7 at 33, lines 17-20 (Rose).

[60] See also, OCC Remand Ex. 1 at 46-48 (Talbot).

with the result that the SRT charge was initially too high and was subject to a true-up in favor of consumers that resulted in a negative SRT charge at the end of 2006.

It is clear, then, that the Reserve Margin charge was inappropriately based on the cost of building new peaking units at a time when there was abundant spare capacity in the region that was available at much lower prices.[61] But what is also clear is that the SRT is the sole successor to the Reserve Margin component; it is the SRT that is the charge for lining up reserve capacity.[62] The total of the charges for the SRT and the IMF only fit within the amount of the Company's Reserve Margin estimate under the Stipulation because costs for the SRT turned out to be much less than the estimates contained in Company Witness Steffen's testimony in support of the Stipulation.[63] As stated by OCC Witness Talbot:

> It is incorrect to say that, between the Stipulation and the current standard service offer, "these underlying costs were merely reduced, repositioned, made avoidable or carved out into the IMF and SRT charges." (Mr. Steffen, Second Supplemental Testimony at page 30) In fact, the IMF is a brand new charge.[64]

The IMF is a new charge from the New Proposal, one that denies customers the benefit of reduced prices that should result from actual tracking of Duke Energy Ohio's reserve margin costs.

---

[61] Id. at 46.

[62] Id. at 48.

[63] Id.

[64] Id. at 48 (Talbot), quoting Company Remand Ex. 3.

c. Neither risk, opportunity cost, nor reliability explanations support the IMF charge, and duplicative charges resulted.

The evidence demonstrates that the IMF comes from thin air, as if the Company was looking for a filler -- i.e., a new charge to add to the SRT to bring it into approximate initial equality with the old Reserve Margin estimate. The Company's justification for the IMF charge was also stated as follows: "[It] is compensation for its opportunity cost associated with committing its assets at first call to MBSSO load."[65] As OCC Witness Talbot explains, Duke Energy Ohio's arguments in support for such a charge are couched in terms of three concepts -- risk, reliability and opportunity cost -- that the Company misapplies.[66]

Regarding "risk," the Company's claim that the standard service offer adds to its level of risk is not substantiated. As OCC Witness Talbot pointed out:

> The Company cannot show what level of risk it is taking on. [I]t cannot even claim that it is taking on any net risk at all and on the face of it[, the] [sic] standard service offer reduces risk. And the Company has not justified its claims in terms of any quantitative risk analysis."[67]

More fundamentally, Mr. Talbot points out that the Company has completely misused the concept of risk. In financial parlance, risk results from having an open or uncovered position in the market, either as buyer or seller. Absent the standard service offer, the Company would be selling the electricity from its generating units into the competitive market, but with the standard service offer it has a relatively assured market for the

---

[65] DE-Ohio's response to OCC-INT-04-RI67, made part of the presentation by OCC Witness Talbot. OCC Remand Ex. 1, Attachment NHT-5.

[66] OCC Remand Ex. 1 at 37-42 (Talbot).

[67] Id. at 39 (Talbot).

output of its generating plants and therefore has a less exposed position -- i.e., one with *reduced* risk.[68]

The second concept on which the Company bases its claim for the IMF is opportunity cost. The evidentiary basis for the Company's claim in this area is non-existent. The Company has not performed any opportunity cost analysis,[69] let alone submitted such an analysis to the Commission for its review and the review of intervening parties.

The third concept misapplied by the Company is "reliability." The SRT has that specific function, providing for the acquisition of capacity corresponding to a reserve margin over expected peak demand.[70] The definition of the risks or costs for which the IMF is supposed to compensate the Company suffers from a serious problem: the IMF duplicates costs and compensates for risks that are covered by other components of Duke Energy Ohio's standard service offer. These components are those that relate to capacity, the SRT, the RSC, and also "little g." As noted above, the SRT is, by definition, a tracker that compensates the Company for acquiring a 15 percent reserve margin over and above predicted peak demand for the year ahead. Surely this is adequate for the purpose of assuring system reliability, and nothing more should be claimed for achieving this

[68] Id. at 38, 41, and 53 (Talbot). Regarding the testimony of Company Witness Steffen, Mr. Talbot stated that "Mr. Steffen does not provide a balanced assessment in which, absent the assurance of sales to standard service offer consumers, the Company would also be subject to 'price volatility in the energy and capacity markets.'" Id. at 41 (quoting Steffen's Second Supplemental Testimony at 27, Company Remand Ex. 3 at 27). Mr. Talbot also states that the testimony of Company Witness Meyer suffers from the same misrepresentation of the risk situation. Id. at 39 (referring to Company Remand Ex. 1 at 9).

[69] OCC Remand Ex. 1 at 39 and 42, citing DE-Ohio's response to OCC Interrogatory RI 140 ("The Company has not performed such a calculation," OCC Remand Ex. 1, NHT Attachment 4).

[70] See, e.g., OCC Remand Ex. 1 at 41 (Talbot).

purpose. The SRT is the sole successor to the Reserve Margin component under the Stipulation Plan.

It cannot be emphasized enough that the Company's claim that the IMF is included within the overall amount earlier claimed under the Reserve Margin portion of the provider of last resort charge contained in the Stipulation is erroneous. As shown in Company Witness Steffen's Testimony, Attachment JPS-SS1, the level of the IMF was set at 4 percent of "little g."[71] That percentage is only applicable to 2005-2006; in 2007 the percentage increases to 6 percent, which increases the Company's revenue from this charge from approximately $30 million (as shown in the attachment) to $45 million.[72] Together, with the estimated $15 million for the SRT, this increases the total of the two new charges to $60 million that customers would pay.[73] Such collections by the Company would be larger than the $52,898,560 claimed under the Reserve Margin component despite the significant reductions in the Reserve Margin estimate from that stated in Company testimony regarding the SRT in the Stipulation Plan. The Company proposes to increase the IMF to 9 percent of "little g" in 2008, which would increase the revenue from this charge to approximately $67,500,000.[74] The resulting revenue figure provides further evidence that the IMF is not only a new charge not contemplated by the Stipulation Plan, but is a *major source of an increasing level for standard service offer charges that customers would pay.*

[71] Company Remand Ex. 3 (Steffen).

[72] OCC Remand Ex. 1 at 48 (Talbot).

[73] Id.

[74] That is, each additional percentage of "little g" would collect approximately $7.5 million.

Turning to the RSC, according to the Company: "The RSC is the Company charge for providing a stable market price over a prolonged period of time."[75] This purpose is also the basis upon which Duke Energy Ohio attempts to support the IMF, which is supposed to be compensation for the dedication of assets to standard service offer service. If the RSC had legitimacy at any point, it was for ratemaking purposes by being a component of legacy generation costs in "little g"; i.e. it was fifteen percent of "little g" and was based upon historical accounting costs as determined in the Company's last rate case that included generation costs.[76] The IMF lacks any claim to legitimacy, and is for some unexplained reason expressed as an additional percentage of "little g" that increases over time without any lineage from these legacy generation costs. "Little g" itself, which includes a rate of return on generation rate base, implicitly compensates the Company for some degree of risk related to generation assets.

The proposed charges for the IMF have not been properly supported by Duke Energy Ohio, and are unreasonable. Analysis of the IMF -- on a stand-alone basis and even more so in combination with the RSC, the SRT, and "little g" -- reveals that the IMF has no reasonable basis or rationale.

The IMF is, as conjectured by the Supreme Court of Ohio, "some type of surcharge and not a cost component." *Consumers' Counsel 2006* at ¶30. The IMF should be removed from the Company's standard service offer charges.

---

[75] OCC Remand Ex. 1, NHT Attachment 12 (Company Response to OCC-INT-04-RI62(a)).

[76] The alleged historical basis of the RSC is, or was, that it was a component of "little g," namely a portion of the generation charge approved by the Commission in the Company's last rate case. The difference between the 15 percent of "little g" recovered through the RSC and the remaining 85 percent is that the former portion was made non-bypassable by a percentage of customers. OCC Remand Ex. 2(A) at 53.

3. The Commission should ensure reasonably priced standard service offer rates based upon verification of all costs.

These cases feature, for the first time, a review of Duke Energy Ohio's proposed AAC charge. The Commission has already moved the Company's standard service offer in the direction of a cost-based proxy for market prices as it has approved the Company's SRT and FPP pricing components, which are based upon costs actually incurred by the Company to acquire goods or services in the marketplace.[77] The Commission should tighten its review over these components,[78] and should also take this step regarding its review of the AAC in order to formulate a measurable and verifiable cost-based proxy for market-based rates.[79] The Commission should take the next logical step in its review process and exclude all elements where producers do not recover costs until they sell products or services.[80] This subject will be revisited by the OCC in light of testimony in the second phase of this proceeding.[81]

[77] OCC Remand Ex. 1 at 6 (Talbot).

[78] OCC Witness Talbot testified that "Duke Energy Ohio has too much latitude in making decisions regarding the setting of its FPP charges" (OCC Remand Ex. 1 at 25) and echoed the concern that "'DE-Ohio continues to purchase fuel and emission allowances in a manner that is inconsistent with best industry practices among regulated utilities." Id. at 27 (quoting the Auditor).

[79] Id.

[80] Id. at 33 (Talbot).

[81] Exclusion of the "CWIP" portion of the AAC calculation is the subject of testimony OCC Witness Talbot. Id. The exclusion of CWIP is also addressed in the prefiled testimony of OCC Witness Haugh that will be further discussed in the OCC's post-hearing brief for phase II of the case on remand.

4. Duke Energy Ohio compared its standard service offer rates to the fiction first created as the Company's Competitive Market Option.

a. Duke Energy Ohio's CMO has been shown to be useless as a basis for comparison for other standard service offer proposals.

The Company, through Witness Rose, presented a range of estimates for market prices based on a variety of different assumptions.[82] As pointed out by OCC Witness Talbot in both 2004 and 2007, the prices presented by Mr. Rose are speculative, have changed based upon the changing needs of Duke Energy Ohio's litigation position, and present such a wide range of prices that the testimony does not provide a useful benchmark from which the Commission can judge a reasonable standard service offer.[83]

Duke Energy Ohio's comparisons to its CMO creation should not be mistaken as comparisons to the "market." The market indices that Duke Energy Ohio uses are not reliable measures of a market price and the adjustments that the Company uses to the market indices are duplicative, imprecise, and in some cases do not represent costs or risks that the market-based standard service offer provider would face.[84] The Commission should not rely upon such a questionable and unverifiable approach as the measure of whether Duke Energy Ohio's New Proposal provides rates that are comparable to the market. Furthermore, the Commission should recall from testimony in the 2004 hearing that Company Witness Rose made it abundantly clear that the pricing

[82] See, e.g., OCC Remand Ex. 1 at 68-69 ("The range of Mr. Rose's 'market' prices was so large that the pricing exercise lost all credibility.") (Talbot).

[83] OCC Remand Ex. 1 at 67-69 (Talbot) (e.g. "complex, artificial, and imprecise" and "it all depends upon how you assess those factors" which "was not a sound basis for determining electricity market prices in 2004 and it is not a sound basis today").

[84] Id. 67.

method was not designed to be a market-based standard service offer for small customers.[85]

Following the submission of the Stipulation, Duke Energy Ohio presented downward adjustments to the CMO calculations in an attempt to demonstrate that one of its rate proposals was not too low so as to be predatory when compared with market rates.[86] Duke Energy Ohio's opportunistic manipulation of the CMO results to fit the circumstances of the Company's Stipulation proposal showed that the CMO "was 'padded' so as to be on the high side."[87] OCC Witness Talbot testified that Duke Energy Ohio Witness Rose's "five major downward adjustments to his earlier estimates"[88] "totally undermine[d] the MBSSO edifice [Rose] created last year."[89] As a result, Duke Energy Ohio's testimony regarding the CMO is worthless regarding the comparison of the New Proposal to "market" rates.[90]

b. Duke Energy Ohio's market indices are not reliable measures of market prices that are required by R.C. 4928.14.

Although Duke Energy Ohio Witness Rose attempted to justify Duke Energy Ohio's reliance upon indices to develop the CMO on the basis that "the index is a non-

[85] Tr. Vol. III at 59, lines 22-24 (2004).

[86] OCC Ex. 2 at 2 (Talbot Supplemental), referring to Company Ex. 8 (Rose Supplemental).

[87] Id. at 3.

[88] Id. at 2.

[89] Id. at 6.

[90] Id. ("[n]or should it be used * * * to create a competitive pricing benchmark against which to test the reasonableness or ERRSP pricing"), also OCC Remand Ex. 1 at 69 (Talbot) ("not a sound basis for determining electricity market prices").

utility source of information widely used by power suppliers,"[91] the market indices selected by Duke Energy Ohio are not currently a reliable measure of market prices. Witness Rose seemed to recognize that the indices are not yet reliable when he added to his testimony that "the integrity of the market and market indices is being further reinforced by more oversight at regional and federal levels."[92]

Additionally, Witness Rose alleged that "the FERC staff has come out with a view that the 'into' Cinergy indices that are being used and contemplated being used in the CMO are in substantial compliance with FERC requirements."[93] Witness Rose noted that the FERC Staff's view was presented in *Report on Natural Gas and Electricity Prices Indices.*[94] However, there is no specific reference to the "Into Cinergy" indices in that report. Upon cross-examination, Witness Rose pointed to the following paragraph in that report to support his assertion:

> Argus Energy Intelligence, ICE, Io, NGI and Platts [should] be deemed to be in substantial compliance with the standards of the Policy Statement (a) on condition that they publish direct volume and transaction number data on which index prices are calculated (or indicate when no such data is available) and (b) on condition that they affirm the Commission will, upon an appropriate request, have access to relevant data in the event of an investigation of possible false price reporting or manipulation of prices.[95]

---

[91] Company Ex. 7 at 34 (Rose).

[92] Id. at 35.

[93] Tr. Vol. III at 64, line 23 through 65 (2004).

[94] OCC Ex. 11.

[95] Id. at 60, referred to by Witness Rose (Tr. Vol. III at 144 (2004)).

Therefore, the FERC Staff did not find that the "Into Cinergy" index in particular[96] is in compliance, but found that the ICE and the Platts index publishers (that Duke Energy Ohio has proposed to rely on) may be in compliance under certain conditions.

As stated in the quote directly above, the "substantial compliance" designation by FERC Staff is dependent upon two conditions that have not yet been made by the publishers and may not be made. In particular, the FERC Staff noted in the paragraph preceding the one quoted above:

> [W]hile Platts states that it is open to assisting the Commission, it also reserves the right not to comply with a request for disclosure. This also does not meet the Policy Statement expectation that, in a specific and targeted investigation of possible false reporting or manipulation of market prices, price index publishers would provide the Commission access to the transaction data needed to determine whether price reporters violated applicable rules or statutes.[97]

Therefore, it appears that the index publishers may not be willing to meet the conditions the Commission Staff stated that they must meet to be in "substantial compliance."

Even more disconcerting about Duke Energy Ohio's CMO construct, the Company relies upon forward index prices.[98] The FERC Staff made a very particular comment regarding forward price reporting:

> [T]he results clearly indicate that few companies report long-term transactions to index developers; over 75 percent of respondents indicated that they reported no forward fixed price natural gas or electricity transactions to index developers. Staff assumes that few long-term transactions are reported and the prices for such

[96] In fact some respondents to the surveys complained about "the need for index developers to provide greater transparency in the development of their indices and additional information about reported transactions, such as the level of market activity at specific trading points and how reported prices are used in calculating their indices." Id. at 17.

[97] Id at 59.

[98] Company Ex. 7 at 7 (Rose).

> transactions reflected in index developers' publications are based upon a very small self-selected sample coupled with journalistic judgment.[99]

This statement shows that the FERC Staff's view of forward price indices, such as those Duke Energy Ohio relies upon in its CMO, is not favorable and that such indices would not likely be relied upon by the FERC Staff to determine the appropriateness of tariff rates. For that reason, the CMO, which relies on forward indices, is not appropriate and the Commission should not rely upon it for comparison to proposed standard service offer prices (or any other purpose). Additionally, as OCC Witness Talbot demonstrated, forward prices vary drastically from year to year.[100]

Under Company Witness Rose's CMO construct, forward price indices are adjusted by nine factors, six of which are not justified in principle and three of which were not been properly developed.[101] In the more recent hearing on remand from the Supreme Court of Ohio, Company Witness Rose made no attempt to support his questionable constructs. Instead, he stated that he made various new assumptions and relied upon "updated parameters" that he does not describe or defend.[102] The Commission should lend no weight to the comparisons made by Duke Energy Ohio with the CMO fiction that the Company has created.

The reasonable alternative to the Company's artificial, CMO construct is to place "[g]reater reliance on actual accounting costs -- rather than costs estimated from pricing

---

[99] OCC Ex. 11 at 31.

[100] OCC Ex. 1 at 18-19 (Talbot).

[101] OCC Post-Hearing Merit Brief at 45-49 (June 22, 2004).

[102] Company Remand Ex. 2 at 12, lines 8-11 (Rose).

theories and models -- [that] can provide a relatively stable proxy for market prices."[103] This is the direction that the Commission seems to have headed in its determinations regarding Duke Energy Ohio's standard service offer rates.[104] This reasonable alternative supports the elimination of the duplicative charges sought by Duke Energy Ohio in the New Proposal that the Company proposed in its October Application for Rehearing.

B. The Agreements Entered Into by Duke Energy Ohio to Gain Support for its New Proposal Reveal that the Company has Exerted Market Power and is Not Providing Reasonably Priced Retail Electric Service.

1. Overview - its "All in the [corporate] Family"

The supplemented record in these cases reveals the side agreements that Duke Energy Ohio undertook to gain support for the Company's proposals for standard service offer generation rates -- i.e., the proposal in the Stipulation and also the proposal contained in the Company's Application for Rehearing. [redacted][105] [redacted]

The Commission should approve standard service offer rates that are reasonable for all customers and move to cost-based rates, encourage the development of a

[103] OCC Remand Ex. 1 at 70 (Talbot).

[104] Id. at 70-71; see also Entry on Rehearing at 10 (November 23, 2004) ("not . . . cede this review").

[105] [redacted]

competitive market for generation service, and more closely scrutinize the activities of Duke Energy Ohio. [redacted] The rates proposed by the Company, as stated above (based upon the supplemented record on remand), are not reasonable and the Company has not satisfied its burden of proof regarding proposed standard service offer rates. The Commission should scrutinize the cost basis for Duke Energy Ohio's standard service offer rates as a reasonable proxy for market-based rates, and these rates should be bypassable in order to provide customers the opportunity to choose between providers of competitive retail electric generation service.

2. The Company's plan for standard service offer rates lacks substantial support, and the stated support did not result from serious bargaining.

a. Overview

In *Consumers' Counsel 2006*, the Supreme Court of Ohio agreed that "if CG&E and one or more of the signatory parties agreed to a side financial or some other consideration to sign the stipulation, the information would be relevant to the commission's determination of whether all parties engaged in 'serious bargaining'"[106] under the three-prong test approved in *Consumers' Counsel v. Pub. Util. Comm.* (1992), 64 Ohio St. 3d 123, 125. [redacted]

[106] *Consumers' Counsel 2006* at ¶84.

[redacted], and the first prong of the test for the reasonableness of a Stipulation was not met.

[redacted][107] [redacted][108] [redacted]

[107] [redacted]

[108] [redacted]

[redacted][109]

[redacted][110]

i. The Stipulation lacked substantial support

[redacted][111]

[redacted][112] [redacted]

[redacted][113] [redacted]

---

109 [redacted]

110 [redacted]

111 [redacted]

112 [redacted]

113 [redacted]

[redacted][114]

[redacted][115][116][117]

[redacted]

[redacted]

[redacted][118]

[redacted]

[redacted]

[redacted][119]

[redacted]

[redacted]

[redacted][120]

[redacted][121]

---

114 [redacted]

115 [redacted]

116 [redacted]

117 [redacted]

118 [redacted]

119 [redacted]

120 [redacted]

121 [redacted]

[redacted][122] [redacted]

[redacted][123] [redacted]

[redacted][124]

The supplemented record also reveals that the City of Cincinnati ("City") -- an intervenor in the *Post-MDP Service Case* that withdrew from the cases on July 13, 2004 without filing a brief -- entered into an agreement with Duke Energy Ohio (the "City Agreement"). The side agreement, executed on June 14, 2004 by CG&E attorney John Finnigan and City Manager Valerie Lemmie, provided the City with $1 million and required the City to withdraw from the *Post-MDP Service Case.*[125] The City did not file an initial brief by the June 22, 2004 deadline, and did not file a reply brief by the July 6, 2004 deadline -- and the City did, in fact, withdraw from the *Post-MDP Service Case.*

[redacted][126] The Stipulation was executed and supported by the Company and the PUCO

---

[122] [redacted]

[123] [redacted]

[124] [redacted]

[125] OCC Remand Ex. 6 at ¶4.

[126] [redacted]

Staff as well as the OHA, OEG (including AK Steel[127]), IEU, Cognis, and Kroger.[128] Also supporting the Stipulation were People Working Cooperatively and Communities United for Action[129] who were interested in the contracts for weatherization and energy assistance that were extended as part of the Stipulation.[130] Other supporting parties were marketers Dominion Retail and Green Mountain Energy whose support appears to have been tied to billing credits included in the Stipulation that were later eliminated (along with the marketer support) by the Company's New Proposal.[131] Parties that did not sign the Stipulation were the OCC, the Ohio Partners for Affordable Energy, the Ohio Manufacturers Association, the Ohio Marketers Group (comprised of Constellation NewEnergy, Inc., MidAmerican Energy, Strategic Energy, and WPS Energy Services), Constellation Power Source, PSEG Energy Resources & Trade, and the National Energy Marketers Association. The support for the Stipulation relied upon by the Commission, as the Stipulation was adjusted by the November Entry on Rehearing [redacted]

[127] [redacted]

[128] Joint Ex. 1 at 26-30 (Stipulation).

[129] People Working Cooperatively and Communities United for Action.

[130] Joint Ex. 1 at 18, ¶16.

[131] See *Post-MDP Service Case*, Green Mountain Memorandum in Response to CG&E Application for Rehearing (November 8, 2004) and Dominion Retail Memorandum in Response to CG&E Application for Rehearing (November 8, 2004).

[redacted] Such support does not constitute "substantial support from a number of interested stakeholders" that might support waiver from the post-MDP pricing rules.[132]

[redacted] Duke Energy Ohio (formerly CG&E) was a named party in the City Agreement [redacted][133] [redacted][134] [redacted]

[redacted][135]

[redacted]

[132] Ohio Adm. Code 4901:1-35-02(C).

[133] [redacted]

[134] [redacted]

[135] [redacted]

[redacted][136][redacted][137][redacted][138][redacted][139][redacted][140][redacted]

136 [redacted]

137 [redacted]

138 [redacted]

139 [redacted]

140 [redacted]

[redacted][141] [redacted]

[redacted][142] [redacted][143]

[redacted]

[redacted]

[redacted][145] [redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted][146]

[redacted]

---

141 [redacted]

142 [redacted]

143 [redacted]

144 [redacted]

145 [redacted]

146 [redacted]

[redacted]

[redacted][147]

[redacted]

[redacted][148] [redacted]

[redacted]

[redacted][149]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

147 [redacted]

148 [redacted]

149 [redacted]

[redacted]

[redacted][150] [redacted]

[redacted][151] [redacted]

[redacted][152]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted][153] [redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted]

---

150 [redacted]

151 [redacted]

152 [redacted]

153 [redacted]

[redacted]

154 [redacted]

155 [redacted]

156 [redacted]

157 [redacted]

158 [redacted]

[redacted][159] [redacted]

[redacted]

[redacted][160] [redacted]

[redacted][161] [redacted]

[redacted]

[redacted]

[redacted][162] [redacted]

[redacted]

[redacted]

iii. The stated support for the Company's proposals did not result from serious bargaining.

[redacted]

[redacted][163] [redacted]

[redacted]

[redacted]

[redacted]

[redacted]

[160] [redacted]

[161] [redacted]

[162] [redacted]

[163] [redacted]

[redacted]

[redacted]The OCC was not "left by the wayside . . . because [its] interests [were] not negotiable,"[164] [redacted]

[redacted]

[redacted]

[redacted]

i. The Stipulation lacked substantial support.

The Commission's evaluation of the terms of the Stipulation, largely in areas outside the core scope of Duke Energy Ohio's post-MDP pricing proposals for generation service, changed the course of the Company's plans and those of its fellow stipulating parties. The Commission's September 29, 2004 Order increased the percentage of nonresidential shopping customers who could avoid the RSC[165] in an environment where switch rates were declining,[166] adjusted provisions for the AAC1 charge (making it depend on "legitimate expenses,"[167] reduced the pass-through of costs because "CG&E

[164] Order, Concurring Opinion of Chairman Alan R. Schriber at 1 (September 29, 2004).

[165] Order at 19 (September 29, 2004).

[166] Id. at 23.

[167] Id. at 32.

may be recovering some percentage of these costs through off-system sales,"[168] and left undetermined the degree to which it could be bypassed[169]), eliminated a deferral that would increase later distribution rates for residential customers,[170] prohibited a provision in the Stipulation that would require "any consumers to waive their statutory POLR rights,"[171] and refused to "allow the RTC collection from residential consumers to be extended beyond 2008."[172] The main change to standard service offer pricing, therefore, was refusal of the Commission to cede ongoing review of the Company's claimed capacity costs.[173]

The Company protested the Commission's oversight in Duke Energy Ohio's Application for Rehearing on October 29, 2004. [redacted][174] [redacted][175]

[168] Id. See discussion of Talbot testimony in Section IV.A.2.a. of this brief referring to the Company's response to OCC Interrogatory RI 140.

[169] Id.

[170] Id. at 35.

[171] Id.

[172] Id. at 36. However, the five percent reduction in residential rates past 2005 that was contained in the Stipulation was eliminated, providing CG&E with compensating revenue. Id.

[173] As argued above, such scrutiny is appropriate, and is supported by the results of *Consumers' Counsel 2006*.

[174] [redacted]

[175] [redacted]

[redacted][176] [redacted][177] [redacted][178]

The Company's Application for Rehearing proposed post-MDP pricing based upon a price to compare and a provider of last resort ("POLR") charge made up of the RSC, a revised annually adjusted component ("AAC"), the SRT (the successor to the previous Reserve Margin charge), and an additional charge in the form of the IMF adder.[179] [redacted][180]

[176] [redacted]

[177] [redacted]

[178] [redacted]

[179] Company Application for Rehearing, Attachment 1 at 1-2.

[180] [redacted]

[redacted][181] [redacted]

[redacted]

[redacted][182] [redacted]

[redacted][183] [redacted]

[redacted][184]

[redacted]

[redacted]

[redacted][185] [redacted]

[redacted] Such support does not constitute "substantial support from a number of interested stakeholders" that might support waiver from the post-MDP pricing rules.[186]

---

[181] [redacted]

[182] [redacted]

[183] [redacted]

[184] [redacted]

[185] [redacted]

[186] Ohio Adm. Code 4901:1-35-02(C).

[redacted]

[redacted] [187]

[redacted]

[redacted]

[redacted]

[redacted]

[redacted] [188] [redacted]

[redacted] [189]

[redacted]

[redacted]

[redacted] [190] [redacted]

---

[187] [redacted]

[188] [redacted]

[189] [redacted]

[190] [redacted]

[redacted][191]

[redacted][192]

iii. The stated support for the Company's proposals did not result from serious bargaining.

[redacted][193]

[redacted][194]

[redacted]

191 [redacted]

192 [redacted]

193 [redacted]

194 [redacted]

[redacted]

[redacted][195] [redacted]

[redacted][196].

Second, the record also shows that another set of customers received favored treatment over other customers [redacted]. One example of such favored treatment is the City Agreement, according to which the City received $1 million and agreed to withdraw from the *Post-MDP Service Case*.[197]

[redacted]

[redacted][198] [redacted]

[redacted][199] [redacted]

[redacted]

[195] [redacted]

[196] [redacted]

[197] Company Remand Ex. 3 at 33 (Steffen).

[198] [redacted]

[199] [redacted]

[redacted]

200 [redacted]

[redacted]

201 [redacted]

[redacted]

202 [redacted]

[redacted]

203 [redacted]

[redacted]

204 [redacted]

[redacted]

---

200 [redacted]

201 [redacted]

202 [redacted]

203 [redacted]

204 [redacted]

[redacted]205 [redacted]

[redacted]206 [redacted]

[redacted]207 [redacted]

[redacted]208

[redacted]

[redacted]209 [redacted]

[redacted]210 [redacted]

[redacted]211 [redacted]

---

205 [redacted]

206 [redacted]

207 [redacted]

208 [redacted]

209 [redacted]

210 [redacted]

211 [redacted]

[redacted]

212 [redacted]

213 [redacted]

214 [redacted]

215 [redacted]

216 [redacted]

[redacted][217][redacted]

[redacted][218]

[redacted]

[redacted]

[redacted]

[redacted][219][redacted]

[redacted][220][redacted]

[redacted]

[redacted][221][redacted]

[redacted]

[redacted][222][redacted]

[redacted][223]

[redacted]

---

217 [redacted]

218 [redacted]

219 [redacted]

220 [redacted]

221 [redacted]

222 [redacted]

223 [redacted]

[redacted]

[redacted][224] [redacted]

[redacted]

[224] [redacted]

[225] [redacted]

[redacted]

3. The Company's approach to post-MDP service is discriminatory and has dealt the development of competitive markets a serious blow.

a. Overview

The Order in this case cites the "good cause shown" exception to the Commission's post-MDP pricing rules, Ohio Adm. Code 4901:1-35-02(B),[226] and emphasizes the need to encourage a competitive market for generation service.[227] [redacted] The record also demonstrates that the wholly or partly non-bypassable charges among the components of the Company's post-MDP pricing, along with conditions placed on the bypassability of some charges, create barriers to entry for the competitive provision of generation service to customers of Duke Energy Ohio.

During 2004, when the Commission held its last full hearing in this matter, the switching rates to competitive retail electric service ("CRES") providers for commercial, industrial, and residential customers were 22.04, 19.87, and 4.91 percent.[228] It was hoped that Duke Energy Ohio's standard service offer would usher in a period in which the competitive electricity market would further develop and mature. In fact, the switching statistics had fallen to 8.40, 0.36, and 2.32 percent for commercial, industrial, and

[226] Order at 21 (September 29, 2004).

[227] See, e.g., Order at 18-20.

[228] Tr. Vol. II at 133 (CG&E Witness Stevie) (2004) (cited in OCC Remand Ex. 2(A) at 62, as corrected in OCC Remand Ex. 2(B)) (Hixon)).

residential customers by December 31, 2006.[229] The record provides evidence of the source of the decline in switching levels. [redacted][230] [redacted]

The record reveals that the Commission needs to make adjustments to invigorate the competitive market.

[redacted] R.C. 4905.35 states:

> No public utility shall make or give any undue or unreasonable *preference or advantage* to any person, firm, corporation, or locality, or subject any person, firm, corporation, or locality to any undue or unreasonable prejudice or disadvantage.

[229] OCC Remand Ex. 2(A) at 63 (Hixon).

[230] [redacted]

[231] [redacted]

Furthermore, R.C. 4928.14(A) states:

> After its market development period, an electric distribution utility in this state shall provide consumers, on a comparable and *nondiscriminatory* basis within its certified territory, a market-based standard service offer of all competitive retail electric services necessary to maintain essential electric service to consumers.[232]

The latter statute forms the backbone of what Duke Energy Ohio refers to as its "provider of last resort" obligation, but it also requires that the Company provide its services free of discriminatory treatment of its customers.

[redacted]

[232] Emphasis added.

[233] [redacted]

[234] [redacted]

[235] [redacted]

[redacted][236]

[redacted][237] [redacted]

[redacted][238] [redacted]

[redacted]

236 [redacted]

237 [redacted]

238 [redacted]

[redacted][239]

[redacted][240]

[redacted]

239 [redacted]

240 [redacted]

[redacted]

[redacted][241][redacted]

[redacted][242][redacted]

[241] [redacted]

[242] [redacted]

[redacted][243]

c. Duke Energy Ohio's standard service offer price components should be bypassable.

An important feature of Duke Energy Ohio's standard service offer is that four of its six price components are not fully bypassable by customers who switch to CRES providers. Only the tariff generation rate (i.e. 85 percent of "little g") and the FPP are fully bypassable.[244] In spite of the fact that all the standard service offer charges are generation-related, the IMF, the AAC, the RSC and the SRT are not fully bypassable. [redacted]

[243] [redacted]

[244] OCC Remand Ex. 2(A) at 53 (Hixon).

[redacted][245][redacted]

While the Company argues that at least some percentage of customers can bypass all but a small percentage of standard service offer charges, OCC Witness Talbot pointed out that even an apparently small non-bypassable charge can threaten a large percentage of competitive retailers' profit margins -- margins that can be very small.[246] Mr. Talbot explained that non-bypassable charges, for an entire class of customers or for part of a customer class, impose a barrier to competitive supply of generation service.[247] In particular, the termination of the IMF charge (which is totally non-bypassable in the Company's tariffs) would remove a barrier to competitive entry into the electricity marketplace.

4. The Company's approach to post-MDP service has raised additional problems that should be addressed.

[redacted][248][redacted]

[245] [redacted]

[246] Tr. Vol. II at 84-85 (2007) (Talbot).

[247] OCC Remand Ex. 1 at 62-63 (Talbot).

[248] [redacted]

[redacted][249] [redacted]

[redacted]

[redacted][250] [redacted]

[redacted]

[redacted][251]

[redacted]

[redacted]

[redacted]

[redacted]The concerns of the Supreme Court of Ohio in *Time Warner AxS v. Pub. Util. Comm.* (1996), 75 Ohio St.3d 229, 234, 661 N.E.2d 1097 are worth repeating:

> [W]e feel compelled to note our grave concern regarding the partial stipulation adopted in the case at bar. The partial stipulation arose from settlement talks from which an entire customer class was intentionally excluded. This was contrary to the commission's negotiations standard . . . . * * * Ameritech managed to either settle its competitive issues or defer them until a later date, all without having its competitors at the settlement table. Under these circumstances, we question whether the stipulation, even assuming the commission's authority to approve it, promotes competition in the telephone industry as intended by the General Assembly. We could not create a requirement that all parties participate in all settlement meetings. However, given the facts in this case, we have grave concerns regarding the commission's adoption of a partial stipulation which arose from the exclusionary settlement meetings.[252]

---

[249] [redacted]

[250] [redacted]

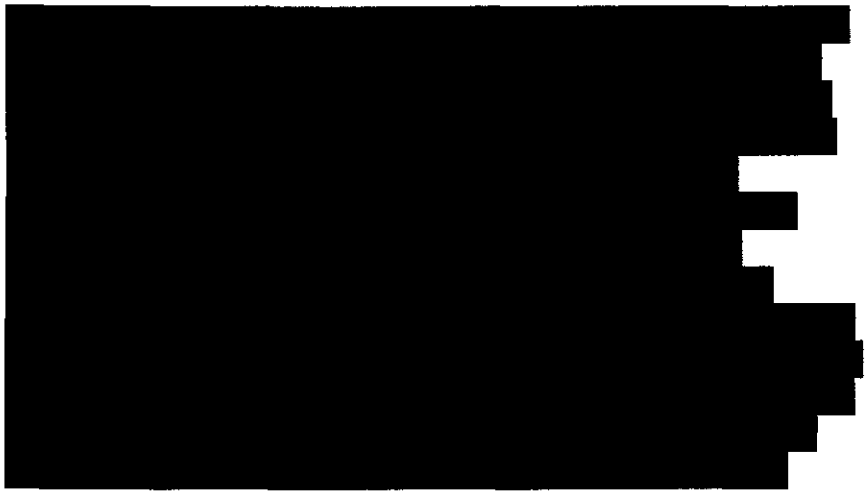
[251] [redacted]

[252] *Time Warner AxS v. Public Util. Comm.*, 75 Ohio St. 3d 229.

Problems in the negotiating process in the *Post-MDP Service Case* stem from not listening to the Court's concerns.

The *Post-MDP Service Case* addressed the post-MDP pricing of generation service, including the applicability of the Commission's post-MDP pricing rules (i.e. Ohio Adm. Code 4901:1-35) and the extent to which competitive markets would set pricing for generation services. [redacted] *Time Warner* states that the Court does not prohibit "caucuses" between parties during the course of negotiations, but a rush to adopt a partial settlement without addressing core concerns in a case is against public policy and will be scrutinized by the Court.

[redacted]



[redacted][253]

Proceedings to set rates for large portions of the public should be conducted so as to as provide the Commission and the public with a broad view of issues, and to permit parties to develop and present their cases as provided for under Ohio's statutes and the Commission's rules. The Commission should take notice and respond appropriately to the additional information that the OCC has elicited and presented in the *Post-MDP Remand Case.*

V. CONCLUSION

Two fundamental topics were covered by the remand from the Supreme Court of Ohio: whether the Company's New Proposal was supported by evidence and whether evidence of side financial arrangements should affect the outcome of these cases. The evidence presented by the OCC, principally in the form of testimony by Mr. Neil Talbot, demonstrates that the Company cannot support the charges in its New Proposal using the evidence submitted during the hearing in 2004 and the Company has not provided any supplemental testimony that supports the level of its standard service charges. The duplication in the Company's capacity charges should be eliminated, and the standard service offer rates should be based more closely on verifiable costs that reflect market-based prices.

The evidence presented by the OCC, principally in the form of testimony by Ms. Beth Hixon, [redacted]

253 [redacted]

[redacted] The Commission, with the assistance of its Staff, should exert its supervisory authority over Duke Energy Ohio to resolve the problems identified in the OCC's testimony.

The Commission should re-evaluate this case given the overwhelming evidence demonstrating that signatories to the Stipulation, who largely became the supporters of the Company's New Proposal, [redacted] The Commission should base Duke Energy Ohio's standard service offer rates for the period ending December 31, 2008 on verifiable costs. Revenues from shared resources should be used to arrive at net costs for standard service offer rates, and rate components such as the IMF that have no cost basis should be eliminated.

The Commission's intent to foster competition [redacted] in order to promote reasonable rates for all customers and to encourage competition. The Commission should also encourage the development of the competitive market for generation service by making all standard service offer rates bypassable.

Finally, the Commission should direct its Staff [redacted]

[redacted][254][redacted]

Respectfully submitted,

Janine L. Migden-Ostrander
Consumers' Counsel

Jeffrey L. Small, Trial Attorney
Ann M. Hotz
Larry S. Sauer
Assistant Consumers' Counsel

Office Of The Ohio Consumers' Counsel
10 West Broad Street, Suite 1800
Columbus, Ohio 43215-3485
Telephone: 614-466-8574
Fax: 614-466-9475
E-mail small@occ.state.oh.us
hotz@occ.state.oh.us
sauer@occ.state.oh.us

254 [redacted]

CERTIFICATE OF SERVICE

The undersigned hereby certifies that a true and correct copy of the foregoing (public version) *Initial Post-Remand Brief, Hearing Phase I, by the Office of the Ohio Consumers' Counsel,* has been served upon the below-named persons in unredacted form (pursuant to the Attorney Examiners' instructions) via electronic transmittal this 13th day of April 2007.

Jeffrey L. Small
Assistant Consumers' Counsel

WTTPMLC@aol.com
tschneider@mgsglaw.com
cgoodman@energymarketers.com
sbloomfield@bricker.com
TOBrien@Bricker.com
dane.stinson@baileycavalieri.com
korkosza@firstenergycorp.com