

FILE

BEFORE

THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Duke)
 Energy Ohio for Approval of a Market)
 Rate Offer to Conduct a Competitive)
 Bidding Process for Standard Service) Case No. 10-2586-EL-SSO
 Offer Electric Generation Supply,)
 Accounting Modifications, and Tariffs for)
 Generation Service.)

VOLUME IV

TESTIMONY

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DIRECT TESTIMONY OF

CHARLES R. WHITLOCK

ON BEHALF OF

DUKE ENERGY OHIO, INC.

November 15, 2010

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Attachment

CRW-1 Duke Energy Ohio Legacy Generation

CRW-2 Press Release Approving First Energy Auction

I. INTRODUCTION

1 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

2 A. My name is Charles R. Whitlock, and my business address is 139 East Fourth
3 Street, Cincinnati, Ohio 45202.

4 **Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?**

5 A. I am employed by Duke Energy Business Services, LLC (DEBS) as President,
6 Midwest Commercial Generation (MCG), Commercial Businesses. DEBS
7 provides various administrative and other services to Duke Energy Ohio, Inc.
8 (Duke Energy Ohio or the Company) and other affiliated companies of Duke
9 Energy Corporation (Duke Energy).

10 **Q. PLEASE DESCRIBE YOUR EDUCATION AND PROFESSIONAL**
11 **EXPERIENCE.**

12 A. I am a graduate of the University of Alaska at Anchorage with a Bachelor of
13 Business Studies Degree in Accounting. I am also a graduate of the Mahler
14 School Advanced Management Skills Program and the Center for Creative
15 Leadership Developing Strategic Leadership Program. I have also taken
16 advanced course work in business management at Harvard University.

17 Prior to joining Cinergy Corp. (Cinergy), I was a Senior Power Trader for
18 Statoil Energy. I also held various positions with Vitol Gas and Electric, which
19 included responsibilities for energy trading, marketing and risk management. I
20 joined Cinergy in May 2000 as a power trader for Cinergy Services, Inc. I held
21 positions of increasing responsibility within the trading organization, culminating
22 in the position of Vice President, Power Trading. In 2004, I became Vice
23 President, Portfolio Optimization. In this role, I managed the commodity exposure

1 related to the generation assets. I remained in this position through the merger
2 with Duke Energy. I was named to my current position in October 2009.

3 **Q. WHAT IS MIDWEST COMMERCIAL GENERATION?**

4 A. Midwest Commercial Generation is the organization within Duke Energy
5 Corporation that manages all aspects of non-regulated generation and market
6 participation in the Midwest.

7 **Q. PLEASE DESCRIBE YOUR RESPONSIBILITIES AS PRESIDENT, MCG,**
8 **COMMERCIAL BUSINESSES.**

9 A. I am responsible for the Midwest commercial generation fleet, which includes the
10 generating assets that are owned by Duke Energy Ohio but are operated as a
11 separate affiliate under Ohio's corporate separation rules and regulations. A list
12 of these assets, including Duke Energy Ohio's current ownership share, is
13 attached to my testimony as Attachment CRW-1. I am responsible for the safe,
14 reliable and economic supply of capacity and power, including fuel and emission
15 allowances, to Duke Energy Ohio's standard service offer (SSO) customers. I am
16 also responsible for the commercial risk management of all components of Duke
17 Energy Ohio's non-SSO generation, including risk management associated with
18 prices for power, capacity, fuel, emission allowances, and congestion, as well as
19 the Company's participation in wholesale auctions. I have managerial
20 responsibility for over 600 employees in the MCG organization. Finally, I
21 continue to function as the President of Duke Energy Retail, a competitive retail
22 electric service and retail natural gas provider in Ohio and Pennsylvania.

23 **Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THE PUBLIC**
24 **UTILITIES COMMISSION OF OHIO?**

1 A. Yes.

2 Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS
3 PROCEEDING?

4 A. The purpose of my testimony is to describe the current and future ownership
5 structure of the MCG fleet of generating assets, which includes Duke Energy
6 Ohio's owned generation that is treated as functionally separate from the
7 distribution utility. I also explain how transferring the generating assets currently
8 owned by Duke Energy Ohio into a separate company advances competition in
9 Ohio and how it benefits Duke Energy Ohio and its customers. I also address
10 MCG's participation in Duke Energy Ohio's future competitive bidding process
11 (CBP) auctions.

12 Q. WHAT ARE THE ATTACHMENTS FOR WHICH YOU ARE
13 RESPONSIBLE?

14 A. I am sponsoring two Attachments. CRW-1 is a list of Duke Energy Ohio's Legacy
15 Generating Assets, as I further describe below. CRW-2 are copies of press releases
16 from the Public Utilities Commission of Ohio approving recent competitive bidding
17 processes.

II. SUMMARY OF DUKE ENERGY OHIO'S GENERATION PORTFOLIO

18 Q. PLEASE IDENTIFY DUKE ENERGY OHIO'S GENERATING ASSETS.

19 A. Duke Energy Ohio's current portfolio of generating assets consists of two different
20 types of assets. For sake of simplicity, I will refer to these as Legacy Generating
21 Assets and Non-Legacy Generating Assets in the remainder of my testimony.

22 Q. WHAT ARE THE LEGACY GENERATING ASSETS?

1 A. The Legacy Generating Assets are assets currently owned by Duke Energy Ohio
2 that were, prior to January 1, 2001, regulated assets used and useful in providing
3 retail electric service in Duke Energy Ohio's certified territory. When Ohio
4 deregulated electric generation service, this set of generating assets became
5 merchant plants effective January 1, 2001, and were functionally separated from
6 Duke Energy Ohio, the regulated utility. Since 2001, the energy and capacity of
7 these generating assets have been dedicated to serving Duke Energy Ohio's retail
8 electric customers.

9 **Q. WHAT DO YOU MEAN BY FUNCTIONALLY SEPARATED?**

10 A. The Legacy Generating Assets are still owned by Duke Energy Ohio. However,
11 since early this decade, and due to Ohio's change in law in 1999 that started the
12 path of deregulation, these assets have been managed as if they were wholly
13 owned by a separate generation affiliate and treated as merchant assets. That is, the
14 MCG group is viewed as an affiliate of Duke Energy Ohio, the regulated entity, for
15 purposes of complying with the Commission's rules on corporate separation.
16 Duke Energy Ohio no longer earns a regulated rate of return on these assets, as it
17 does on the transmission and distribution side of its business. And customers may
18 choose not to take generation service from Duke Energy Ohio, limiting the
19 Company's ability to cover its costs to maintain and operate these assets to the
20 vagaries of the market.

21 **Q. PLEASE EXPLAIN WHAT YOU MEAN BY THE ASSETS WERE**
22 **DEDICATED TO DUKE ENERGY OHIO'S RETAIL ELECTRIC**
23 **CUSTOMERS.**

24 A. To respond to this question, I must first briefly discuss the history of deregulation

1 in Ohio. As part of legislation enacted in 1999, it was intended that Ohio's utilities
2 would transfer their owned generation to an exempt wholesale generation (EWG).
3 Indeed, as part of its transition plan, Duke Energy Ohio, like other Ohio utilities,
4 agreed to transfer its assets to a EWG. In 2004, at the request of the Commission,
5 Duke Energy Ohio filed its rate stabilization plan (RSP) in which it agreed, among
6 other things, to provide customers with a stable price and to dedicate the capacity
7 and associated energy of these plants to serve Duke Energy Ohio's load in its
8 certified territory for the duration of the RSP. The intent of the RSP was to allow
9 the competitive retail electric market additional time to develop, while providing
10 customers with a stable price and allow the utility some measure of financial
11 stability. Duke Energy Ohio's RSP was approved by the Commission in Case No.
12 03-93-EL-ATA. In order to provide a stable price during the RSP, the Company
13 did not transfer its Legacy Generating Assets to the EWG as was its right under
14 Ohio law. Similarly, in settling Duke Energy Ohio's Electric Security Plan (ESP)
15 Case No. 08-920-EL-SSO, *et al.*, the Company agreed, among other things, to
16 continue to dedicate the energy and capacity of these Legacy Generating Assets to
17 customers as part of Duke Energy Ohio's provider of last resort (POLR)
18 obligation.

19 **Q. PLEASE DESCRIBE THE MAKE-UP OF DUKE ENERGY OHIO'S**
20 **LEGACY GENERATING ASSET PORTFOLIO.**

21 **A.** Duke Energy Ohio has an ownership share in six coal-fired generating stations:
22 Beckjord (units 1-6), Conesville (unit 4), Killen (unit 2), Miami Fort (units 7 and
23 8), Stuart (units 1-4) and Zimmer (unit 1). Duke Energy Ohio is responsible for
24 the operation of the Zimmer, Miami Fort and Beckjord stations. Attachment CRW-

1 includes a list of the units, the Company's ownership share, and the capacity associated with that ownership share.

In addition, Duke Energy Ohio owns, either in whole or in part, combustion turbine (CT) facilities. These Legacy Generating Assets include Beckjord CTs (units 1, 2, 3, 4), Miami Fort CTs (units 3, 4, 5, 6), and Dicks Creek CTs (units 1, 3, 4, 5).

Q. WHAT ARE THE COMPANY'S NON-LEGACY GENERATING ASSETS?

A. The Non-Legacy Generating Assets consist of the gas-fired plants acquired by Duke Energy Ohio as a result of the merger between Cinergy and Duke Energy in 2006 and Duke Energy Ohio's ownership share of the Ohio Valley Electric Corporation (OVEC) coal plants. These Non-Legacy Generating Assets have never been in a regulated rate base or deemed used and useful in Duke Energy Ohio's certified territory. Further, these assets are not dedicated to serve Duke Energy Ohio's load in any way and thus have always been merchant plants.

Q. PLEASE IDENTIFY THE DUKE ENERGY OHIO'S NON-LEGACY GENERATING ASSET PORTFOLIO.

A. The Non-Legacy Generating Assets in which Duke Energy Ohio has an ownership interest include the following gas-fired generating stations: Fayette, located in western Pennsylvania and connected to Allegheny Power Transmission System; Hanging Rock, located in southeastern Ohio and connected to the American Electric Power (AEP) transmission system; Lee, located in Illinois and connected to Commonwealth Edison Transmission System; Washington, located in eastern Ohio and connected to the AEP Transmission System; and, Vermillion, located in Indiana and connected to the Duke Energy Indiana transmission system. The

1 Company has a 9% interest in 2,365 MW of generation from the OVEC coal
2 plants, located in Cheshire, Ohio and Madison, Indiana.

3 **Q. DOES DUKE ENERGY OHIO CURRENTLY OWN THE NON-LEGACY**
4 **GENERATING ASSETS?**

5 A. Duke Energy Ohio is in the process of transferring the gas-fired Non-Legacy
6 Generating Assets to an affiliated generating company. As part of the Stipulation
7 and Recommendation in Duke Energy Ohio's ESP in Case No. 08-920-EL-SSO,
8 *et al.*, the Stipulating Parties agreed, and the Commission approved, that Duke
9 Energy Ohio could transfer those assets subject to approval by the Federal Energy
10 Regulatory Commission (FERC). The FERC approved this transfer by its Order
11 dated February 19, 2009 in Docket No. EC08-78 (126 FERC ¶ 61,146). The
12 Company expects the transfer of all of those Non-Legacy Generating Assets to be
13 completed in early 2011. The Company further expects to seek necessary
14 approvals to transfer the ownership in the OVEC plants in the near future.

15 **Q. DID THE STIPULATION AND RECOMMENDATION IN CASE NO. 08-**
16 **920-EL-SSO, ET AL., PROVIDE FOR ANY FURTHER TERMS AND**
17 **CONDITIONS REGARDING DUKE ENERGY OHIO'S OWNERSHIP OF**
18 **GENERATION ASSETS?**

19 A. Yes. As part of the settlement in that case, Duke Energy Ohio agreed to withdraw
20 its request to transfer its Legacy Generating Assets both at the Commission and
21 the FERC. The Parties agreed, and the Commission approved, that Duke Energy
22 Ohio could file an application to transfer these assets at a later date, provided the
23 transfer itself was not effective prior to January 1, 2012.

24 **III. TRANSFER OF LEGACY GENERATING ASSETS**

1 **Q. WHAT DOES DUKE ENERGY OHIO PROPOSE RELATIVE TO ITS**
2 **LEGACY GENERATING ASSET PORTFOLIO IN THIS PROCEEDING?**

3 A. Duke Energy Ohio is not seeking Commission approval to transfer its Legacy
4 Generating Assets in this filing. Rather, it merely informs the Commission here of
5 its intention to subsequently file, in a separate proceeding, for approval to transfer
6 its Legacy Generating Assets to an affiliate. Duke Energy Ohio wants to explain its
7 position now to assure the Commission that a future transfer of the assets would
8 not harm retail customers and will not hinder the Company's ability to provide for
9 its SSO. Duke Energy Ohio will provide a detailed plan and seek approval to
10 transfer its Legacy Generating Asset portfolio to an affiliated generating company
11 in a subsequent proceeding, to be filed in the near future.

12 **Q. WHY IS DUKE ENERGY OHIO PROPOSING TO FILE A SUBSEQUENT**
13 **APPLICATION TO TRANSFER ITS LEGACY GENERATING ASSETS?**

14 A. The purpose of the pending Application is to establish Duke Energy Ohio's next
15 SSO. Once the Company has further insight from the Commission on the
16 migration to market and more specifically, when that migration will be completed,
17 it can incorporate that determination into the application to transfer the assets.

18 **Q. PLEASE DESCRIBE THE OBJECT AND PURPOSE OF TRANSFERRING**
19 **THE LEGACY GENERATING ASSET PORTFOLIO FROM DUKE**
20 **ENERGY OHIO TO AN AFFILIATE.**

21 A. The object and purpose of the transfer is simply to change the legal ownership of
22 the Legacy Generating Assets currently owned by Duke Energy Ohio (but already
23 treated as a functionally separate affiliate), to a another legal entity. Now that a
24 competitive market has fully developed in Duke Energy Ohio's service territory,

1 Duke Energy Ohio is simply seeking to exit the retail electric generating function
2 of the business. The purpose of the transaction is no different than what the
3 Company originally committed to do nearly a decade ago, as part of its transition
4 plan approved at the outset of deregulation. And in the past several years, other
5 Ohio utilities have successfully fulfilled their SSO obligations for un-switched
6 customers without directly owning generation.

7 **Q. WHY SHOULD DUKE ENERGY OHIO TRANSFER ITS LEGACY**
8 **GENERATING ASSETS TO AN AFFILIATE?**

9 A. There are several reasons why Duke Energy Ohio should transfer the Legacy
10 Generating Assets to an affiliate. First, the transfer reflects the fact that there is no
11 longer a nexus between Duke Energy Ohio's generation and its load. The lack of
12 an association is apparent due to the changes to Ohio's regulatory scheme enacted
13 in 2008 that made competitive bidding a defined process, and the fact that Duke
14 Energy Ohio's switching levels demonstrate that customers see the competitive
15 market as a viable alternative to Duke Energy Ohio's generation. Other Ohio
16 utilities have successfully fulfilled their SSO obligations via the market rather than
17 through continued ownership of generation. Second, the transfer of assets allows
18 Duke Energy Ohio to effectively plan for reliable service in the wake of
19 competition and assure customers get the lowest possible price available in the
20 market. Third, the transfer is timely as the competitive market envisioned more
21 than a decade ago is fully functioning. Therefore, the circumstances are ripe for
22 transferring the assets and the Company will make its application in the very near
23 future. Fourth, the asset transfer will protect Duke Energy Ohio's financial
24 stability by removing the uncertainty of future capital deployment and operation

1 expenditures. Today, Duke Energy Ohio's ability to fund the operation and
2 maintenance of its generation fleet is dependent upon the level of customers who
3 do not switch to a competitive supplier. Transferring the assets means that Duke
4 Energy Ohio's financial stability will no longer suffer from the volatility that
5 comes with customer switching and the Company will not have to be concerned
6 with risks associated with inability to fully hedge its positions because of the
7 limited terms of ESPs. The assets will be managed according to the market, by a
8 company that is able to plan operations farther into the future and fully hedge the
9 fleet without the risk that hedge is negated by customer switching or limited by the
10 duration of the regulatory cycle for the utility's approved pricing plan.

11 **Q. PLEASE EXPLAIN THE REFERENCE TO A LACK OF NEXUS**
12 **BETWEEN DUKE ENERGY OHIO'S GENERATION AND ITS LOAD.**

13 A. The prevalence of customer switching is the most obvious demonstration of the
14 absence of a nexus between Duke Energy Ohio's generation and its load.
15 Customers clearly see the market as vibrant and a way to obtain value and
16 savings. As the Commission is aware, the FirstEnergy Ohio electric distribution
17 utilities (FirstEnergy Companies) have successfully provided for their SSO load
18 without ownership of generation for several years. So it can be done.

19 Also, as more fully discussed in the Direct Testimony of William Don
20 Wathen Jr., in developing the MRO alternative, the Ohio General Assembly has
21 clearly broken the link between the utility generation and load by legislatively
22 constructing a process where load is secured through a competitive auction,
23 without regard to a utility's ownership of generating assets. The Ohio General
24 Assembly, in authoring the MRO process, made it clear that an electric

1 distribution utility need not own generating assets in order to provide its
2 customers with a safe, reliable, and economic supply of energy and capacity.
3 Rather, as I understand, the MRO structure is based upon a competitive auction
4 process with a minimum number of bidders and where at least 25% of the
5 auctioned load is bid upon by entities other than the electric distribution utility.

6 The MRO statute requires a utility owning generation to migrate from its
7 current ESP SSO price to a full market price over time. This migration is
8 accomplished through a phasing in or blending period during which the utility's
9 current ESP price is blended with the market price (MRO Blending Period). As
10 the Company progresses through the MRO Blending Period, an increasingly
11 higher percentage of the SSO price is comprised of market prices established
12 through a competitive bid. Ultimately, the SSO price will be made up entirely of
13 the competitively bid price and Duke Energy Ohio will no longer need to dedicate
14 its Legacy Generating Assets to provide SSO service. Transferring the Legacy
15 Generating Assets, therefore, is also consistent with the MRO because the
16 Company would procure the requisite generation supply for its load through an
17 open, fair, and transparent competitive bidding process, rather than through a
18 dedication of assets at a Commission-determined price based upon the utility's
19 own costs of providing generation service.

20 **Q. PLEASE EXPLAIN HOW A TRANSFER OF THE LEGACY**
21 **GENERATING ASSETS ALLOWS DUKE ENERGY OHIO TO**
22 **EFFECTIVELY PLAN FOR RELIABLE SERVICE AND ENSURE THE**
23 **LOWEST PRICE AVAILABLE IN THE MARKET.**

24 **A.** The provision of reliable service is not impacted by the transfer of the legacy

1 generating assets. Under either ownership structure, the generating assets,
2 transmission assets and all ultimate customers will be in the PJM Interconnection,
3 LLC, which is the reliability coordinator for the PJM region. In addition to its
4 primary function of ensuring reliability, PJM also administers and operates
5 markets for capacity, energy and ancillary services under FERC-approved tariffs.
6 These competitive markets, not the ownership structure, will be the most
7 significant component in determining the CBP. Numerous load-serving entities in
8 PJM (*i.e.* load-serving entities in Ohio, Pennsylvania, and New Jersey) rely
9 exclusively on PJM's markets and associated attributes (*i.e.*, forward capacity
10 markets and trading hubs) for price discovery and to facilitate the CBP. With a
11 CBP, the procurement of reliable generation service is not dependent upon the
12 utility's ownership of the generation assets.

13 As I discussed before, as long as Duke Energy Ohio owns generation, its
14 ability to deploy capital and plan ahead to maintain its assets is dependent upon
15 the level of customers who choose not to switch and is thus limited. In a volatile
16 switching market, Duke Energy Ohio finds itself with assets dedicated to serving
17 all of its customers irrespective of switching, but at the same time, a rapidly
18 dwindling customer base to help pay those costs. Transferring the assets to an
19 affiliate means Duke Energy Ohio is no longer concerned with levels of customer
20 switching in terms of maintaining a generation fleet. The Company will procure
21 adequate resources to serve SSO load through firm commitments from third
22 parties in the CBP.

23 **Q. HOW DOES TRANSFERRING THE ASSETS MAKE DUKE ENERGY**
24 **OHIO INDIFFERENT TO RISKS OF SWITCHING?**

1 A. Under Ohio law, Duke Energy Ohio's retail electric customers are allowed to
2 select their generation supplier and there is little to no restriction on their ability to
3 switch from Duke Energy Ohio. But Duke Energy Ohio cannot be adequately
4 compensated for assuming the risks of being prepared to supply power to
5 customers who are able to switch to alternative suppliers except through a
6 completely, and unconditional, non-bypassable charge. Otherwise, customers
7 essentially receive a free option to take service from Duke Energy Ohio. In fact, as
8 more Duke Energy Ohio customers exercise their right to switch, Duke Energy
9 Ohio has fewer and fewer retail customers over whom to spread its generation
10 cost. As such, the Company cannot effectively hedge its generation supply as it
11 cannot control (nor does it want to control) the competitive choices made by its
12 customers.

13 In transferring the Legacy Generating Assets, however, Duke Energy Ohio
14 no longer has to be concerned with those financial risks, and becomes completely
15 and financially indifferent to customer switching, as it relates to owning and
16 maintaining generation assets. Transferring the assets also transfers those risks to
17 a non-regulated affiliate that can manage them fully in the market. Winners of the
18 CBP take on the financial risk of customer switching. Customers can choose when
19 to purchase their generation service, either through a discrete competitive offer by
20 a CRES or through the CBP determined SSO.

21 Once the Company transfers its generation assets, it will procure supply to
22 serve its SSO load through the CBP. Customers can rest assured that Duke Energy
23 Ohio is procuring resources to serve non-switched load through a transparent CBP,
24 overseen by the Commission, at the lowest possible price. It merely and

1 importantly eliminates the nexus between load and the generator. That nexus is an
2 artifact of a bygone era now replaced with robust wholesale and retail markets.

3 **Q. HOW CAN AN AFFILIATE BETTER HANDLE THOSE RISKS IF IT**
4 **OWNED THE TRANSFERRED GENERATION ASSETS?**

5 A. An affiliate does not have the constraints of quasi-regulation that the utility has
6 with respect to generation. The affiliate can take a broader view of the market to
7 maximize the value of the asset without regard to customer switching. An affiliate
8 is more nimble in responding to sudden changes in the market and can develop a
9 longer term business plan without regard to limitations on earnings or an inability
10 to optimize the use of the assets in a broader market. For example, Ohio law
11 provides that if an ESP is longer than three years, the Commission may re-open the
12 ESP, including its entire pricing structure, and change it. There is no incentive for
13 a utility to propose an ESP for a term longer than three years, when there is a risk
14 that the price will be changed anyway. Thus, at best, the utility that owns
15 generation can only effectively plan or hedge for what can happen in three year
16 intervals.

17 **Q. WHY IS THE TRANSFER OF ASSETS TIMELY?**

18 A. Over ten years ago, the Ohio legislature passed Senate Bill 3, which deregulated
19 electric generation service with the intention of developing a competitive market.
20 Two years ago, with Amended Substitute Senate Bill 221 (S.B. 221), the
21 legislature again made changes to Ohio law intended to encourage and promote the
22 competitive environment that had not yet been realized. But that competitive
23 market is now functioning in Ohio. Indeed, Duke Energy Ohio has experienced
24 customer switching in significant proportion, with more than 60% of its load

1 changing to the more than a dozen alternative suppliers since 2009. Competition is
2 working for customers and, unlike prior periods, it is now an appropriate time for
3 Duke Energy Ohio to transfer its Legacy Generating Assets. Simply put, the nexus
4 between generation and load has been severed as customers are actively choosing
5 to rely on the market for generation services.

6 **Q. PLEASE EXPLAIN WHY DUKE ENERGY OHIO IS UNABLE TO FULLY**
7 **REALIZE THE VALUE OF ITS LEGACY GENERATION ASSETS IN**
8 **THE MARKET DURING THE ESP.**

9 A. As long as Duke Energy Ohio owns generation, there is unlimited downside and
10 limited upside in terms of its ability to earn a return on generation assets. This
11 limited upside is a product of both the Significantly Excessive Earnings Test
12 (SEET) and the blend to market requirement when the SSO price is lower than the
13 market price. Because the Legacy Generating Assets are "dedicated" to customers,
14 the utility is not completely free to try to obtain value for the assets beyond the
15 current ESP period. No matter how much load has switched, the Company must
16 be ready to serve these customers if the SSO load is not completely bid out. The
17 utility is not adequately compensated through an entirely non-bypassable charge
18 for its costs incurred to maintain its generation as an alternative for customers who
19 maintain the right to switch away at any time. In this situation, the Company is
20 burdened with the costs of having these assets available if customers return for
21 whatever reason and burdened with the fact that, because of this standby service, it
22 will be compelled to forgo other market opportunities that may be more lucrative.
23 Transferring the assets to an affiliate makes Duke Energy Ohio indifferent to
24 switching in terms of covering its costs in maintaining generation assets.

1 Transferring the assets to an affiliate provides greater flexibility in managing the
2 assets and an opportunity to receive whatever value those assets have in the
3 competitive market and beyond the limited term of an ESP if it so desires. This
4 allows for a more efficient deployment of capital and operating and maintenance
5 dollars as the market will be the litmus test for whether or not investments in the
6 plants are necessary or required.

7 Today, Duke Energy Ohio incurs costs to maintain its Legacy Generating
8 Assets and to have them available to serve customers who are either served by
9 Duke Energy Ohio and who switch away but may someday return. However, the
10 costs the Company incurs to keep those assets operating are included in the base
11 generation price determined as part of the last ESP. And that price is paid almost
12 exclusively by customers who do not switch away from Duke Energy Ohio.
13 Admittedly, Duke Energy Ohio's current ESP has its capacity dedication rider
14 (Rider SRA-CD) that is conditionally bypassable for non-residential customers and
15 unavoidable for residential customers. However, this rider does not provide
16 adequate compensation for the risks the Company is absorbing when nearly two
17 thirds of its load has switched to an alternative provider of generation service.

18 The utility's SSO price in an ESP is inflexible and only changes pursuant
19 to formulas approved in its ESP plan. And, the utility's inflexible price, whether it
20 is relatively high or low compared to the market, will always be the price for
21 marketers to beat. In its current ESP, the Company's assets are dedicated to serve
22 customers but customers are free to switch away. With an inflexible SSO price
23 that is substantially above the current market prices, significant customer switching
24 has occurred. Unfortunately, because of the commitments made in its current ESP

1 and the dramatic decline in market prices that occurred after the ESP was
2 approved, the utility's earnings and its ability to cover its costs have suffered.
3 Conversely, if the utility's retail generation price is below the market, similar to
4 what was experienced during the RSP periods, there is no switching. However, in
5 that circumstance, the Company cannot receive full value for its generation
6 because when its price is below the market, customers are likely to return to the
7 lower price SSO service and the Company would have little opportunity to sell into
8 the higher priced market. Compounding this asymmetrical paradigm is the fact
9 that, even in this situation where its price was below the market, and most or all of
10 its customers returned, the utility's earnings are subject to an excessive earnings
11 test that could result in the requirement to refund any profit deemed excessive.
12 This places the Company in the untenable situation where it cannot even rely upon
13 times where its financial position is better to make up for the times where the
14 Company's financial position was worse.

15 Under this paradigm, there is no similar mechanism in the statutes to assist
16 the utility when it is effectively under-earning because of changes in market prices
17 and customer switching. This essentially provides capped upside and unlimited
18 downside to Duke Energy Ohio's continued ownership of generation assets. For
19 the risks taken by the Company, this is not a palatable solution.

20 **Q. HOW DOES TRANSFERRING THE ASSETS TO AN AFFILIATE**
21 **RELIEVE THIS ASYMMETRY?**

22 **A.** The asymmetry only exists for electric distribution utilities that own generation
23 assets. Neither competitive providers of retail electric service nor wholesale
24 providers face this risk and limitation on obtaining the full value of their assets.

1 Transferring the assets to an affiliate removes the penalty of owning a generation
2 asset in a competitive market and levels the playing field for all market
3 participants. The asymmetry was not contemplated when the path to competition
4 was first envisioned but was created in S.B. 221. Under an MRO or an ESP, when
5 the entire SSO load is procured by auction, Duke Energy Ohio's generation assets
6 will no longer need to be dedicated to serve SSO load. The Company will indeed
7 procure the firm generation supply necessary to serve its load through the CBP
8 process, which will ensure that customers have SSO service available at the lowest
9 price available in the market. As explained by Mr. Wathen, as the Company
10 progresses through the MRO Blending Period, this transition of the SSO price to a
11 fully competitive market will be done in increasing proportion through a
12 competitive auction. Eventually, all of the Company's load will be procured
13 through the auction format. As I previously explained, Duke Energy Ohio's
14 continued ownership of generation assets thus becomes irrelevant and unnecessary
15 under the MRO. It is reasonable to transfer these assets to an affiliate such that
16 their value can be maximized. The affiliate will be able to hedge the generation in
17 the market.

18 **Q. PLEASE EXPLAIN HOW TRANSFERRING THE LEGACY**
19 **GENERATING ASSETS TO AN AFFILIATE IS REASONABLE AND IN**
20 **THE PUBLIC INTEREST?**

21 **A.** Transferring the assets supports competition and it allows the assets to be held by
22 the best owner in terms of managing the risks of the market. The competitive
23 market contemplated by the Ohio General Assembly and this Commission has
24 finally arrived. Duke Energy Ohio's customers have clearly accepted the retail

1 electric market as an opportunity to extract value by choosing the entity that
2 provides their electric commodity. Duke Energy Ohio, as a load serving entity, is
3 experiencing large volumes of switching among all customer classes. At the time
4 of this filing, more than 60% of the Company's total load has switched to
5 competitive retail electric service (CRES) providers certified by the Commission.
6 Of that total customer migration, approximately 89% of industrial load, 70% of
7 commercial load, 90% of Other Public Authority load and 29% of residential load
8 has switched to a competitive supplier. Duke Energy Ohio anticipates that
9 switching will persist at least at this level. The separation of the assets will further
10 enhance the competitive retail electric service market by placing the generation
11 function on a precisely level playing field with other wholesale and retail
12 competitive generation providers. Ultimately, openness, competitiveness, and
13 transparency of even the retail market are advanced by the Company's proposal
14 herein. Further, once Duke Energy Ohio transfers those generation assets, the
15 utility will no longer be exposed to the market risks associated with owning those
16 assets, including but not limited to fuel, and whether or not those assets will be
17 dispatched into the market. After Duke Energy Ohio implements a CBP and its
18 price for retail electric generation service is determined by the market, there is no
19 reason for Duke Energy Ohio, as a pure electric distribution utility, to continue to
20 own generation assets. All customers will benefit from the prices available from
21 the competitive retail and wholesale electric markets. This is precisely what was
22 originally contemplated with the transition plans in the early part of the decade and
23 what is further supported by the 2008 legislation that established the MRO
24 alternative.

1 Duke Energy Ohio will satisfy its obligation to provide retail electric
2 service at the lowest available price in the market through a CBP. Customers who
3 do not wish to rely upon Duke Energy Ohio will still have the opportunity to find
4 alternative pricing options through CRES providers.

5 **Q. WHEN IS DUKE ENERGY OHIO PROPOSING TO COMPLETE THE**
6 **TRANSFER OF ITS LEGACY GENERATING ASSETS?**

7 A. Duke Energy Ohio proposes to complete the transfer of its Legacy Generating
8 Assets no later than the expiration of the MRO Blending Period that the Company
9 recommends in its Application in this proceeding.

10 **Q. IF THE COMMISSION DOES NOT APPROVE THE COMPANY'S**
11 **PROPOSED MRO BLENDING PERIOD, WILL THIS AFFECT THE DATE**
12 **BY WHICH THE COMPANY WOULD SEEK TO TRANSFER ITS**
13 **LEGACY GENERATING ASSETS?**

14 A. No. Again, the expiration of the proposed MRO Blending Period reflects the latest
15 date by which the Company would seek to transfer its Legacy Generating Assets.
16 Thus, if the Commission does not accept the Company's proposal with regard to
17 when the transition to market is complete, the Company still reserves the right to
18 seek approval of, and to complete the transfer the assets no later than May 31,
19 2014.

20 **Q. SHOULD THE COMMISSION OR ANY OTHER STAKEHOLDER BE**
21 **CONCERNED WITH DUKE ENERGY OHIO'S DECISION TO**
22 **TRANSFER ITS LEGACY GENERATING ASSETS?**

23 A. No. The FirstEnergy Companies previously transferred their generating assets and
24 have implemented auctions in the past two years to procure the generation

1 necessary to serve their SSO load through at least the next few years. That process
2 has resulted in lower retail electric service prices and no degradation in reliability
3 for the FirstEnergy Companies' customers and has been endorsed by the
4 Commission. In its May 14, 2009, press release accepting the results of the
5 FirstEnergy Auction, the Commission acknowledged the success of the auction,
6 stating:

7 "We are more than pleased that ratepayers in northern
8 Ohio, many of whom have been victimized by the
9 economy, will benefit from the outcome of this energy
10 auction," PUCO Chairman Alan R. Schriber stated. "We're
11 proud of the way the auction was conducted and commend
12 the participants, the auction manager and our consultant for
13 making this such a success."

14 I have attached a copy of the entire press release to my testimony as Attachment
15 CRW-2, as well as a copy of the more recent press release discussing the success
16 of FirstEnergy's October 20, 2010 auction. There is no reason to doubt that Duke
17 Energy Ohio's own CBP, will be just as successful. The FirstEnergy Companies'
18 successes show that a utility does not need to own generation to serve load and
19 that the auction process is a fair and reasonable approach to obtaining the best
20 price in the market for customers.

IV. EFFECT OF THE TRANSFER ON DUKE
ENERGY OHIO'S STANDARD SERVICE OFFER

21 Q. IF THE COMPANY COMPLETES THE TRANSFER OF LEGACY
22 GENERATING ASSETS PRIOR TO END OF THE MRO BLENDING
23 PERIOD, HOW WILL IT ENSURE THAT ITS SSO CUSTOMERS ARE
24 PROVIDED WITH A RELIABLE SOURCE OF GENERATION WITH
25 REGARD TO THAT PORTION OF THE SSO OFFER THAT IS NOT

1 **SUBJECT TO A COMPETITIVE BID?**

2 A. Duke Energy Ohio witness Julia S. Janson addresses this circumstance in her
3 testimony. But briefly, if the transfer of Legacy Generating Assets is completed
4 prior to the expiration of the proposed MRO Blending Period, Duke Energy Ohio
5 would enter into a purchase power agreement, subject to approval by the FERC, to
6 procure the necessary generation services.

7 **Q. HOW WILL THE PROPOSED ASSET TRANSFER AFFECT DUKE**
8 **ENERGY OHIO'S CURRENT ESP OR THE MRO PROPOSED IN THIS**
9 **PROCEEDING?**

10 A. The proposed transaction will have absolutely no effect on either the current ESP
11 or the proposed MRO. Since the effective date of the transfer will not be until
12 after January 1, 2012, the transfer will occur after the current ESP expires on
13 December 31, 2011. Because the General Assembly, in authoring the MRO
14 process, requires a Blending Period for utilities that own generation on or after
15 July 31, 2008, the Company's MRO must include the Blending Period. Duke
16 Energy Ohio will submit a detailed plan that will detail how the assets will be
17 transferred in a manner consistent with the transition to full market that is
18 ultimately approved by the Commission. In the interim, customers will continue to
19 receive the benefits of the Company's ownership of these assets.

20 **Q. HOW WILL DUKE ENERGY OHIO'S TRANSFER OF THE LEGACY**
21 **GENERATING ASSETS AFFECT THE COMMISSION'S OVERSIGHT OF**
22 **DUKE ENERGY OHIO'S PROCUREMENT OF SUPPLY FOR**
23 **STANDARD SERVICE OFFER CUSTOMERS?**

24 A. The Commission will continue to maintain all of its current oversight over Duke

1 Energy Ohio. This oversight will surely extend to its procurement of SSO supply.
2 Further, the Company must provide, on an annual basis, a detailed report on the
3 CBP during the MRO Blending Period. Similarly, upon the expiration of the MRO
4 Blending Period, the Company must submit to the Commission an annual report on
5 the CBP. The transfer of assets will not affect the level of Commission oversight of
6 the CBP.

7 **Q. WILL THE TRANSFER OF DUKE ENERGY OHIO'S GENERATION**
8 **ASSETS NEGATIVELY AFFECT THE CONTEMPLATED**
9 **COMPETITIVE BIDDING PROCESS?**

10 A. In my opinion as a potential wholesale auction participant, the transfer of
11 generating assets will not adversely affect the CBP or the auctions. It has not in
12 the two auctions that worked in the FirstEnergy Companies' service areas. The
13 CBP has absolutely no bearing on whether Duke Energy Ohio owns generation. In
14 fact, as I previously discussed, under an MRO with Duke Energy Ohio's price
15 determined either in whole or in part by an auction, there is no link between the
16 utility's load and the ownership of generation. Under the CBP, the market, by way
17 of transparent competitive auction, will ensure that Duke Energy Ohio supplies its
18 SSO through the most economic resources.

19 **Q. DID MCG OR ANY AFFILIATE OF DUKE ENERGY OHIO THAT**
20 **OFFERS COMPETITIVE RETAIL ELECTRIC SERVICE IN OHIO**
21 **PARTICIPATE IN THE DESIGN OR DEVELOPMENT OF DUKE**
22 **ENERGY OHIO'S PROPOSED MRO AUCTION DESIGN?**

23 A. No. Neither MCG nor any Duke Energy Ohio affiliate offering competitive retail
24 electric service in Ohio had any involvement in the MRO auction design. This was

1 intentional so that MCG, which operates Duke Energy Ohio's generation, could
2 potentially participate in the auction during the MRO Blending Period and after the
3 transition to market is complete.

4 **Q. WILL DUKE ENERGY OHIO PARTICIPATE IN THE CBP DURING THE**
5 **MRO BLENDING PERIOD AND PRIOR TO COMPLETING THE ASSET**
6 **TRANSFER?**

7 A. Yes.

8 **Q. WILL MCG HAVE ANY ADVANTAGE IN ITS PARTICIPATION IN**
9 **DUKE ENERGY OHIO'S PROPOSED MRO AUCTION?**

10 A. No. MCG will have no advantage. MCG, and upon transfer completion, the
11 affiliate owning the legacy generation assets, must meet the same criteria as any
12 other competitive bidders in order to participate in the auction. Again, as shown in
13 the auctions in the FirstEnergy Companies' territories, affiliates can participate in
14 the utility's CBP in a fair and transparent process that is independently managed
15 without any concern of advantage, undue preference or discrimination.

V. CONCLUSION

16 **Q. WAS ATTACHMENT CRW-1 AND CRW-2 PREPARED BY YOU OR**
17 **UNDER YOUR DIRECTION AND CONTROL?**

18 A. Yes.

19 **Q. DOES THIS CONCLUDE YOUR PRE-FILED DIRECT TESTIMONY IN**
20 **THIS PROCEEDING?**

21 A. Yes.

Summary of Duke Energy Ohio Legacy Generation		
Station	Ownership	MW (April-May/ Oct-Nov)
Beckjord 1	100.00%	94
Beckjord 2	100.00%	94
Beckjord 3	100.00%	128
Beckjord 4	100.00%	150
Beckjord 5	100.00%	238
Beckjord 6	37.50%	158
Beckjord CT 1	100.00%	53
Beckjord CT 2	100.00%	53
Beckjord CT 3	100.00%	53
Beckjord CT 4	100.00%	53
Conesville 4	40.00%	312
Dick's Creek CT 1	100.00%	101
Dick's Creek CT 3	100.00%	15
Dick's Creek CT 4	100.00%	18
Dick's Creek CT 5	100.00%	18
Killen 2	33.00%	198
Miami Fort 7	64.00%	326
Miami Fort 8	64.00%	326
Miami Fort CT 3	100.00%	15
Miami Fort CT 4	100.00%	15
Miami Fort CT 5	100.00%	15
Miami Fort CT 6	100.00%	15
Stuart 1	39.00%	225
Stuart 2	39.00%	225
Stuart 3	39.00%	225
Stuart 4	39.00%	225
Zimmer 1	46.50 %	605



**Public Utilities
Commission**

Ted Strickland, Governor
Alan R. Schriber, Chairman

**News Release
For Immediate Release
Contact: Shana Eiselstein
614 | 468 7750**

PUCO accepts FirstEnergy auction results

COLUMBUS, OHIO (May 14, 2009) – The Public Utilities Commission of Ohio (PUCO) today accepted the final wholesale auction price of \$61.50 per megawatt hour for FirstEnergy's operating companies standard service offer supply. The results of this wholesale auction determined FirstEnergy's generation and transmission service rates from June 1, 2009 through May 31, 2011.

"We are more than pleased that ratepayers in northern Ohio, many of whom have been victimized by the economy, will benefit from the outcome of this energy auction," PUCO Chairman Alan R. Schriber stated. "We're proud of the way the auction was conducted and commend the participants, the auction manager and our consultant for making this such a success."

The percentage change in the retail rates for individual rate classes will vary. On an annual total bill basis, retail rates for a standard residential customer using 1,000 kilowatt hours (kWh) per month will decrease by 16 percent for Ohio Edison, 12.6 percent for Toledo Edison and 7.4 percent for Cleveland Electric Illuminating. The rates around these annual total bill percentages will vary between summer and winter.

The auction began on May 13, 2009 and concluded on May 14, 2009. There were 12 bidders registered for the auction and nine submitted winning bids. The auction consisted of 25 rounds and procured all of the necessary tranches to supply FirstEnergy's load. CRA International served as the independent auction manager. Boston Pacific Company, Inc., a consultant retained by the PUCO, monitored the auction process.

FirstEnergy must file tariffs for Commission review and approval containing retail rates consistent with the results of the auction within seven days.

The names of the winning bidders who won tranches in the auction, the number of tranches won by each bidder and the first round ratio of tranches offered compared to tranches needed will be subject to public release in 21 days. This will allow the winning bidders to procure any additional necessary capacity to serve the load.

A copy of today's Commission finding and order and redacted version of the report issued by the auction manager will be available at <http://www.puco.ohio.gov/>. Click on the link to DIS and enter the case number 08-935-EL-SSO.

-30-
08-935-EL-SSO

The Public Utilities Commission of Ohio (PUCO) is the sole agency charged with regulating public utility service. The role of the PUCO is to assure all residential, business, and industrial consumers have access to adequate, safe, and reliable utility services at fair prices while facilitating an environment that provides competitive choices. Consumers with utility-related questions or concerns can call the PUCO hotline at (800) 686-PUCO (7826) and speak with a representative.

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**Public Utilities
Commission**

Ted Strickland, Governor
Alan R. Schriber, Chairman

**News Release
For Immediate Release**
Contact: Shana Eiselstein
614 | 466 7750

PUCO accepts results of FirstEnergy auction

COLUMBUS, OHIO (Oct. 22, 2010) – The Public Utilities Commission of Ohio (PUCO) today accepted the results of the first of six wholesale auctions that will determine FirstEnergy's retail generation service rates from June 1, 2011 through May 31, 2014.

"We are pleased with the results of this first wholesale generation auction," PUCO Chairman Alan R. Schriber stated. "If wholesale generation rates hold at this level or better in the auction held in January, customers of FirstEnergy will see a reduction in their 2011 retail generation rates."

The auction began on Oct. 20, 2010 and concluded that same day. There were 10 bidders registered for the auction and four submitted winning bids. The auction consisted of 12 rounds. The auction resulted in a clearing price of \$54.55 per megawatt hour (MWh) for the June 1, 2011 to May 31, 2012 delivery period, \$54.10 per MWh for the June 1, 2011 to May 31, 2013 delivery period and \$56.58 per MWh for the June 1, 2011 to May 31, 2014 delivery period.

Another auction will be held in January 2011. The prices received in that auction will be blended with the prices received in the Oct. 20, 2010 auction to determine the retail generation service price for the June 1, 2011 to May 31, 2012 delivery period. Additional auctions will also be held in October 2011, January 2012, October 2012, and January 2013 which will establish the retail generation prices for the 2012 and 2013 delivery periods.

CRA International served as the independent auction manager. Boston Pacific Company, Inc., a consultant retained by the PUCO, monitored the auction process.

The names of the winning bidders who won tranches in the auction, the number of tranches won by each bidder and the first round ratio of tranches offered compared to tranches needed will be subject to public release in 21 days.

A copy of today's Commission finding and order and redacted version of the report issued by the auction manager will be available at www.PUCO.ohio.gov. Click on the link to DIS and enter the case number 10-1284-EL-UNC.

-30-

10-1284-EL-UNC

The Public Utilities Commission of Ohio (PUCO) is the sole agency charged with regulating public utility service. The role of the PUCO is to assure all residential, business, and industrial consumers have access to adequate, safe, and reliable utility services at fair prices while facilitating an environment that provides competitive choices. Consumers with utility-related questions or concerns can call the PUCO hotline at (800) 686-PUCO (7826) and speak with a representative.

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