

LARGE FILING SEPERATOR SHEET

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Duke Energy Ohio
Case No. 10-2586-EL-SSO
IEU Supplemental First Set Production of Documents
Date Received: November 17, 2010

IEU--SUPP-POD-03-005 (s) CONFIDENTIAL

REQUEST:

Please provide any documents identified in response to Interrogatory No. 10.

RESPONSE:

CONFIDENTIAL PROPRIETARY TRADE SECRET

See Confidential Attachment IEU-Second- Supp-POD-03-005 (s) being sent on CD: Drafts of Analyses.

PERSON RESPONSIBLE: Lee Barrett

Commercial Businesses – TRC Scrub Review Guidelines**Corporate Review Team Single Point of Contact (SPOC)****TRC Scrub Report and Checklist**

Commercial Business Unit: Commercial Asset Management

Project Name: MISO:PJM Asset Transfer

TRC Scrub SPOC: Kelly Little

Scrub Materials Distributed: 10/Var/2009

Scrub Meeting: 11/02/2009

TRC Scrub Sign-off: 1/11/2010

TRC Draft Materials: 1/13/2010

TRC Review (final materials): 1/19/2010

TRC Date: 1/27/2010

BoD Date: _____

Commercial Business DEGS / CAMS / Telecommunications /Strategic /Commercial Strategy TRC Scrub Members		Sign-off	Commercial Business DEI TRC Scrub Members	
Financial Analysis	Charlie Wilson, Steve Trabucco	X		
Foreign Exchange	Kitty McDonough	n/a		
Credit	John Gatto	X		
Risk	Swati Daji, Bob Bolubaz			
Accounting	Gwen Pate, Bryan Buckler, Jim Huddle, Keith Weidman, Tom Heath	X-C		
Tax – State	Cooper Monroe	X		
Tax – Federal	Marcus Shore	X		
Legal	Kodwo Ghartey-Tagoe, Kate Moriarity	X		
Forecasting	Mark Krabbe, Lisa Cullen	X		
FE&G	Kevin King, Patty Mullins, Kate Passarelli	X-C		

Project Business Team:

Lee Barrett, Ken Jennings, Walt Yeager

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TRC Scrub Review Meeting Notes

See project file for documentation.

TRC Review – Presentation Points and Notes

1. Proposed project is to move the load, generation, and transmission for DEO/DEK from MISO to PJM.
2. Move transfers DEO [REDACTED] position to PJM; DEO gas assets already in PJM.
3. PJM system attributes viewed more favorably than MISO: 3-yr auction, interconnections, etc.; consolidation of DEO into single market area.
4. No presumed [REDACTED] to DEO/DEK customers, [REDACTED]
5. Costs presumed to be primarily one-time, up-front, in 2014; include exit fees and MTEP payout.
6. Capacity Pricing forecast, [REDACTED].

Discussion required for additional details specifically to address impact to DEK (regulated).

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TRC Scrub Considerations

Recommend revisiting the project status and economics once we have completed the regulatory process and prior to execution.

Risk

[REDACTED]

Accounting

1. PJM capacity contracts for Ohio generation

These contracts would meet the accounting definition of derivatives; however, we believe these contracts would be eligible for the "normal sale" exemption and if elected by Duke Energy would allow for "accrual" accounting for the contracts as opposed to "mark to market" accounting. Therefore [REDACTED]

2. [REDACTED] one-time MISO exit fee

Expect to record in Q1 2011. Amount would need to be expensed when incurred. Timing of expense – although the legal obligation to pay the fee may not technically exist until the exit date in 2014, the auction of the generation assets in May 2011 for the June 2014-May 2015 period would seem to indicate that an unavoidable obligation has been incurred, and thus expense recognition should occur in 2011. In fact, Duke Energy, in January or February 2011, would expect to sign a form of agreement with PJM (and share information needed to effectively participate in the May 2011 auction) that formally obligates Duke Energy to transfer the Ohio Transmission assets to PJM (thus, expense occurs in Q1 2011 as opposed to Q2 2011).

3. [REDACTED] MISO Transmission Expansion Fee

Expect to record in Q1 2011. Amount would need to be expensed when incurred. Timing of expense – although the legal obligation to pay the fee may not technically exist until the exit date in 2014, the auction of the generation assets in May 2011 for the June 2014-May 2015 period would seem to indicate that an unavoidable obligation has been incurred, and thus expense recognition should occur in 2011. In fact, Duke Energy, in January or February 2011, would expect to sign a form of agreement with PJM (and share information needed to effectively participate in the May 2011 auction) that formally obligates Duke Energy to transfer the Ohio Transmission assets to PJM (thus, expense occurs in Q1 2011 as opposed to Q2 2011). At that time, Duke Energy cannot back out of the asset transfer. [TENTATIVE CONCLUSION].

Before liability can be booked, legal will need to opine that obligation is "probable" of occurrence, and the business team will have to demonstrate that amount is a reasonable estimate.

2.B. and 3.B. – the only way to avoid expense recognition of both amounts is to [REDACTED]

4. Goodwill impairment analysis for [REDACTED] Ohio T&D business [REDACTED]

We have 2 SEC financial statements to consider with respect to Ohio T&D Goodwill – our equity SEC registrant Duke Energy Corporation and our debt equity registrant Duke Energy Ohio.

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DE Corp has approximately [REDACTED] of goodwill recorded on its books related to the Ohio T&D business. An annual [REDACTED] of [REDACTED] beginning in 2014 has no effect on the goodwill impairment test for DE Corp (i.e., the enterprise valuation for this business has plenty of "cushion").

DE Ohio has approximately [REDACTED] of goodwill recorded on its books related to the Ohio T&D business. This goodwill [REDACTED] its 2009 impairment test by roughly [REDACTED] meaning the sum of the forecasted discounted cash flows of the business [REDACTED] its net book value by [REDACTED]. An annual [REDACTED] of [REDACTED] beginning in 2014 into perpetuity would make the DCF of the business [REDACTED] to a level that approximates the [REDACTED] putting additional [REDACTED] on the goodwill impairment test at the DE Ohio level.

Tax The majority of the [REDACTED] associated with switch should be deductible because the costs are primarily [REDACTED] comprised of payments to discharge DE-Ohio's share of MISO liabilities at the time it exits MISO. The remaining costs also should be deductible, although the determination of whether the payments are currently deductible or must be capitalized and deducted over time will depend on future developments relating the project.

FE&G

- 1) The WH states "...DEO customers are [REDACTED] because the [REDACTED] Isn't it more appropriate to state that the [REDACTED] since they will be [REDACTED] to PJM capacity prices via the [REDACTED]"

LB – we have added "Under an ESP and the current generation to load profile"

LB – right now DEO is not [REDACTED] to serve its POLR load so [REDACTED]

However, the footprint is still [REDACTED] regardless who serves the load

- 2) Please clarify or elaborate on the following stmts within the WP:

- (1) "...PJM's market design better accommodates customer switching than MISO's design."

LB – PJM has systems that allow it to calculate a customer's daily capacity obligation and assign that obligation to that customer's supplier. MISO has no such system and a supplier only finds out after the fact (45 days) if the customer has switched. The supplier then either procured too much capacity or too little – it is an inefficient process. With ARRs/FTRs, PJM again determines the obligation daily and the ARR dollars follow the customer when it switches. In MISO, there is no mandatory process to reallocate ARR dollars to accommodate intra-month switching – again an inefficient process. Central forecasting by PJM is the key to both and MISO does not do that.

- (2) "RPM also enforces PJM's capacity obligation and supports the daily transfer of a customer's obligation from one supplier to another."

LB – MISO's resource adequacy construct is loose with respect to enforcement thereby undermining reliability

- 3) Comment on the level of uncertainty and/or conservatism inherent in the following assumptions, and identify any other significant assumption uncertainties not listed here. The desire here is to simply identify any potentially significant upside or downside in the modeling or other whitepaper statements.

- a) Amount of MTEP costs, which will be due as of a 6/1/14 departure date

LB – [REDACTED] MTEP costs approved [REDACTED] because projects are not built but have been approved. MTEP costs could [REDACTED] as new projects are approved prior to our departure. Midwest Transmission provided this analysis and is comfortable with the [REDACTED] MTEP costs [REDACTED] – we have [REDACTED] but First Energy is seeking recovery.

- b) MISO exit fee –

LB [REDACTED] – could [REDACTED] is based on the estimate FE got from MISO

- c) Cost of energy to DEO & DEK customers

[REDACTED] to DEK customers, in fact our analysis shows [REDACTED] to customers

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LB – [REDACTED] could be [REDACTED] to customers as well
d) Cost to pseudo-tying Madison back to MISO

[REDACTED] has been done before - just metering

e) [REDACTED]
[REDACTED] I think this [REDACTED] could have a fair variance given Duke would have no leverage

- 4) What is being done to help [REDACTED] the potentially [REDACTED] for DEI in MISO?
we are trying to avoid direct comparison of quantification of cost/benefit between MISO & PJM, don't know how successful this will be if KyPSC requires such a comparison
LB – Agreed, as we will continue to be a member both Duke and MISO have an [REDACTED] to keep the relationship [REDACTED] We will try to avoid the accusations made by FE and our case will be center around all other OH utilities are in PJM and we have legacy issues with DPL and AEP.
- 5) Comment on how this move may impact results of future hearings with the three state commissions? In particular, is it conceivable that the move could [REDACTED] future decision-making by any of the state commissions?
LB – Sure, but I think it is easier now the FE has gone and don't we have this risk with all deals
- 6) Which business unit(s) will bear the cost of the additional 11 FTEs?
LB – Midwest Transmission
- 7) When do we expect FE's PUCO protest to be finalized? Could the PUCO action prevent FE from participating in the forthcoming RPM auction?
LB – don't know when it will be finalized. If FE wants to settle with PUCO then maybe 60 days – unlikely. If they want to litigate then years. We don't know what path they will choose yet. FE will be participating in the upcoming auction – they don't need PUCO approval to do so. Also, they intend to try to recover all FERC costs, MTEP, RTEP, Exit fee, etc.
- 8) WP states that "...IURC will intervene at FERC and request DEI is [REDACTED]" Could the IURC insist that other LSE's within their jurisdiction also be held harmless, adding to potential [REDACTED]
[REDACTED] primarily for [REDACTED] in DEI territory
- 9) Consideration should be given to evaluating the proposed project economics in today's dollars. Applying consistent assumptions as reflected in the project economics and discounting the NPV to reflect 2010 and 2011 values, the comparative information would be as follows:

	2010	2011	2012	2014
Initial Cost (in millions)	[REDACTED]			
10-year NPV @ 9.25%	[REDACTED]			
15-year NPV @ 9.25%	[REDACTED]			

There is concern that the cost adjustment factor being applied to the Initial Costs is overly conservative. Applying a less conservative (more realistic) cost adjustment factor, would reduce the Initial Cost from [REDACTED] to [REDACTED]. Reducing this cost would result in the following comparative information:

	2010	2011	2012	2014
Initial Cost (in millions)	[REDACTED]			
10-year NPV @ 9.25%	[REDACTED]			
15-year NPV @ 9.25%	[REDACTED]			

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Furthermore, it is important to note:

- NPV values assume mid-year cash flows;
- There are no actual cash expenditures expected to be paid until 2014; and
- The Accounting Liability will be booked in either 2011 or 2012.

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TRC Date	Draft TRC Materials to Donna Council	Final TRC Materials to Donna Council	Draft Board Materials due to Sue Harrington	Board Date
Monday, January 11, 2010	28-Dec-09	4-Jan-10		
Wednesday, January 27, 2010	13-Jan-10	20-Jan-10		
Monday, February 08, 2010	25-Jan-10	1-Feb-10	9-Feb-10	Monday-Tuesday, February 22-23, 2010 (Mailing February 16, 2010)
Wednesday, February 24, 2010	10-Feb-10	17-Feb-10		
Monday, March 08, 2010	22-Feb-10	1-Mar-10		
Monday, March 22, 2010	8-Mar-10	15-Mar-10		
Wednesday, April 07, 2010	24-Mar-10	31-Mar-10		
Monday, April 19, 2010	5-Apr-10	12-Apr-10	21-Apr-10	Wednesday-Thursday, May 5-6, 2010 (Mailing April 29, 2010)
Tuesday, May 04, 2010	20-Apr-10	27-Apr-10		
Monday, May 24, 2010	10-May-10	17-May-10	8-Jun-10	Monday-Tuesday, June 21-22, 2010 (Mailing June 15, 2010)
Monday, June 14, 2010	31-May-10	7-Jun-10		
Monday, June 28, 2010	14-Jun-10	21-Jun-10		
Monday, July 12, 2010	28-Jun-10	5-Jul-10		
Monday, July 26, 2010	12-Jul-10	19-Jul-10		
Monday, August 09, 2010	26-Jul-10	2-Aug-10	10-Aug-10	Monday-Tuesday, August 23-24, 2009 (Mailing August 17, 2010)
Wednesday, August 25, 2010	11-Aug-10	18-Aug-10		
Wednesday, September 08, 2010	25-Aug-10	1-Sep-10		
Monday, September 20, 2010	6-Sep-10	13-Sep-10		
Monday, October 04, 2010	20-Sep-10	27-Sep-10	12-Oct-10	Monday-Tuesday, October 25-26, 2010 (Mailing October 19, 2010)
Monday, October 18, 2010	4-Oct-10	11-Oct-10		
Monday, November 01, 2010	18-Oct-10	25-Oct-10		
Monday, November 15, 2010	1-Nov-10	8-Nov-10	24-Nov-10	Wednesday-Thursday, December 8-9, 2010 (Mailing December 2, 2010)
Monday, November 29, 2010	15-Nov-10	22-Nov-10		
Monday, December 13, 2010	29-Nov-10	6-Dec-10		

**UNITED STATES OF AMERICA
BEFORE THE
FEDERAL ENERGY REGULATORY COMMISSION**

Duke Energy Ohio, Inc. and)	Docket No. ER10-1562-_____
Duke Energy Kentucky, Inc.)	Docket No. ER10-2254-_____

**COMPLIANCE FILING OF DUKE ENERGY OHIO, INC. AND
DUKE ENERGY KENTUCKY, INC.**

Duke Energy Ohio, Inc. ("DEO") and Duke Energy Kentucky, Inc. ("DEK") (collectively, "Duke") hereby submit this filing in compliance with the Commission's October 21, 2010, Order Addressing RTO Realignment Request ("Realignment Order")¹ in the above-captioned dockets. DEO and DEK have been authorized by PJM to state that PJM has reviewed this filing and does not object to anything set forth herein.

BACKGROUND

On June 25, 2010, in Docket No. ER10-1562, DEO and DEK submitted an Initial Filing requesting Commission approval of the first phase of their proposed move from the Midwest Independent Transmission System Operator, Inc. ("Midwest ISO") to the PJM Interconnection, LLC ("PJM").² On August 16, 2010, in Docket No. ER10-2254, Duke submitted another filing, representing the second step of the series of filings required to complete its proposed RTO move, detailing the process by which Duke plans to satisfy their zonal capacity procurement commitments and obligations under PJM's Reliability Assurance

¹ *Duke Energy Ohio, Inc. and Duke Energy Kentucky, Inc.*, Order Addressing RTO Realignment Request, 133 FERC ¶ 61,058 (2010).

² Duke also filed an Answer and Motion to Leave Answer to protests and comments to its Initial Filing on August 10, 2010.

Agreement Among Load-Serving Entities in the PJM Region ("RAA") and the obligations under Attachment DD of the PJM Open Access Transmission Tariff ("OATT") with respect to all load within the Duke Energy Zone in the 29 month period beginning January 1, 2012 ("FRR Filing"). The FRR Filing requested approval for the aspects of DEO and DEK's Out of Time Fixed Resource Requirement ("FRR") Integration Plan (the "Duke FRR Plan") that differ from PJM's ordinary FRR process.³

The Realignment Order authorized DEO and DEK to terminate their existing obligations to the Midwest ISO and accepted the proposed Duke FRR Plan and requested waivers, subject to conditions. The Realignment Order directed us to address several issues in a compliance filing.⁴ This Compliance Filing addresses those issues.

COMPLIANCE RESPONSES

Two paragraphs from the Realignment Order imposed compliance requirements on Duke. For ease of reference, we set out here the first such paragraph, and then address the compliance requirements from that paragraph, and then do the same for the second paragraph.

I. Paragraph 113 Compliance Requirements

113. We grant Duke's requested waivers of Sections C.1, C.2, and D.1 of Schedule 8.1 of the Reliability Assurance Agreement. We will further accept, subject to a compliance filing to be filed within 30 days of the date of this order, Duke's requested waivers of Sections D.2, E.2, and E.4 of the same agreement. **With respect to the waiver of Section E.4, which involves summer compliance period testing of Demand Resources and measurement and**

³ On September 22, 2010, DEO filed an Answer and Motion to Leave for Answer, responding to comments and protests filed with regard to the FRR Filing.

⁴ Realignment Order at Ordering Paragraphs A and B.

verification of Energy Efficiency Resources, Duke explains that PJM is in the process of comparing its testing measures to that of Midwest ISO to ensure that participation by these resources in the FRR Integration Plan will not cause PJM to fail to satisfy its reliability requirements. We will require Duke to consult further with PJM on this issue and to include in its compliance filing either a complete description of how PJM plans to make this determination or a timeline detailing when it will know how PJM plans to make this determination. We further condition our acceptance of Duke's waivers of Sections D.2 and E.2 on Duke providing in its compliance filing a more thorough explanation of the need for these particular waivers. Duke has withdrawn its request for waiver of Section F.2, as explained in its answer.⁵

A. Section E.4 of Schedule 8.1 of the RAA

It has come to our attention that due to a typographical error in Duke's FRR Filing, we requested waiver of Section E.4 of Schedule 8.1, when we intended to request waiver of Section D.4 of Schedule 8.1.⁶ The substance of our waiver request stands, and the response provided herein to this compliance directive addresses Section D.4 of Schedule 8.1. Duke has consulted with PJM as required, and PJM has developed and provided the following:

PJM requires Demand Resources to be available for the entire delivery year and to perform a test during the summer period which represents June

⁵ Realignment Order at P 113 (emphasis added).

⁶ Section D.4 provides, in relevant part: "Capacity Resources identified and committed in an FRR Capacity Plan shall meet all requirements under this Agreement and the PJM Operating Agreement applicable to Capacity Resources, including, as applicable, requirements and milestones for Planned Generation Capacity Resources and Planned Demand Resources... All demand response, load management, energy efficiency, or similar programs on which such FRR Entity intends to rely for a Delivery Year must be included in the FRR Capacity Plan submitted three years in advance of such Delivery Year and must satisfy all requirements applicable to Demand Resources or Energy Efficiency Resources, as applicable, including, without limitation, those set forth in Schedule 6 to this Agreement and the PJM Manuals; provided, however, that previously uncommitted Unforced Capacity from such programs may be used to satisfy any increased capacity obligation for such FRR Entity resulting from a Final Zonal Peak Load Forecast applicable to such FRR Entity."

through September if such Demand Resources are not dispatched by PJM under Emergency conditions. If the Demand Resources do not deliver the committed amount of energy they are subject to a penalty. Since Duke will not integrate into PJM until January 1, 2012, Duke requested a waiver from FERC regarding the PJM test requirement for Demand Resources.

PJM has reviewed Duke's request to allow Demand Resources to be used in the Duke FRR Plan for the period of January 1, 2012, through May 31, 2012, ("Partial Year Demand Resources") and determined that it is not necessary to complete the PJM mandatory test for this period of time to maintain system reliability because the Midwest ISO-required test is sufficient, the partial year is outside the normal mandatory event compliance period, and such waiver will only be applicable for the partial year. Demand Resources used in the Duke FRR Plan after May 31, 2012, are required to comply with all PJM Tariff and Manual requirements including associated Demand Response tests.

Partial Year Demand Resources will only be approved in the Duke FRR Plan if they are certified and effective in the Midwest ISO as a Load Modifying Resource ("LMR") from June 1, 2010, through December 31, 2010. LMR Resources are similar to PJM Demand Resources where they have a mandatory commitment to provide energy to the grid during an emergency. As a Midwest ISO LMR they will be subject to all Midwest ISO required provisions, including event compliance, testing and all associated penalties through such period of time.

Partial Year Demand Resources are also required to have all registrations submitted and approved by PJM by June 1, 2011, and as outlined in the PJM tariff and business rules. Partial Year Demand Resources will be subject to all PJM rules and provisions effective on January 1, 2012. Since such resources are under the control of the Midwest ISO from June 1, 2011 through December 31, 2011, they are not subject to PJM rules and are not required to respond to PJM emergency conditions or test during this period.

B. Section D.2 of Schedule 8.1 of the RAA

In the FRR Filing, DEO stated that it sought waiver of Section D.2 of Schedule 8.1 of the RAA regarding the Preliminary Peak Load Forecast used, so that it can use a Preliminary Peak Load Forecast that is based on the preliminary forecast peak load of the Duke Energy Zone that takes into account summer 2010 peaks.

Section D.2 requires that the Preliminary Forecast Peak Load be determined according to PJM-related calculations for the applicable Delivery Year. Specifically, "the Preliminary Forecast Peak Load for each such entity shall be the FRR Entity's Obligation Peak Load last determined prior to the Base Residual Auction for such Delivery Year."⁷ Schedule 8.A of the RAA defines

⁷ Section D.2 states in its entirety: "The FRR Capacity Plan of each FRR Entity that commits that it will not sell surplus Capacity Resources as a Capacity Market Seller in any auction conducted under Attachment DD of the PJM Tariff, or to any direct or indirect purchaser that uses such resource as the basis of any Sell Offer in such auction, shall designate Capacity Resources in a megawatt quantity no less than the Forecast Pool Requirement for each applicable Delivery Year times the FRR Entity's allocated share of the Preliminary Zonal Peak Load Forecast for such Delivery Year, as determined in accordance with procedures set forth in the PJM Manuals. If the FRR Entity is not responsible for all load within a Zone, the Preliminary Forecast Peak Load for such entity shall be the FRR Entity's Obligation Peak Load last determined prior to the Base Residual Auction for such Delivery Year, times the Base Zonal FRR Scaling Factor. The FRR Capacity Plan of each FRR Entity that does not commit that it will not sell surplus Capacity

"Obligation Peak Load" as the "daily summation of the weather-adjusted coincident summer peak, last preceding the Delivery Year, of the end-users in such Zone (net of operating Behind the Meter Generation, but not to be less than zero) for which such Party was responsible on that billing day, as determined in accordance with the procedures set forth in the PJM Manuals." At the time that the Preliminary Forecast Peak Load was calculated by PJM for Delivery Year 2011-2012, DEO was not a member of PJM and did not have its Peak Load Obligation determined prior to the Base Residual Auction ("BRA"), as required by Section D.2, for the 2011-2012 Delivery Year. Our request for waiver is limited to a request that the Preliminary Peak Load Forecast instead be based upon 2010 summer peaks for the Duke Energy Zone while DEO was a member of the Midwest ISO.

C. Section E.2 of Schedule 8.1 of the RAA

DEO sought waiver of Section E.2 of Schedule 8.1 of the RAA, regarding the limit on the sale of Capacity Resources above the Threshold Quantity into auctions conducted under Attachment DD to the PJM OATT, solely to the extent necessary to exclude from calculation of that limit Capacity Resources of DEO or of any Duke Energy Zone wholesale load choosing to enter its own Independent FRR Plan ("Independent FRR Entity") that have already cleared in an RPM

Resources as set forth above shall designate Capacity Resources at least equal to the Threshold Quantity. To the extent the FRR Entity's allocated share of the Final Zonal Peak Load Forecast exceeds the FRR Entity's allocated share of the Preliminary Zonal Peak Load Forecast, such FRR Entity's FRR Capacity Plan shall be updated to designate additional Capacity Resources in an amount no less than the Forecast Pool Requirement times such increase; provided, however, any excess megawatts of Capacity Resources included in such FRR Entity's previously designated Threshold Quantity, if any, may be used to satisfy the capacity obligation for such increased load."

auction conducted before the RTO Realignment was announced. Section E.2 states:

An FRR Entity that designates Capacity Resources in its FRR Capacity Plan(s) for a Delivery Year based on the Threshold Quantity may offer to sell Capacity Resources in excess of that needed for the Threshold Quantity in any auction conducted under Attachment DD of the PJM Tariff for such Delivery Year, but may not offer to sell Capacity Resources in the auctions for any such Delivery Year in excess of an amount equal to the lesser of (a) 25% times the Unforced Capacity equivalent of the Installed Reserve Margin for such Delivery Year multiplied by the Preliminary Forecast Peak Load for which such FRR Entity is responsible under its FRR Capacity Plan(s) for such Delivery Year, or (b) 1300 MW.

DEO owns several peaking units within PJM, and these units have already been offered in to, and cleared, the auctions for Delivery Years 2011-2012, 2012-2013, and 2013-2014, with approximately 3000 MW cleared per Delivery Year. Accordingly, we are above the 25%/1300 MW threshold that would apply if we had been in PJM in an FRR plan when this generation was offered into the auction. We therefore request waiver to avoid violation of this provision.

DEO was not in PJM at the time the generation was offered in to the auction, nor had it even given its withdrawal notice to the Midwest ISO.⁸ Neither was any other Independent FRR Entity in the Duke Energy Zone that may have offered generation into RPM in a previous BRA. Because there was no FRR plan in existence or even proposed when such generation was offered in to prior auctions, no purpose would be served by counting such generation against the threshold. Grant of the requested waiver would mean that (a) neither DEO nor

⁸ DEO and DEK submitted written notice of their withdrawal to the Midwest ISO on May 20, 2010.

any Independent FRR Entity would be deemed to have exceeded the threshold requirement already, and (b) that uncommitted generation of DEO or an Independent FRR Entity in the Duke Energy Zone could be offered into incremental auctions for the Delivery Years in question, up to the threshold amount. As with all of the other waivers we have requested, this waiver would apply only to the 29 month period until the expiration of the Duke FRR Plan approved in the Realignment Order.

II. Paragraph 119 Compliance Requirements

119. American Municipal raised a number of questions and asked for assurances on certain issues from Duke. Based on the information posted on PJM's website pertaining to the September 17, 2010 stakeholder meeting, Duke answered some of the questions raised by American Municipal. For example, Duke explained that load serving entities serving wholesale load will be notified of their wholesale area capacity obligation by January 31, 2011. To complete the record, we will require Duke to file responses to address American Municipal's concerns in the above-ordered compliance filing. **Specifically, we will require Duke to: confirm the date by which wholesale load will be notified of their wholesale area obligations; clarify the deliverability status of existing resources that Midwest ISO has deemed "deliverable" and the date by which resources will be notified of their deliverability statuses; address the allocation of nonperformance penalties; and provide more information about the proposed agreement that opt-out entities will have to enter into with Duke Ohio reflecting the commitments and obligations of the opt-out provision.**⁹

A. Date by which wholesale load will be notified of their wholesale area capacity obligations

DEO confirms that it plans to notify wholesale load of their capacity obligations by January 31, 2011.

⁹ Realignment Order at P 119.

B. Clarification of the deliverability status of existing resources that Midwest ISO has deemed "deliverable" and the date by which resources will be notified of their deliverability statuses

PJM is conducting Generator Deliverability Testing. We are currently waiting for the results of this testing, which will cover generation in the Duke Energy Zone (Ohio and Kentucky) only. More rounds of deliverability studies will follow as well. We expect that the testing will be completed in time for us to provide feedback on deliverability status by February 15, 2011.

C. Allocation of nonperformance penalties

Per the RAA, an LSE with its own Independent FRR Plan will be responsible for its own non-performance penalties.¹⁰ An alternative retail LSE (referred to in Ohio as a Certified Retail Electric Supplier ("CRES")) participating in the Duke FRR Plan but choosing to opt out will also be responsible for its own non-performance penalties, up to the opt out amount.¹¹ Loads who participate in the Duke FRR Plan will not be responsible for providing capacity resources for load that is not opted out, and hence will not be subject to non-performance penalties with respect to that load.

D. LSE Opt-Out Agreements and LSE Capacity Payment Agreements

All LSEs in the Duke Energy Zone that do not enter into an Independent FRR Plan, including all CRESEs serving load within the Duke Energy Zone during any of the three Delivery Periods,¹² will be required to enter into a

¹⁰ Sections F.2 and G of Schedule 8.1 of the RAA.

¹¹ Section D.9 of Schedule 8.1 of the RAA.

¹² The Delivery Periods are January 1, 2012 – May 31, 2012, June 1, 2012 – May 31, 2013, and June 1, 2013 – May 31, 2014.

Capacity Payment Agreement. In addition, CRESEs serving load within the Duke Energy Zone during any of the three Delivery Periods, and electing to opt out of the Duke FRR Plan (each an "Opt-Out LSE") also must sign an LSE Opt-Out Agreement for that Delivery Period. Each CRES will be able to make opt-out elections separately for each Delivery Period. Any such election, for any of the three Delivery Periods, must be made by March 31, 2011.

Each applicable agreement must be entered into between the LSE and DEO by March 31, 2011. Both agreements are under development, but will be posted on the PJM website by the end of 2010, fully three months before any LSE will be required to make any elections or execute either agreement. While the contracts are under development and subject to change, the following discussion reflects our expectations as to the agreements.

Each LSE Opt-Out Agreement will reflect the commitments and provisions of Section D.9 of Schedule 8.1 of the RAA¹³ and set out the obligations of each Opt-Out LSE, as described in further detail below. The initial determination of each LSE's reliability obligation will be made by January 31, 2011, based on

¹³ Section D.9 of Schedule 8.1 to the RAA provides: "Notwithstanding the foregoing, in lieu of providing the compensation described above, such alternative retail LSE may, for any Delivery Year subsequent to those addressed in the FRR Entity's then-current FRR Capacity Plan, provide to the FRR Entity Capacity Resources sufficient to meet the capacity obligation described in paragraph D.2 for the switched load. Such Capacity Resources shall meet all requirements applicable to Capacity Resources pursuant to this Agreement and the PJM Operating Agreement, all requirements applicable to resources committed to an FRR Capacity Plan under this Agreement, and shall be committed to service to the switched load under the FRR Capacity Plan of such FRR Entity. The alternative retail LSE shall provide the FRR Entity all information needed to fulfill these requirements and permit the resource to be included in the FRR Capacity Plan. The alternative retail LSE, rather than the FRR Entity, shall be responsible for any performance charges or compliance penalties related to the performance of the resources committed by such LSE to the switched load. For any Delivery Year, or portion thereof, the foregoing obligations apply to the alternative retail LSE serving the load during such time period. PJM shall manage the transfer accounting associated with such compensation and shall administer the collection and payment of amounts pursuant to the compensation mechanism."

2010 load data. After the initial determination of each Opt-Out LSE's reliability obligation is made and each makes its declaration of its opt-out plans, the opt out amount cannot be increased or decreased, because after that point DEO will procure capacity to serve any load that is not opted out.

The obligations of each Opt-Out LSE will be included in each LSE Opt-Out Agreement. Each Opt-Out LSE will provide DEO with a resource plan setting forth its means to attain the capacity required to satisfy its Capacity Obligation (as determined by DEO and provided to the LSE by mid-January of 2011) during the applicable Delivery Period. The Opt-Out LSE must own or have the contractual authority to control the output or load reduction capability of the capacity resources listed in its resource plan. The Opt-Out LSE must commit such capacity resources exclusively to DEO during the applicable Delivery Period.

The Opt-Out LSEs, along with all other LSEs that do not select an Independent FRR Option (each a "Participating LSE") must sign a Capacity Payment Agreement with DEO by March 31, 2011, for each Delivery Period. Under each Capacity Payment Agreement, DEO must procure and manage the capacity necessary to meet each Participating LSE's capacity obligations—including, for Opt-Out LSEs, that portion of these LSEs' capacity obligations that was not opted out—during the Delivery Period, and each Participating LSE will pay DEO to procure and manage that capacity during the applicable Delivery Period. Specifically, for load that is not opted out, the Participating LSE must pay DEO an amount equal to its daily unforced capacity obligation in megawatts

multiplied by the PJM Final Zonal Capacity Price for unforced capacity in the unconstrained region.

Opt-Out LSEs will be directly responsible to PJM for any performance penalties associated with the opt-out amount, and so will be responsible to PJM directly for any credit requirements associated with that amount. Each Opt-Out LSE or Participating LSE must also maintain typical credit ratings or provide a guarantee to DEO with respect to non-opted out amounts.¹⁴ If an Opt-Out LSE or Participating LSE is unable to meet the credit requirement, it must provide performance assurance in the amount of \$14,500¹⁵ per MW of that portion of its capacity obligation beyond the portion of the obligation that was opted-out.¹⁶

Both the LSE Opt-Out Agreements and the Capacity Payment Agreements will require that the Opt-Out LSE or the Participating LSE, as applicable, be a member of PJM and be bound by PJM operating instructions, policies, and procedures during the applicable Delivery Period. Both agreements will also require the Opt-Out LSE or the Participating LSE to maintain throughout the applicable Delivery Period all regulatory authorizations necessary to perform its obligations, and to cooperate in good faith with DEO in any related regulatory compliance efforts.

¹⁴ Wholesale customers that enter into Independent FRR Plans with PJM have no credit obligations to Duke and are only subject to PJM credit requirements.

¹⁵ This amount is not yet finalized.

¹⁶ Specifically, an Opt-Out LSE must provide performance assurance in the amount of \$14,500 per MW of the portion of its capacity obligation beyond that which it opts-out, which capacity obligation is the initial capacity obligation based on load being served by the Opt-Out LSE as of December 31, 2010.

To the extent necessary, these contracts will be entered into pursuant to an appropriate market-based rate or other Commission authorization, and will be reflected in EQR filings. DEO will post these agreements to the FAQ section of the PJM web site regarding the RTO move by the end of 2010. This timing will provide LSEs three months to evaluate whether to elect to participate in the Duke FRR Plan or otherwise. DEO notes that during the proceeding involving FirstEnergy's move from the Midwest ISO to PJM, LSEs had approximately two weeks between the time they received their respective capacity obligations, instructions about the process to opt out of FirstEnergy's FRR plan, and opt out and capacity payment agreements, and the deadline for those LSEs to make a determination whether to opt-out of FirstEnergy's FRR Plan.¹⁷

CONCLUSION

In light of the foregoing, DEO and DEK respectfully request that the Commission accept this Compliance Filing and grant their requests for waiver of Sections D.4, D.2, and E.2 of PJM's RAA.

¹⁷ Compliance Filing of American Transmission Systems, Inc., submitted January 15, 2010, in Docket No. ER09-1589-000, accepted for filing by Letter Order issued March 12, 2010, in Docket No. ER09-1589-002 (in response to directive of the Commission's Order Addressing Realignment Request and Complaint that the ATSI Utilities address the means by which ATSI-Zone LSEs will be able to determine their respective capacity obligations for the relevant Delivery Years before the opt-out deadline of January 31, 2010, ATSI responded that on January 14, 2010, it sent letters to each affected wholesale LSE in the ATSI Zone containing that LSE's capacity obligation for the relevant delivery years, as well as instructions about the process and applicable deadlines by which the LSE could opt out of ATSI's capacity procurement process); *see also* <http://pjm.com/markets-and-operations/market-integration/atsi.aspx> (on January 15, 2010, the Opt-Out LSE Agreement and Capacity Payment Agreement for Certain ATSI Zone LSEs were posted to the PJM web site page dedicated to the FirstEnergy RTO transition).

Respectfully Submitted,

/s/ Noel Symons

James B. Gainer
Vice President
Federal Regulatory Policy
Duke Energy Corporation
526 South Church Street
P.O. Box 1006
Charlotte, NC 28202
(704) 382-5618
james.gainer@duke-energy.com

Noel Symons
Andrea R. Kells
Caroline A. Harmon
McGuireWoods LLP
Washington Square
1050 Connecticut Avenue, NW
Suite 1200
Washington, D.C. 20036
(202) 857-2929

nsymons@mcguirewoods.com

*Counsel for Duke Energy Ohio, Inc. and
Duke Energy Kentucky, Inc.*

Jeffrey M. Trepel
Associate General Counsel
Duke Energy Corporation
EC03T
526 South Church Street
Charlotte, NC 28202
(704) 382-8131
Jeffrey.trepel@duke-energy.com

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