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**BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO**

In the Matter of the Application of Duke Energy)
Ohio, Inc. for Approval of a Market Rate Offer)
to Conduct a Competitive Bidding Process for)
Standard Service Offer Electric Generation)
Supply, Accounting Modifications, and Tariffs)
for Generation Service.)

Case No. 10-2586-EL-SSO

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**OHIO PARTNERS FOR AFFORDABLE ENERGY'S
REPLY BRIEF**

Introduction

Ohio Partners for Affordable Energy ("OPAE") hereby submits its reply brief to the Public Utilities Commission of Ohio ("Commission") in this proceeding to consider the application of Duke Energy Ohio, Inc., ("Duke"), an Ohio electric distribution utility, for approval of a market rate offer ("MRO") and a competitive bidding process ("CBP") for standard service offer ("SSO") electric generation supplies. Herein, OPAE replies to Duke's initial brief.

A. Duke's MRO application should be rejected because it denies Duke's customers the protections set forth in Revised Code Sections 4928.142(D) and (E).

R.C. §4928.142(D) requires a transition from the existing SSO price of a utility's electric security plan ("ESP") to full market based pricing over a minimum of five years for an electric distribution utility that owned generating resources as of July 31, 2008 that had been used and useful, which includes Duke. R.C. §4928.142(D) requires that a portion of the utility's SSO load for the first five years of the MRO be competitively bid under R.C. §4928.142(A) as follows: 10% in year one, not less than 20% in year two, 30% in year three, 40% in year four, and 50% in year five. Thus, there is a minimum five-year transition period before implementing 100% market rates. R.C. §4928.142(E) provides the Commission

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with the ability to alter prospectively the blending proportions specified in R.C. §4928.142(D) and to extend the time of the blending period so that it can last as long as ten years. Under R.C. §4928.142(E), beginning in the second year of a blended price, the Commission may alter prospectively the blending proportions to mitigate any effect of an abrupt or significant change in the SSO price. Any such alteration shall be made not more often than annually. The Commission will evaluate the potential rate impact on customers annually beginning in the second year of the blending period. If market rates cause an abrupt or significant change in the MRO SSO price, the Commission may alter the blending period, including extending the blending period for an additional five years.

Duke's initial brief quotes Revised Code Sections 4928.142(D) and (E) and offers Duke's unique perspective on the legislative intent and meaning of these statutes. The crux of Duke's argument is simple: R.C. §4928.142(E) does not state how long before the second year alterations to the blending percentages may be made. Duke Brief at 25. Therefore, because the statute does not explicitly state how long before the second year alternations may be made, Duke argues that the Commission may alter **now** the blending percentages that are applicable in year three and beyond. Duke requests that the Commission find **now** that the blending period will terminate in 29 months, moving to a 100% market rate beginning June 1, 2014. In short, according to Duke, the Commission may alter the blending periods before the MRO has even begun.

Contrary to Duke's interpretation, the statute requires that the Commission make a determination to alter the proportions based on actual circumstances that exist at some future time. Staff Exhibit ("Ex.") 2 at 3-4. There is no validity to Duke's argument that the Commission is free to alter the blending period

percentages now without any reference to or knowledge of abrupt or significant changes in the SSO price during any of the ten years of blending periods. Therefore, the Commission should reject the notion that the statutory blending periods can be altered in this proceeding before the MRO has even begun.

Duke states that if the market price in year three is less than the most recent ESP/SSO price, altering the blend to enable full market prices at that time allows the Commission to provide Duke's customers with lower rates. Duke claims that under its MRO ratepayers would be paying the lowest possible rates if the market price is less than the most recent ESP/SSO price and would be paying market price "as intended by the legislature." Duke Brief at 29. However, in reality, the statute does not show that the legislature intended that ratepayers would have no option beyond market-based rates. The statute demonstrates precisely the opposite. After the legislature enacted SB 3 in 1999, ratepayers had the option to take power from a competitive retail electric service ("CRES") provider and thereby pay full market-based rates. This option, of course, still exists. There was no reason to enact the new legislation of SB 221 if the legislature merely intended that ratepayers pay full market-based rates. R.C. 4928.142(D) and (E) demonstrate that the legislature intends to protect customers from full market-based rates when warranted. That is what the statutes do.

Duke's proposal to have the Commission make a determination now that the blending period will terminate after only 29 months transfers substantial risk to retail customers. The blending provisions of R.C. §4928.142(D) allow for a sharing of risk between Duke and its customers. By shortening the blending period to a mere 29 months, market risk is shifted to customers who would no longer have the legacy ESP/SSO price options in years three through ten as the

statutes contemplate. Again, it makes no sense for the Commission to approve Duke's MRO as filed and thereby deny customers the protections of R.C. §§4928.142(D) and (E). Duke states that SB 221 "was not designed as consumer protection legislation" but contrary to Duke's belief, SB 221 does protect consumers. Duke Brief at 29. Consumer protection is the purpose of R.C. Sections 4928.142(D) and (E).

It is the policy of the state of Ohio to ensure reasonably priced retail electric service. R.C. Section 4928.02(A). It is also the policy of the state of Ohio to protect at-risk populations. R.C. Section 4928.02(L). The purpose of R.C. Sections 4928.142(D) and (E) is to provide for market-based rates to be blended with existing ESP/SSO rates for a period of up to ten years in order to protect consumers from abrupt and significant market price increases. While there has been some shopping by residential customers in Duke's service territory, there has certainly not been enough shopping to place great confidence in residential customer interest in the competitive retail market nor interest among marketers in serving the residential market. In terms of load, only 29% of residential load has switched; in terms of accounts by customer class, only 26% of residential accounts have switched to CRES providers. Duke Ex. 2 at 8. This low level of shopping has persisted even when Duke's ESP/SSO price is higher than market. Under these circumstances, it is likely that most residential customers will still be served by Duke's SSO in 2014 and beyond. It makes no sense for the Commission to deny these customers the consumer protection of the blended ESP/SSO price as set forth in Revised Code Sections 4928.142(D) and (E) for the maximum time period allowed by the statutes, i.e., ten years.

Thus, Duke's application does not provide for the level of consumer protection required in R.C. Sections 4928.142(D) and (E), which require at least

five years of blending of competitively bid generation pricing with adjusted pre-existing SSO rates and the potential for an additional five years after the initial minimum five years. The Commission should reject Duke's request to have the Commission determine now a blending period of only 29 months. The full five-year minimum blending period consistent with R.C. §4928.142(D) should be required. Moreover, the Commission should establish annual reviews of current market rates and the impact on the blended MRO SSO rate. If the Commission determines that an abrupt or significant change in SSO rates may result, it should make appropriate changes in the blending proportions and evaluate whether an extension of the blending period up to ten years is appropriate.

B. There is no evidentiary basis upon which the Commission could alter the blending period in this proceeding.

Duke asks under what circumstances the Commission is permitted to alter the blending percentages. Duke Brief at 27. The statute states that the Commission can take such action to mitigate any effect of an abrupt or significant change in the utility's standard service offer price. According to Duke, the legislature based the requirement for a blending period on the assumption that market prices and previous ESP/SSO prices would be substantially divergent. Duke Brief at 28. According to Duke, the lengthy blending requirement would otherwise have a negligible effect and would not have been of concern to the legislators. *Id.*

Duke then asserts that the "evidence" confirms that, in the third year of Duke's proposed MRO, the market price and the most recent ESP/SSO price will converge or the market price will be lower than the most recent ESP/SSO price. Duke Brief at 28. In short, Duke argues that there will be no reason in 2014 for blending market prices with the current ESP/SSO price, because the two blended

prices will essentially be the same or the market price will be lower than the blended price.

There is no evidence to support Duke's position on future market prices. Duke presents a projection of anticipated electricity market pricing to show "convergence" of market pricing with existing ESP/SSO rates. Duke presented the testimony of Judah Rose who claimed that projected ESP/SSO rates and projected market rates will be equal by 2014 when Duke's proposed transition period terminates. According to Duke, when Duke's 29-month transition period ends May 31, 2014, there will be no difference between the ESP/SSO rates and market rates so that the blending would result in the same rates as 100% market rates.

Of course, this projection for the 2014 market price from Mr. Rose is merely a projection, nothing more. Presented by Duke, the projection serves Duke's case and has even less validity than a projection from a non-biased source. If Mr. Rose's projection is wrong, market rates could substantially exceed the blended ESP/SSO rates. In that case, Duke's revenues would be higher as a result of the shortened blending period.

Moreover, there is good reason to believe that Mr. Rose is wrong about the "convergence" of market prices and the ESP/SSO rates. The record amply demonstrates that Mr. Rose's theory of convergence has no validity. First, Mr. Rose has no forecast after 2014. Transcript ("Tr.") I at 125. He is merely claiming that there will be convergence in 2014. After 2014, the market price could continue to increase over the ESP/SSO price. Tr. I at 126. Mr. Rose agreed that if there is convergence in 2014, it is reasonable to expect that the prices would change over time. He admits that trends are causing prices to

increase over time and that prices could continue to do so after 2014. Tr. I at 140.

Mr. Rose made forecasts for the pricing period 2007-2008 prior to that period, just as his forecast for 2014 was made three years before 2014. His forecast for the 2007-2008 period did not take into account the global recession and its effect on energy prices. Tr. I at 131. The current lower prices in the market right now are not something that Mr. Rose anticipated. Tr. I at 131. Mr. Rose also made a forecast in 2008 for prices in 2009, 2010 and 2011 in Duke's SSO case, Case No. 08-920-EL-SSO. In that case, he did the same analysis using basically the same sources as he did for this proceeding. Tr. I at 149. His conclusion in Case No. 08-920 was that in 2011 the competitive market price option would be higher than Duke's ESP/SSO price. Tr. I at 149-150. Mr. Rose was wrong and his forecast was "exactly the opposite" of what actually happened. Tr. I at 150. Mr. Rose agreed that the future is uncertain. Tr. I at 132. On the other hand, he testified that under the statute, if the Commission approves a 100% market rate for 2014 in this proceeding now, the Commission cannot go back and rectify a bad decision. The Commission's decision would be irrevocable. Tr. I at 152. Mr. Rose would ask the Commission to make this irrevocable decision even though his previous forecasts were wrong and he agreed that there is no certainty about what is going to happen. Tr. I at 154.

If anything, current trends are that the market price will increase substantially above the ESP/SSO price. There would have to be substantial increases in market prices through 2014 to close the current gap between market prices and the Duke ESP/SSO rates by May 2014. If market prices increase substantially up to 2014, there is reason to believe that market prices could further accelerate beyond the ESP/SSO rates in 2015 and 2016. If market rates

increase beyond the ESP/SSO rates in 2015 and 2016, then customers will need the protections of the minimum five year blend set forth in R.C. §4928.142(D) at precisely the same time that Duke proposes to deny customers the protections provided under the law. Ohio Energy Group ("OEG") Exhibit ("Ex.") 1 at 8. Under the circumstances, it makes no sense for the Commission to approve the Duke application.

Duke claims that there is no "evidence" to suggest that market prices will exceed the most recent ESP/SSO price in 2012, 2013, or 2014. Duke Brief at 28. According to Duke, no party offered any "evidence" to suggest that market prices would exceed the most recent ESP/SSO price in 2015 and beyond. *Id.* There is no dispute about that. No one is offering "evidence" in this proceeding about market prices in 2015 and beyond. It would be nothing but a projection, a speculation, and almost certainly, as with Mr. Rose's previous forecast, wrong. Under SB 221, the determination to alter the blending proportions is to be made based on the actual circumstances that exist in the future years of the MRO. As Staff witness Strom noted, any forecast is subject to error and using a forecast to make a current determination to alter the percentages to be used several years in the future is not in compliance with the statute. Staff Ex. 2 at 3-4. Given the lack of any evidence to support Duke's proposal, the Commission must not make an irrevocable decision in this case to deny customers the protections set forth in SB 221.

C. The Commission should reject Duke's proposal to transfer its generation assets to an affiliate to the extent that such a transfer will frustrate the consumer protections provided by R.C. Sections 4928.142(D) and (E).

Duke is proposing to transfer its legacy generation assets to an affiliate on or before May 31, 2014. According to Duke witness Wathen, the blended rate

after the asset transfer would be comprised of a weighted average of the price of power under the purchased power agreement and a market rate. Since both would be priced at market, Duke argues that once the generation assets have been transferred, there would be no need for any blending of the ESP/SSO and market rates. This is why Duke seeks to end the blending period in 29 months, or on May 31, 2014.

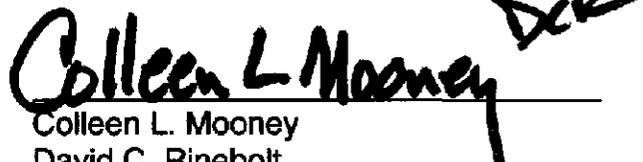
SB 221 mandates a different approach. In order to effectuate the consumer protections of the legislation, the generation assets must be retained as long as necessary to accommodate the blending of the ESP SSO rates with market rates. These are the consumer protections set forth at Revised Code Sections 4928.142(D) and (E) as discussed above. Thus, it would be logical for the Commission to deny the generation asset transfer during the transition periods set forth in R.C. §§4928.142(D) and (E). Otherwise, Duke's customers would not have access to ESP/SSO generation at legacy pricing as required by the blending periods set forth in the statute. The statute provides for a five to ten year transition period before full market pricing is in effect for those who do not shop. To allow the asset transfer to take place before the end of the transition period would deny customers the statutory protections. OEG Ex. 1 at 10. The Commission should make no orders that deny these consumer protections set forth in R.C. §4928.142(D) and (E).

Conclusion

Duke's application does not provide for the consumer protection required in R.C. Sections 4928.142(D) and (E), which mandate at least five years of blending of competitively bid generation pricing with adjusted pre-existing SSO rates and the potential for an additional five years after the initial minimum five

years. The Commission should reject Duke's request to have the Commission determine immediately a blending period of only 29 months. The full five-year minimum blending period consistent with R.C. §4928.142(D) should be required. Moreover, the Commission should establish annual reviews of current market rates and the impact on the blended MRO SSO rate. If the Commission determines that an abrupt or significant change in SSO rates may result, it should make appropriate changes in the blending proportions and evaluate whether an extension of the blending period for up to ten years is appropriate. The Commission should also deny the generation asset transfer during the transition periods set forth in R.C. §§4928.142(D) and (E). The Commission should adopt the recommendations of Staff witness Strom with respect to the CBP. The Commission should also adopt the recommendations of Staff witness Turkenton with respect to the various riders proposed by Duke.

Respectfully submitted,

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CERTIFICATE OF SERVICE

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