BEFORE

THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Authority to Establish a Standard Service Offer Pursuant to §4928.143, Ohio Rev. Code, in the Form of an Electric Security Plan.	)))))	Case No. 11-346-EL-SSO Case No. 11-348-EL-SSO
In the Matter of the Application of Columbus Southern Power Company and Ohio Power Company for Approval of Certain Accounting Authority.	))))	Case No. 11-349-EL-AAM Case No. 11-350-EL-AAM

REPLY BRIEF
BY
DUKE ENERGY COMMERCIAL ASSET MANAGEMENT, INC.
AND
DUKE ENERGY RETAIL SALES, LLC

Ohio Power Company (OP), in its brief in these proceedings, persists in its fallacious assertions that the Public Utilities Commission of Ohio (Commission) must seek "balance" in its consideration of an Electric Security Plan (ESP) under R.C. 4928.143. And it continues to err in its application of the legally mandated ESP test, especially in light of the newly established state capacity mechanism for Fixed Resource Requirement (FRR) entities.

The Commission's recently issued order establishing a state capacity pricing mechanism reinforces the need to reject the application in these proceedings, as it is now impossible for OP's proposal to meet the legal requirements for an ESP. Although Duke Energy Commercial Asset Management, Inc. (DECAM), and Duke Energy Retail Sales, LLC (DER), believe that numerous aspects of OP's proposed ESP are illegal or inappropriate, this reply brief will be limited to the

most important issues of (1) the legal standards for adoption of an ESP, (2) the proper comparison of the proposed ESP to an MRO, and (3) the illegality of the proposed Retail Stability Rider (RSR).

Legal Standards for Adoption of an ESP

OP correctly points to statutory provisions governing the Commission's consideration of an ESP. As OP states, an ESP must be found, by the Commission, to be better in the aggregate than a plan based on a Market Rate Offer (MRO). OP is also correct in noting that it ultimately may choose to accept or reject modifications made by the Commission.[1]

Unfortunately, following this accurate description of governing law, OP then attempts to argue for the adoption of various aspects of its proposal, applying entirely different standards, not based on any statutory provisions. Looking at the proposal overall, OP contends that the Commission should approve its plan on the grounds that the plan is "balanced," "reasonable," and "lawful." While it DER and DECAM do not dispute that the plan must be "lawful," nothing in Chapter 4928 of the Revised Code requires it to be "balanced." And the plan is only "lawful" if the charges it would impose cover nothing more than those items enumerated under R.C. 4928.143.[2]

OP seeks approval of this plan on the basis that the various provisions are either "reasonable" or "balanced." For example, OP argues that the RSR should be approved because it provides "financial stability" in exchange for "rate stability" and "other benefits."[3] The biggest "benefit" pointed to by OP is what it deems to be "highly discounted capacity pricing."[4] As will be discussed below, the Commission's recent order establishing a state capacity pricing

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[1] OP Initial Post-Hearing Brief at 24-25.
[2] *In re Application of Columbus S. Power Co.*, 128 Ohio St.3d 512, 2011-Ohio-1788, at ¶¶ 32-35.
[3] OP Initial Post-Hearing Brief at 36.
[4] OP Initial Post-Hearing Brief at 34 (citing testimony of Witness Dias).

mechanism entirely negates this alleged benefit. Even if the cited rate stability and benefits were legitimately present in this proposal, which they are not, R.C. 4928.143 does not allow adoption of an ESP on the basis of such an exchange.

It is critically important to recognize that nothing in R.C. 4928.143 would allow imposition of the proposed RSR, a rider that would seek to guarantee OP's non-fuel generation revenues. Such a guarantee is not part of the legislative approach to competition in the supply of generation services and undeniably results in this plan not being "lawful."

Proper Comparison of the Proposed ESP to an MRO

As the Commission is fully aware, Ohio law requires comparison of a proposed ESP to the expected results under an MRO.[5] OP's effort at a comparison fails, however, in one critically important way: OP calculates that its proposal provides a benefit quantifiable at almost a billion dollars on the premise that the capacity prices it proposes to charge to competitive retail electric service (CRES) providers are "discounted" as compared with the cost-based rates that it thinks it has the right to charge. This calculation is flawed, under any theory that might reasonably apply.

The Commission has recently issued its order establishing a state capacity pricing mechanism applicable to FRR entities.[6] Finding jurisdiction under its general supervisory powers, entirely separate from Chapter 4928 that governs competitive services and ESPs, the Commission based its decision on capacity for CRES providers being a regulated service rather than a competitive service. The order provides that FRR entities, such as OP, are allowed to recover their embedded cost of capacity, although the price to be actually charged by OP to CRES providers is set at the final zonal capacity price in the unconstrained territory of PJM

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[5] R.C. 4928.143(C)(1).

[6] As argued in their initial brief in this proceeding, DER and DECAM maintain that an FRR entity's capacity charges to CRES providers should be at auction-based rates.

Interconnection, LLC (PJM). The difference between the charge and the cost, according to the Commission's order in that proceeding, will be addressed in OP's ESP.

This new state capacity pricing mechanism directly impacts the calculation of whether an ESP is better than an MRO. There are several approaches that might be taken. First, and most appropriately, in light of the Commission's conclusion that capacity services provided for the benefit of shopping customers and their CRES suppliers are not competitive services, the charges for such services should be eliminated from the MRO comparison test. If the provision of capacity is not a competitive service, then it is outside the bounds of R.C. 4928.142 and 4928.143.

Without the inclusion of the capacity pricing "benefit," the MRO test fails. OP's testimony indicated that the ESP pricing, as compared to anticipated MRO pricing, was a benefit worth approximately $256 million. The RSR, on the other hand, was described as having a "benefit" worth approximately a negative $284 million. The capacity "benefit" – now irrelevant to the calculation – was valued at about $989 million, resulting in an aggregate "benefit" of about $961 million. Simply using OP's figures and deleting the capacity from the calculation leaves a net detriment from the OP ESP proposal, as compared to an MRO, of approximately $28 million. The proposal fails the test and therefore must be rejected.

The second possible approach would be to include the capacity charge in the test, even though it is now declared to be a noncompetitive service. Under this approach, the Commission-allowed charge for capacity would be included, whether the standard service offer takes the form of an ESP or an MRO, since the capacity charges are mandated by the Commission under its establishment of the state capacity mechanism. OP's proposed ESP would offer no advantage to any customers beyond the mandate of that mechanism. This results, by definition, in there being

absolutely no advantage to the ESP on the basis of capacity pricing. Thus, again the alleged billion dollar "benefit" of "discounted" capacity does not help OP in the comparison of the proposal to the expected outcome under an MRO.

Illegality of the RSR

As noted above, an ESP may only include items that are enumerated in the governing statute. The RSR is not such an item and, thus, must be rejected. OP attempts to justify the charge, arguing that the RSR's purpose is to protect the financial integrity of OP.[7] OP, similarly, describes the RSR as being "tied to the total ESP package." But protection of a utility's finances and support of package deals are not included within any of the subsections of R.C. 4928.143. The section simply does not allow for such a provision.

OP also tries to argue that the RSR is a decoupling mechanism of some sort. While decoupling mechanisms are allowed under R.C. 4928.143, the true nature of the RSR is not that of decoupling. Rather, the RSR merely guarantees a particular dollar level of nonfuel generation revenues. The RSR is more akin to a make-whole payment than it is to traditional decoupling. OP's self-serving nomenclature should not be considered.

The RSR must be rejected.

Conclusion

DER and DECAM respectfully urge the Commission to conclude that the ESP, as proposed, must be entirely rejected as not passing the statutorily required test. Alternatively, the proposal must be substantially modified, as discussed in the initial brief filed by DER and DECAM. Critical in such modifications is the outright rejection of the proposed RSR.

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[7] OP Initial Post-Hearing Brief at 34.

Respectfully submitted,

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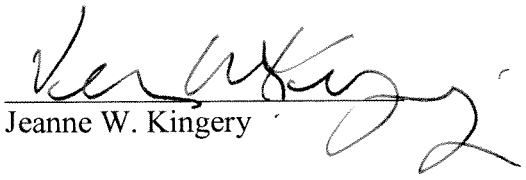

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