

**BEFORE  
THE PUBLIC UTILITIES COMMISSION OF OHIO**

In the Matter of the Application of The       )  
Dayton Power and Light Company to       ) Case No. 12-2881-EL-FAC  
Establish a Fuel Rider.                       )

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**POST-HEARING BRIEF  
BY  
THE OFFICE OF THE OHIO CONSUMERS' COUNSEL  
(\*\*\*\*\*PUBLIC VERSION\*\*\*\*\*)**

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BRUCE J. WESTON  
OHIO CONSUMERS' COUNSEL

Kyle L. Kern  
Assistant Consumers' Counsel  
**Office of the Ohio Consumers' Counsel**  
10 West Broad Street, Suite 1800  
Columbus, Ohio 43215-3485  
Telephone: (614) 466-9585  
[kyle.kern@occ.ohio.gov](mailto:kyle.kern@occ.ohio.gov)

March 3, 2014

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**I. INTRODUCTION**

In this proceeding, the Public Utilities Commission of Ohio (“PUCO” or “Commission”) must determine whether the costs paid by The Dayton Power & Light Company’s (“DP&L” or the “Utility”) Standard Service Offer (“SSO”) customers for fuel for 2012 were prudently incurred.<sup>1</sup> Ohio law protects customers from paying costs that DP&L fails to show were prudent.<sup>2</sup>

On October 10, 2008, DP&L filed an application for a SSO in the form of an electric security plan (“ESP”) (Case No. 08-1094-EL-SSO), pursuant to R.C. 4928.143. The DP&L ESP proceeding was resolved through a Stipulation approved by the PUCO on June 24, 2009. That PUCO Order allowed DP&L to implement a by-passable fuel rider to collect prudently incurred fuel and purchased power costs from customers,<sup>3</sup> consistent with provisions of Senate Bill 221.<sup>4</sup>

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<sup>1</sup> *In the Matter of the Application of the Dayton Power and Light Company To Establish a Fuel Rider*, Case No. 12-2881-EL-FAC, 2012 Audit Report at 1-2 (June 14, 2013) (hereinafter “2012 Audit Report”).

<sup>2</sup> R.C. 4928.143(B)(2)(a).

<sup>3</sup> *In the Matter of the Application of The Dayton Power and Light Company for Approval of Its Electric Security Plan, et al.*, Case No. 08-1094-EL-SSO, Opinion and Order at 4 and 13 (June 24, 2009).

<sup>4</sup> See R.C. R.C. 4928.143(B)(2)(a).

DP&L subsequently filed an application to establish a Fuel Rider in Case No. 09-1012-EL-FAC. In that case, the PUCO selected Energy Ventures Analysis, Inc. (“EVA”) and its subcontractor, Larkin & Associates PLLC (“Larkin”) to perform management/performance and financial audits regarding DP&L’s fuel procurement practices for 2010.<sup>5</sup> The PUCO selected EVA and Larkin to audit DP&L’s fuel procurement practices for 2011 in Case No. 11-5730-EL-FAC. The 2010 and 2011 DP&L Fuel Rider cases resulted in PUCO-approved Stipulations.<sup>6</sup>

This proceeding pertains to the management/ performance and financial audit of DP&L’s 2012 fuel purchases (“2012 Audit”) by EVA and Larkin (“collectively, “Auditors”). The Auditors identified a number of issues with the Utility’s Fuel Rider for 2012, and the amounts DP&L’s SSO customers were ultimately charged.<sup>7</sup> In this regard, the Auditors recommend a total disallowance of \$4.8 million<sup>8</sup> from the Utility’s Fuel Rider for 2012 fuel charges paid by DP&L’s SSO customers.

An evidentiary hearing took place in December of 2013. The evidence supports that Auditors’ recommendations.

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<sup>5</sup> See *In the Matter of the Application of the Dayton Power and Light Company To Establish a Fuel Rider*, Case No. 09-1012-EL-FAC, Entry at 2 (November 10, 2010), OCC Exhibit 2.

<sup>6</sup> See Case No. 09-1012-EL-FAC, Opinion and Order (November 9, 2011), and 11-5730-EL-FAC, Opinion and Order (January 23, 2013).

<sup>7</sup> 2012 Audit Report at 1-16.

<sup>8</sup> Management Disallowance 1 was for \$3.4 million dollars (see Case No. 12-2881-EL-FAC, Transcript Volume II at 329 (Smith)) and Management Disallowance No. 2 totaled \$1.4 million dollars (see Case No. 12-2881-EL-FAC, Transcript Volume II at 299-300 (Smith)) for a total of \$4.8 million.

The OCC submits this post-hearing brief<sup>9</sup> on behalf of the DP&L's approximately 374,000 residential customers. In accordance with the Auditors' findings, the PUCO should order DP&L to credit the Fuel Rider in the amount of \$4.8 million for trading and optimization activities that were not prudent and for failing to properly implement the least cost methodology for the benefit of SSO customers.

## **II. STANDARD OF REVIEW AND BURDEN OF PROOF**

The standard of review in this case is set forth in R. C. 4928.143(B)(2)(a), which provides that the PUCO may authorize an electric distribution utility to collect from customers the utility's prudently incurred cost of fuel used in the generation of electricity.<sup>10</sup> In addition, R.C. 4928.02 mandates that the PUCO should ensure that the cost of electric service for DP&L's customers is reasonable. Within the environment of competitive retail electric service, the PUCO's authorization of the collection of DP&L's prudently incurred and actual fuel costs must be consistent with the state policy enumerated in R.C. 4928.02.

The burden of proof in this case is set forth in R.C. 4928.143(C)(1), which provides that the burden of proof in an ESP proceeding shall be on the electric utility.<sup>11</sup> Because the origin of this case is DP&L's ESP case, the burden of proof remains with the

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<sup>9</sup> The January 29, 2014 Entry in this proceeding set February 28, 2014 as the deadline for Initial Briefs, and March 14, 2014, as the deadline for Reply Briefs (see Entry at 2). But the PUCO's offices were closed on February 28, 2014 due to a power outage. Per Ohio Adm. Code 4901-1-7(D), "[i]f the commission office is closed to the public for the entire day that constitutes the last day for doing an act or closes before its usual closing time on that day, the act may be performed on the next succeeding day that is not a Saturday, Sunday, or legal holiday." Accordingly, Initial Briefs are due on March 3, 2014 (see March 3, 2014 Entry in PUCO Case No. 14-038-AU-UNC at ¶ 5).

<sup>10</sup> R.C. 4928.143(B)(2)(a).

<sup>11</sup> R.C. 4928.143(C)(1).

electric utility. Thus, DP&L bears the burden of proving that the fuel costs it collected from customers are prudently incurred and reasonable.

The PUCO's rules give even further guidance on the burden that DP&L must meet in order to charge its customers for fuel. Specifically, the Ohio Adm. Code mandates that:

Each electric utility for which the commission has approved an electric security plan (ESP) which includes automatic adjustments under division (B)(2)(a) of section 4928.143 of the Revised Code shall file for such adjustments in accordance with the provisions of this rule.<sup>12</sup>

\* \* \*

On an annual basis, the prudence of the costs incurred and recovered through quarterly adjustments shall be reviewed in a separate proceeding outside of the automatic recovery provision of the electric utility's ESP. **The electric utility shall demonstrate that the costs were prudently incurred as required under division (B)(2)(a) of section 4928.143 of the Revised Code** and, if a significant change in costs has incurred, include an analysis comparing the electric utility's resource and/or environmental compliance strategy with supply and demand-side alternatives.<sup>13</sup> (Emphasis added)

Ohio law and the PUCO's rules (discussed above) both mandate that the burden of proof for automatically recoverable costs, such as fuel costs, is on the utility. And only those costs that are proven (by the utility) to be prudently incurred and reasonable may be collected from customers.

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<sup>12</sup> Ohio Adm. Code 4901:1-35-09(A).

<sup>13</sup> Ohio Adm. Code 4901:1-35-09(C). (Emphasis added).

### III. LAW AND ARGUMENT

#### A. DP&L's SSO Customers Should Not Have Paid \$4.8 Million Of DP&L's Charges To The 2012 Fuel Rider.

The Auditors supported a number of adjustments to DP&L's Fuel Rider that either partially adjusted or totally removed several of DP&L's optimization transactions<sup>14</sup> for 2012.<sup>15</sup> To this end, the Auditors made two disallowance recommendations. Management Disallowance No. 1 was for \$3.4 million dollars,<sup>16</sup> and Management Disallowance No. 2 totaled \$1.4 million dollars.<sup>17</sup> These disallowance recommendations encompass both adjustments for optimizations claimed by the Utility, and an adjustment based on the Utility's imprudent management decision.<sup>18</sup> The PUCO should order DP&L to credit the Fuel Rider for these imprudent costs that SSO customers should not pay.<sup>19</sup>

Specifically, DP&L reported thirteen optimization transactions for 2012 (labeled by the Auditors as optimizations A through M).<sup>20</sup> From these optimizations, DP&L charged customers approximately \$■ million through the Fuel Rider.<sup>21</sup> But the Auditors recommend, and the evidence supports, a total or partial disallowance of costs

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<sup>14</sup> "Optimizations" are transactions where the Utility improves upon an existing coal position by selling the coal and replacing it with a lower priced coal. See Direct Testimony of DP&L witness Aaron Cooper at 3 (October 31, 2013).

<sup>15</sup> *In the Matter of the Application of The Dayton Power and Light Company to Establish a Fuel Rider*, Case No. 12-2881-EL-FAC, Audit Report at 6-87 (June 14, 2013) (hereinafter, "2012 Audit Report").

<sup>16</sup> *In the Matter of the Application of The Dayton Power and Light Company to Establish a Fuel Rider*, Case No. 12-2881-EL-FAC, Transcript Volume II at 329 (Smith) (January 28, 2014).

<sup>17</sup> Id. at 299-300 (Smith).

<sup>18</sup> 2012 Audit Report at 1-16.

<sup>19</sup> In the 2011 Fuel Audit proceeding (11-5730-EL-FAC) the signatory parties explicitly reserved the right to challenge the calculations of any optimizations for coal deliveries in 2012, regardless of the execution date of the optimization transactions. See Direct Testimony of David Crusey at DJC-2 (Stipulation and Recommendation from 11-5730-EL-FAC) at 8.

<sup>20</sup> Id. at 4-1.

<sup>21</sup> Id. at 1-16. The \$■ million is prior to adjustments for DPLER (DPLER or DPL Energy Resources is a retail electric service provider) customers.



in regard to many of the thirteen optimizations DP&L claimed for 2012.<sup>22</sup> The table below summarizes the Auditors' reasons for the recommended disallowances of certain 2012 optimizations claimed by the Utility and the corresponding amounts.

Optimization <sup>23</sup>	Auditors' Reasons for Recommended Disallowance	Amount
Optimization A	The transaction took place before DP&L's Fuel Rider existed.	██████
Optimization B	The coal purchased as part of this optimization was only purchased because DP&L failed to exercise a competitive option for this coal in 2010.	██████
Optimization C	The coal purchased as part of this optimization was only purchased because DP&L failed to exercise a competitive option for this coal in 2010.	██████
Optimization D	Quality swap issue. Low-sulfur coal sold and high-sulfur coal purchased. Low-sulfur coal purchased only because DP&L failed to exercise competitive option for high-sulfur coal in 2010.	██████
Optimization H	The sale of the low-sulfur coal was disconnected with the purchase of the high-sulfur coal so it was not possible to connect the two transactions as being part of a single optimization.	██████
Optimization I	The sale of the low-sulfur coal does not correlate with the purchase of the replacement coal. In addition over half of the low-sulfur contracts sold were imprudently acquired.	██████
Optimization J	DP&L exercised an option in a contract and because the action was discretionary, felt it merited an optimization gain. Auditor believes it would be imprudent for failure to exercise an option that is in the money.	██████
Optimization K	Contractual volumes options with coal company. Auditor believes it would be imprudent for failure to exercise an option that is in the money.	██████
<b>Total Disallowance</b>		██████

In addition to the optimization disallowances discussed above, the Auditors also supported a disallowance of \$████ million dollars based on the Utility's imprudent

<sup>22</sup> The Auditors' recommended disallowances related to optimizations A, B, C, D, H, I, J and K.

<sup>23</sup> The Auditors' reasons for recommended disallowances are described in the 2012 Audit Report at 4-1 through 4-16, and the dollar figures in the "Amount" column are taken from the 2012 Audit Report at 6-87, Table 6-51. Note that the 2010 and 2011 Fuel Audit Stipulations do not preclude disallowances related to imprudent purchases by DP&L. See Direct Testimony of David Crusey at DJC-1 at 8.

management decision. Specifically, the finding is in regard to DP&L's failure (in 2010) to exercise a contract option for [REDACTED] tons of high-sulfur coal for delivery in 2012, combined with DP&L's decision to purchase similar quantity of low-sulfur coal for delivery in 2012.<sup>24</sup> These Auditor findings, and the evidentiary support of the Auditors' recommendations, are discussed in detail later in this brief.

**B. DP&L Has A Financial Incentive To Create Coal Optimizations (By Initially Purchasing Low-Sulfur Coal Instead Of Purchasing High-Sulfur Coal) Because Coal Optimizations Allow The Utility To Charge Customers For Costs It Never Incurs.**

The Auditors define optimizations as transactions involving fuel or power which reduce costs.<sup>25</sup> More specifically, DP&L witness Aaron Cooper testified that a fuel optimization is a "process by which [DP&L] reviews and compares its existing portfolio of coal supply contracts, including both price and quality characteristics, against the current prices available in the market were it to sell coal in its portfolio and buy a replacement coal for delivery to DP&L-operated generating stations."<sup>26</sup> The concept of fuel optimizations was developed in DP&L's Application for a Fuel Rider (Case No. 09-1012-EL-FAC).<sup>27</sup> In that case, DP&L proposed to calculate the Fuel Rider by netting jurisdictional emission allowance proceeds and twenty-five percent of jurisdictional coal sales gains against the fuel and purchased power costs.<sup>28</sup>

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<sup>24</sup> 2012 Audit Report at 1-9.

<sup>25</sup> Id. at 4-1.

<sup>26</sup> *In the Matter of the Application of The Dayton Power and Light Company to Establish a Fuel Rider*, Case No. 12-2881-EL-FAC, Direct Testimony of DP&L witness Aaron Cooper at 3 (October 31, 2013), DP&L Exhibit 3.

<sup>27</sup> Case No. 09-1012-EL-FAC-, Application at 6 (October 20, 2009), OCC Exhibit 2.

<sup>28</sup> Case No. 11-5730-EL-FAC at 4-1, Staff Exhibit 4.

Subsequently, in DP&L's Application to establish a Fuel Rider, DP&L stated that its optimization objective was to "act on opportunities to reduce costs by transactions to optimize the fuel and purchased power portfolio and to reduce the risks of market price fluctuations."<sup>29</sup> DP&L went on to explain the concept of an optimization transaction by stating that "the net proceeds of optimization transactions, where there is a sale of coal or power and a replacement purchase, are based on the price of coal or power sold, net of the cost of the replacement coal or power."<sup>30</sup> According to DP&L, "no optimization transaction [would] take place unless the net effect of the transaction results in a net decrease of costs to the retail ratepayer."<sup>31</sup>

While the structure and description of optimization transactions have been further developed over the past two DP&L Fuel Rider proceedings,<sup>32</sup> it is clear that the original intent of the optimization process, as approved by the PUCO, was designed to benefit retail customers by decreases to fuel costs. But it is also evident that the lack of structure and rules around how an individual optimization is actually created and calculated allowed DP&L to use the optimization process to generate revenue for itself, at the expense of customers, by charging the Fuel Rider for expenses it never incurred.

As initially described in DP&L's Application for a Fuel Rider, an optimization gain appeared to be a relatively simple and beneficial transaction for Standard Service Offer (non-shopping) customers responsible for paying the Fuel Rider. If coal under contract could be sold and replaced with a lower priced coal, then both the Fuel Rider

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<sup>29</sup> Case No. 09-1012-EL-FAC, Application to Establish a Fuel Rider at 6 (October 20, 2009), OCC Exhibit 2.

<sup>30</sup> Id. at 4 (October 20, 2009), OCC Exhibit 2.

<sup>31</sup> Id. at 7 (October 20, 2009), OCC Exhibit 2.

<sup>32</sup> Case Nos. 09-1012-EL-FAC and 11-5730-EL-FAC.

(customers) and the Utility would share in the savings.<sup>33</sup> But coal is a complicated fuel that comes in many different qualities.<sup>34</sup> Most notably coals come with different heat and sulfur contents. Generally, coals with higher heat content have a higher price, and conversely, coals with higher sulfur content have a lower price.<sup>35</sup> As DP&L began to install emission equipment on its boilers in 2007, the Utility was able to gradually move away from burning low-sulfur coal to burning less expensive high-sulfur coal almost exclusively.<sup>36</sup> This newly created ability to burn high-sulfur coal created the opportunity for DP&L to generate significant new revenues using the optimization gain concept—but often—at the expense of SSO customers.

**i. Explanation of an optimization transaction.<sup>37</sup>**

DP&L witness Aaron Cooper categorized an optimization transaction as one where the Utility improves upon an existing coal position by selling the coal and replacing it with a lower priced coal.<sup>38</sup> DP&L then charges the Fuel Rider for the cost of the newly purchased coal plus 75 percent of the savings produced by selling the original coal position and purchasing the replacement coal.<sup>39</sup> For example, if DP&L purchases low-sulfur coal for \$40 a ton and sells that same coal for \$40 a ton, there would be no

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<sup>33</sup> Case No. 09-1012-EL-FAC, Application to Establish a Fuel Rider at 6 (October 20, 2009), OCC Exhibit 2.

<sup>34</sup> See generally, Case No. 12-2881-EL-FAC, Direct Testimony of DP&L witness David Crusey at Exhibit DJC-12.

<sup>35</sup> Id.

<sup>36</sup> 2012 Audit Report at 2-5. See also, Case No. 12-2881-EL-FAC, Transcript Volume II at 232-233 (Cooper) (January 28, 2014).

<sup>37</sup> Case No. 12-2881-EL-FAC Transcript Volume II at 119, this example assumes that the cost to deliver and consume the coals is built into the \$30 and \$40 prices.

<sup>38</sup> Case No. 12-2881-EL-FAC, Direct Testimony of Aaron Cooper at 3 (October 31, 2013), DP&L Exhibit 3.

<sup>39</sup> Case No. 12-2881-EL-FAC, Transcript Volume II at 229 – 230 (Cooper) (January 28, 2014).

gain or loss on the transaction.<sup>40</sup> The \$40 coal is considered the then existing position. If DP&L subsequently purchases high-sulfur Illinois Basin (“ILB”) replacement coal for \$30 a ton, there is a \$10 optimization gain on the transaction. This is because the replacement coal is \$10 cheaper than the original price of coal (i.e.,  $\$40 - \$30 = \$10$ ). DP&L then charges SSO customers (through the Fuel Rider) \$37.50 for the replacement coal (\$30 for the coal plus \$7.50 for 75 percent of the \$10 optimization gain.)<sup>41</sup> At first glance, this would seem to be a good deal for DP&L’s SSO customers because they ultimately pay \$37.50 for the coal instead of the original price of \$40. But the reality is that this optimization concept is flawed because retail customers can end up paying a higher price for the coal that DP&L actually burns.<sup>42</sup> This unfair result is evident in the example above where SSO customers are charged \$37.50 for coal that DP&L only paid \$30 for.

The dilemma when evaluating the optimization process (in the example above) is whether or not the Utility should have purchased the higher priced low-sulfur coal in the first place. The optimization process itself does not evaluate this concern.<sup>43</sup> And there is an inherent flaw in the structure of optimization transactions generally because DP&L will always have a financial incentive to buy coal (initially) at the highest price available (i.e., low-sulfur coal) with the option to later purchase a lower-priced (high-sulfur) coal

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<sup>40</sup>  $\$40 - \$40 = 0$ .

<sup>41</sup> Case No. 12-2881-EL-FAC, Transcript Volume II at 232 (Cooper) (January 28, 2014).

<sup>42</sup> DP&L witness Aaron Cooper agreed that this example (though simplified) was an accurate representation of an optimization transaction, provided the cost to deliver and consume the coals was built into the \$30 and \$40 dollar figures. See Id. at 232 (Cooper).

<sup>43</sup> Case No. 12-2881-EL-FAC, Direct Testimony of Aaron Cooper at 3 (October 31, 2013), DP&L Exhibit 3. The optimization process only compares the Utility’s existing portfolio of coal supply contracts against the current prices available in the market were it to sell coal in its portfolio and buy a replacement coal for delivery to DP&L-operated generating stations.

and make a profit off of SSO customers. Using the example above, DP&L would have a financial incentive to always (initially) purchase the higher priced low-sulfur coal, rather than buy the lower priced high-sulfur ILB coal. As DP&L witness David Crusey admitted, there would be virtually no optimization gains in 2012 for DP&L without DP&L first purchasing low-sulfur coal that it would later resell and replace with a lower-priced high-sulfur ILB coal, which the plants would eventually burn.<sup>44</sup> And as discussed in the example above, by initially purchasing the \$40 high-sulfur coal, DP&L is able to generate a \$7.50 per ton profit that it collects from customers through the Fuel Rider. However, if the lower priced ILB coal was purchased initially, there is very little, if any, opportunity for the Utility to transact an optimization, as it has already purchased the lowest priced coal it will be able to burn.

DP&L witness Crusey acknowledged that low-sulfur NYMEX coal is generally more expensive to purchase than high-sulfur ILB coal.<sup>45</sup> In addition, Mr. Crusey testified that NYMEX coal has more price volatility than high-sulfur ILB coal.<sup>46</sup> Thus, if the market price of NYMEX coal is more volatile than the market price of ILB coal, then it follows that the price of ILB coal is more likely to remain stable, or move very little, when compared with more volatile price of NYMEX coal.

The movement of the price of NYMEX coal will almost always be in the same direction (up, or down) as the movement of the price of the ILB coal.<sup>47</sup> If DP&L initially purchases NYMEX coal instead of ILB coal, and coal prices increase, there is a high

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<sup>44</sup> Case No. 12-2881-EL-FAC, Transcript Volume I at 83 (Crusey) (January 28, 2014).

<sup>45</sup> Id. at 38 (Crusey).

<sup>46</sup> Id. at 201 (Heller).

<sup>47</sup> Case No. 12-2881-EL-FAC, Direct Testimony of DP&L Witness James N. Heller at 15, Exhibit JNH-7, DP&L Exhibit 2.

probability that the price of the NYMEX coal increased more than the price of the ILB coal.<sup>48</sup> When DP&L sells the NYMEX coal and replaces it with the cheaper high-sulfur ILB coal, the Utility has a built-in optimization gain. If DP&L initially purchases NYMEX coal instead of high-sulfur ILB coal, and coal prices decrease, the Utility has three options: 1) burn the NYMEX coal and the expense is added to the Fuel Rider and seek collection from customers, 2) sell the NYMEX coal, take a loss on the coal and purchase the lower priced ILB coal, if the optimization gain is enough to offset the loss on the NYMEX coal sold, or 3) sell the NYMEX coal without replacing it with another coal, if the supply is no longer needed.<sup>49</sup>

This issue is significant for this proceeding because DP&L has claimed a number of optimizations by purchasing NYMEX coal, selling that NYMEX coal, and replacing it with cheaper high-sulfur coal.<sup>50</sup> The potential revenues generated by creating coal optimizations (i.e., purchasing NYMEX coal and then selling the coal and replacing it with a cheaper ILB coal) are much greater than the potential costs of paying more for the ILB coal at purchased later point in time. In fact, DP&L witness Cooper acknowledged that the vast majority of the optimization-gained revenues charged to DP&L's customers for 2012 were the result of NYMEX coal (or another low-sulfur coal position) that was sold and replaced by a high-sulfur coal purchased at a lower price.<sup>51</sup>

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<sup>48</sup> Case No. 12-2881-EL-UNC, Transcript Volume I at 203 (Heller) (January 28, 2014).

<sup>49</sup> Case No. 12-2881-EL-FAC, Transcript Volume II at 261 (Cooper) (January 28, 2014).

<sup>50</sup> 2012 Audit Report at 4-3 through 4-15.

<sup>51</sup> Case No. 12-2881-EL-FAC, Transcript Volume II at 231 (Cooper) (January 28, 2014).

**C. DP&L Acted Imprudently When It Failed To Exercise An “In-The-Money” Option To Purchase High-Sulfur Illinois Basin Coal In October 2010 For Delivery In 2012.**

The Auditors proposed a disallowance of costs because of a contract option that was available to DP&L in October 2010 for high-sulfur coal deliveries in 2012 that was not exercised by the Utility.<sup>52</sup> Simply stated, the Auditors concluded that if a utility has an option that is “in-the-money”<sup>53</sup> it would be imprudent for that utility to fail to exercise the option.<sup>54</sup> And DP&L failed to demonstrate the option was not “in-the-money. Accordingly, the Auditors recommended that the Fuel Rider be adjusted to reflect the costs associated with the 2010 imprudent management decisions related to DP&L’s failure to exercise a competitive supply option, and DP&L’s subsequent purchase of excessive low-sulfur coal for 2012 delivery.<sup>55</sup> The evidence supports a PUCO-finding that these management decisions were imprudent and SSO customers should not have to pay the costs of such imprudent decisions.

DP&L witness Crusey, disputes the Auditors’ findings and testified that there was no imprudence on the part of the Utility in not exercising the 2010 option.<sup>56</sup> Mr. Crusey contends that at the end of October, when DP&L made the decision not to exercise the option for the high-sulfur coal, DP&L reviewed the market prices for coal, and concluded that the option was “not in-the-money.”<sup>57</sup> Yet Mr. Crusey offered no record of any

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<sup>52</sup> 2012 Audit Report at 4-12.

<sup>53</sup> The terms “in-the-money” and “out-of-the-money” mean the market alternative is cheaper or more expensive, Case No. 12-2881-EL-FAC, Transcript Volume II at 355 (Medine) (January 28, 2014).

<sup>54</sup> 2012 Audit Report at 4-12.

<sup>55</sup> Id. at 1-16.

<sup>56</sup> Case No. 12-2881-EL-FAC, Direct Testimony of David Crusey at 32 (October 31, 2013), DP&L Exhibit 1.

<sup>57</sup> Id. at 32-33, DP&L Exhibit 1.



analysis DP&L actually conducted in 2010 to support his contention. He offered no documents discussing the analysis or any supplier response to a Request for Proposal soliciting market offers, nor did he offer any documents related to any analysis of the contract option available to DP&L verses the then market price of ILB coal. The only evidence witness Crusey offered to support DP&L's decision not to exercise the option in the contract was an "analysis" Mr. Crusey conducted for the purpose of his testimony in this case.<sup>58</sup> But that "analysis" is flawed for the reasons explained below. Accordingly, the PUCO should find that DP&L failed to provide any evidence that supports a finding that DP&L acted prudently when it did not exercise the option to purchase the high-sulfur coal in 2010.

Mr. Crusey testified that the Utility relied on the ICAP<sup>59</sup> United report from October 2010 ("ICAP Report" or "Report") (sometimes referred to as Vaughn's Index or Vaughn's View) to make the decision whether or not to exercise the option.<sup>60</sup> Using the ICAP Report, DP&L calculated the then current market price for the high-sulfur coal that DP&L held an option for delivery in 2012.<sup>61</sup> Then DP&L compared the then current market price with the option price to complete the analysis.<sup>62</sup> Because the coal specifications for the ILB coal option available to DP&L in 2010 had a higher Btu value than the market prices listed on the ICAP Report, Mr. Crusey made a calculation to adjust

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<sup>58</sup> Id. at 31-, DP&L Exhibit 1.

<sup>59</sup> ICAP United, Inc. provides real-time price discovery of coal and other products.

<sup>60</sup> Case No. 12-2881-EL-FAC, Direct Testimony of David Crusey, at 32-33 (October 31, 2013), see specifically, "V. Prudence of the Decision Not to Exercise an Option." DP&L Exhibit 1.

<sup>61</sup> Case No. 12-2881-EL-FAC, Transcript Volume I at 65 (Crusey) (January 28, 2014).

<sup>62</sup> Id. (Crusey).

for the difference.<sup>63</sup> Based on the result of that calculation, Mr. Crusey maintains that DP&L made a “prudent” decision not to exercise the option because the then current market price high-sulfur ILB coal was lower than the option strike price available in the contract.<sup>64</sup>

DP&L offered only this “analysis” (apparently completed in 2013 for this proceeding) to justify its decision not to exercise the 2010 option. In fact, there is no evidence that DP&L completed an analysis at the time the decision was made in 2010 to not exercise the option. A prudent decision is defined as “one which reflects what a reasonable person would have done in light of conditions and circumstances which were known or reasonably should have been known **at the time the decision was made.**”<sup>65</sup> Thus, an after-the-fact analysis does not satisfy the Ohio Supreme Court’s standard of prudence. And DP&L’s after-the-fact analysis is flawed for two additional reasons. First, DP&L failed to include certain crucial factors in its analysis to determine whether the option was “in-the-money” or not. Specifically, DP&L failed to adjust for differences in SO<sub>2</sub> levels and transportation costs - both of which are factors that can influence the price of coal, according to Auditor Emily Medine.<sup>66</sup> Second, DP&L’s decision not to exercise the option was to the detriment of customers. This decision was to detrimental because DP&L later purchased a more expensive high-sulfur coal and charged customers for this higher price, and DP&L charged customers an optimization gain for buying and

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<sup>63</sup> Id. (Crusey).

<sup>64</sup> Id. at 66 (Crusey).

<sup>65</sup> *City of Cincinnati v. Pub. Util. Comm.*, (1993) 67 Ohio St.3d 523, 527-528, 620 N.E.2d 826, 830. (Emphasis added).

<sup>66</sup> Case No. 12-2881-EL-FAC, Transcript Volume II at 344-345 and 347 (Medine) (January 28, 2014).

selling low-sulfur NYMEX coal that would not have been purchased if the option had been exercised.

It was imprudent when DP&L failed to exercise the contract option in 2010 that would have saved customers money. And for the reasons explained further below, DP&L's own evidence shows that its decision not to exercise the contract option in 2010 was not prudent because that management decision was based on an analysis that is flawed on its face. Any way DP&L wants to argue it—DP&L failed to exercise the contract option in 2010 that resulted in higher coal prices for SSO customers in 2012. Those higher prices were a result of imprudent management decisions that SSO customers should not have to pay for.

**i. DP&L's analysis is flawed because it does not include a price adjustment for the level of sulfur dioxide in the coal.**

The ICAP Report that DP&L alleges it used as a basis for its analysis lists two prices for ILB coal. That ICAP Report lists a price of \$50.75 per ton for the 11,500 Btu,<sup>67</sup> 2.5 pound sulfur dioxide ("SO<sub>2</sub>") coal and a price of \$67.25 per ton for the 11,500 Btu, 5.0 pound SO<sub>2</sub> coal.<sup>68</sup> This Report illustrates that there was a significant difference in price (\$16.50 per ton) for the same Btu coal (ILB) with different levels of SO<sub>2</sub>.<sup>69</sup> But DP&L's analysis 1) did not take this difference into account, and 2) did not explain why this price difference is irrelevant to a prudence analysis.

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<sup>67</sup> Id. at 347 (Medine) and Volume I at 66-67 (Crusey) (January 28, 2014).

<sup>68</sup> Case No. 12-2881-EL-FAC, Transcript Volume I at 67 (Crusey) (January 28, 2014).

<sup>69</sup> Id.

The specification for the ILB coal that DP&L had under option in 2010 for delivery in 2012 was for 11,800 Btu, 4.5 pound SO<sub>2</sub>.<sup>70</sup> As acknowledged by Mr. Crusey, the ICAP Report lists different specifications and prices for SO<sub>2</sub> levels.<sup>71</sup> But the SO<sub>2</sub> specification for the ILB coal that DP&L had under option in 2010 for delivery in 2012 did not contain the same SO<sub>2</sub> levels shown on the ICAP Report.<sup>72</sup> Despite this apparent difference, Mr. Crusey did not make an adjustment for the level of SO<sub>2</sub> for the purposed of his analysis.<sup>73</sup>

When asked (upon cross-examination) the reason why he didn't make an adjustment for SO<sub>2</sub> in his analysis, Mr. Crusey responded that the price for SO<sub>2</sub> emission allowances was "very minimal" at present.<sup>74</sup> But Mr. Crusey's response referred to the low market price of SO<sub>2</sub> emission allowances, which has no relevance to the market price difference between two 11,500 Btu/lb. coals with two different SO<sub>2</sub> levels.<sup>75</sup> And when questioned why he did not include an adjustment for SO<sub>2</sub> when there was a \$16.50 per ton price difference listed on the ICAP Report (between the two 11,500 Btu/lb. coals with different SO<sub>2</sub> levels), he responded:

I can't say exactly what that coal is, but that coal is not comparable to the coal that we purchased. I don't have it in front of me, the spec for the 11, 5, 2.5-pound sulfur coal, but it's an Eastern coal. It's an export coal. There's something different about that coal that does not make it comparable to the [ILB Option] Coal, and I can't address it as I sit here today, but it is not comparable or we would

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<sup>70</sup> Case No. 12-2881-EL-FAC, Transcript Volume II at 273 (Cooper) (January 28, 2014).

<sup>71</sup> Case No. 12-2881-EL-FAC, Transcript Volume I at 67 (Crusey) (January 28, 2014).

<sup>72</sup> Id. (Crusey).

<sup>73</sup> Id. at 68 (Crusey).

<sup>74</sup> Id. (Crusey).

<sup>75</sup> Id. (Crusey).

have used that if it was comparable. Our alternative would be to purchase an 11.5, 5-pound coal or something similar to that.<sup>76</sup>

Mr. Crusey's response is nonsensical because it is the same ICAP Report, and the same market pricing data for coal, that he used in his analysis to adjust for Btu differences.<sup>77</sup> If the data in the ICAP Report, which Mr. Crusey relied upon in his analysis that concluded that the coal option was out of-the-money by \$1.43 per ton,<sup>78</sup> was a valid comparable for making an adjustment for differences in the Btu specifications, then that same data should have been a valid comparable for making an adjustment for differences in the levels of SO<sub>2</sub>. Mr. Crusey cannot have it both ways.

Additionally, Auditor Emily Medine testified about the relevance of SO<sub>2</sub> to the market pricing of coal. Ms. Medine explained that "you would need to include a value for SO<sub>2</sub>, not based upon emission allowances, but actually based upon what the market perceived the value is and how the market assessed the value for sulfur."<sup>79</sup> Evaluating SO<sub>2</sub> levels is a material step in analyzing coal contracts,<sup>80</sup> something that Mr. Crusey failed to do when he developed his testimony in an effort to offer some justification for DP&L's imprudent management decision that resulted in higher coal prices for SSO customers in 2012. Ms. Medine explained that a SO<sub>2</sub> analysis is "not irrelevant" and that it is something that one would evaluate in a prudent position.<sup>81</sup> Despite its relevance, Mr. Crusey failed to take SO<sub>2</sub> into account in his analysis. Mr. Crusey's answers upon cross-

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<sup>76</sup>Id. (Crusey).

<sup>77</sup>Case No. 12-2881-EL-FAC, Direct Testimony of David Crusey 32-34 (October 31, 2013), DP&L Exhibit 1.

<sup>78</sup> Id. at 34, DP&L Exhibit 1.

<sup>79</sup> Case No. 12-2881-EL-FAC, Transcript Volume II at 344-345 (Medine) (January 28, 2014).

<sup>80</sup> Id. at 358. (Medine).

<sup>81</sup> Id. at 358-359. (Medine).

examination and the testimony of other witnesses show that Mr. Crusey's analysis is flawed. And it was imprudent for DP&L to rely upon an analysis that is flawed on its face to make such an important decision for customers.

**ii. DP&L's analysis is flawed because it does not include a price adjustment for transportation costs.**

As Auditor Medine testified, since a decision of whether the option was in-the-money must be done on a delivered basis, and any such analysis must also include the transportation costs to deliver the coal to the power plant.<sup>82</sup> According to Ms. Medine, "when you are looking at two coals that have different Btu contents, you absolutely must take into account transportation costs."<sup>83</sup> But DP&L did not consider transportation costs in its analysis. Auditor Medine testified that it would not be appropriate to calculate the pricing for the 11,800 Btu ILB coal by only making a comparison of the Btu value of the option coal to the then current market price for ILB coal from the ICAP Report provided in Mr. Crusey's testimony.<sup>84</sup>

DP&L chose not to purchase coal in 2010 for delivery in 2012 priced at \$53.50 per ton.<sup>85</sup> That price was for coal located on a barge along the lower Ohio River.<sup>86</sup> The location of the ILB coal that DP&L used for its analysis from the ICAP Report may not have been transported from the lower Ohio River area.<sup>87</sup> Thus, the price to transport these coals could vary by as much as a couple of dollars, dependent on location.<sup>88</sup> As

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<sup>82</sup> Id. at 344. (Medine).

<sup>83</sup> Id. at 347. (Medine).

<sup>84</sup> Id. at 344. (Medine).

<sup>85</sup> Id. at 348. (Medine).

<sup>86</sup> Id. (Medine).

<sup>87</sup> Id. at 348-349. (Medine).

<sup>88</sup> Id. at 349. (Medine)

Auditor Medine affirmed, the location of the coal is important when conducting an analysis because there is a transportation charge to get the coal to the power plant.<sup>89</sup> By making only a Btu adjustment and not considering the transportation cost differences in the analysis, Mr. Crusey's justification of the prudence of the Utility's decision to not exercise the option is incomplete.

DP&L witness Aaron Cooper acknowledged that there may need to be an adjustment to account for transportation costs of the coal.<sup>90</sup> Mr. Cooper explained that the factors that influence or affect transportation rates of coal are typically the distance from the power plant, and the number of locks that the tow has to move through.<sup>91</sup> Whether or not the coal is traveling upstream or downstream could also have an effect on the price as well.<sup>92</sup> Because transportation costs could have a significant effect on price, and therefore influence an analysis of whether an option is "in-the-money," transportation costs should always be considered. DP&L failed to consider this factor in its analysis.<sup>93</sup> Such an oversight undermines DP&L's allegation that its decision not to exercise the contract option was prudent.

**iii. DP&L's failure to exercise the option in 2010 to buy coal for delivery in 2012 resulted in higher 2012 coal costs for SSO customers.**

DP&L's decision not to exercise the 2010 option, choosing instead to purchase low-sulfur coal that it would later sell and claim an optimization gain, was to the

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<sup>89</sup> Id. (Medine).

<sup>90</sup> Case No. 12-2881-EL-FAC, Transcript Volume II at 274 (Cooper) (January 28, 2014).

<sup>91</sup> Id. at 275. (Cooper).

<sup>92</sup> Id. (Cooper).

<sup>93</sup> Case No. 12-2881-EL-FAC, Direct Testimony of David Crusey at 32-33 (October 31, 2013). Mr. Crusey why, in his opinion, the Utility acted prudently in not exercising the option in 2010 in his direct testimony. However, the only factor Mr. Crusey considers for purposes of his analysis is Btu.

detriment of customers. This decision by the Utility disadvantaged customers not only because DP&L purchased a more expensive low-sulfur coal instead of exercising the option in 2010, but also because DP&L purchased a high-sulfur ILB coal in 2011 that was \$[REDACTED] per ton more expensive than the high-sulfur ILB coal it could have purchased under the 2010 option.<sup>94</sup> DP&L's imprudent decisions are directly responsible for its failure to exercise a competitive supply option which resulted in DP&L's imprudent purchase of low-sulfur coal rather than supplies of less expensive high-sulfur coal. This decision cost DP&L's SSO customers money. The Auditors recommend that DP&L's Fuel Rider be adjusted to reflect a total disallowance of \$3.4 million related to the Utility's failure to exercise the option.<sup>95</sup> The evidence supports that Auditors' recommendation.

**D. DP&L's Decision To Purchase Low-Sulfur Coal Rather Than A Less Expensive High-Sulfur Coal Was Not A Prudent Decision.**

A key issue in determining the validity of an optimization claim by DP&L is the prudence of the initial coal purchase. The 2012 Audit Report explains that if the Utility is aware that it can burn a given amount of high-sulfur coal, yet it purchases more expensive low-sulfur coal instead, later selling the coal and replacing it with the lower priced coal that could have been purchased initially, then the Utility is making an imprudent decision and no optimization gain should be allowed.<sup>96</sup> This very issue has

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<sup>94</sup> 2012 Audit Report at 1-10.

<sup>95</sup> *In the Matter of the Application of The Dayton Power and Light Company to Establish a Fuel Rider*, Case No. 12-2881-EL-FAC, Transcript Volume II at 329 (Smith) (January 28, 2014).

<sup>96</sup> See 2012 Audit Report at 1-9. Specifically, the Audit Report states: "EVA noted in the report of the 2010 Audit that DP&L had successfully used [REDACTED] contracts to hedge its position when DP&L burned exclusively [low-sulfur] coal in its units but questioned the prudence of this strategy in the context of DP&L's new supply mix."



been an ongoing concern for the Auditors since the first Fuel Audit in 2010.<sup>97</sup> In fact, one of the Auditors' major concerns highlighted in the 2010 Fuel Audit was DP&L's discounting of the importance of the initial purchase of coal and the prudence of that purchase. DP&L argued that since its "calculation of the optimization does not incorporate the initial cost of the coal being sold, the initial cost is not relevant."<sup>98</sup> The Auditors were concerned about DP&L's desire to ignore the importance of the initial coal purchase when they stated "DP&L also does not consider what it could have acquired the high sulfur coal for at the time it purchased the hedge."<sup>99</sup> The Auditors went on to explain that "DP&L should develop clear policies that limit optimization sharing to those circumstances in which the optimization improves upon an existing position (**that was acquired in a prudent manner**) to the benefit of jurisdictional customers."<sup>100</sup>

As previously discussed, in October 2010 DP&L chose not to exercise an option to purchase high-sulfur ILB coal for delivery in 2012, because in the Utility's opinion, the option was not in-the-money.<sup>101</sup> DP&L also chose not to purchase other high-sulfur coal at that time, choosing to purchase higher-priced low-sulfur coal instead. But, as explained below, in October 2010, the Utility's coal supply position for 2012 versus its projected coal requirements for 2012 showed a greater need for high-sulfur coal than for low-sulfur coal.

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<sup>97</sup>*In the Matter of the Application of The Dayton Power and Light Company to Establish a Fuel Rider*, Case No. 09-1012-EL-FAC, Report of the Management/Performance and Financial Audit of the Fuel and Purchased Power Rider of the Dayton Power and Light Company, at 1-5 (April 29, 2011), Staff Exhibit 3.

<sup>98</sup> Id. at 1-4, Staff Exhibit 3.

<sup>99</sup> Id., Staff Exhibit 3.

<sup>100</sup> Id. at 1-6. (Emphasis added), Staff Exhibit 3.

<sup>101</sup> Case No. 12-2881-EL-FAC, Direct Testimony of David Crusey at 34 (October 31, 2013).

DP&L first began contracting for future-year delivery of high-sulfur ILB coal in 2007.<sup>102</sup> In September of 2010, DP&L was forecasting a high-sulfur coal burn level of 62.5% at Stuart Station,<sup>103</sup> and as of January 4, 2010, Stuart Station was projected to use six million total tons of coal in 2012.<sup>104</sup> Thus, the amount of high-sulfur coal needed for 2012 was approximately 3.75 million tons.<sup>105</sup> In October 2010 DP&L had only 1.75 million tons of high-sulfur coal under contract for 2012, or 46.6% of its 2012 projected needs.<sup>106</sup> At this same time, DP&L had a projected need of only 2.25 million tons<sup>107</sup> of low-sulfur coal at Stuart Station for 2012. And in October 2010 DP&L already had [REDACTED] million tons of low-sulfur coal under contract for delivery in 2012, or [REDACTED]% of its 2012 projected requirements ([REDACTED]).<sup>108</sup> Thus, when DP&L chose not to exercise the option to purchase high-sulfur coal ILB coal for delivery in 2012 (choosing instead to purchase low-sulfur coal that they would eventually turn into an optimization gain), the Utility had a much greater need for high-sulfur coal than it did for low-sulfur coal. Again, several of DP&L's decisions in regard to coal purchases for 2012 were imprudent. Customers should not have to pay for imprudent costs.

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<sup>102</sup> Case No. 12-2881-EL-FAC, Transcript Volume II at 233-234 (Cooper) (January 28, 2014).

<sup>103</sup> Case No. 12-2881-EL-FAC, Transcript Volume I at 80 (Crusey) (January 28, 2014).

<sup>104</sup> Id. at 59. (Crusey).

<sup>105</sup> 6 million tons x 0.625 = 3.75 million tons.

<sup>106</sup> 1.75 million tons / 3.75 million tons = 46.6%

Case No. 12-2881-EL-FAC, Transcript Volume I at 58-59 (Crusey) (January 28, 2014).

<sup>107</sup> 6 million tons x 0.375 = 2.25 million tons.

<sup>108</sup> Case No. 12-2881-EL-FAC, Direct Testimony of David Crusey at DJC-9 (October 31, 2013).

**E. Most Of The 2012 Coal Optimization Gains Claimed By DP&L Should Be Disallowed By The PUCO.**

DP&L claimed credits for thirteen optimizations during the 2012 audit period, which consisted of both basin and quality swaps.<sup>109</sup> The Auditors concluded that five of the thirteen claimed optimizations should not qualify in their entirety, and the optimization gains claimed in two of the remaining eight optimizations should be reduced.<sup>110</sup> The reasons for the optimization disallowances are explained in more detail below.

**i. One of the optimization gains claimed by the Utility occurred prior to the existence of the DP&L's Fuel Rider.**

The Auditors found that one of the five optimizations did not qualify as an optimization because the entire transaction took place prior to the effective period of the Fuel Rider.<sup>111</sup> DP&L claimed this optimization based on a 2009 sale of [REDACTED] tons of [REDACTED] coal for 2012 delivery and a corresponding 2009 purchase of [REDACTED] coal at a slightly lower price, also for 2012 delivery.<sup>112</sup> The transaction (sale) date was December 30, 2009.<sup>113</sup> But DP&L's Application for a Fuel Rider was not approved by the PUCO until December 16, 2009, with the effective date of the new tariffs not earlier than

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<sup>109</sup> A basin swap refers to coals produced in different geographical locations and a quality swap refers to coals with different levels of Btu, SO<sub>2</sub>, ash, moisture, etc.

<sup>110</sup> 2012 Audit Report at 1-16.

<sup>111</sup> 2012 Audit Report at 4-4. DP&L witness Cooper agreed on cross-examination that the entire optimization transaction in question took place prior to DP&L's Fuel Rider going into effect. See Case No. 12-2881-EL-FAC, Transcript Volume II at 240 (Cooper) (January 28, 2014).

<sup>112</sup> Id.

<sup>113</sup> Case No. 12-2881-EL-FAC, Transcript Volume II at 237 (Cooper) (January 28, 2014). Mr. Cooper explained that "the sale date was December 30, 2009. **Obviously, if we sold it on December 30, 2009, we had it in our position prior to that** because we don't make coal; we buy coal." (Emphasis added). 237-238.

January 1, 2010.<sup>114</sup> As the sale and purchase occurred in 2009 - before the Fuel Rider was in place - only the replacement purchase was in place during the effective period of the Fuel Rider (not the initial purchase/position). It is undisputed that DP&L sold the coal and bought the replacement coal at issue for this optimization prior to January 1, 2010.<sup>115</sup> And as DP&L agreed in the 2011 Fuel Rider Stipulation, an optimization occurs when there is an improvement on a then existing coal position.<sup>116</sup> Therefore, as the Auditors point out, no optimization of an existing position took place (as the existing position was the replacement coal purchased on December 30).<sup>117</sup> The Auditors recommended 100 percent disallowance for this optimization, which amounts to \$[REDACTED].<sup>118</sup> DP&L argues that this transaction was an optimization, despite the fact the transaction took place prior to DP&L's Fuel Rider going into effect and before optimizations was even permitted by the Commission.<sup>119</sup>

DP&L maintains that this optimization is valid because there was a similar situation with a 2010 optimization (i.e., the optimization transaction took place prior to the Fuel Rider's existence) and that optimization was not disallowed.<sup>120</sup> DP&L witness Cooper testified that "Optimization A is an optimization in every respect of every optimization we have ever performed at DP&L. We bought coal. It was in our position. We sold coal. We replaced it with a lower priced coal on the delivered and consumed

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<sup>114</sup> See Case No. 09-1012-EL-FAC, Opinion and Order (November 9, 2011).

<sup>115</sup> Case No. 12-2881-EL-FAC, Transcript Volume II at 240 (Cooper) (January 28, 2014).

<sup>116</sup> *In the Matter of the Application of the Dayton Power and Light Company to Establish a Fuel Rider*, Case No. 11-5730-EL-FAC, Opinion and Order at 4 (January 23, 2013). The "then-existing position" means the costs of the coal portfolio as of the time a sale from such coal portfolio is made.

<sup>117</sup> 2012 Audit Report at 4-4.

<sup>118</sup> *Id.* at Exhibit 6-51 on 6-87.

<sup>119</sup> Case No. 12-2881-EL-FAC, Transcript Volume II at 240 (Cooper) (January 28, 2014).

<sup>120</sup> *Id.* at 241. (Cooper).

basis, and that is an optimization.”<sup>121</sup> In other words, as far as DP&L is concerned, the fact that the Commission had not yet actually *approved* optimizations for the Utility is irrelevant. Even worse, using witness Cooper’s concept of an optimization, a purchase of a low-sulfur coal, even if it is an imprudent purchase, which is later sold and replaced with a lower priced ILB coal, would also constitute an optimization.

Mr. Cooper argued that Optimization A is valid because the Auditors did not object to a similar transaction during the 2010 Fuel Audit. Mr. Cooper implied that the Auditors’ lack of objection to the transaction in 2010 means all similar transactions should be allowed in the future.<sup>122</sup> Mr. Cooper is wrong.

The 2011 Audit Report contained discussion of problems related to obtaining complete information and documentation from DP&L related to optimizations.<sup>123</sup> And Mr. Cooper did agree that it was likely that the Auditors might have a better understanding of the nuances surrounding optimization transaction by the third audit than they did the very first Audit.<sup>124</sup> Mr. Cooper also agreed that the 2010 optimization had no bearing on DP&L’s conduct towards optimization transactions in 2012.<sup>125</sup> Notably, DP&L did not cite to any law, PUCO precedent, or rule that supports its argument. DP&L’s argument regarding the disallowance of Optimization A should therefore be rejected. The PUCO should disallow this optimization in accordance with the Auditors’ findings.

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<sup>121</sup> Id. at 240. (Cooper).

<sup>122</sup> Case No. 12-2881-EL-FAC, Direct Testimony of Aaron Cooper at 13.

<sup>123</sup> 2011 Audit Report (11-5730-EL-FAC) at 1-9 and 4-6.

<sup>124</sup> Case No. 12-2881-EL-FAC, Transcript Volume II at 254 – 255 (Cooper) (January 28, 2014).

<sup>125</sup> Id. at 259-260. (Cooper).

- ii. **DP&L did not adhere to the principles for optimization transactions because the sale of the low-sulfur coal was disconnected with the purchase of the high-sulfur coal so it was not possible to connect the two transactions as being part of a single optimization.**

The concept of optimizations was presented as a win for DP&L and its customers. That was evident when DP&L stated in its application that no optimization transaction would occur unless it saved the customers money.<sup>126</sup> However, optimizations have the potential to be much more complicated, as evidenced by some of the optimization gains claimed by the Utility in the 2012 Fuel Audit. For instance, DP&L is claiming an optimization for coal it had under contract, which it sold and replaced with multiple purchases of coal. But this coal was purchased –months, up to even a year later, making it virtually impossible to tie the transactions together.<sup>127</sup> However, in its Application to establish a Fuel Rider, DP&L described an optimization transaction as one where “there is a sale of coal or power and a replacement purchase.”<sup>128</sup> Later in the Application, when describing how an optimization would occur, the Utility stated “DP&L would consider selling the original coal and replacing it with the alternative supply.”<sup>129</sup> In other words, the Utility is selling the coal because it has a cheaper option to replace it. When coal is sold and replaced with multiple purchases over several months, up to even up to a year, it is evident that the initial coal was sold without having replacement coal lined up. DP&L is gambling with customers’ money. This disallowance is supported by evidence and should be granted by the Commission.

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<sup>126</sup> *In the Matter of the Application of the Dayton Power and Light Company to Establish a Fuel Rider*, Case No. 09-1012-EI-UNC, Application, at 7 (October 30, 2009), OCC Exhibit 2.

<sup>127</sup> 2012 Audit Report at 1-19 and 1-20.

<sup>128</sup> *In the Matter of the Application of the Dayton Power and Light Company to Establish a Fuel Rider*, Case No. 09-1012-EI-UNC at 4, Application, (October 30, 2009), OCC Exhibit 2.

<sup>129</sup> *Id.* at 7.

#### IV. CONCLUSION

This proceeding is significant for DP&L's SSO customers because they pay for the Utility's fuel costs through the Fuel Rider as part of their electric bills. The Auditors recommended disallowances of fuel costs that DP&L collected from SSO customers are based on sound, long-standing regulatory principles and practices in addition to Ohio law that mandates that customers should only be charged for those fuel purchases that are prudently incurred.

For these reasons the PUCO should accept the Auditors' recommendations which would disallow \$4.8 million in imprudent fuel costs (incurred in 2012) that have been included in the Fuel Rider. Accordingly, the Fuel Rider should be credited \$4.8 million plus carrying costs, where applicable.

Respectfully submitted,

BRUCE J. WESTON  
OHIO CONSUMERS' COUNSEL

/s/ Kyle L. Kern  
Kyle L. Kern  
Assistant Consumers' Counsel  
**Office of the Ohio Consumers' Counsel**  
10 West Broad Street, Suite 1800  
Columbus, Ohio 43215-3485  
Telephone: (614) 466-9585  
[kyle.kern@occ.ohio.gov](mailto:kyle.kern@occ.ohio.gov)

## **CERTIFICATE OF SERVICE**

I hereby certify that a copy of the *Post-Hearing Brief by the Office of the Ohio Consumers' Counsel, Public Version*, was served on the persons stated below via electronic transmission, this 3rd day of March, 2014.

/s/ Kyle L. Kern

Kyle L. Kern

Assistant Consumers' Counsel

## **SERVICE LIST**

Thomas McNamee  
Steven Beeler  
Attorney General's Office  
Public Utilities Commission of Ohio  
180 East Broad St., 6<sup>th</sup> Fl.  
Columbus, OH 43215  
[Thomas.mcnamee@puc.state.oh.us](mailto:Thomas.mcnamee@puc.state.oh.us)  
[Steven.beeler@puc.state.oh.us](mailto:Steven.beeler@puc.state.oh.us)

Judi L. Sobecki  
Randall J. Griffin  
The Dayton Power and Light Company  
1065 Woodman Dr.  
Dayton, OH 45432  
[Judi.sobecki@dplinc.com](mailto:Judi.sobecki@dplinc.com)  
[Randall.griffin@dplinc.com](mailto:Randall.griffin@dplinc.com)

AEs: [Bryce.mckenney@puc.state.oh.us](mailto:Bryce.mckenney@puc.state.oh.us)  
[Gregory.price@puc.state.oh.us](mailto:Gregory.price@puc.state.oh.us)



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Summary: Brief Post-Hearing Brief by the Office of the Ohio Consumers' Counsel (Public Version) electronically filed by Ms. Deb J. Bingham on behalf of Kern, Kyle L.