BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Duke Energy Ohio, Inc., for Approval of an Alternative Rate Plan Pursuant to Section 4929.05, Revised Code, for an Accelerated Service Line Replacement Program.	)))))	Case No. 14-1622-GA-ALT

REPLY BRIEF OF DUKE ENERGY OHIO, INC.

December 23, 2015

I. INTRODUCTION

Duke Energy Ohio, Inc., (Duke Energy Ohio or the Company) instituted this proceeding for approval of an accelerated service line replacement program (ASRP) and related cost recovery. The proposal would continue the more rapid replacement of obsolete, high-risk service lines, as is currently being done under the Company's recognized accelerated main replacement program (AMRP). The ASRP is necessary so that Duke Energy Ohio can comply with recent requirements imposed by the Pipeline and Hazardous Materials Safety Administration (PHSMA) and the directives of that agency as well as those from the U.S. Department of Transportation (DOT). The proposed ASRP also enables adherence to Ohio's natural gas pipeline safety laws – laws through which the General Assembly directed the Public Utilities Commission of Ohio (Commission) to ensure public safety.

The parties to this proceeding remarkably oppose the ASRP. The Office of the Ohio Consumers' Counsel (OCC), Commission Staff (Staff), and the Ohio Partners for Affordable Energy (OPAE) complain that the ASRP is not needed; that customers are sufficiently protected against the risks of obsolete pipe that is subject to irreversible corrosion and ground forces. These parties fail to comprehend PHMSA's mandate to Duke Energy Ohio that it develop and implement a distribution integrity management program (DIMP) and the relationship between federal and state regulators in respect of pipeline safety. They attack every aspect of the proposal, discarding public safety and rewriting the law in the process. These parties further ignore the fact that, if their arguments had merit, *every* infrastructure replacement program in the state of Ohio would be illegal and would have to be terminated immediately. These parties – that failed to offer any witnesses experienced in pipeline regulation – urge the Commission to ignore its own precedent, to deny its recognition of the potential for service lines to cause catastrophic harm and to reject its laudable expectation that known threats on a natural gas distribution

system be eliminated before imminent harm occurs. As demonstrated herein and its initial Merit Brief, Duke Energy Ohio has proven the need for its ASRP and the arguments of the parties to the contrary must be rejected.

II. EVIDENTIARY RULINGS

A. The Attorney Examiner Properly Admitted into the Record Demonstrative Evidence that is Relevant to this Proceeding.

Although the OCC correctly recognizes that the Commission is not bound by the rules of evidence, it argues here that the Commission should be so bound.[1] As the OCC reasons, anything other than strict adherence to the rules of evidence is "bad legal precedent and public policy."[2] In addition to ignoring established precedent on this topic, the OCC patently fails to appreciate the level of sophistication that the Commission possesses in respect of assessing evidence. It further fails to acknowledge that, although the Commission is capable of assessing evidence admitted into the record, any decision of the Commission must be predicated upon that record.[3]

The Ohio Supreme Court has affirmed that the Commission "is not stringently confined by the Rules of Evidence."[4] Indeed, the Commission has "broad discretion in the conduct of its hearings."[5] As the Commission has explained:

> This latitude stems from the recognition that Commission proceedings lack certain distinctive features of judicial trials; importantly, fact-finding by a lay jury. Indeed, a substantial risk of misuse by the jury is the basis for many exclusionary rules of evidence, such as the opinion rule and the hearsay rule, and

---

[1] OCC Merit Brief, at pp. 8-9.
[2] OCC Merit Brief, at pg. 9.
[3] R.C. 4903.09. See also, *Elyria Foundry Company v. Public Utilities Commission of Ohio*, 114 Ohio St.3d 305, ¶ 30, 2007-Ohio-4164, citing, *Cleveland Electric Illuminating Company v. Public Utilities Commission of Ohio,* 76 Ohio St. 3d 163, 166, 1996-Ohio-296.
[4] *Greater Cleveland Welfare Rights Organization, Inc. v. Public Utilities Commission of Ohio*, (1982), 2 Ohio St.3d 62, 68, 442 N.E.2d 1288. See also, *Ohio Bell Telephone Co. v. Public Utilities Commission of Ohio*, (1984), 14 Ohio St.3d 49, 50, 471 N.E.2d 475; *In the Matter of the Regulation of the Purchased Gas Adjustment Clause Contained within the Rate Schedules of the East Ohio Gas Company dba Dominion East Ohio and Related Matters*, Case No. 05-219-GA-GCR, Entry, at pg. 7 (July 28, 2006); *In the Matter of the Complaint of Pro Se Commercial Properties v. The Cleveland Electric Illuminating Company*, Case No. 07-1306-EL-CSS, Entry on Rehearing, at pg. 9 (November 5, 2008).
[5] *Greater Cleveland Welfare Rights Organization, Inc. v. Public Utilities Commission of Ohio*, (1982), 2 Ohio St.3d at 68.

> other controlling devices such as limiting instructions. The evidence is excluded, thus, not because it lacks relevance or probative force, but because it is feared that a jury may accord undue weight to a potentially unreliable piece of evidence.[6]

The OCC argues that demonstrative evidence of corroded service lines was improperly admitted into the record in this proceeding because, as it contends, such evidence was irrelevant.[7] In doing so, however, the OCC fails to acknowledge the criteria for demonstrative evidence, the discretion afforded the Commission in respect of its admission, and the OCC's own failure to timely object.

"Demonstrative evidence is an object, picture, model, or other device intended to clarify or qualify facts for the jury… ."[8] The admission of demonstrative evidence is within the sound discretion of the court.[9] It is also well settled that such evidence is properly admitted when it is relevant, substantially reflects that which it is intended to represent, and will neither confuse issues or mislead the fact finder.[10] Significantly, and as ignored by the OCC, "it is up to the jury or trier of fact to decide what weight to give such evidence."[11] Thus, any purported dissimilarity does not render demonstrative evidence inadmissible.[12]

Here, the portions of service lines removed from the Duke Energy Ohio service territory are relevant to the question of whether obsolete, high-risk service lines should be replaced on an accelerated basis. And an understanding as to the physical composition of such obsolete lines, which are subject to irreversible corrosion, undeniably tends to establish the need for the Company's proposed ASRP. Further, the weight to be afforded such evidence rests with the

---

[6] *In the Matter of the Complaint of Brothers Century 21, Inc. v. The East Ohio Gas Company*, Case No. 84-866, GA-CSS, 1986 Ohio PUC LEXIS 1954, *4 (February 24, 1986).
[7] OCC Merit Brief, at pg. 6.
[8] *In the Matter of A.H.*, 2015-Ohio-2174, ¶ 54 (Clark Cty. 2015).
[9] *State v. Jackson*, 86 Ohio App.3d 568, 570, 621 N.E.2d 710 (Clark Cty. 1993).
[10] *State v. Abner*, 2006-Ohio-4510, ¶99 (Montgomery Cty. 2006); See also, *Masi v. Alida's Art Studios of California*, 1996 Ohio App. LEXIS 1791, *8 (Mahoning Cty. 1996) (demonstrative evidence admissible where it is substantially similar to that which it is intended to represent).
[11] *In the Matter of A.H.*, 2015-Ohio-2174, ¶ 54 (Clark Cty. 2015) (internal citations omitted).
[12] *Leichtmamer v. American Motors Corp.*, (1981), 67 Ohio St.2d 456, 473, 424 N.E.2d 568 (dissimilarity of demonstrative evidence "goes to the weight, not the admissibility of evidence").

Commission, as the Attorney Examiner observed during the evidentiary hearing.[13] And there is clearly no risk of confusing the issues or misleading the Commission, especially given the fact that the OCC was provided an opportunity to engage in cross examination in respect of the obsolete service lines. Further, to strike such evidence now would only create confusion in the record, thereby prejudicing Duke Energy Ohio. As the evidence in this proceeding confirms, counsel for the OCC and Staff examined Company witness Gary J. Hebbeler as to the physical evidence; the obsolete, corroded service lines.[14] Well after several exchanges for which no objections were lodged, counsel for Staff finally claimed opposition to the references and only then did counsel for the OCC voice any concern.[15] But with the uncontested references already in the record, such opposition is untimely. And precluding the Commission from viewing the very service lines about which counsel actively engaged in cross examination is blatantly improper and prejudicial.

B. The OCC's Reference to Materials Outside the Evidentiary Record is Improper and Such References Must be Stricken.

The OCC's insistence, in this proceeding, that court rules be strictly followed rings hollow. Throughout its Merit Brief, the OCC mocks the rules of practice and relies upon documents that were not admitted into the record in this case and for which Duke Energy Ohio was thus deprived of the right to engage in witness examination. For example, the OCC references, as if controlling authority here, literature issued by the surgeon general and the U.S. Department of Health and Human Services.[16] It relies upon incomplete and incorrectly identified materials issued by the U.S. Department of Transportation (DOT) that the OCC conveniently

[13] Tr. II, at pg. 203.
[14] Tr. I, at pg. 151 and pp. 162-163.
[15] Tr. I, at pp. 163-164.
[16] OCC Merit Brief, at pg. 15 and footnote 72.

failed to introduce during the hearing.[17] None of these documents was introduced into the record in this proceeding. Indeed, the OCC never attempted to authenticate these documents or identify them as prospective evidence and it is wholly improper for the OCC to now claim such documents as authority in this proceeding. These documents are not Commission decisions or case law. They are completely devoid of any evidentiary or persuasive value. And they are not part of the evidentiary record in this proceeding. If the OCC prevails in altering the Commission's rules of practice such that demonstrative evidence is stricken from the record, then every single reference to extraneous information, including all discussion concerning same, must similarly be stricken from the OCC's Merit Brief.[18]

III. DISCUSSION

A. Federal and State Regulations Contemplate Approval of the ASRP.

1. The parties to this proceeding irresponsibly claim that public safety is not worthy of protection.

Buried well within the Merit Briefs of the OCC, Staff, and OPAE is, by far, the most alarming contention. These parties contend that the proposed ASRP is not necessary because the likelihood of service line failure causing harm to a customer is "almost non-existent."[19] Put another way, the OCC, Staff, and OPAE are of the opinion that no detriment will come to those who work or live in southwest Ohio because of obsolete, high-risk service lines that, as the Commission admitted, "have the potential to cause catastrophic damage."[20] Such a position is irresponsible, especially given the physical nature of these obsolete, high-risk service lines.

---

[17] OCC Merit Brief, at pg. 25 and footnote 129; pg. 26 and footnotes 132 and 134; pg. 28 and footnote 144.
[18] Duke Energy Ohio does address the OCC's arguments that are based, in part, on the impermissible documents. In doing so, it does not waive its opposition to those documents.
[19] OCC Merit Brief, at pp. 18-20, 24-26; Staff Merit Brief, at pp. 6-8; OPAE Merit Brief, at pg. 9.
[20] *In the Matter of the Application of Vectren Energy Delivery of Ohio, Inc., for Approval of an Alternative Rate Plan for Continuation of its Distribution Replacement Rider*, Case No. 13-1571-GA-ALT, Opinion and Order, at pg. 29 (February 19, 2014).

The OCC, Staff, and OPAE hope to convince the Commission that there is no need for the ASRP because it is unlikely that obsolete, unprotected service lines susceptible to corrosion will fail. Staff contends that the risk of such a failure equates to a 1 in 11.9 million chance.[21] But as was demonstrated during witness examination, Staff's calculations were wrong. Indeed, the Attorney Examiner quickly appreciated the lack of credibility associated with Staff's probability analysis, noting that it failed to "control for differences in each utility's system to account for different state jurisdictions, different programs that each utility has before you could find a more accurate number based on that utility[.]"[22] And even Staff's witness admitted that his selective analysis failed to consider information specific to Duke Energy Ohio's service territory.[23]

Importantly, an accurate assessment was conducted by Duke Energy Ohio. As Company witness Edward A. McGee explained, examining risks across the nation is immaterial to the Company's need to accelerate the replacement of high-risk service lines in its area. Rather, the correct assessment concerns the likelihood of a service line failure happening in the Duke Energy Ohio service territory.[24] And that risk is one in twenty-nine – a risk that perpetuates year after year after year.[25] Although the OCC, Staff, and OPAE may be comfortable with a broader, irrelevant risk analysis, Duke Energy Ohio is not so imprudent as to rely on inapplicable analyses in advancing the safety of its customers, its employees, and the general public in southwest Ohio.[26] Nor should the Commission.

Also alarming is the view held by both the OCC and Staff that a damaging incident caused by the failure of an obsolete or unprotected metallic service line is inconsequential. Remarkably, both the OCC and Staff admitted that they would continue to oppose the need for

[21] Staff Exhibit 3 (Direct Testimony of Kerry Adkins), at pg. 14.
[22] Tr. II, at pg. 297.
[23] Tr. III, at pp. 540-541.
[24] Duke Energy Ohio Exhibit 9 (Direct Testimony of Edward A. McGee), at pg. 21.
[25] Tr. II, at pp. 275-276.
[26] Tr. I, at pg. 14.

an accelerated, coordinated replacement of obsolete, high-risk service lines if a catastrophic incident involving such a service line occurred.[27] Thus, although Staff admits that public safety is furthered by avoiding an incident on a natural gas service line that transports combustible material,[28] it is actually indifferent to ensuring public safety and to realizing the Commission's Mission Statement, which includes assuring all customers access to adequate, safe, and reliable service. The OCC believes that damages exceeding a significant monetary threshold must first be inflicted before it could even consider the replacement of high-risk pipe.[29] These reckless positions cannot be adopted – they run afoul of pipeline regulation, the Commission's stated Mission and its expectation, and common sense.

2. The parties to this proceeding lack a proficient understanding of federal pipeline safety regulation.

The OCC carelessly posits that the Commission should ignore directives from the federal government, trivializing their significance and disregarding the relationship between federal and state regulators in respect of pipeline safety.

In attempting to divert the Commission's attention away from these directives, the OCC relies primarily upon the testimony of Staff's only witness in this proceeding. Specifically, the OCC claims, as if persuasive, that Staff's witness "was not even aware of the letter, White Paper, or 'Call to Action.'"[30] The OCC continues that Staff's lone witness "was not even aware that PHMSA had made a determination regarding certain pipes being 'high-risk.'"[31] Both Staff's unawareness and the OCC's reliance on same are troubling.

The Commission is responsible for enforcing PHMSA's regulations. And this partnership is confirmed in state law, which allows the Commission, in protecting public safety, to accept

[27] Tr. III, at pg. 612; Tr. II, at pp. 394-396.
[28] Tr. III, at pg. 584.
[29] Tr. II, at pp. 394-396.
[30] OCC Merit Brief, at pg. 15.
[31] OCC Merit Brief, at pg. 15.

funds from the federal government to carry out the federal Natural Gas Pipeline Safety Act and enforce the pipeline safety code, including the DIMP regulations.[32] Staff's sole witness in this proceeding, Kerry Adkins, did understand the obligations of the Commission in respect of ensuring adherence to federal regulation.[33] But that was the extent of his understanding. Mr. Adkins is not responsible for enforcing DIMP requirements or the DOT's pipeline safety requirements.[34] He admitted that he is "not familiar enough" with Ohio's pipeline safety code to even know what it says.[35] Although he was identified by Staff as the *only* witness to support the entirety of the Staff Report, including those portions specific to pipeline safety, Mr. Adkins possessed admittedly limited knowledge of federal pipeline safety regulations. He further conceded that this limited knowledge was derived simply from what other people may have told him.[36] He admitted that he did not know enough about documents issued by PHMSA "to dispute or agree with them."[37] With regard to the Call to Action, Staff's witness claimed not to have known about it until the hearing and further denied that it was even mentioned in the Company's Application.[38] That Staff chose to ignore the Call to Action clearly referenced in the Company's Application or chose to offer a witness unfamiliar with pipeline safety regulations does not render directives related to those regulations inconsequential. It merely renders questionable the reliability of Staff's witness.

The OCC further attempts to minimize former DOT Secretary Ray LaHood's Call to Action by suggesting that the government simply cannot abide by every call to action that is

[32] R.C. 4905.91. See also, O.A.C. 4901:1-16(O), defining the Natural Gas Pipeline Safety Act to include 49 C.F.R. 192.
[33] Tr. III, at pp. 526-527, 555.
[34] Tr. III, at pg. 518.
[35] Tr. III, at pg. 521.
[36] Tr. III, at pp. 529-530.
[37] Tr. III, at pg. 531.
[38] Tr. III, at pp. 530, 532. See also Duke Energy Ohio Exhibit 1 (Application), at pg. 1 and footnote 1.

issued.[39] This contention is a sad reflection of the OCC's lack of concern for the safety of Duke Energy Ohio's natural gas customers. In his Call to Action, Secretary LaHood was not asking regulators and pipeline operators to take walks, stand up every thirty minutes, or eat more vegetables. Secretary LaHood was identifying a real threat, hidden below city streets and in the front yards of homes, and urging those involved in pipeline operation and its oversight to help eliminate the threat. He was responding to horribly tragic incidents that resulted in significant losses.[40] Under his urging, PHMSA implored the states' regulators to enable the accelerated replacement of risky infrastructure and to remove known high-risk pipes, including service lines. Even the Commission appreciates the risks presented by obsolete, buried natural gas infrastructure and that the prudent course is to remove such risks before imminent hazards materialize.[41] The directives from the federal government do, in fact, urge the accelerated removal of high-risk pipes, including service lines.[42] As proven by Duke Energy Ohio, the proposed ASRP is consistent with these important directives.

3. The parties to this proceeding lack a proficient understanding of DIMP regulations.

The OCC also contends that the Company's proposed ASRP should be rejected because DIMP regulations do not expressly require it to replace obsolete, unprotected metallic service lines that have been classified by PHMSA as high risk.[43] Staff and OPAE assert similar contentions.[44] Again, these parties miscomprehend the law.

---

[39] OCC Merit Brief, at pg. 15.
[40] Duke Energy Ohio Exhibit 9, Attachment EAM-2, at pg. 31 (recent pipeline accidents "resulted in fourteen fatalities, thirty-three injuries, thirty-eight homes destroyed, and over two million dollars in other property damage").
[41] *In the Matter of the Application of Vectren Energy Delivery of Ohio, Inc., for Approval of an Alternative Rate Plan for Continuation of its Distribution Replacement Rider*, Case No. 13-1571-GA-ALT, Opinion and Order, at pg. 16 (February 19, 2014).
[42] Duke Energy Ohio Exhibit 10 (Appendix C to Direct Testimony of Edward A. McGee, Whitepaper), at pp. 1, 5.
[43] OCC Merit Brief, at pp. 12-14.
[44] Staff Merit Brief, at pp. 4-5; OPAE Merit Brief, at pp. 11-12.

The Natural Gas Pipeline Safety Act, promulgated in 1968, authorized the DOT to regulate the pipeline transportation of natural gas. Within the DOT, PHMSA oversees the safety of gas pipelines and, in respect of pipeline safety, has codified *minimum* safety standards under 49 C.F.R. Part 192.[45] And given the relationship between federal and state regulators and applicable jurisdiction, these minimum safety standards cannot be prescriptive.

Interstate pipelines are directly regulated by PHMSA; however, intrastate pipelines prompt state involvement. Ohio, like most other states in the nation, "is responsible for the inspection and enforcement of state pipeline safety laws for the natural gas pipeline systems within" its borders.[46] Importantly, therefore, PHMSA has not, under the auspices of federal regulation, preempted state authority to impose more stringent pipeline safety laws. This interaction between federal and state regulators is aptly demonstrated in federal law. For example, under the Pipeline Safety Improvement Act of 2002, the federal government implemented a program for transmission pipelines "with nationally uniform *minimal* standards and with enforcement administered through a Federal-State partnership."[47] This act preserved the right of state authorities to adopt, under certain conditions, additional or more stringent safety standards for intrastate facilities.[48]

Similarly, when PHMSA expanded its focus to distribution systems, it prescribed *minimum* requirements for distribution integrity management programs.[49] Such requirements include the obligation of a gas distribution operator to adopt an integrity management program that would "ensure the integrity of its gas distribution system."[50] It is undisputed that the DIMP

---

[45] 49 C.F.R. Subtitle B, Chapter I, Subchapter D, Part 192, "Transportation of Natural and Other Gas by Pipeline: Minimum Safety Standards.
[46] Duke Energy Ohio Exhibit 10, at pg. 1.
[47] 49 U.S.C. § 60102(a)(1)(emphasis added).
[48] 49 U.S.C. §§ 60104(c) and 60105.
[49] 74 FR 63934 (December 4, 2009)(emphasis added).
[50] 74 FR 63934.

regulations also "impose upon the Company an obligation to continuously evaluate the risks associated with its distribution system and to maintain and improve its safety and performance.[51]

Significantly, PHMSA's DIMP regulations are intended to recognize the active nature of the natural gas industry and the dynamic environment in which that industry exists. For example, under the DIMP regulations, a gas distribution operator must continually assess the risks on its system, monitor the effectiveness of its program, and refine and improve its program as needed.[52] The federal DIMP regulations further require a gas distribution operator to understand its system based upon information that is reasonably available. Thus, as information subsequently becomes available, the DIMP is likely to change. It is thus contrary to law and the federal government's intent to suggest, as the OCC, Staff, and OPAE do here, that PHMSA regulations should be so rigid as to have incorporated specific infrastructure replacement programs and that the absence of such detail warrants denial of the proposed ASRP.

PHMSA has established *minimum* requirements, allowing each gas distribution company to assess its respective, individual system and adopt an appropriate DIMP that would ensure the integrity of its system. The Commission, in adopting the federal regulations as part of the state's natural gas pipeline safety code, similarly allows local distribution companies the ability to assess risks on their own systems and adopt appropriate programs to ensure public safety. The level of prescriptiveness suggested by the parties now would destroy the relationship between federal and state regulators and hamper the implementation of appropriate safety measures in an ever-evolving industry in which there is not absolute uniformity among gas distribution companies. It would, to borrow from the OCC, prevent government from properly functioning.

The ASRP is not precluded by PHMSA regulation. Rather, as Duke Energy Ohio established in this proceeding, the ASRP is indeed consistent with DIMP regulations and

[51] Duke Energy Ohio Exhibit 3 (Direct Testimony of John A. Hill, Jr.), at pp. 3-4.
[52] 74 FR 63934.

PHSMA directives concerning obsolete infrastructure. Duke Energy Ohio witness McGee, the only witness in this proceeding with over fifty years of experience in the natural gas industry, independently assessed the considerations for accelerated replacement of service lines under PHMSA regulation. As Mr. McGee observed:

> PHMSA has sent a Call to Action to all pipeline stakeholders, including the National Association of Regulatory Utility Commissioners (NARUC) and its members, and in it specifically called on Public Utility Commissions to establish cost recovery mechanisms that effectively address infrastructure. ...Included is an overview of natural gas ratemaking, a discussion of the need to take prompt action to remediate high-risk pipeline infrastructure, and a description of the various State programs that are being used for that purpose.
>
> In this document, PHMSA states: 'We believe that the timely repair, rehabilitation, and replacement of high-risk gas pipeline infrastructure are critical to ensuring public safety. A series of recent gas pipeline accidents, including the September 9, 2010, San Bruno, California accident, the January 19, 2011 Philadelphia, Pennsylvania accident, and the February 10, 2011 accident, show the terrible loss of life and property that can occur without adequate attention to the integrity of pipeline infrastructure. PHMSA believes that an effective program for ensuring the timely rehabilitation, repair, or replacement of high-risk gas pipelines might have helped prevent these accidents.'
>
> PHMSA often uses the term "high-risk" pipeline segments or infrastructure when describing its replacement targets. ...It is critically important to define and understand the term "*high-risk*" to clarify the objectives that PHMSA and the public would want – and the PUCO would support – for the ASRP proposed by Duke Energy. PHMSA's definition of "high-risk" pipe...is piping or equipment that is no longer fit for service. ...[53]

As Mr. McGee further testified, PHMSA has explained that such lack of fitness for service is found in:

- Cast iron mains and service lines.
- Certain vintages of plastic pipe.
- Mechanical coupling installations.
- Pipelines without adequate installation records.
- Installations of bare steel pipe without adequate corrosion control and copper piping.
- Older pipe.[54]

[53] Duke Energy Ohio Exhibit 9, Attachment EAM-2, at pp. 31-32.
[54] Id, at pg. 32.

Evaluating the service lines in the Duke Energy Ohio service territory intended for replacement under the ASRP, the one witness having the most experience with pipeline safety observed that those service lines meet five of the six criteria for high-risk pipe.[55] And the high-risk service lines in the Duke Energy Ohio service territory are a real threat. As Mr. McGee further confirmed, "the number of service line leaks, especially the number of hazardous service line leaks, has far exceeded the number of leaks on mains in recent years. Also, service leaks caused by factors such as corrosion or materials and welds have not been declining as expected, throughout the AMRP."[56] As Mr. McGee concluded, the accelerated removal of high-risk service lines is indeed expected under DIMP regulations.

4. The parties to this proceeding lack an accurate understanding of compliance with DIMP regulations.

The OCC maintains that the ASRP is not needed because Duke Energy Ohio is currently in compliance with the state's minimum pipeline safety standards and its DIMP obligations because it treats grade three leaks as grade two leaks. Such a conclusion reflects a significant misunderstanding of DIMP regulations.

Pipeline infrastructure can leak. But PHMSA did not enact its DIMP regulations because of leaks. Rather, the DIMP regulations are directed to the "replacement of materials that could have problems in the future. Leaks are only an indication of the bad materials."[57] As confirmed by every party in this proceeding, the DIMP regulations pertain to *risk* identification and *risk* mitigation. And through its methodical relative risk model, Duke Energy Ohio has determined that the second highest risk on its distribution system is corrosion leaks, with the majority of those leaks occurring on service lines.[58] And it is because of the material of which these service

[55] Id, at pg. 33.
[56] Duke Energy Ohio Exhibit 9, at pp. 28-29.
[57] Tr. II, at pp. 290-291.
[58] Duke Energy Ohio Exhibit 3, at pp. 3, 7.

lines are constructed that they need to be proactively replaced.[59] Reacting to service line leaks due to corrosion or reclassifying those leaks does not mitigate the risk created by the existence of buried service lines that are more susceptible to failing; it is merely a response to a failure.

The OCC's contention that the status quo is acceptable ignores both the success of the AMRP and its rapidly approaching conclusion. It is undisputed that the AMRP has resulted in an overall reduction in leaks on mains in the Duke Energy Ohio service territory.[60] The scope of that program included, as a safety element,[61] the replacement of pre-1971 and other unprotected metallic service lines, including those that were not leaking. And it must now be accepted that those replacements prevented catastrophic incidents over the last fifteen years. But with the AMRP's conclusion will come the end of the accelerated, proactive replacement, on an annual basis, of approximately 6,000 to 8,000 obsolete, high-risk service lines. And if the Company merely adopts a reactive approach, responding to discovered leaks in these obsolete service lines, public safety will not be advanced. Indeed, leak rates on service lines are expected to increase after the AMRP concludes next week and, as the evidence in this proceeding confirms, deterioration rates are already exceeding replacement rates.[62] Additionally, accepting the OCC's reactive approach to risky service lines does not comply with DIMP requirements, as the Company will not have addressed a confirmed threat to its system, and it undermines the Commission's expectation that a known safety threat be systematically replaced before imminent harm occurs.[63]

---

[59] Tr. II, at pg. 236.
[60] Duke Energy Ohio Exhibit 2 (Direct Testimony of Charles R. Whitlock), at pg. 5; Duke Energy Ohio Exhibit 3, at pg. 6; Duke Energy Ohio Exhibit 6 (Direct Testimony of Gary J. Hebbeler), at pg. 11.
[61] Tr. III, at pg. 549; Duke Energy Ohio Exhibit 6, at pg. 5.
[62] Duke Energy Ohio Exhibit 9, at pg.11.
[63] *In the Matter of the Application of Vectren Energy Delivery of Ohio, Inc., for Approval of an Alternative Rate Plan for Continuation of its Distribution Replacement Rider*, Case No. 13-1571-GA-ALT, Opinion and Order, at pg. 16 (February 19, 2014).

5. The parties to this proceeding fail to accept that DIMP regulations contemplate attention to *all* risks on the distribution system.

The OCC, Staff, and OPAE also believe that Duke Energy Ohio should focus its efforts only on the highest risk confronting its natural gas distribution system – excavation damage.[64] In fact, Staff actually argues that before "considering the ASRP, the Commission should first require Duke to take measures to reduce risks to its system from excavation damage."[65] But in advancing this argument, Staff is admittedly uninformed as to the efforts the Company has already implemented in respect of excavation damage and the decline in incidents as a result thereof. Indeed, while criticizing Duke Energy Ohio for failing to address excavation damage, Staff witness Adkins acknowledged that he did not review the direct testimony of Duke Energy Ohio witness John A. Hill, Jr., prior to forming this opinion.[66] And had Mr. Adkins actually reviewed the testimony available to him, he would have learned that the Company has implemented several measures to mitigate the risk associated with excavation damage; measures that include public awareness programs, training for contractors that work near gas facilities, community outreach initiatives, participation in seminars for excavators and emergency responders, and engagement in legislative reform.[67] And through these efforts, the number of incidents or leaks due to third-party excavation has declined over the last several years.[68]

Moreover, these beliefs espoused by the parties are admittedly inconsistent with DIMP compliance. As Staff witness Adkins conceded, the DIMP regulations do not dictate any particular cadence to compliance.[69] They do not preclude a gas distribution company from addressing more than one risk at a time. They are not prescriptive and, as such, it is incorrect to conclude that the ASRP is prohibited because Duke Energy Ohio is restricted to addressing

[64] OCC Merit Brief, at pp. 29-30; Staff Merit Brief, at pp. 7-8; OPAE Merit Brief, at pg. 7.
[65] Staff Merit Brief, at pp. 7-8.
[66] Tr. III, at p. 587.
[67] Duke Energy Ohio Exhibit 3, at pg. 13.
[68] Id, at pg. 14.
[69] Tr. III, at pg. 606.

another risk. And as confirmed by the undisputed evidence in this proceeding, the Company is already focusing on the risks associated with third-party excavation damage, as required by its DIMP. There is nothing further for the Commission to require in this regard.

6. The parties to this proceeding lack an accurate understanding of the requirements for approval of an alternative rate plan under Ohio law.

The OCC and Staff contend that the Company's request to eliminate a known safety risk does not meet the requisite conditions for approval of an alternative rate plan. In doing so, they misconstrue the foundational requirements for approval. Specific to the OCC, it maintains that the Company's proposal must fail because it does not satisfy *one* aspect of state policy as set forth in R.C. 4929.02(A).[70] Staff and OPAE similarly point to isolated policy provisions and contend that the ASRP does not advance same.[71] But this is not the test.

Ohio law unambiguously provides that the proposed ASRP *must* be approved if Duke Energy Ohio has demonstrated compliance with the following three criteria:

- Current compliance with R.C. 4905.35 and current *substantial* compliance with R.C. 4929.02.
- *Substantial* compliance with R.C. 4929.02 after approval of the alternative rate plan.
- The alternative rate plan is just and reasonable.

The law does not render approval of an alternative rate plan contingent upon future, absolute compliance with state policy and it is thus improper to inject such criteria into the statutory framework.[72]

The OCC further misconstrues the law, contending that, because the policy of the state does not explicitly demand replacement of obsolete, high-risk service lines, the Company's

[70] OCC Merit Brief, at pg. 10.
[71] Staff Merit Brief, at pg. 4; OPAE Merit Brief, at pg. 13.
[72] See, *e.g.*, *Columbus-Suburban Coach Lines, Inc. v. Public Utilities Commission of Ohio*, (1969), 20 Ohio St.2d 125, 127, 254 N.E.2d 8. ("In determining legislative intent it is the duty of this court to give effect to the words used, not to delete words used or to insert words not used.") See also, *Wheeling Steel Corp. v. Porterfield*, (1970), 24 Ohio St.2d 24, 27, 263 N.E.2d 249 (observing that, had the General Assembly intended a certain requirement, it would have written it into the statute).

Application must be denied.[73] But state policy is not, and should not be, so rigid. Indeed, if the General Assembly had intended to implement inflexible and exacting mandates for natural gas companies, it would have done so through appropriate language. It would not have provided the Commission with discretion to ascertain whether, after certain investments made or replacement programs undertaken, the local distribution company was in substantial compliance with state policy. But as the Ohio Supreme Court has confirmed, the General Assembly was not so dogmatic.[74] Rather, the legislature "left it to the commission to determine how best to carry out the state's policy goals... ."[75]

As confirmed by the evidence in this proceeding, Duke Energy Ohio is and will remain in substantial compliance with state policy after approval of its proposed ASRP. In addition to adherence to other policy goals, the ASRP does "facilitate the state's effectiveness in the global economy."[76] Through the ASRP, the Company will engage contractors to assist in the coordinated, efficient replacement of obsolete, high-risk service lines in Ohio.[77] It will result in the installation of modern infrastructure to continue to serve homes and businesses in Ohio, consistent with the Commission's Mission of "promoting utility infrastructure investment through appropriate regulatory policies and structures."[78] And, importantly, the Commission will retain its position in the forefront of pipeline safety.[79]

---

[73] OCC Merit Brief, at pg. 10.
[74] *Ohio Partners for Affordable Energy v. Public Utilities Commission of Ohio* 115 Ohio St.3d 208, 2007-Ohio-4790, ¶27. ("The policy established in R.C. 4929.02(A)(4) is a guideline for the commission to consider... .") See also, *Ohio Office of Consumers' Counsel v. Public Utilities Commission of Ohio*, 125 Ohio St.3d 57, 2010-Ohio-134, ¶40 (confirmed that the Commission is vested with broad discretion where "a statute does not prescribe a particular formula"); *In re Application of Columbus Southern Power Company*, 128 Ohio St.3d 512, 2011-Ohio-1788, ¶62 (recognizing that state policy "does not *require* anything")(emphasis in original).
[75] *Ohio Office of Consumers' Counsel v. Public Utilities Commission of Ohio*, 125 Ohio St.3d 57, 2010-Ohio-134, ¶40.
[76] R.C. 4929.02(A)(10).
[77] Duke Energy Ohio Exhibit 6, at pg. 15.
[78] Id, at pg. 10. See also, PUCO Mission.
[79] Duke Energy Ohio Exhibit 10, at pp. 6-17 (review of various state legislation and regulatory structures indicates that Ohio was frontrunner in approving accelerated replacement programs, with the approval of Duke Energy Ohio's AMRP in 2000).

7. The parties to this proceeding lack an accurate understanding of state policy and the deference afforded the Commission's in respect of that policy.

The OCC continues with its unrealistic and incorrect interpretation of Ohio law, arguing that H.B. 95 does not compel the accelerated replacement of obsolete service lines.[80] Staff offers a similarly misguided refrain.[81] And, again, the OCC and Staff ignore all precedent in respect of utility regulation. As the Ohio Supreme Court has repeatedly confirmed, "[w]hen a statute does not prescribe a particular formula, the PUCO is vested with broad discretion."[82] Accordingly, it is patently incorrect to conclude, as the parties do here, that the Company's proposed ASRP must be rejected because H.B. 95 does not expressly demand the accelerated replacement of risky service lines.

H.B. 95 modified the process by which companies request and the Commission approves alternative rate plans.[83] Importantly, through these amendments, the General Assembly expressly authorized local distribution companies such as Duke Energy Ohio to pursue an alternative rate plan outside of a base rate case, thereby articulating its expectation that such plans could be more efficiently pursued. And the legislature removed, as criteria for approval, the determination of whether resulting rates were just and reasonable, thereby conveying its expectation that the Commission focus on the purpose of the plan. The relevant inquiry is not, as the OCC and Staff suggest, whether a provision of Ohio law requires the specific proposal as offered by the Company. If that were true, regulatory practice as it currently exists in the state of Ohio would be upended – the Commission would be stripped of its broad, rate-making authority; the expertise held by the Commission would be for naught, as it would have no discretion to assess the

[80] OCC Merit Brief, at pg. 11.
[81] Staff Merit Brief, at pg. 4.
[82] *Payphone Association of Ohio v. Public Utilities Commission of Ohio*, 109 Ohio St.3d 453, 2006-Ohio-2988, ¶ 25, citing, *City of Columbus v. Public Utilities Commission of Ohio*, (1984), 10 Ohio St. 3d 23, 24, 460 N.E.2d 1117. See also, *Ohio Office of Consumers' Counsel v. Public Utilities Commission of Ohio*, 125 Ohio St.3d 57, 2010-Ohio-134, ¶40.
[83] Duke Energy Ohio Merit Brief, at pp. 8-9.

justness and reasonableness of any request; and the Commission's status as an independent body would end. In short, the Commission would simply become an administrative arm of the General Assembly, idly carrying out the legislators' mandates. But this is not the law in Ohio[84] and the OCC's and Staff's efforts to transform that law now must be rejected.

B. The Company has Demonstrated the Need for the Accelerated Replacement of Obsolete, High-Risk Service Lines.

Duke Energy Ohio's natural gas distribution system is safe today. And the Company has been able to efficiently maintain a safe and reliable system through programs such as its AMRP and its leak detection programs.[85] But in a matter of days, the AMRP will conclude and the Company will not be proactively replacing service lines, including non-leaking service lines that were installed before 1971 or that are otherwise comprised of unprotected metallic, at a level commensurate with that under the AMRP. And the consequences of the decelerating replacement of these obsolete service lines are already becoming evident. Indeed, as confirmed by Duke Energy Ohio witness Hebbeler, the deterioration rate on service lines is already starting to exceed the leak rate.[86] Leaks on services lines due to corrosion – both Grade I and Grade II – are increasing. Significantly, from 2012 to 2014, Grade I leaks due to corrosion increased from 6.9 percent to 11:8 percent and Grade II leaks increased from 24.3 percent to 43.6 percent.[87] And they are expected to increase.[88] As Mr. McGee confirmed, "the company has been conducting a mains replacement program which includes replacement of service lines, and from this, I would

---

[84] See, *e.g.*, *Weiss v. Public Utilities Commission of Ohio*, 90 Ohio St.3d 15, 17-18, 2000-Ohio-5. ("Due deference should be given to statutory interpretations by an agency that has accumulated substantial expertise and to which the General Assembly has delegated enforcement responsibility.") See also, *Migden-Ostrander, Ohio Consumers' Counsel v. Public Utilities Commission of Ohio*, 102 Ohio St.3d 451, ¶ 23, 2004-Ohio-3924 (acknowledging Commission's expertise and giving its statutory interpretation due deference); *Constellation NewEnergy, Inc. v. Public Utilities Commission of Ohio*, 104 Ohio St.3d 530, 2004-Ohio-6767, ¶ 51, overruled, in part, on other grounds and followed by *Ohio Consumers' Counsel v. Public Utilities Commission of Ohio*, 111 Ohio St.3d 300, 2006-Ohio-5789.

[85] Tr. I, at pp. 99-100, and at pp. 151-152. See also, Tr. II, at pp. 221-222.

[86] Duke Energy Ohio Exhibit 6, at pg. 12. *See also* Tr. I, at pg. 165.

[87] Duke Energy Ohio Exhibit 4 (Discovery Responses to OCC Second Set of Interrogatories).

[88] Tr. II, at pg. 278.

have expected certain causes – the number of certain causes of leaks to decline. They have not necessarily declined… . In spite of the mains replacement program, corrosion is continuing."[89]

The parties challenge the need for the program, contending that pinhole leaks in service lines are not problematic and that obsolete, corroded service lines can simply be repaired.[90] But this conclusion is incorrect. As Duke Energy Ohio witness McGee explained, the risk of corrosion affects all of the approximate 58,000 service lines intended for inclusion in the ASRP.[91] To the extent a failure, or leak, due to corrosion is detected on a service line, industry practice is to replace that service line.[92]

The OCC suggests that the service line leaks are not cause for concern because of operating pressure.[93] Although the OCC is correct in concluding that service lines operate at the same pressure as the mains to which they are attached, it ignores the uncontroverted evidence in this case that service line risks exceed risks on mains in five critical areas. Service lines:

- Duke Energy Ohio's system were found to have higher leaks;
- have higher numbers of hazardous leaks;
- are closer to buildings and their occupants;
- can have incomplete records of age and material type; and
- have thinner pipe wall than mains, which makes them more susceptible to corrosion pits penetrating through the wall.[94]

Further, the OCC patently ignores the fact that the Company's relative risk model incorporates criteria such as operating pressure.[95] And with that criteria, the risk due to corrosion is the second highest risk on Duke Energy Ohio's natural gas distribution system. The OCC further criticizes the Company's proposal, contending that it does not include the same level of

[89] Tr. II, at pg. 263.
[90] See, *e.g.*, OCC Merit Brief, at pp. 18-19, 27.
[91] Tr. II, at pg. 213.
[92] Tr. II, at pg. 216.
[93] OCC Merit Brief, at pg. 18.
[94] Duke Energy Ohio Exhibit 9, at pg. 5.
[95] Duke Energy Ohio Exhibit 3, Attachment JAH-1, at pp. 2-3.

detail as that provided in respect of its request for the AMRP.[96] This criticism is misplaced. As an initial matter, the Stone and Webster Report was not admitted into the record in this proceeding and it is thus improper for the OCC to attempt to enlarge that closed record with extraneous documents. However, assuming the Commission to allow such inappropriate references, Duke Energy Ohio observes that the replacement of all bare steel and cast iron service lines, regardless of the connected main material, was recommended in the Stone and Webster Report, a report that was promulgated long before DIMP regulations were enacted or PHMSA urged the removal of high-risk pipe. And Duke Energy Ohio further notes that, in 2001, its proposed replacement rate for service lines was deemed too conservative and a more aggressive rate was recommended.[97] Moreover, the proponent of the Stone and Webster Report confirmed that not replacing obsolete service lines would leave unabated the risks associated with those service lines.[98] And unlike Staff, which recommended approval of the AMRP, the OCC opposed the proactive replacement of obsolete pipe, preferring instead that the Company simply react to failures.[99] But the OCC's opposition has undeniably been proven wrong, given the admitted benefits of the AMRP, which has been largely replicated by every other local distribution company in Ohio and more recently recognized by PHMSA, and consumer advocate support for an ASRP in the Commonwealth of Kentucky.[100]

The Company now intends to build upon its successful execution of the AMRP to continue the accelerated replacement, annually, of about 5,000 to 6,000 obsolete, high-risk

---

[96] OCC Merit Brief, at pp. 20-22.
[97] *In the Matter of the Application of the Cincinnati Gas & Electric Company for an Increase in its Gas Rates in its Service Territory*, Case No. 01-1228-GA-AIR, *et al.*, Stone and Webster Report, at Section11, at pg. 2, Section 16, at pp. 1-2.
[98] Id, Direct Testimony of Sevket Torpis, at pg. 14.
[99] Id, Direct Testimony of Scott J. Rubin.
[100] *In the Matter of the Application of Duke Energy Kentucky, Inc., for a Certificate of Public Convenience and Necessity Authorizing the Implementation of an Accelerated Service Line Replacement Program, Approval of Ownership of Service Lines, and a Gas Pipeline Replacement Surcharge*, Case No. 2015-00210, Stipulation and Recommendation (December 18, 2015).

service lines. But the OCC continues to complain about infrastructure replacement, now attempting to portray the Lummus Report as deficient because it did not "provide any information specific to the actual number of leaks…that have occurred on the 58,000 pre-1971 metallic and non-protected service lines that Duke proposes to replace under the ASRP… ."[101] In other words, the OCC believes that Duke Energy Ohio should currently possess information on whether all or any of these service lines have leaked. This statement demonstrates the OCC's misunderstanding of Duke Energy Ohio's current operations and its proposed ASRP. If any one of the approximate 58,000 service lines intended for inclusion in the ASRP were previously discovered to have been leaking, it would have been replaced given its characteristics, the Company's DIMP, and the established industry of replacing corroded service lines. The OCC also wrongly complains that Duke Energy Ohio did not provide detail specific to the 21,000 service lines for which it proposes to gather additional information.[102] The Company does not own these curb-to-meter service lines and, as such, it does not have complete or reliable data about them. It is through the ASRP that such information will be obtained and, again, the OCC misunderstands the proposal at issue here.

In addition to these errors, the OCC fails to appreciate procedural and regulatory requirements. The Company's Application was submitted pursuant to R.C. 4929.01, as revised by H.B. 95, and related Commission regulation. And the filing was deemed compliant with the applicable filing requirements.[103] Thus, the Commission could have approved the Application without a hearing. Here, however, the Commission, through its Attorney Examiner, scheduled a hearing and, in connection therewith, established deadlines for the submission of written

[101] OCC Merit Brief, at pg. 21.
[102] OCC Merit Brief, at pg. 21.
[103] Entry (March 18, 2015).

testimony.[104] Thereafter, the record of this proceeding was fully developed over three days of hearing. This evidentiary information collectively supports the Company's request. That the Lummus Report was provided after the Application was filed is immaterial as the Commission will render its decision based upon the record – a record that includes testimony as to the lack of decline in service line leaks; a record that confirms that the ASRP is contemplated under DIMP regulations; a record that undeniably establishes leaks due to corrosion as the second highest risk on the Company's distribution system; and record that clearly confirms the desire of federal regulations to accelerate the removal of high-risk pipe. Through the cumulative evidentiary record in this proceeding, Duke Energy Ohio has demonstrated the need for its ASRP.

C. Neither State Law Nor Commission Regulation Mandates the Evaluation of Alternatives or a Cost/Benefit Analysis.

The OCC, Staff, and OPAE argue that the Company's proposed ASRP must be denied because, in their view, Duke Energy Ohio did not consider alternatives or conduct a cost/benefit analysis.[105] But their arguments are incorrect. As an initial matter, the fundamental question resulting from the H.B. 95 amendments to R.C. 4929.05 is whether the proposed ASRP is just and reasonable.[106] The question is not whether the resulting rates are just and reasonable, as the General Assembly removed that issue from the Commission's consideration. The question also is not whether the Company has evaluated its proposal against dissimilar, reactive approaches to incident response.

Significantly, in implementing the filing requirements for an alternative rate plan under R.C. 4929.05, the Commission did not require applicants to compare and contrast possible options. Rather, with regard to substantive requirements, the Commission instructed applicants to submit testimony in support of their request, detail the facts and grounds on which the

[104] Entry, at pg. 3 (August 28, 2015).
[105] OCC Merit Brief, at pp. 31-35; Staff Merit Brief, at pp. 8-11; OPAE Merit Brief, at pg. 12.
[106] The Company has demonstrated conformity with R.C. 4905.35 and R.C. 4929.02.

application is based, and demonstrate how the alternative rate plan is just and reasonable.[107] The Commission did not further require an evaluation of every possible alterative that could be imagined. Moreover, as these filing requirements have been applied, the Commission has not denied a request for an alternative rate plan because the application failed to address possible alternatives or include a cost/benefit analysis.[108] As the law instructs and prior Commission decisions confirm, the Commission is capable of evaluating the justness and reasonableness of a proposal, such as the ASRP, based on the merits of that proposal. And as neither prevailing law nor administrative regulation requires the analyses as demanded by the OCC and Staff here, their demands must be ignored.

The Company has demonstrated the justness and reasonableness of its proposal to, upon the expiration of the AMRP, enable the continued replacement of obsolete service lines on an accelerated basis using a structure that has proven successful and that serves as an underlying basis for other infrastructure replacement programs throughout the state. Duke Energy Ohio has established that, in the absence of coordinated efficient programs such as the proposed ASRP, customers will be exposed to more frequent base rate proceedings and additional costs; such costs which may exceed the proposed ASRP by tens of millions of dollars. Further, absent the ASRP, customers will be deprived of the benefit of avoiding future costs that are certain to be

[107] O.A.C. 4901:1-19-06(B)(1), (C)(2), and (C)(5).

[108] See, *e.g.*, *In the Matter of the Application of Vectren Energy Delivery of Ohio, Inc., for Authority to Amend its Filed Tariffs to Increase the Rates and Charges for Gas Services and Related Matters,* Case No. 07-1080-GA-AIR, *et al.*, Opinion and Order, at pp. 7, 18 (January 7, 2008)(approving alternative rate plan to accelerate replacement of aging distribution systems); *In the Matter of the Application of The East Ohio Gas d/b/a Dominion East Ohio for Authority to Increase Rates for its Gas Distribution Service*, Case No. 07-829-GA-AIR, *et al.*, Opinion and Order, at pp. 12, 32 (October 15, 2008)(approving alternative rate plan for accelerated infrastructure replacement, which will enhance service and safety). It should be noted that the OCC cites this case as having an order dated October 27, 2015. That is incorrect.

incurred, given DIMP requirements.[109] However, Duke Energy Ohio addresses the shortcomings with the alternatives suggested by Staff and adopted by the OCC.

Staff's first suggestion is that the Company simply continue to replace service lines *after* they have been found to be leaking.[110] The other suggestion is to employ more resources to conduct surveys and potentially discover leaks more quickly.[111] These approaches must be put in their proper context. First, it must be recognized that the proponent of these approaches is not qualified to opine on pipeline safety regulation. Staff witness Adkins admitted that he does not know what Ohio's pipeline safety laws require and is not responsible for overseeing compliance with federal pipeline regulations. He is not versed in PHMSA-related activities, failed to review documents on which the Company's request is based, and is of the misguided belief that it is prudent to continually repair obsolete, corroded, leaking service lines.[112] Next, it must be understood that Staff's approaches would be implemented after the expiration of the AMRP, at a time when Duke Energy Ohio will not be proactively replacing 6,000 to 8,000 obsolete, unprotected steel service lines on an annual basis for admitted safety reasons.[113] And, finally, these approaches are being offered by a party that concedes that "customers benefit from the accelerated replacement of aging infrastructure and that this enhances public safety."[114]

Significantly, neither of these approaches addresses the admitted risk included on the Company's DIMP and neither can be considered an improvement over the current, accelerated replacement of service lines under the AMRP. Thus, neither approach complies with federal DIMP regulations. Further, neither approach can be reconciled with the Commission's expectation that risky infrastructure be replaced before imminent harm occurs. These reactionary

[109] Duke Energy Ohio Exhibit 1, at pg. 9; Duke Energy Ohio Exhibit 2, at pg. 11; Duke Energy Ohio Exhibit 6, at pg. 13.
[110] Staff Merit Brief, at pp. 8-9.
[111] Staff Merit Brief, at pg. 9.
[112] Tr. III, at pp. 518-519, 551-552, 593, 594.
[113] Tr. III, at pg. 549.
[114] Tr. III, at pg. 550.

approaches also fail to account for the fact that, in the Duke Energy Ohio territory, service line leaks due to corrosion are increasing. In contrast to these ill-conceived approaches, Duke Energy Ohio has undertaken proactive measures outside of its current AMRP to replace obsolete, high-risk service lines. The Company intends to continue these replacements, increasing the scope of this DIMP-compliant program when the AMRP ends.[115]

The OCC describes recent clarifications of and refinements to testimony detailing the Company's current practice as a last "ditch effort to rehabilitate" its proposed ASRP.[116] This argument is non-sensical. The corrections and refinements functioned to clarify efforts in which the Company is currently involved and, notably, reduced the scope of the necessary reconnaissance efforts. To claim, as the OCC does here, that corrections should be viewed with skepticism serves to undermine its own testimony in this proceeding as every OCC witness changed his testimony at the evidentiary hearing.[117]

D. Imprecise Rate Comparisons are Irrelevant to the Commission's Consideration of the Proposed ASRP.

The OCC and OPAE attempt to insert rate comparisons into this proceeding, despite the express intentions of the General Assembly to the contrary.[118] And, in improperly doing so, the OCC and OPAE infer that the Company's natural gas rates are already unjust and unreasonable because they are higher than those of the other Ohio local distribution companies. The arguments of the OCC and OPAE are wrong and irrelevant.

In a proceeding – unlike the one here – in which the Commission is actually determining rates, it must fix rates that are just and reasonable.[119] And the Commission has recently

[115] Duke Energy Ohio Exhibit 2, at pp. 12-13; Tr. I, at pg. 40 (Duke Energy Ohio witness Whitlock commits to pursuing internal authority to increase the replacement rate as the risks demand it.)
[116] OCC Merit Brief, at pg. 35.
[117] Tr. II, at pp. 312, 368; Tr. III, at pp. 408-409.
[118] OCC Merit Brief, at pp. 36-38; OPAE Merit Brief, at pg. 13.
[119] R.C. 4909.15.

confirmed that Duke Energy Ohio's current natural gas base rates are just and reasonable.[120] That these rates are higher than those of other companies does not – and cannot – alter that determination. Importantly, the rates charged by one utility are not determinative of the rates charged by another utility. Rather, Ohio's ratemaking formula is much more precise and considers factors specific to the utility under consideration.[121] This approach properly removes the discrepancies that would otherwise exist in an attempt, such as that made by the OCC and OPAE here, to blindly compare rates without an understanding of the various services received by the customers to whom those different rates apply and of the existing regulatory treatment certain to affect future rates. As observed by Duke Energy Ohio witness Charles R. Whitlock, any comparison of rates, should it be attempted, must be done through the appropriate lens.[122] Thus, where there exists a wide disparity between local distribution companies as to the degree to which they have completed infrastructure replacement programs, such disparity cannot be ignored. And using the appropriate lens, it is evident that no other local distribution company is nearing completion of its infrastructure replacement program and that, unlike Duke Energy Ohio, no other local distribution company has had a base rate case proceeding subsequent to implementing its infrastructure replacement program.[123]

---

[120] *In the Matter of the Application of Duke Energy Ohio, Inc. for an Increase in its Natural Gas Distribution Rates*, Case No. 12-1685-GA-AIR, *et al,* Opinion and Order, at pg. 53 (November 13, 2013).
[121] R.C. 4909.15.
[122] Tr. I, at pg. 23.
[123] Duke Energy Ohio Exhibit 9, Attachment EAM-2, at pg. 4 (confirms that other companies' infrastructure replacement programs were more recently approved and for terms longer than the term of Duke Energy Ohio's AMRP); See also, *In the Matter of the Application of The East Ohio Gas Company d/b/a Dominion East Ohio for Approval to Modify and Further Accelerate its Pipeline Infrastructure Replacement Program and to Recover the Associated Costs*, Case No. 11-2401-GA-ALT, Opinion and Order, at pg. 2 (August 30, 2011)(discussing procedural history of company's pipeline infrastructure replacement program); *In the Matter of the Application of Columbia Gas of Ohio, Inc., for Approval of an Alternative Form of Regulation*, Case No. 11-5515-GA-ALT, Opinion and Order, at pg. 2 (discussing procedural history of company's infrastructure replacement program); *In the Matter of the Application of Vectren Energy Delivery of Ohio, Inc., for Approval of an Alternative Form of Regulation*, Case No. 13-1571-GA-ALT, Opinion and Order, at pp. 1-2 (February 19, 2014)(discussing procedural history of company's distribution replacement rider).

E. The Company's Implementation of its ASRP Cannot be Delayed by the Current Programs Administered by Other Local Distribution Companies.

The OCC and Staff seek to convince the Commission to reject the proposed ASRP because no other local distribution company has such a program. This argument is preposterous. What any given company may be doing in respect of mitigating risks on its system and for purposes of DIMP compliance cannot dictate the Commission's assessment of the justness and reasonableness of another company's alternative rate plan. If that were true, Duke Energy Ohio's AMRP could have never been approved in 2000 and the Company would now have to wait almost two decades, until 2033, before it could even consider requesting an ASRP.[124] And this future date assumes Ohio's other local distribution companies are able to complete their current infrastructure replacement programs on time, which is uncertain.[125] Moreover, decades from now, Duke Energy Ohio could, under the parties' view, only pursue its ASRP if every other local distribution company in Ohio was making a similar request. Sitting idle and responding to an increasing level of failures is not what the federal DIMP regulations demand or state law envisioned.

Staff portends that it prefers consistency as between Ohio's local distribution companies.[126] But this notion is false as Staff's recommendations have repudiated that goal. Indeed, although Staff has previously admitted that DIMP regulations require the accelerated risk reduction on the natural gas distribution system, it is now seeking to retreat from that position on the dubious contention that accelerated risk reduction is acceptable only where related costs will be addressed at a later time.[127] And although it has previously recognized the immediate costs

---

[124] Duke Energy Ohio Exhibit 9, Attachment EAM-2, at pg. 13; Tr. III, at pp. 545-547.
[125] *In the Matter of the Application of the East Ohio Gas Company d/b/a Dominion East Ohio for Approval to Modify and Further Accelerate its Pipeline Infrastructure Replacement Program and to Recover the Associated Costs,* Case No. 11-2401-GA-ALT, *Opinion and Order,* at pg. 3 (August 30, 2011) (discussing Dominion East Ohio's claim that the duration of its program would have to be extended by ten years at approved spending levels).
[126] Tr. III, at pg. 568.
[127] Tr. III, at pg. 568 and at pp. 572-574.

associated with programs necessary to enable accelerated risk reduction on the natural gas distribution system and has supported shifting the burden for those costs, it has recanted that support here in favor of rendering Duke Energy Ohio solely responsible for such costs between rate cases.[128] Staff tries to reconcile its internally conflicting positions on the basis that, only where incidents happen, regulatory approvals should follow. But even that attempt is unconvincing as Staff will not the support the proposed ASRP even after a catastrophic failure.[129] Public safety cannot be ensured under the haphazard, inconsistent framework offered by Staff in this proceeding and, importantly, Duke Energy Ohio's customers should not be forced to accept confirmed risks simply because of the changing whims of witnesses inexperienced in pipeline safety regulations.

F. Meter Relocations, as Proposed Here, Will Benefit Customers.

Staff opposes the relocation of interior natural gas meters to suitable exterior locations solely on the basis that the Company should incur the costs associated with inspecting these meters until such costs are subsequently incorporated into base rates.[130] In asserting this contention, however, Staff ignores the ongoing, recoverable costs the Company seeks to avoid through this proposal, as well as the benefits to customers resulting from the intended meter relocation.

It is undeniable that Duke Energy Ohio must conduct triennial inspections of every interior natural gas meter in its service territory. These inspections include both an atmospheric corrosion inspection and a leak survey.[131] Historically, these inspections were performed by meter readers and thus there were no distinct costs for these inspections included in base rates. However, with the status of the Company's grid modernization efforts, the cost reductions for

[128] Tr. III, at pp. 568-570.
[129] Tr. III, at pp. 611-612.
[130] Staff Merit Brief, at pg. 10.
[131] Duke Energy Ohio Exhibit 6, at pg. 8.

which are accounted for in Rider AU, meter readers are not in customers' premises on a regular basis. Furthermore, the DIMP regulations impose record-keeping requirements upon Duke Energy Ohio. Consequently, the Company needed to develop new inspection protocol, which includes a cost element.[132]

To the extent meters are relocated to exterior locations, they are not subject to the triennial atmospheric corrosion inspection and leak survey. And the costs of completing such inspections would necessarily decrease. Thus, in relocating meters, Duke Energy Ohio will enable its customers to avoid future costs – costs that would continue year after year after year. Staff, however, refuses to position the Company's customers for this benefit, adopting the very short-sighted view that Duke Energy Ohio should bear the costs now. Staff's proposal should be rejected, both because it deprives customers of long-term benefits and because it conflicts with Staff's prior positions on this topic. As to the latter point, Staff has supported deferral treatment for natural gas compliance costs for other local distribution companies in the state.[133] It has, therefore, adopted a position completely at odds with what is it proposing here. Thus, to the extent Staff's preference for consistency has any legitimacy, its arguments in this proceeding must be rejected.

Staff also overlooks the identified long-term benefits associated with relocating interior meters – benefits that remove practical limitations and inconveniences. To complete the mandatory inspections, Duke Energy Ohio must gain access to its customers' homes.[134] But this access is not always readily accomplished. Customers understandably have obligations that complicate the scheduling and completion of inspections and there are instances when the

---

[132] Duke Energy Ohio Exhibit 6, at pg. 4; Duke Energy Ohio Exhibit 5 (Direct Testimony of Peggy A. Laub), at pg. 13.

[133] *In the Matter of the Application of Columbia Gas of Ohio, Inc. for Approval to Change Accounting Methods,* Case No. 14-1615-GA-AAM.

[134] Duke Energy Ohio Exhibit 2, at pg. 10 and Duke Energy Ohio Exhibit 6, at pg. 13.

Company cannot gain access, further creating inefficiencies and strained customer relations.[135] Duke Energy Ohio has proposed a targeted, economical approach to reducing both future costs and the need to impose upon customers. Specifically, as explained by Company witness Hebbeler, incorporating the relocation into the larger, planned ASRP will mitigate additional costs to customers.[136] Furthermore, Duke Energy Ohio is not proposing here to relocate every interior natural gas meter but instead only those associated with service lines replaced under the ASRP.[137] The tailored scope of the proposal and the undeniable, long-standing benefits to customers have been established in this proceeding.

G. Reconnaissance Costs Are Properly Recoverable under Rider ASRP.

Again adopting inconsistent positions, Staff contends that reconnaissance costs are not recoverable under Rider ASRP because such costs should already be in base rates.[138] But the premises on which this contention is made is admittedly false.

As previously discussed, DIMP regulations set forth the required elements of an integrity management plan. Significantly, the federal regulations state that "[a] written integrity management plan must contain procedures for developing and implementing" certain elements.[139] Among those elements is knowledge or "an understanding of [the] gas distribution system developed from *reasonably available information.*"[140] PHMSA, therefore, appreciated the logical progression of obtaining knowledge of a system that may include very obsolete infrastructure and non-owned facilities for which records may be incomplete or unreliable. This progression necessarily commences with a determination of what is known of the system based upon currently available information and, to the extent there are gaps, developing a plan to

[135] Duke Energy Ohio Exhibit 2, at pg. 11.
[136] Duke Energy Ohio Exhibit 6, at pg. 8.
[137] Id.
[138] Staff Exhibit 3, at pg. 18.
[139] 49 C.F.R. 192.1007.
[140] 49 C.F.R. 192.1007(a)(emphasis added).

eliminate those gaps. And PHSMA appreciated that this plan will be rooted in operational feasibility by requiring gas distribution companies to expand their knowledge with information that subsequently becomes available. Consistent with DIMP regulations, Duke Energy Ohio understands its current distribution system. It knows that records are incomplete or inaccurate; it knows it does not own all service lines in its service territory; and it knows, as a result, that it cannot know the age or composition of all service lines in its service territory.[141] Duke Energy Ohio has thus developed a plan to obtain information and as the execution of that plan had not yet been implemented at the time of the Company's last base rate case, these costs are not currently in base rates.[142] Thus, Duke Energy Ohio proposes to include legitimate costs to conduct reconnaissance efforts in Rider ASRP.

H. Duke Energy Ohio is Currently Authorized to Assume Ownership of Service Lines.

The OCC suggests that the Company does not have authority to assume ownership of non-leaking service lines and, as a result, "must obtain authority to replace [those lines] that are currently owned by customers."[143] In advancing this contention, the OCC oddly claims that Duke Energy Ohio does not have authority to replace lines because it was unable, through its witnesses, to identify the authority for the Company's right to own service lines that it installs.[144] The oddity in this claim lies in the fact that the OCC solicited *legal* opinions from witnesses it knew not to have the requisite *legal* training.[145] And now, after those attempts failed, the OCC criticizes Duke Energy Ohio's witnesses for not rendering legal conclusions. That a witness is not qualified to provide legal opinions or interpret legal documents does not support the

[141] Duke Energy Ohio Exhibit 2, at pp. 11-12.
[142] Duke Energy Ohio Exhibit 5, at pg. 4.
[143] OCC Merit Brief, at pg. 4.
[144] Id.
[145] Tr. I, at pp. 18, 59 and 137.

conclusion that the OCC is seeking here; that the Company does not have existing authority to own service lines that it installs. And such authority does, in fact, exist.

To avoid any doubt, the only part of the service line at issue here is the curb-to-meter segment. Duke Energy Ohio has historically owned the main-to-curb segment.[146] As to the curb-to-meter segment, the Commission authorized Duke Energy Ohio to assume ownership of that segment "whenever a new service line...is installed or whenever an existing curb-to-meter service...is replaced."[147] In doing so, the Commission further recognized that Duke Energy Ohio's "ownership of customer service lines advances the public interest and safety."[148] Duke Energy Ohio currently possesses the requisite authority to replace obsolete, high-risk service lines.

Notwithstanding this existing authority, Duke Energy Ohio would be remiss if it did not address the absurdity in the OCC's contention. Specifically, the OCC believes that Duke Energy Ohio does not currently have permission to assume ownership of new curb-to-meter service lines that replace obsolete, high-risk service lines that are not leaking. The corollary to this statement is that the Company does have permission to assume ownership of every other curb-to-meter service line it installs, including similarly obsolete and high-risk curb-to-meter service lines that are leaking. To accept the OCC's contention, which lacks any evidentiary basis, the Commission would necessarily create discrepancies between Duke Energy Ohio's customers. Specifically, certain customers, already exposed to the hidden threat of an obsolete service line, would be deprived of the admitted benefits of relinquishing ownership of the curb-to-meter segment of the service line; benefits that include establishing a clear line of demarcation between customers and

---

[146] Tr. I, at pp. 159-160.
[147] *In the Matter of the Application of Duke Energy Ohio, Inc., for an Increase in Rates*, Case No. 07-589-GA-AIR, *et al.*, Opinion and Order, at pg. 24 (May 28, 2008).
[148] *In the Matter of the Application of Duke Energy Ohio, Inc., for an Increase in Rates*, Case No. 07-589-GA-AIR, *et al.*, Opinion and Order, at pg. 16 (May 28, 2008).

the Company in terms of responsibility for the operation and maintenance of service lines, removing from individual customers the need to arrange, and pay for, repairs to their service line, and aligning ownership with compliance obligations imposed under PHMSA regulation.[149] These benefits were undoubtedly relevant to the Commission when it authorized the Company, years ago, to assume ownership of curb-to-meter services lines that were either replaced or newly installed, regardless of whether they were leaking.

The fallacy in the OCC's argument is also reflected in the commentary of OPAE, which admits that Duke Energy Ohio currently has the ability to replace "*any* service lines that it determines need to be replaced."[150]

I. Rider ASRP's Return on Equity Component Should be Established Now and at the Level Supported by the Company.

1. The Commission should establish the Rider ASRP Return on Equity in this Proceeding.

Duke Energy Ohio is proposing to establish its Rider ASRP calculation, including the return on equity (ROE) to be used when the Rider is initially set in this case. The 9.84 percent ROE that Duke Energy Ohio is proposing to use was established through a settlement of the Company's most recent natural gas base rate case, Case No. 12-1685-GA-AIR, *et. al.*

In this case, Duke Energy Ohio presented conclusive evidence demonstrating that a 9.84 percent ROE remains reasonable today under current market conditions. The OCC, however, argues that if the Commission approves the Company's Application, that the ROE decision should be deferred until the time the Company seeks to establish the actual Rider ASRP collection, which the OCC believes will be in 2017 at the earliest. The Rider ASRP ROE should be established now, irrespective of the timing of the Company's implementation of the Rider ASRP actual charges to customers.

[149] See, *e.g.*, Staff Exhibit 3, at pg. 19; 49 C.F.R. 192.805.
[150] OPAE Merit Brief, at pg. 10.

The OCC's recommendation that the ROE decision be deferred until some future case is myopic. The OCC argues that capital markets and Company financial conditions could change between now and whenever the Company seeks to start collecting ASRP dollars via Rider ASRP from customers.[151] The OCC's argument is precisely why the Commission should establish the ROE now. Changes in capital markets could work in either direction. A reasonable ROE in the future may actually be higher than the 9.84 percent that the Company is requesting in this case. Indeed, Duke Energy Ohio's ROE evidence demonstrates that its current proposed ROE, while still in the range of reasonableness, is at the bottom of that end.[152] Both the Company and its customers deserve certainty in the near term regarding what the reasonable ROE for establishing the Rider ASRP charge should be. Duke Energy Ohio has committed that if the ASRP initiative is approved, it will file at least one base rate case during the term of the program. The ROE for that rider, not to mention the entire Company, will be evaluated at that time. Therefore, the Commission will be assured the necessary oversight to determine that the Company is and will continue to have an opportunity to earn a reasonable return on its Rider ASRP investments.

2. Duke Energy Ohio's proposed 9.84 percent ROE is reasonable.

Duke Energy Ohio's currently authorized ROE of 9.84 percent remains reasonable and should be used to establish the Company's Rider ASRP in this case. Duke Energy Ohio witness Roger A Morin, Ph.D., provided direct testimony in this proceeding that included detailed financial analysis using no less than three different forms of cost of capital analysis including the discounted cash flow (DCF), risk premium, and capital asset pricing model (CAPM) methodologies.[153] Dr. Morin developed a range of reasonable ROE's consisting of 9.8 percent to 10.7 percent with a midpoint of 10.3 percent. As Dr. Morin explains, the 9.84 percent that the

[151] OCC Exhibit 10 (Direct Testimony of Daniel J. Duann), at pp. 4-5.
[152] Duke Energy Ohio Exhibit 11 (Direct Testimony of Roger A Morin, PH. D.), at pg. 64.
[153] Id.

Company proposes to establish its Rider ASRP calculation, although within his range, is "barebones" and at the bottom of what he considers reasonable.[154] Dr. Morin's testimony is the only ROE evidence in the record that includes any detailed financial analysis of capital markets whatsoever that was to evaluate and recommend a reasonable rate of return. His analysis in this case, although similar to that he previously performed when the Company's current ROE was established in Case No. 12-1685-GA-AIR, *et al.*, is based upon new analysis using recent financial data available at the time his testimony was prepared and filed.[155] This fact is conceded by the OCC.[156] Although the OCC presented a single witness, David Duann Ph.D., to discuss ROE in this case, at the end of the day, Dr. Duann's recommendations are neither based upon nor supported by any empirical financial analysis of capital markets. Rather, they are entirely arbitrary and based upon inapplicable assumptions. They should therefore be rejected.

3. The OCC's criticisms of Dr. Morin's analysis are erroneous.

The OCC has only two criticisms of Dr. Morin's testimony and analysis in this proceeding. First, the OCC argues that the Company's use of 4.5 percent forecasted interest rate as a proxy for the risk free return in estimating the range of reasonable ROEs in this proceeding is not justified.[157] Second, the OCC opines that Duke Energy Ohio's proposed ROE is distorted because it uses a high market risk premium.[158] Both of these criticisms are erroneous.

The OCC's criticism of Dr. Morin's use of forecasted interest rates in its analysis as "significantly" overstating the return on risk-free investments is at best a mischaracterization and at worst a gross misstatement.[159] As Dr. Morin discusses, investors base their decisions upon

[154] Id, at pg. 4.
[155] Tr. II, at pp. 344-355.
[156] Id.
[157] OCC Merit Brief, at pg. 38.
[158] Id, at pg. 39.
[159] Id, at pg. 38.

expectations of future events.[160] He explains that noted economic forecasts call for rising trend in interest rates in response to recovering economy, renewed inflation, and record high federal deficits.[161] Further, because the CAPM is a forward-looking model that is based upon future expectations, a forecasted interest rate is used in developing a risk-free rate. Dr. Morin testified that all noted interest rate forecasts point to higher interest rates over the next several years.[162] In fact, on December 16, 2015, the federal government, recognizing the "considerable improvement in labor market conditions this year, and it is reasonably confident that inflation will rise, over the medium term, to its 2 percent objective" did raise the target range for the federal funds rate to 1/4 to 1/2 percent.[163]

The OCC's reliance upon its witness's testimony is questionable. Like nearly all of his testimony, Dr. Duann's opinion that forecasted interest rates are unreliable is not based upon any empirical analysis or consideration of current capital markets today, or where they are likely to be in the near future. Dr. Duann's position ignores recognized financial literature and does not factor analysts' predictions or recent changes to the economy and action by the government. Rather, the only basis for this opinion stated in his testimony, and cited by the OCC in its brief, is that the forecasts for interest rates that existed in 2012, as they related to then future periods of 2013 to 2015, turned out to be incorrect and overstated what actually occurred. In this case, Dr. Duann did not identify or rely upon any forecasts or conduct any empirical analysis that would indicate that future interest rates would either fall or stay the same as they are today. Indeed as recent public information issued by the federal government indicates, the exact opposite is

[160] Duke Energy Ohio Exhibit 11, at pg. 36.
[161] Id, at pg. 32.
[162] Id, at pg. 35.
[163] http://www.federalreserve.gov/newsevents/press/monetary/20151216a.htm

true.[164] As such, the OCC's criticism of using forecasted interest rates is flawed.

Similarly, the OCC's criticism of Dr. Morin's use of a market risk premium (MRP) of 7.1 percent is also misplaced.[165] Dr. Duann suggests that either a geometric average should be used to determine the MRP resulting in his recommended 4.4 percent MRP, or if an arithmetic mean is to be used, it should be based upon total return resulting in a 6.0 percent MRP.[166] Dr. Duann's testimony on these two points contains no explanation or support other than to say that it serves to lower Duke Energy Ohio's MRP.[167] Dr. Duann is wrong and his arguments and positions were disregarded by Dr. Morin through his direct testimony and, as Dr. Morin points out, are not recommended by the author of the very source both Dr. Duann and Dr. Morin cite for obtaining underlying MRP data.[168]

Dr. Morin fully explains the reasonableness of using an arithmetic mean as opposed to a geometric mean to establish a MRP in his testimony. Dr. Morin also explains and supports his 7.1 percent MRP calculation and why its use is appropriate in his testimony.[169] In reaching his conclusions, Dr. Morin explains how he derived his MRP recommendation calculated in his Attachment RAM-7, through an arithmetic mean of the income component of the long-term government bond and that an arithmetic mean is appropriate for forecasting and estimating costs of capital because it reflects volatility in a series of numbers, whereas the geometric mean does

---

[164] *See Transcript of Chair Yellen's December 16, 2015 Press Conference, citing the raising of rates was due to "...* the end of an extraordinary seven-year period during which the federal funds rate was held near zero to support the recovery of the economy from the worst financial crisis and recession since the Great Depression. It also recognizes the considerable progress that has been made toward restoring jobs, raising incomes, and easing the economic hardship of millions of Americans." http://www.federalreserve.gov/mediacenter/files/FOMCpresconf20151216.pdf

[165] OCC Merit Brief, at pg. 39.

[166] OCC Merit Brief, at pg. 40.

[167] OCC Exhibit 10, at pp. 22-23.

[168] Duke Energy Ohio Exhibit 11, at pg. 38, (noting that Morningstar (formerly *Ibbotson Associates*), which compiles the historic returns from 1926-2014 in its 2015 Classic Yearbook, recommends calculating the MRP through the use of the income component of long-term Government Bonds as more reliable than using the total return component.)

[169] Duke Energy Ohio Exhibit 11, at pg. 43.

not.[170] Dr. Morin also explains why it is appropriate and more reliable to calculate the historic MRP based upon the income component of the total bond return (*i.e.*, coupon rate) versus the total return as recommended by the OCC.[171] As Dr. Morin explains, the income component of total bond return is a far better estimate because the realized capital gains and realized loses factored into the total return is largely unanticipated by bond investors.[172] Dr. Morin goes on to explain that investors' expectations are higher for companies whose earnings are volatile than one with stable earnings thus demonstrating the flaw with using a geometric mean.[173] While Dr. Morin does state that his calculated and recommended 7.1 percent MRP is at the upper portion of the 5.0 percent to 8.0 percent range for the MRP in the United States, the fact remains that his recommended MRP is within the acceptable range articulated in multiple authoritative texts.[174] In contrast, Dr. Duann's recommendation to use a geometric mean to establish a MRP of 4.4 percent falls significantly below and outside what is considered an acceptable range by authoritative financial literature. Similarly, his alternative recommendation of a 6.0 percent MRP, while within the acceptable range is at the bottom end and based upon calculations that are less reliable.

4. OCC's recommended ROE reductions lack any empirical support.

The OCC is recommending an overall 100 basis point (1 percent) reduction to the Company's proposed ROE of 9.84 percent if the Commission approves the Company's Application and establishes the ASRP rider calculation in this proceeding. The OCC's position that an ROE no higher than 8.84 percent should be approved is not based upon any empirical financial analysis whatsoever. Rather it is based upon three purely arbitrary and result-oriented

[170] Id, at pp. 40-42.
[171] Id, at pg. 38.
[172] Id.
[173] Id, at pg. 41.
[174] Id, at pg. 43.

negative adjustments that should be ignored. On cross examination, Dr. Duann admitted that in reaching his recommendation that Duke Energy Ohio's proposed ROE should be reduced by 100 basis points, he did not perform any of the typical cost of capital analysis that are regularly undertaken to support ROE recommendations in Commission proceedings.[175] Dr. Duann performed no DCF analysis, no CAPM analysis, and no risk premium analysis in reaching his conclusions in this case.[176]

5. The Company's current/recommended 9.84 percent ROE already factors in changes to capital markets that have occurred since the Company's last rate case and still remains reasonable today.

The OCC first recommends a 25 basis point reduction due to changing conditions in the U.S. Credit and equity markets. The OCC claims there has been a decline in the allowed ROEs set by state regulators for regulated utilities in recent years and, therefore, the Commission should in turn reduce Duke Energy Ohio's proposed ROE in this case. First Dr. Duann offers absolutely no evidence to support his premise that there is a decline in allowed ROEs as set by state regulators for regulated utilities in recent years.[177] Dr. Duann readily admits in his direct testimony that he cannot quantify the magnitude of such a reduction in allowed ROEs.[178]

It is noteworthy to point out that the ROE agreed upon and established in Case No. 12-1685-GA-AIR, *et al.,* was both within Staff's recommended range and at the lower end of Dr. Morin's recommended range in that case.[179] Even assuming Dr. Duann's initial premise that allowed ROEs are trending downward since the time of the Company's last base rate case, the OCC's argument conveniently ignores a key fact conceded by its own witness[180] that Dr. Morin's analysis in this case, albeit similar to the analysis he has previously performed, is based

[175] Tr. II, at pg. 344.
[176] Id.
[177] OCC Exhibit 10, at pg. 16.
[178] Id.
[179] Tr. II, at pg. 333.
[180] Tr. II, at pp. 333-335.

upon the most recent available capital market financial data, and his analysis results in a recommended range of reasonable ROEs that is lower than what he previously supported in Case No. 12-1685, *et al.*[181] Accordingly, the Company's ROE testimony already factors in changes in capital markets that have occurred since the Company's last rate case. Any further adjustment on such basis is double counting. The OCC's first recommended reduction should be rejected.

6. Risk mitigation is already factored into the Company's ROE proposal and any further adjustment is duplicative and unsupported in the record.

The next arbitrary and unsupported reduction in ROE recommended by the OCC is a 25 basis point adjustment associated with a perceived decrease in regulatory lag. Once again, the OCC's 25 basis point valuation for such a reduction is without any empirical evidence or value quantification to support it. Dr. Morin first addressed the impact of riders and cost trackers in his direct testimony and explained why risk mitigation measures do not require downward adjustments to ROE.[182] He explains that the nature of a market-derived cost of common equity analysis already factors into its equations the effect and impacts of these or similar risk reduction mechanisms through the comparable analysis of other utilities in deriving recommended ranges for reasonable returns. In other words, to do as the OCC suggests and arbitrarily reduce a ROE by some factor just because of the implementation of a risk mitigation mechanism such as a cost recover mechanism is double counting.[183] Dr. Morin re-affirmed this position under cross examination.[184] Dr. Morin responded to counsel's questions regarding regulatory lag, that each of the utilities included in his peer group used to develop his ROE recommendation have risk mitigating mechanisms such as trackers, and that such risk reduction is factored into stock prices

[181] Id, at pp. 335-337.
[182] Duke Energy Ohio Exhibit 11, at pg. 60.
[183] Id.
[184] Tr. II, at pp. 307-308.

and bond ratings and that any further adjustment is double counting risk.[185] As such, the OCC's second recommended adjustment should be ignored.

7. The OCC's final recommended adjustment to the Company's ROE of 50 basis points is without merit.

The OCC's final argument to reduce Duke Energy Ohio's proposed ROE by 50 basis points is simply a plea that the Commission arbitrarily reduces the program costs to customers. Like all of its other recommended reductions, the OCC provides no quantification that such a reduction is supportable or representative of any particular factor worthy of a reduction. The OCC's Merit Brief broadly sites to stay policy in promoting availability of "adequate, reliable, and reasonably priced natural services and goods" and to "facilitate the states competitiveness in the global economy" as justification for its reduction.[186] The OCC provides absolutely no explanation or support for how a fifty basis point reduction in ROE satisfies or furthers either of those two policies. Rather, the OCC argues that the Commission has previously considered affordability to customers of services in determining a rate of return.[187] The OCC's brief and its witness Dr. Duann rely upon two prior rate cases for this position, Case No. 09-391-WS-AIR[188] (Ohio American Water Case) and Case NO. 07-829-GA-AIR, (East Ohio Gas Case).[189] Such reliance is misplaced.

First, there is absolutely no record evidence that the economic position of Duke Energy Ohio's customers or the current economy in 2015 is the same as what existed at the time of either of those two case decisions, 2007 and 2008, respectively. In fact, any such evidence would be to the contrary. Second, both cases relied upon by the OCC are distinguishable from the facts

---

[185] Id.
[186] OCC Merit Brief, at pg. 44, citing to R.C. 4929.02.
[187] Id, at pg. 45.
[188] *In the Matter of the Application for Ohio American Water Company to Increase its Rates for Water and Sewer Services to its Entire Service Area,* Case No. 09-391-WS-AIR, Opinion and Order (May 5, 2010).
[189] *In the Matter the Application of the East Ohio Gas Company d\b\a Dominion East Ohio for Authority to Increase Rates for its Gas Distribution Service,* Case No. 07-829-GA-AIR, *et al.* (October 27, 2008).

existing in this case. In the Ohio American Water Case, the Commission adopted a rate of return (7.73 percent) at the lower end of Staff's recommended range (7.6 percent to 8.11 percent) instead of Staff's midpoint of 7.85 percent.[190] This is distinguishable from Duke Energy Ohio's present case in that in reducing Ohio American Water Company's ROE, the Commission cited to both a "harsh economic condition in [Ohio American Water Company's] service territory" and the fact that its rate case was the fourth application in five years.[191] Neither fact is true here. There is absolutely no evidence of a "harsh" economic condition existing in Duke Energy Ohio service territory, nor has the Company filed multiple successive annual rate cases.

Similarly, the OCC's reliance upon the East Ohio Gas case must be put in context. Although the Commission did reduce East Ohio Gas Company's stipulated ROE by 20 basis points due to deteriorating economic conditions and decreased risk, on rehearing the Commission changed its mind and restored the original ROE.[192] Once again, neither of those two factors exists in this proceeding. There is no evidence of deteriorating economic conditions in Duke Energy Ohio service territory and as previously pointed out and explained by Duke Energy Ohio witness Dr. Morin, risk mitigation is already factored into the ROE calculation.[193]

In relying upon the Ohio American Water and East Ohio Gas cases, the OCC is conveniently ignoring more recent and applicable Commission cases. On cross examination, Dr. Duann agreed that in his role as a principal regulatory analyst for the OCC, that it is important to keep apprised of trends in utility rates of return and returns on equity, stating it was, "...part of his job."[194] And that responsibility included regularly reviewing orders by this Commission.[195]

---

[190] *In the Matter of the Application for Ohio American Water Company to Increase its Rates for Water and Sewer Services to its Entire Service Area,* Case No. 09-391-WS-AIR, Opinion and Order, at pg. 31 (May 5, 2010).
[191] Id, at pg. 36.
[192] *In the Matter of the Application of The East Ohio Gas Company d/b/a Dominion East Ohio for Authority to Increase Rates for its Gas Distribution Service,* Case No. 07-829-GA-AIR, *et al.*, Opinion and Order, at pg. 16 (October 15, 2008).
[193] Duke Energy Ohio Exhibit 11, at pp. 60-63.
[194] Tr. II, at pg. 313.

Yet, Dr. Duann is unaware of the terms of Duke Energy Ohio's most recently approved Electric Security Plan (ESP) where the Commission, just six months ago, approved the Company's electric distribution capital investment rider (DCI) and established the ROE as 9.84 percent.[196] This is despite the fact that Dr. Duann not only believes that the risks Duke Energy Ohio faces for its natural gas distribution business are comparable to that of its electric distribution business,[197] but actually testified that the Commission should wait to determine an ROE for the natural gas Rider ASRP until the Company filed its next electric distribution rate case in 2016.[198] In discounting the lack of any knowledge of this recently approved ROE for a cost recovery mechanism for Duke Energy Ohio electric distribution business, the same premise he suggests in this case, Dr. Duann recanted, stating that it was not necessarily important. Indeed, he admitted that he did not have time to review cases pertinent to Duke Energy Ohio and that, in his view, he probably had more important things to do.[199]

The arbitrary nature of the OCC's 50 basis point reduction is apparent and also not supportable by either of the two cases relied upon by the OCC. In both instances, and ignoring both the lack of applicability of facts as they pertain to this case, and that the Commission reversed itself in one instance, the adjustments made by the Commission were far less than the 50 basis points advocated by the OCC. The OCC ignores and its own witness is unaware of more recent precedent that actually supports Duke Energy Ohio's proposed ROE of 9.84 percent. The Commission should disregard the OCC's final recommended 50 basis point ROE reduction.

---

[195] Id, at pg. 314.
[196] *In the Matter of Application of Duke Energy Ohio, Inc. for Authority to Establish a Standard Service Offer Pursuant to 4928.143 in the Form of an Electric Security Plan, Accounting Modifications, and Tariffs for Generation Service,* Case No. 14-841-EL-SSO, *et al.,* Opinion and Order, at pg. 72 (April 2, 2015).
[197] Tr. II, at pg. 325.
[198] Id, *See also* Tr. II, at pg. 339.
[199] Tr. II, at pp. 341, 342.

IV. CONCLUSION

For the reasons stated herein and in its Merit Brief, Duke Energy Ohio respectfully requests that the Commission approve its accelerated service line replacement program and associated Rider ASRP as described in the Company's Application and supporting testimony.

Respectfully submitted,

DUKE ENERGY OHIO, INC.

Amy B. Spiller /AMF

Amy B. Spiller (0047277) (Counsel of Record)
Deputy General Counsel
Rocco D'Ascenzo (84608)
Associate General Counsel
Jeanne W. Kingery (0012172)
Associate General Counsel
Duke Energy Business Services LLC
139 E. Fourth Street, 1303-Main
P.O. Box 960
Cincinnati, Ohio 45201-0960
(513) 287-4359 (telephone)
(513) 287-4385 (facsimile)
Amy.Spiller@duke-energy.com
Rocco.D'Ascenzo@duke-energy.com
Jeanne.Kingery@duke-energy.com

CERTIFICATE OF SERVICE

I hereby certify that a true and accurate copy of the foregoing was delivered via U.S. mail (postage prepaid), personal, or electronic mail delivery, on this the 23rd day of December 2015 to the parties listed below.

Amy B. Spiller /AMF
Amy B. Spiller

Thomas Lindgren
Assistant Attorneys General
180 East Broad Street
Columbus, Ohio 43215
Thomas.Lindgren@puc.state.oh.us

Counsel for Staff of the Commission

Kevin F. Moore
Assistant Consumers' Counsel
Office of the Ohio Consumers' Counsel
10 West Broad Street, Suite 1800
Columbus, Ohio 43215
Kevin.moore@occ.ohio.gov

Counsel for the Office of Ohio Consumers' Counsel

Colleen L. Mooney
Ohio Partners for Affordable Energy
231 West Lima Street
Findlay, Ohio 45839
cmooney@ohiopartners.org

Counsel for Ohio Partners for Affordable Energy

This foregoing document was electronically filed with the Public Utilities

Commission of Ohio Docketing Information System on

12/23/2015 2:50:08 PM

in

Case No(s). 14-1622-GA-ALT

Summary: Brief Reply Brief of Duke Energy Ohio, Inc. electronically filed by Mrs. Adele M. Frisch on behalf of Duke Energy Ohio, Inc. and Spiller, Amy B and Kingery, Jeanne W and Rocco O D'Ascenzo