BEFORE

THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Duke Energy Ohio, Inc., for Recovery of Program Costs, Lost Distribution Revenue and Performance Incentives Related to its Energy Efficiency and Demand Response Programs.	))))))	Case No. 17-781-EL-RDR

DUKE ENERGY OHIO, INC'S COMMENTS TO THE STAFF'S REVIEW AND RECOMMENDATION

I. INTRODUCTION

Now comes Duke Energy Ohio, Inc., (Duke Energy Ohio or the Company) and hereby submits its comments to the Staff Review and Recommendations in regard to the application filed by Duke Energy Ohio, Inc., to recover costs associated with it Energy Efficiency Demand Response Rider, in Case No. 17-781-EL-RDR (Staff Recommendation). Staff's recommendation to disallow what amounts to $386,544 is unreasonable, includes incorrect calculations based upon Staff's own explanation of justification for disallowances and as further explained below, contrary to Commission precedent.

In its Staff Recommendation, the Staff of the Public Utilities Commission of Ohio (Staff) makes several adjustments to the Company's Energy Efficiency and peak Demand Reduction Rider (Rider EE-PDR) recovery for 2016 costs. Duke Energy Ohio is willing to accept Staff's recommended disallowances for Sponsorships, Miscellaneous Expenses, or for Meals, Snacks and Drinks as described in the Staff Recommendation. While we believe the meals, sponsorships and gifts cards are legitimate expenses associated with offering energy efficiency programs in Ohio, we accept the Staff's recommended disallowances in this proceeding. However, Duke Energy Ohio does object to the Staff's recommended disallowances related to Incentives, Employee Expenses, and De Minimis Expenses. As further described below, Staff's recommended disallowances for these expenses are improperly calculated, misconstrue what is reflected in the Company's base rates, and are without any justification.

II. DISCUSSION

A. Incentive Compensation.

Staff recommends disallowance of approximately $299,822 in incentive compensation paid in the form of short-term incentives, performance awards, and restricted stock units (RSUs). Staff's justification for proposing these disallowances is that "Staff does not normally support recovery of financial incentives *based upon a utility's financial goals* being passed on to its ratepayers."[1] Duke Energy Ohio believes that its total compensation paid to employees should be recoverable from customers as it is the total compensation that is required to attract and retain employees in order to provide safe and reliable service. Nevertheless, the Company is aware that Staff frequently recommends against recovery of incentive pay linked to the Company's financial performance.

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[1] Staff Report, pg. 2 Emphasis added.

The Staff argues again, in this case, that incentive compensation linked to the achievement of the Company's financial goals should be excluded. However, in this instance, Staff eliminates far more than just incentive pay tied to financial goals in direct contradiction of its own stated policy. In Duke Energy Ohio's most recent rate case, Case No. 17-32-EL-AIR, *et al.*, Staff submitted a number of data requests to the Company including the formulae for the Company's various incentive programs. The Company provided this information to Staff, which clearly shows the structure of the Company's incentive programs applicable during 2016, including the actual percentages tied to achievement of financial goals. Staff's adjustments here disregard the actual structure of the Company's incentive programs. Again, the Company believes that there should be no disallowance of any incentive compensation; however, if the Commission agrees with the Staff to exclude incentive compensation tied to the Company's financial goals, Staff's recommended disallowance adjustment must be adjusted to correct errors in the calculation and to align with and accurately reflect the Company's actual incentive programs. This information was available to the Staff as it was provided in response to Staff-DR-11 in Case No. 17-32-EL-AIR, attached hereto as Confidential Attachment A. This policy was in effect for 2016 and there has been no change to the formula since that time.

In reaching its total disallowance, Staff eliminated 80 percent of Executive Short Term Incentive (STI) goals as being tied to achieving corporate financial targets. Staff's adjustment is unreasonable and excessive insofar as it is not reconcilable with the actual structure of the Company's short-term incentive plans in effect thereby over adjusting for the actual amount of STI that is actually attributable to achieving financial goals. In actuality, only 50 percent of STIs are related to achieving corporate financial targets, not 80 percent.[2] Therefore, Staff's adjustment to remove $16,348 is unreasonable based upon Staff's own justification for such a disallowance.

[2] Confidential Attachment A, pg. 6 of 51.

Reflecting the true and accurate amount of STI related to financial goals would result in an adjustment of only $10,218, if the Commission accepts the Staff's recommendation to disallow incentive compensation related to achieving the Company's financial goals.

Similarly, Staff recommends a disallowance of 100 percent of Allocated Employee Incentives for an unreasonable adjustment of $250,340. What Staff identifies as "Allocated Employee Incentives" is actually the STI program for non-executives. Again, Staff's removal of 100 percent of Allocated Employee Incentives is unreasonable, unsupportable and contradicts its own historical policy. The Company has already shared with the Staff the formula for this non-executive STI program. As shown in Confidential Attachment A, only a portion of the non-executive STI program is tied to achieving financial goals or financial performance. In fact, only 30 percent of the incentive has any relation to achievement of financial goals or performance. Therefore, even following Staff's policy of excluding incentive compensation tied to achieving financial goals, Staff unreasonably, excessively, and, perhaps, punitively recommended disallowance of more than $175,000 unrelated to achievement of financial goals. Accordingly, the Staff's adjustment should have been no more than $75,102 (30 percent of $250,340).

Staff has excessively adjusted is recommended disallowance related to Performance Awards by eliminating 100 percent of this component from Rider EE-PDR's costs. The Performance Award at issue is a component of the Executive LTI program. In fact, only 75 percent of the Performance Award component is actually tied to achieving financial goals. The remaining 25 percent is not, but rather is related to achieving safety goals (TICR).[3] Therefore, by removing 100 percent of Performance Awards, Staff has over adjusted this component.

The details of this program were also provided to the Staff in the rate case and the same document is provided in Attachment B. Correcting Staff's adjustment to accurately reflect the

[3] *See* Confidential Attachment A, pg. 42 of 51, and 47 of 51.

impact of its own policy removes only 75 percent of the Performance Award component, $5,475 compared to the Staff's adjustment of $7,300.

Finally, Staff inappropriately removes 100 percent of RSUs from the calculation of the recoverable costs in Rider EE-PDR. In making this recommendation Staff apparently misunderstands the purpose of RSUs or what it means for incentive compensation to be "tied to" achieving financial goals. For the incentive programs discussed above, the magnitude of the incentive compensation awarded to employees will vary somewhat depending on the degree to which the Company actually achieves its goals. In other words, there is a causal relationship between the incentive compensation and the Company's overall performance for all goals. For those employees whose compensation package includes RSUs, that component of their overall compensation is completely independent of the Company's financial performance. Regardless of how well or how poorly the Company does in achieving its financial goals, RSUs are paid to certain employees at a fixed number of units, *i.e.*, there is no causal relationship between financial performance and this component of the Company's compensation program.[4] RSUs, in fact, are designed to retain existing employees through vesting requirements and, therefore, are a form of deferred compensation. In other words, the "incentive" is for employee retention and has nothing to do with achieving financial goals. Eligible employees receive these incentives, as a fixed percentage of their base salary, for remaining with the Company. As such, Staff's adjustment to remove 100 percent of the RSU component is improper, unreasonable, and at odds with Staff's stated policy.

[4] Confidential Attachment A at pp. 49-51.

Table 1 below provides reconciliation for the appropriate adjustments based upon Staff's explanation of eliminating incentives tied to achieving financial goals:

TABLE 1

Incentive Type	Incentive Amount	Disallowance by Staff		Actual Amount tied to DEO's Financial Goals	
		Percent	Dollars	Percent	Dollars
Exec STI	$20,435	80%	$16,348	50%	$10,218
Incentives Allocated	250,340	100%	250,340	30%	75,102
Performance Award	7,300	100%	7,300	75%	5,475
RSUs	25,834	100%	25,834	0%	-
Total	$303,909		$299,822		$90,795

Again, the Company believes that no adjustment is warranted as incentive compensation is no less important than any other component of overall compensation but, if the Commission were to adopt Staff's philosophical adjustment to remove incentives that are tied to achievement of the Company financial goals, then the appropriate adjustment should only be $90,795. This revised adjustment would be consistent with the Stipulation pending in Case No. 17-32-EL-AIR, *et al*, whereby the Company and Signatory Parties, including Staff, agreed to a capitalization policy for the Company's Distribution Capitalization Investment (Rider DCI) and Power Forward (Rider PF) to eliminate the estimated revenue requirement impact of capitalizing employee bonus expenses for incremental investment for its Ohio retail customers.[5] As defined in the Stipulation, bonus expenses referred to the portion of the Company's incentive

[5] Stipulation at 9.

compensation attributable to the achievement of financial goals. For consistency sake, the Commission should only adjust, accurately, for incentives that are in fact attributable to achievement of financial goals. Staff has recommended much more than that in its Staff Recommendation.

It should be noted that Staff has frequently distinguished incentive pay related to financial goals from other components of incentive pay. Although Staff has not always recommended disallowance of incentive compensation, in some cases it has done so and, in some of those cases, described the basis for the adjustment. For example,

- In the Staff's reports in Case No. 11-351-EL-AIR, *et al.*, and Case No. 11-352-EL-AIR, *et al.*, the Staff recommended a reduction in "incentive pay attributable to the obtainment of financial goals."[6]
- In testimony supporting the Staff's report in Case No. 07-551-EL-AIR, *et al.*, Staff clarified a recommendation regarding incentive compensation in that case. On behalf of Staff, Trisha J. Smith testified that "[i]ncentive pay based on the achievement of specific financial goals should be the responsibility of shareholders and not included in test year labor." (emphasis added)[7]

Staff's recommendation in this proceeding to eliminate all RSUs is a significant departure from its previously stated policy of only objecting to compensation tied to financial goals. Applying a different standard in this case is arbitrary, unfair, and completely out of line with the rationale it has relied upon in the past to justify its recommendations related to incentive compensation.

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[6] Staff's Report, in Ohio Power's and Columbus Southern Power's electric rate case, filed on September 15, 2011.
[7] Pre-Filed Testimony of Trisha J. Smith, pg. 7, in Case No. 07-551-EL-AIR, *et al.*, February 11, 2008.

B. Employee Expenses.

Duke Energy Ohio objects to the Staff's recommended disallowance of $18,208 related to employee expenses. Staff's justification for the disallowance of these costs are that telephone communication devices have uses beyond those associated with EE-PDR and that the Company has allowances in base rates for mileage reimbursement. Staff is incorrect in both of these assessments. The personnel whose time is allocated to EE-PDR do not have any time allocated elsewhere or included in the Company's base rates. The Company has always accounted for its energy efficiency program expenses, including personnel labor and other costs separately from base rates. Indeed, as part of the Company's pending settlement in Case No. 17-32-EL-AIR, the Staff acknowledged that it was withdrawing its recommendation from the Rate Case Staff Report that all energy efficiency labor expenses should be included in rate base rather than in the energy efficiency rider.[8] Staff clearly understands the fact that energy efficiency costs are not in the Company's base rates as Staff tried to insert them into base rates. The Commission should not undermine this prior precedent or allow penalize the Company for the recovery of reasonable and prudently incurred costs based upon Staff's flawed statement that such costs are in base rates, especially when Staff itself is aware they are not, and agreed to withdraw that recommendation.[9]

C. De Minimis Expenses.

Finally, Staff recommends disallowance of what it describes as "numerous, small allocations that appeared to be non-incremental expenses or not directly associated with energy efficiency."[10] Of these charges, Staff arbitrarily and unreasonably recommends deduction of all such expenses that are $10.00 or less be disallowed from recovery. Staff provides absolutely no basis for its disallowance except that these costs are less than some arbitrary threshold of $10.00.

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[8] Stipulation at pg. 8.
[9] *Id.*
[10] Staff Report at 4.

While this may seem like a benign recommendation, Staff's disallowance, when added up, is a substantial disallowance of more than $27,000 or approximately 7 percent of the total disallowance recommended by Staff. When one factors in that Staff's total disallowance should be far less, as explained above, the proportion of this so called "de minimus" deduction grows exponentially. Staff's characterization of this unsupported disallowance as de minimus does not support disallowance. These costs were reasonably incurred and there was no finding by Staff that they were imprudent. Just small. Small is not a sufficient justification to disallow cost recovery.

III. CONCLUSION

For the foregoing reasons, Staff's recommended disallowance of more than $386,544 is unreasonable, unsupportable, arbitrary and inconsistent with both prior positions of this Commission and terms and conditions recently agreed to in a settlement currently pending before this Commission. The Company respectfully requests that the Commission disregard Staff's recommended disallowances as described in its Staff Recommendation for the reasons set forth herein. Insofar as the Company does not dispute the disallowances for: 1) Sponsorships ($34,025); 2) Meals ($6,211); 3) Miscellaneous Expense Charges ($793); and 4) Incentives that are actually tied to the Company's financial targets ($90,795); the appropriate adjustment should be approximately $131,824.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that a true and accurate copy of the foregoing was delivered by U.S. mail (postage prepaid), personal, or electronic mail, on this 11th day of October 2018, to the parties listed below:

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Please provide staff with the following:

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ATTACHMENT A

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