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BEFORE

THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the	:		
Consolidated Duke Energy Ohio, Inc.	:	Case Nos.	03-93-EL-ATA
Rate Stabilization Plan Remand and	:		03-2079-EL-AAM
Rider Adjustment Cases	:		03-2081-EL-AAM
	:		03-2080-EL-ATA
	:		05-725-EL-UNC
	:		06-1069-EL-UNC
	:		05-724-EL-UNC
	:		06-1068-EL-UNC
	:		06-1085-EL-UNC

DUKE ENERGY OHIO'S REMAND RIDER MERIT BRIEF

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INTRODUCTION:

The Ohio Supreme Court's Order remanded Case No. 03-93-EL-ATA, *et al.*, on two narrow points: (1) Does the record evidence support the Public Utilities Commission of Ohio's (Commission) November 23, 2004, Entry on Rehearing; and (2) Are there side agreements that precluded serious bargaining among capable and knowledgeable Parties, the first prong of the three part test regarding the adoption of partial stipulations.¹ Based upon the Court's narrow remand order the Ohio Consumers' Counsel (OCC) moved the Commission to consolidate and suspend cases involving components of Duke Energy Ohio's (DE-Ohio) market-based standard service offer (MBSSO).² The cases that OCC sought to suspend and stay included cases seeking to set the 2007 market

¹ *Ohio Consumers' Counsel v. Pub. Util. Comm'n*, 111 Ohio St. 3d 300, 309, 323 856 N.E.2d 213, 225, 236 (2006).

² *In re DE-Ohio's MBSSO*, Case No. 03-93-EL-ATA, *et al.* (OCC's Motion to Stay the AAC, FPP, and SRT) (December 12, 2006).

price for the Annually Adjusted Component (AAC), System Reliability Tracker (SRT), and the Fuel and Purchased Power (FPP) component of DE-Ohio's MBSSO.³ Ultimately, the Commission, stayed the proceeding regarding the AAC, SRT, and FPP until the conclusion of litigation regarding the issues set forth in the Court's remand order.

After the close of litigation concerning the evidence and reasoning supporting DE-Ohio's MBSSO and various contracts that OCC and other Parties mischaracterize as "side agreements," DE-Ohio entered settlement discussions with Parties to resolve the suspended AAC, SRT, and FPP cases. All interested Parties participated in the settlement discussions and several drafts of the Stipulation were circulated to all Parties, including the Stipulation ultimately agreed upon by DE-Ohio, Staff, People Working Cooperatively (PWC), Ohio Energy Group (OEG), the Ohio Hospital Association (OHA), and the City of Cincinnati.⁴ Only OCC and Ohio Partners for Affordable Energy (OPAE) oppose the Stipulation.

Staff and DE-Ohio presented substantial evidence supporting the Stipulation. OCC was the only Party that presented evidence against the Stipulation and, as was the case with its proposal for a market price during the first phase of the hearing, OCC has performed no analysis, and has no idea, what effect its proposal may have on the market price paid by consumers.⁵

³ *Id.*

⁴ *In re DE-Ohio's MBSSO*, Case No. 03-93-EL-ATA, *et al.* (Joint Remand rider Exhibit 1 at 8-9) (April 9, 2007).

⁵ *In re DE-Ohio's MBSSO*, Case No. 03-93-EL-ATA, *et al.* (Remand Rider Tr. II. At 52-53) (April 19, 2007).

Timely action by the Commission approving the Stipulation, and DE-Ohio's AAC, SRT, and FPP, is necessary to benefit all consumers. Because the costs associated with the AAC and SRT are accumulating; the costs must be recovered from consumers over the few months remaining in the year instead of over the normal twelve month period. The sooner the Stipulation is approved the lower the market prices for the remainder of the year. DE-Ohio respectfully requests that the Commission approve its applications to implement the AAC, SRT, and FPP, as amended by the Stipulation.

ARGUMENT:

DE-Ohio filed applications to initiate the annual review of its AAC, SRT, and FPP representing cost recovery of specified costs it incurs in the provision of its MBSSO service to consumers. DE-Ohio does not make any return on these MBSSO components with the exception of a return of and on capital investments included in the AAC MBSSO component needed to comply with environmental, homeland security, and tax requirements.

Regardless of the MBSSO ultimately approved by the Commission, all of the cost elements included in the AAC, SRT, and FPP must be part of DE-Ohio's MBSSO. No Party, including OCC, has suggested otherwise. OCC has merely suggested that Construction Work In Progress (CWIP) should not be included as part of DE-Ohio's AAC calculation, but has not suggested it is improper for DE-Ohio to recover the underlying environmental costs.

I. The Stipulation offered by some, but not all of the Parties to these proceedings is the product of serious bargaining among knowledgeable parties, benefits the public, and does not violate any regulatory principle.

All of the Parties to these proceedings were invited to all of the settlement discussions.⁶ The Parties participating in the settlement discussions, including Staff, OCC, OPAE, The City of Cincinnati, PWC, Industrial Energy Users-Ohio (IEU-Ohio), OEG, OHA, the Ohio Marketers Group (OMG), and Dominion Retail Sales (Dominion) represent all of the stakeholder groups interested in these proceedings including residential, industrial, and commercial consumers, and CRES providers. Ultimately, DE-Ohio, Staff, The City of Cincinnati, PWC, OEG, and OHA signed the Stipulation.⁷ The signatories represent every stakeholder group except CRES providers and no CRES provider, including the Ohio marketer Group (OMG) and Dominion Retail Sales (Dominion), opposed the Stipulation. In fact, IEU-Ohio and Dominion Retail did not oppose the Stipulation. The only Parties opposing were OCC and OPAE. All of the Parties have extensive experience before the Commission. Clearly, the Stipulation resulted from serious bargaining among knowledgeable Parties.

Similarly, the evidence shows that the Stipulation will benefit the public. DE-Ohio witness Paul Smith testified that the Stipulation furthers the Commission's three goals for rate stabilized MBSSOs: (1) rate certainty for

⁶ *In re DE-Ohio's MBSSO*, Case No. 03-93-EL-ATA, *et al.* (DE-Ohio Remand Rider Ex. 6 at 5) (April 6, 2007).

⁷ *In re DE-Ohio's MBSSO*, Case No. 03-93-EL-ATA, *et al.* (Joint Remand Rider Ex. 1 at 8-9) (April 9, 2007).

consumers; (2) financial stability for electric distribution utilities; and (3) the continued development of the competitive retail electric service market.⁸ Specifically, Mr. Smith testified that the Stipulation permits DE-Ohio appropriate cost recovery through various MBSSO components, which meets the goal of: (1) financial stability for DE-Ohio; (2) the provision of MBSSO service at a reasonable price for consumers; and (3) rate certainty for consumers.⁹ Finally, Mr. Smith testified that the Stipulation requires DE-Ohio to issue a bill credit related to a confidential contract settlement in an amount greater than that recommended by the FPP auditor during 2007, which will help offset the MBSSO rider component prices resulting from the Stipulation.¹⁰

OCC was the only Party, through its witness Michael Haugh, alleging that the Stipulation does not benefit the public interest.¹¹ Mr. Haugh testified that parts of the Stipulation are ambiguous and meaningless, and other parts are harmful to ratepayers.¹² First, Mr. Haugh argues that paragraph 3 of the Stipulation, which commits the Parties to meet and use their best efforts to address the FPP auditor's finding at page 1-8 of the audit report that DE-Ohio actively seeks to limit its purchases of emission allowances and coal for the period after December 31, 2008, is meaningless.¹³ The auditor made no

⁸ *In re DE-Ohio's MBSSO*, Case No. 03-93-EL-ATA, *et al.* (DE-Ohio Remand Rider Ex. 6 at 7) (April 6, 2007).

⁹ *Id.*

¹⁰ *Id.*

¹¹ *In re DE-Ohio's MBSSO*, Case No. 03-93-EL-ATA, *et al.* (OCC Remand Rider Ex. 2 at 2) (April 17, 2007).

¹² *Id.*

¹³ *In re DE-Ohio's MBSSO*, Case No. 03-93-EL-ATA, *et al.* (Joint Remand Rider Ex. 1 at 8-9) (April 9, 2007).

recommendation regarding this issue; it simply made a finding, leaving future action to the Parties and the Commission.

Mr. Haugh testified that paragraph 3 accomplishes nothing and there is a docket established to resolve the issue.¹⁴ On cross examination, Mr. Haugh agreed that discussions regarding the issue of future fuel purchases are important and was only suggesting that Case No. 06-986-EL-UNC is the proper forum for such discussions.¹⁵ In the end Mr. Haugh could not explain why it was better to hold discussions in Case No. 06-986-EL-UNC, a case where the Commission has not yet set a procedural schedule, rather than the current docket.¹⁶ The fact is there is no reason to delay discussions and hold them in Case No. 06-986-EL-UNC when discussions can begin immediately. Further, there is no reason why the Parties cannot recommend a solution to the issue in Case No. 06-986-EL-UNC if that is appropriate. What is not appropriate is to ignore the auditor's finding and fail to address it prior to the next FPP case.

The only other issue that Mr. Haugh believes is ambiguous or meaningless is Stipulation paragraph 8 regarding the use of DE-Ohio's assets formerly owned by Duke Energy North America (DENA).¹⁷ That issue was resolved by a Stipulation between Staff and DE-Ohio.¹⁸ Staff and DE-Ohio clarified any ambiguity relating to the use of DE-Ohio's DENA assets to meet

¹⁴ *In re DE-Ohio's MBSSO*, Case No. 03-93-EL-ATA, *et al.* (OCC Remand Rider Ex. 2 at 2) (April 17, 2007).

¹⁵ *In re DE-Ohio's MBSSO*, Case No. 03-93-EL-ATA, *et al.* (Remand Rider Tr. II at 140-141) (April 19, 2007).

¹⁶ *Id.* at 141-142.

¹⁷ *In re DE-Ohio's MBSSO*, Case No. 03-93-EL-ATA, *et al.* (OCC Remand Rider Ex. 2 at 3) (April 17, 2007).

¹⁸ *In re DE-Ohio's MBSSO*, Case No. 03-93-EL-ATA, *et al.* (OCC Remand Rider Ex. 3) (April 19, 2007).

the SRT reserve capacity requirements in a Stipulation entered on the record at hearing on April 19, 2007.¹⁹

Mr. Haugh's testimony also demonstrates OCC's lack of technical understanding of the competitive wholesale capacity market. Mr. Haugh testified that the market price DE-Ohio is paid for its DENA asset capacity should be capped at "the median price DE-Ohio has paid for capacity during the time frame in which the emergency occurs."²⁰ The very nature of a capacity purchase in an emergency makes the market price unpredictable. Prior to the advent of stand-alone capacity markets there have been many instances where combined capacity and energy prices have exceeded \$1000 per MWh. The Commission well remembers the last such instance in August of 2003 immediately after the blackout. In the late 1990s prices reached as much as \$10,000 per MWh. DE-Ohio cannot predict when an emergency requiring additional capacity will occur or the circumstances of the emergency. It is not possible to predict the price of capacity in such a market. There is no reasonable method to set a price cap under such circumstance. DE-Ohio is committed to providing consumers with the capacity necessary to maintain reliable service at a reasonable price. DE-Ohio is willing to negotiate a reasonable pricing methodology to set the price and has suggested several such methodologies set forth in the Stipulation. A price cap is not a reasonable

¹⁹ *Id.*

²⁰ *In re DE-Ohio's MBSSO*, Case No. 03-93-EL-ATA, *et al.* (OCC Remand Rider Ex. 2 at 5) (April 17, 2007).

pricing methodology under the circumstances for committing DE-Ohio's DENA capacity set forth in the Stipulation in these cases.

OCC's final objection is that the collection of financing costs related to DE-Ohio's environmental construction work in progress (CWIP) investment is harmful to consumers.²¹ Beside the fact that the Commission approved the inclusion of CWIP as part of the original AAC calculation, as presented on JPS-4,²² approved in these cases as part of its November 23, 2004, Entry on Rehearing, OCC has no idea what price consumers will pay if DE-Ohio is denied the ability to recover CWIP as part of its market price.²³ Mr. Haugh admits that low sulfur coal, emission allowances, and purchased power are all substitutes for the scrubbers that represent the bulk of DE-Ohio's capital environmental investments at issue in these proceedings.²⁴ If DE-Ohio cannot recover CWIP on its environmental investments it will be forced to substitute emission allowances, low sulfur coal, and purchased power for the scrubbers to meet environmental requirements. Such substitutes will result in a more expensive FPP for all consumers as the costs of emission allowances, low sulfur coal, and purchased power flow through the FPP. OCC has no idea whether the resulting FPP price will yield a higher overall market price to consumers than the recovery of CWIP through the AAC.²⁵

²¹ *Id.* at 6.

²² *In re DE-Ohio's MBSSO*, Case No. 03-93-EL-ATA, *et al.* (DE-Ohio Remand Rider Ex. 4 at WDW-1) (September 1, 2006).

²³ *In re DE-Ohio's MBSSO*, Case No. 03-93-EL-ATA, *et al.* (Remand Rider Tr. II at 52) (April 19, 2007).

²⁴ *Id.* at 53.

²⁵ *Id.* at 52.

The record evidence demonstrates that DE-Ohio's used and useful environmental asset net book value has increased from \$389,416,025 as of June 30, 2004, to \$461,405,497 as of December 31, 2006, an increase of \$71,989,472, without taking into account CWIP.²⁶ Despite this increase in environmental investment, OCC recommends that the Commission decrease the AAC market price.²⁷ On cross examination Mr. Haugh acknowledged that the evidence demonstrated increased environmental capital investment, as well as increased CWIP, by DE-Ohio.²⁸ Because Mr. Haugh acknowledges DE-Ohio's increased environmental capital investment, but has performed no analysis to determine the effects of his recommendation on consumers, and has failed to make a recommendation permitting DE-Ohio to comply with environmental regulations at a reasonable cost to consumers, his testimony is not credible and the Commission should disregard it.

II. DE-Ohio's FPP, AAC, and SRT Applications, and the Stipulation resolving the issues contained therein, does not violate any regulatory principle or practice.

OCC further alleges that the inclusion of CWIP in the AAC is inconsistent with regulatory practice because the Stipulation permits DE-Ohio to recover CWIP that would not be recoverable in a traditional rate case.²⁹ OCC is confused

²⁶ *In re DE-Ohio's MBSSO*, Case No. 03-93-EL-ATA, *et al.* (DE-Ohio Remand Rider Ex. 4 at WDW-1) (September 1, 2006); *In re DE-Ohio's MBSSO*, Case No. 03-93-EL-ATA, *et al.* (Staff Remand Rider Ex. 2A at LET-1, page 2 of 6) (March 9, 2007).

²⁷ *In re DE-Ohio's MBSSO*, Case No. 03-93-EL-ATA, *et al.* (OCC Remand Rider Ex. 2 at 5) (April 17, 2007).

²⁸ *In re DE-Ohio's MBSSO*, Case No. 03-93-EL-ATA, *et al.* (Remand Rider Tr. II at 145-149) (April 19, 2007).

²⁹ *In re DE-Ohio's MBSSO*, Case No. 03-93-EL-ATA, *et al.* (OCC Remand Rider Ex. 2 at 6) (April 17, 2007).

because this is not a traditional rate case but a proceeding to set DE-Ohio's market price. Thus, the principles and practice are different.

Fundamentally, the Commission's jurisdiction over DE-Ohio's market price and the principles and practices that result there from, result from R.C. 4928.05, which states in pertinent part:

On and after the starting date of competitive retail electric service, a *competitive retail electric service supplied by an electric utility* or electric services company *shall not be subject to supervision and regulation* by a municipal corporation under Chapter 743. of the Revised Code or *by the public utilities commission* under Chapters 4901. to 4909., 4933., 4935., and 4963. of the Revised Code, *except section 4905.10, division (B) of 4905.33, and sections 4905.35...*³⁰

In rejecting OCC's claims that DE-Ohio's MBSSO violated R.C. 4905.32 and R.C. 4905.34 the Court relied on the same language from R.C. 4928.05 to frame the Commission's jurisdiction.³¹ Plainly, this is not a cost-based regulated ratemaking proceeding. This is a proceeding involving the Commission's oversight of DE-Ohio's market price to ensure that DE-Ohio does not offer a price below cost for the purpose of destroying competition and does not offer a discriminatory price, nothing more.³²

OCC, through the testimony of Mr. Haugh, mistakenly requests the Commission to apply the same principles as it would apply in a traditional rate case.³³ As previously discussed, this is not a regulated rate proceeding.

³⁰ Ohio Rev. Code Ann. § 4928.05 (Baldwin 2007) (emphasis added).

³¹ *Ohio Consumers' Counsel v. Pub. Util. Comm'n*, 111 Ohio St.3d 300, 314, 856 N.E.2d 213, 229 (2006).

³² Ohio Rev. Code Ann. §§ 4928.05, 4905.33(B), 4905.35 (Baldwin 2007).

³³ *In re DE-Ohio's MBSSO*, Case No. 03-93-EL-ATA, *et al.* (OCC Remand Rider Ex. 2 at 6) (April 17, 2007).

Additionally, DE-Ohio faces far more risk in the market than it faced in a regulated environment. Regarding CWIP, under regulation, DE-Ohio was assured of recovering all costs associated with its environmental investments through rate proceedings. In the market, DE-Ohio has no assurances of long term cost recovery; so it must seek to recover its costs in the market place when the market price permits as there is no long term price guarantee. Even under the rate stabilization plan MBSSO adopted by the Commission DE-Ohio has no price assurance beyond December 31, 2008. DE-Ohio's circumstance is made abundantly clear by statute which states that "*an electric utility that receives transition revenues shall be wholly responsible for how to use those revenues and wholly responsible for whether it is in a competitive position after the market development period.*"³⁴

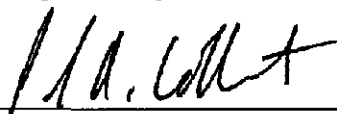
Absent a recommendation that affords DE-Ohio long-term recovery of its environmental investments through a market price, OCC's recommendation is contrary to statute and would result in a deterioration of DE-Ohio's ability to invest in infrastructure and provide reliable service. OCC's recommendation would violate regulatory principles and practices under the applicable statutes and should be rejected.

³⁴ Ohio Rev. Code Ann. § 4928.38 (Baldwin 2007) (emphasis added).

CONCLUSION:

For the reasons set forth above, DE-Ohio respectfully requests the Commission approve DE-Ohio's applications to implement an SRT, FPP, and AAC market price as amended by the Stipulation before it.

Respectfully Submitted,



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CERTIFICATE OF SERVICE

I certify that a copy of the foregoing was served electronically on the following parties this 17th day of May 2007.



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