

FILE

**BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO**

In the Matter of the Application of The)
Cincinnati Gas & Electric Company) Case No. 03-93-EL-ATA
To Modify its Non-Residential)
Generation Rates to Provide for)
Market-Based Standard Service Offer)
Pricing and to Establish a Pilot)
Alternative Competitively-Bid Service)
Rate Option Subsequent to Market)
Development Period.)

In the Matter of the Application of The)
Cincinnati Gas & Electric Company) Case No. 03-2079-EL-AAM
for Authority to Modify Current)
Accounting Procedures for Certain)
Costs Associated with The Midwest)
Independent Transmission System)
Operator.)

In the Matter of the Application of The)
Cincinnati Gas & Electric Company) Case No. 03-2081-EL-AAM
for Authority to Modify Current) Case No. 03-2080-EL-ATA
Accounting Procedures for Capital)
Investment in its Electric)
Transmission and Distribution)
System And to Establish a Capital)
Investment Reliability Rider to be)
Effective After the Market)
Development Period.)

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**APPLICATION FOR REHEARING
OF
OHIO PARTNERS FOR AFFORDABLE ENERGY
AND MEMORANDUM IN SUPPORT**

Respectfully submitted,

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November 23, 2007

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**APPLICATION FOR REHEARING
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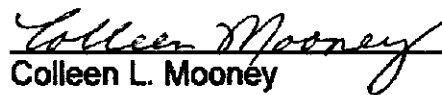
Pursuant to R.C. §4903.10 and Ohio Adm. Code 4901-1-35, Ohio
Partners for Affordable Energy ("OPAE") hereby applies to the Public Utilities
Commission of Ohio ("Commission") for rehearing of the Commission's October
24, 2007 Order on Remand in the above-captioned cases filed by The Cincinnati

Gas & Electric Company ("CG&E"), now Duke Energy Ohio, Inc. ("Duke"). The Commission's October 24, 2007 Order on Remand is unreasonable and unlawful in the following respects.

1. The Commission acted unreasonably and unlawfully when, having rejected the May 19, 2004 stipulation on the basis of the remand record of the side agreements, it approved Duke's application; given that the statutory requirements of R.C. §§4928.14 and 4909.18 and the Commission's own rate stabilization plan ("RSP") goals were not met, the Commission should have dismissed the application and ordered Duke to file a new application for the provision of standard service electric generation in its service territory.
2. The Commission acted unreasonably and unlawfully when it found that the infrastructure maintenance fund ("IMF") charge was reasonable.

The reasons supporting OPAE's Application for Rehearing are set forth in the attached Memorandum in Support pursuant to Ohio Adm. Code 4901-1-35(A).

Respectfully submitted,



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MEMORANDUM IN SUPPORT OF APPLICATION FOR REHEARING

- I. **The Commission acted unreasonably and unlawfully when, having rejected the May 19, 2004 stipulation on the basis of the remand record of the side agreements, it approved Duke's application; given that the statutory requirements of R.C. §§4928.14 and 4909.18 and the Commission's own rate stabilization plan ("RSP") goals were not met, the Commission should have dismissed the application and ordered Duke to file a new application for the provision of standard service electric generation in its service territory.**

On October 24, 2007, the Commission issued its Order on Remand in these proceedings. Based on the Supreme Court's concern about the integrity and openness of the negotiation process that led to the May 19, 2004 stipulation and the Court's requirement that the Commission seek evidence that the stipulation was the product of serious bargaining, the Commission found that the side agreements raised serious doubts about the integrity and openness of the negotiation process. The Commission reached the "inevitable conclusion" that there was a question whether the parties engaged in serious bargaining. Therefore, the Commission found that it should not have adopted the stipulation and rejected it. Remand Order at 27.

Without a stipulation to consider, the Commission found itself "compelled" to consider Duke's original application, as filed on January 26, 2004, and subsequently modified. The Commission found that it would review the reasonableness of the application in light of the record evidence developed in the initial hearing and the hearing on remand. The Commission did not consider whether the evidence presented at the hearings was affected by the bilateral bargaining among some of the parties outside the formal settlement process. The Commission simply found, as it had when the stipulation was before it, that Duke's rate stabilization plan ("RSP") provides consumers a market-based standard service offer and appropriately balances goals of protecting consumers from risk, assuring Duke some level of financial stability, and encouraging the development of a competitive market. Therefore, Duke's RSP, as modified on remand, was approved. Remand Order at 43.

For the low-income and small commercial consumers that OPAE represents, there is no difference between the RSP approved pursuant to the now-rejected stipulation and the RSP approved on remand. On remand, the Commission reached essentially the same outcome as it had when it approved

the now-rejected stipulation. While the Commission made changes to what charges are “avoidable” by shopping customers, such “avoidability” has no relevance to residential customers or small commercial customers. No shopping choices are available to these customers; and it is unlikely that the additional avoidable charges will make any difference, given the failure of competitive markets to develop. There is little likelihood that these customers will ever shop for electric generation service.

Ohio’s electric restructuring law clearly envisioned the development of a fully competitive retail electric market where consumers would be able to choose from a large number of competitive retail electric service providers to supply their electricity. Staff Comments, *Application of FirstEnergy*, Case Nos. 07-796-EL-ATA and 07-797-EL-ATA (September 21, 2007) at 2. This retail market has not developed. *Id.* Given the lack of customer choice in retail markets, the standard service offer set pursuant to R.C. §4928.14 is not a “fall back” option for customers who are in the process of finding a competitive supplier or switching from one competitive supplier to another. It is the only price available to the vast majority of customers. Ohio customers must “bargain” with a deregulated monopoly. *Id.* Customers simply have no leverage to control their bills.

The market development period for retail electric generation ended on December 31, 2005. R.C. §4928.14(A) states that after the market development period, an electric distribution utility shall provide consumers a market-based standard service offer of all competitive retail electric services necessary to maintain essential electric service to consumers, including a firm supply of electric generation service. In reality, the market for retail electric generation never developed, at least not for residential and small commercial customers, and the provision of a market-based standard service offer for these customers is not possible.

The market had not developed as the law anticipated it would, so the Commission created the RSP concept and the RSP goals, which include rate certainty, the financial stability of the utility and the development of a competitive market. The Ohio Supreme Court affirmed the Commission's RSP concept on the basis of stipulations made by diverse interested parties. In *Constellation NewEnergy, Inc. v. Pub. Util. Comm.*, 104 Ohio St.3d 530, 2004-Ohio-6767, the Court affirmed the Commission's approval of an RSP on the basis of the reasonableness of a stipulation. *Constellation* is nothing more than the Court's affirmation of the Commission's approval of a stipulation to which parties from all customer classes agreed. *Id.*

The Court stated in a subsequent case involving the RSP of FirstEnergy Corp., as follows:

The absence of a stipulation signed by customer groups factually distinguishes this case from *Constellation*. In *Constellation* we also noted that "no entire customer class was excluded from settlement negotiations and that the following classes were represented and signed the stipulation: residential customers, low-income customers, commercial customers, industrial customers, and competitive retail electric service providers." When it enacted R.C. 4928.14, the General Assembly anticipated that at the end of the market-development period, customers would be offered both a market-based standard service as required by R.C. 4928.14(A) and service at a price determined through a competitive-bidding process as required by R.C. 4928.14(B); one very narrow exception contained in R.C. 4928.14(B) permits the commission to determine that a competitive-bidding process is not required. In *Constellation*, the customer groups, by stipulation, agreed to accept a market-based standard service offer and waive any right to a price determined by competitive bid. Those facts are not present in this case.

Ohio Consumers' Counsel v. Pub. Util. Comm., 2006-Ohio-2110 ¶18.

The Court made it clear that the stipulation signed by a wide range of parties was the determining factor that allowed the Court to affirm the Commission's RSP order. The Court made a strong distinction between

Commission RSP orders that could be approved pursuant to a stipulation supported by a wide range of parties and RSP orders that could not be approved absent such a stipulation. In the same opinion, the Court also stated:

In contrast to the customer groups in *Constellation*, the customer groups here did not agree to the FirstEnergy rates, and most customer groups, including the OCC, which represents all residential customers, opposed them. Under these circumstances, the PUCO had no authority to adopt the rate-stabilization plan without also ensuring that a reasonable means for customer participation had been developed.

Id. ¶19.

Reliance on a stipulation was also central to the Court's decision in *Elyria Foundry v. Pub. Util. Comm.*, 2007-Ohio-4164 (August 29, 2007), which the Commission cites in the Remand Order. In *Elyria*, the Court stated as follows:

¶64. Moreover, several parties representing divergent groups of ratepayers signed the stipulation on the rate-certainty plan. Those include IEU and the Ohio Energy Group (consortia of large industrial customers); the cities of Akron, Cleveland, Parma, and Toledo; Ohio Consumers' Counsel; and Ohio Partners for Affordable Energy and the Neighborhood Environment Coalition (low-income and energy-efficient customer programs). In addition, the Northeast Ohio Public Energy Council and the Northwest Ohio Aggregation Coalition (northern Ohio residential customer aggregators) pledged not to oppose it.

On remand in the instant case, the Commission finds that it can reach essentially the same outcome without a stipulation as it did with a stipulation. There continues to be no support for the CG&E-Duke RSP from any class of customers or any non-affiliated marketer. The evidence of the side agreements shows that consideration was provided to eliminate the opposition of certain large users of electricity to the RSP. The RSP is supported only by customers with side agreements that absolve them from the burden of the rate increases under the RSP. On remand, the Commission shows no concern for the fact, confirmed

by its own finding, that a stipulation presented to it was not the product of serious bargaining. Instead of showing outrage for the behavior of Duke and certain of its large customers who together presented a sham stipulation (knowing that a stipulation would facilitate Commission and Court approval of the RSP), the Commission astonishingly approves the RSP. The Commission fails to note the lack of support for the RSP by any customer group affected by its decision. The Commission also fails to consider whether the evidence before it has been tainted by the unacceptable settlement process.

There is good reason why the residential class does not support the CG&E-Duke RSP. In spite of the Commission's professed goals for RSPs, the approved plan vastly enriches CG&E-Duke at the expense of residential and small commercial customers. Rates increase dramatically; they certainly are not stabilized. The RSP offers no benefits to ratepayers; it merely sanctions charges. The RSP is not balanced to represent the interests of all parties. The RSP cannot be found to be in the public interest when it dramatically increases rates without sufficient regard to the costs incurred by the utility. Thus, ratepayers, and especially residential ratepayers, are harmed by the RSP and the higher rates it enforces. The RSP fails to meet the standards for approval established by the Commission and approved by the Supreme Court.

In addition, the RSP does not conform to Ohio law. R.C. §4928.14(A) states that after the market development period, an electric distribution utility shall provide consumers, on a comparable and nondiscriminatory basis within its certified territory, a market-based standard service offer of all competitive retail

electric services necessary to maintain essential electric service to consumers, including a firm supply of electric generation service. Such offer shall be filed with the Commission under R.C. §4909.18. Thus, the standard service offer under R.C. §4928.14(A) must be just and reasonable pursuant to R.C. §4909.18. Given that a functioning market does not exist, as the Commission's Staff has recently acknowledged, the Commission cannot now determine what constitutes a market-based standard service offer. Nevertheless, the Commission must assure that the R.C. §4928.14(A) standard service offer is just and reasonable pursuant to R.C. §4909.18. It is, therefore, unlawful for the Commission to approve a standard service offer, as it does in this case, without proper consideration of the just and reasonable requirements of R.C. §4909.18 and the extensive state and federal precedents that give meaning to this statutory requirement.

OCC witness Talbot noted that the various charges in the RSP are caught between a market-pricing framework and a cost-based justification. OCC Ex. R-1 at 73-74. While the Commission finds some components to be cost based, it also uses in other instances an alternate justification, namely that the component is part of market-based pricing. This allows the Commission to claim that non-cost based components, such as the infrastructure maintenance fund ("IMF"), are reasonable because they are "market based." In the absence of a functioning market, there is no clear evidence as to what exactly a market-based price is. Market-based prices are anything the Commission wants them to be. This does

not result in a just and reasonable standard service offer pursuant to R.C. §4909.18.

Using a cost basis is the only available proxy for the market, and a precisely estimated cost-based proxy is better than an approximate one. In the absence of a functioning market, a cost basis for charges is a reasonable response to the challenge of developing a consistent and sensible framework for standard service offer pricing that provides just and reasonable rates. OCC Ex. R-1 at 72-73.

Wholesale and retail markets for electric generation have not developed in the manner assumed by Ohio's electric restructuring legislation. Current electric markets, both wholesale and retail, are highly concentrated and dysfunctional; such markets produce prices set at a level that is politically possible rather than prices set at a level that an effectively competitive market would provide. R.C. §4928.14(A) requires a standard service offer filed under R.C. §4909.18, which, in turn, requires just and reasonable rates.

The evidence on remand demonstrates that the current standard service offer does not have a reasonable basis. It is not consistently cost-based, and, given the failure of a market to develop, it cannot be market based. If the market cannot determine prices for the standard service offer (because a functioning market does not exist), then the only proxy is a consistently cost-based standard service offer. The Commission must consider cost as the basis for approved charges; it cannot justify disregarding costs on the basis that it is setting a market-based rate. The Commission must approve just and reasonable standard

service rates. R.C. §4909.18. The Commission should grant rehearing, dismiss the application, and require Duke to file an application for a standard service offer reflecting Duke's actual costs to provide standard service offer generation.

- II. The Commission acted unreasonably and unlawfully when it found that the infrastructure maintenance fund ("IMF") charge was reasonable for determination of a market-based charge to compensate for the pricing risk incurred by Duke in its provision of POLR service.**

The Court found that the Commission approved Duke's infrastructure maintenance fund ("IMF") as a component of a provider of last resort ("POLR") charge without reference to record evidence and without explanation. The Commission offered no factual basis or other justification for approving the IMF charge; therefore, the Court could not determine what the IMF was without explanation from the Commission. On remand, the Commission found that the terms proposed by Duke for its IMF were reasonable for determination of a market-based charge to compensate for the pricing risk incurred by Duke in its POLR service. The Commission recognized that this component is not cost-based, but claimed that it is not necessary, under R.C. §4928.14, for components of a market price to be based on cost.

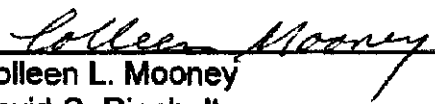
The evidence on remand demonstrates that the IMF charge should be eliminated as a new and duplicative charge. OCC witness Talbot confirmed the suspicions of the Court that the IMF may be "some type of surcharge and not a cost component." *Ohio Consumers' Counsel v. Pub. Util. Comm.* (2006), 111 Ohio St.3 300, 308. The system reliability tracker ("SRT") and the IMF charges

together amount to \$45,080,000, which is only slightly less than the \$52,898,560 original reserve margin calculation supporting the stipulation, to which the IMF is erroneously compared. The original reserve margin estimate was too high because it was based on the cost of building a new peaking unit. The cost of acquiring existing capacity in the market is far less. In Mr. Talbot's words, "the SRT . . . is the sole successor to the Reserve Margin charge." OCC Ex. R-1 at 4. The IMF charge is a new and duplicative charge, not justified on the basis of risk, reliability or opportunity cost; therefore, the evidence of record clearly demonstrates that the IMF should be eliminated.

Moreover, as OPAE argued in its first allegation of error, the Commission must not disregard cost and then claim, as it did with respect to the IMF, that a market-based charge need not be based on cost. Functioning markets do not exist; therefore, the resort to a claim that a charge is market based (and not cost based) is essentially a justification for any and every charge. It merely fulfills the desires of Duke for a certain revenue amount. The standard service offer must be just and reasonable under R.C. §4909.18. It is unreasonable to base a charge on a market that does not exist. The IMF charge should be eliminated.


Wherefore, OPAE respectfully requests that the Commission grant this application for rehearing. Duke's RSP applications should be dismissed. Duke should be ordered to file a new application reflecting the actual costs to provide standard service offer generation. Finally, the IMF charge should be eliminated.

Respectfully submitted,


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CERTIFICATE OF SERVICE

I hereby certify that a copy of this Application for Rehearing and Memorandum of Support was served electronically upon the parties of record identified below on this 23rd day of November 2007.


Colleen L. Mooney
Counsel for Ohio Partners for
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