

FILE

BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Duke)
Energy Ohio, Inc. to Establish and)
Adjust the Initial Level of its Distribution)
Reliability Rider)

Case No. 09-1946-EL-RDR

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COMMENTS OF THE KROGER CO.

I. INTRODUCTION

Pursuant to the Entry filed on February 2, 2010 in the above captioned proceeding, The Kroger Co. respectfully submits these comments on Duke Energy Ohio, Inc.'s ("Duke") application to establish and adjust the initial level of Rider DR ("Application"). In the Application, Duke seeks to recover costs associated with damage to Duke's distribution network caused by a wind storm that occurred on September 14, 2008 ("2008 Wind Storm").

Generally, The Kroger Co. does not object to Duke recovering reasonable costs associated with the 2008 Wind Storm. However, Duke's Application must not be approved unless it is modified to properly align the design of the cost recovery mechanism with the underlying cost allocation. Duke proposes to allocate the 2008 Wind Storm costs to customer classes based solely on class coincident peak demand. Duke then seeks to recover these costs from customers through a fixed monthly customer charge, which is appropriate to recover fixed customer costs, but not costs that are classified as demand related. The result of Duke assigning costs to customer classes based on class peak demand, and then recovering those costs from customers as if they were fixed customer costs, is to produce a distorted and fundamentally unreasonable rate impact on customers, as will be demonstrated below. Duke's allocation/rate design proposal fails to adhere to standard rate design principles in any way and should be rejected.

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The Kroger Co. strongly objects to Duke's proposal to allocate costs based solely on class peak demand, as this methodology grossly over-allocates costs to the DP class for no legitimate reason. However, if the Commission finds it reasonable for costs to be assigned to customer classes based solely on class peak demand, then the costs assigned to demand billed classes should be recovered exclusively through a demand charge. In no circumstance should Duke assign costs to demand billed customer classes based solely on class demand, and then recover the costs from those customers through a monthly fixed customer charge. This scrambled approach to recovering costs has no basis in cost causation and is contrary to the general principals of distribution rate making.

II. COMMENTS

A. The Use of a Customer Charge to Recover Costs Allocated on the Basis of Class Peak Demand is Unreasonable, Inequitable, and Inappropriate.

In the Application, Duke proposes to allocate costs of the 2008 Wind Storm to each class (except TS) based on class system peak (i.e., the average of the twelve monthly coincident peaks). While the adoption of this allocation approach is without merit in the first instance, the greatest problem with Duke's proposal is the gross mismatch between the Company's proposed cost allocation method and the rate design of the proposed Rider DR. After allocating the cost to customer classes based on peak demand, Duke proposes to recover these costs from all customer classes through a monthly customer charge.¹ Thus, 2008 Wind Storm costs are allocated entirely on the basis of class peak demand but are recovered entirely through a fixed customer charge. The use of this dichotomy to recover costs has no reasonable basis and produces egregious inequities.

It is a fundamental principle of ratemaking that rate design should reflect cost causation.

¹ Wathen Testimony at 10.

That is, customer-related costs should be recovered through customer charges and cost related to demand should be recovered (from demand-billed classes) through demand charges to the greatest extent practicable. Failure to adhere to this principle will create cross subsidies, inequities, and poor price signals. Duke's failure to adhere to the principles of cost causation is evidenced by the great disparity of rate impacts on customers that would result from Duke's proposal.

For DS customers, Duke proposes a Rider DR charge of \$15.64 per month, whereas for DP customers Duke proposes a Rider DR charge of \$361 per month. The distribution rate impacts on DS and DP customers from Duke's proposal are shown in Table 1 below.

Table 1

DS Customers		DP Customers	
kW	% Revenue Increase	kW	% Revenue Increase
50	6.15%	300	27.13%
100	3.20%	400	21.15%
150	2.16%	500	17.32%
300	1.10%	750	11.93%
500	0.66%	1,000	9.10%
1000	0.33%	2,000	4.67%
		5,000	1.90%
		10,000	0.95%

As shown in Table 1, a DS customer with a billing demand of 50 kW would experience a 6.15% increase in its distribution service bill, whereas as a 1,000 kW customer would experience an increase of just 0.33%. This disparity in rate impact is without justification. As Duke is proposing to allocate Rider DR cost to classes on the basis of class peak demand, there is no reason for customer impacts within a rate schedule to vary significantly when customer kW

demand varies, let alone swing wildly as occurs under Duke's proposal.

The inequities of Duke's proposal are even more pronounced in the case of DP customers. A 300-kW DP customer would experience a distribution service increase of 27.13% under Duke's proposal, whereas a 10,000-kW customer would experience a distribution rate increase of 0.95%. This disparity is nothing short of outrageous. The unfair treatment of smaller DP customers is underscored when comparing the impact of Duke's proposal between DS and DP: a 300 -kW DS customer would experience a rate increase of 1.10% while the DP customer would suffer the 27.13% increase noted above. Duke offers no justification why customers with the exact same level of demand, should pay such a significantly different portion of the 2008 Wind Storm costs, just because the customer receives electric service under a different rate schedule.

The causes of the outlandish rate impacts from Duke's proposal are not difficult to grasp. *Within* the DS and DP rate schedules the disparities are the result of allocating costs to DS and DP based on class demand, but then failing to recover these costs through a demand charge, but instead, recovering them through a fixed customer charge. The disparities *between* DS and DP customers are rooted in the flaws of Duke's cost allocation methodology, discussed below.

In summary, Kroger does not object to recovering a portion of Rider DR costs through a customer charge *to the extent that costs are allocated among classes using a customer allocator*. However, if costs are allocated exclusively on the basis of demand, then cost recovery for demand-billed classes should occur exclusively through a demand charge.

B. Duke's Cost Allocation Methodology for Distribution Cost of Service Over-Allocates Costs to the DP Class.

As stated above, Duke proposes to allocate costs of the 2008 Wind Storm to each class (except TS) based on class system peak (i.e., the average of the twelve monthly coincident

peaks). Duke justifies this allocation approach on the grounds that it was used by Duke to allocate distribution O&M expenses in Duke's last distribution cost of service study. Duke's witness Don Wathen testifies that "the cost of service study included in the Company's [rate case] application was not the subject of controversy and no party to the case offered any objection to the allocation factors proposed in the case. Therefore, it is reasonable to conclude that there is no opposition to the proposed allocation factors for establishing the proposed Rider DR charges."²

Duke's characterization of the response of parties to its last distribution cost of service study is incorrect. In Duke's last distribution rate case, The Kroger Co. objected to allocating distribution costs to customer classes based solely on peak demand. The Kroger Co. noted that certain distribution costs, such as the cost of poles and conductors, should be classified in part as "customer related" and those costs should be allocated to customer classes in part based on the number of customers in the class rather than exclusively on the basis of class demand.³ As a result of Duke's failure to classify a portion of these costs as customer-related, Duke's cost of service study under-assigned cost responsibility based on number of customers served and over-assigned cost responsibility on the basis of demand, shifting costs unreasonably to the larger customers served on the distribution system, such as the DP customer class.⁴ Attached to these Comments is the testimony of The Kroger Co.'s witness Kevin C. Higgins filed in that proceeding which more fully describes the flaws in Duke's customer class allocation

² Wathen Testimony at 8-9.

³ See PUCO Case No. 08-709-EL-AIR; Testimony of Kevin C. Higgins (2/26/2009) at 3. Mr. Higgins testified that Duke's distribution costs associated with poles and conductors should be classified as customer related and therefore a portion of Duke's class allocation factor should be classified as customer related; See also NARUC Electric Utility Cost Allocation Manual "The customer component of distribution facilities is that portion of costs which varies with the number of customers. Thus the number of poles, conductors, transformers, services, and meters are directly related to the number of customers on the utility's system." The NARUC Manual goes on to describe methodologies for incorporating the influence of customer-related costs in the allocation of costs for these accounts.

⁴ Id. at 3-4.

methodology.

For the purposes of recovering 2008 Wind Storm costs, the marriage between Duke's flawed cost-of-service approach and its arbitrary rate design produces the "worst of all worlds" for smaller DP customers. The cost allocation to the DP class is based exclusively on class peak demand, and fails to properly allocate any portion of costs using a customer allocator. Thus, the 2008 Wind Storm cost allocated to DP customers is overstated in the first instance. Then, in no small irony, Duke proposes to recover the costs allocated to DP exclusively through a customer charge, producing the extreme rate impacts on smaller DP customers shown in Table 1.

As stated above, Kroger does not object to recovering a portion of Rider DR costs through a customer charge *to the extent that costs are allocated among classes using a customer allocator*. Moreover, Kroger believes that some portion of Wind Storm costs *should* be allocated using a customer allocator (as should be the case for the cost of poles and conductors generally). However, Duke has not presented such an analysis.

The use of Duke's proposed class allocation factor in this proceeding would again over-assign the cost of the 2008 Wind Storm to the DP class which primarily serves large energy users. Duke's last distribution rate case was resolved by Stipulation entered into between the parties so the issue of Duke's class cost allocation methodology was not fully addressed by the Commission. However, Duke's flawed class allocation methodology should not be accepted as precedent to be used in future distribution rate proceedings. If the Commission is to approve the Application, then ideally, Duke's class cost allocation methodology should be modified to allocate costs based on an appropriate combination of customer-related and demand-related costs, consistent with the principles and methodologies described in the NARUC Electric Utility Cost Allocation Manual. In addition, the Commission should order Duke to use a proper class

allocation methodology in future distribution rate proceedings.

C. If the Commission Finds Duke's Proposed Customer Class Allocation Factor Reasonable, Then Costs Must Be Recovered Through a Demand Charge in Customer Classes That Are Demand Billed.

As The Kroger Co. has already noted, Duke's proposed class allocation factor is unreasonable because it over-assigns the 2008 Wind Storm costs to customer classes that contain large energy users. However, if the Commission finds it appropriate to assign costs to customer classes based solely on class demand, then a demand charge is the appropriate mechanism for such recovery. In no circumstance should Duke assign costs solely on the basis of class demand to demand billed customer classes, and then recover the costs from those customers through a fixed monthly customer charge.

The 2008 Wind Storm costs, like all distribution costs, should be classified as demand-related and/or customer-related, depending on the cost item being recovered.⁵ By allocating costs to customer classes on the basis of peak demand, Duke has chosen to classify the 2008 Wind Storm costs as demand-related. After classifying the costs as demand related, there is no reasonable basis to recover these costs through a customer charge. In customer classes that are not demand billed, such as the residential class, it may be appropriate to recover demand related cost by means other than a demand charge (such as a fixed customer charge or an energy charge). However, in customer classes that are demand billed, such as the DP class, the principles of distribution rate making require that costs allocated to customer classes based on demand must be recovered through charges based on demand.

III. CONCLUSION

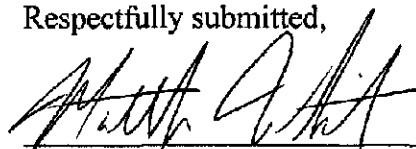
The cost recovery mechanism proposed by Duke is the worst of all worlds for certain

⁵ See NARUC Electric Utility Cost Allocation Manual, 1992, p. 89. "To ensure that costs are properly allocated, the analyst must first classify each account as demand-related, customer-related, or a combination of both"

customers in the DP class. On one hand, the DP class is assigned a disproportionate amount of costs as a result of a flawed class allocation methodology that assigns costs to customer classes based solely on customer demand. On the other hand, DP class customers are then charged a fixed monthly customer charge which recovers a disproportionate amount of costs from smaller customers in the DP class. As a result of this "double whammy", smaller customers in the DP class receive substantial rate increases under Duke's proposal, despite a relatively minor overall rate increase for all customers.

There is no reasonable basis to adopt a combination of cost allocation and rate design that produces such disparate and contorted rate impacts in the cost recovery for the 2008 Wind Storm. If Duke's Application is to be approved by the Commission it must be modified to ensure that the cost of the 2008 Wind Storm is shared equitably by all distribution service customers. Ideally the Commission should order Duke to correct the errors in its distribution rate allocation factor so that cost allocation to classes is based on the appropriate mix of fixed customer costs and demand costs. However, if the Commission finds it reasonable for costs to be assigned to customer classes based solely on class peak demand, the costs assigned to demand billed classes should be recovered exclusively through a demand charge. In addition, going forward the Commission should order Duke to use an appropriate class allocation factor in future distribution rate proceedings.

Respectfully submitted,



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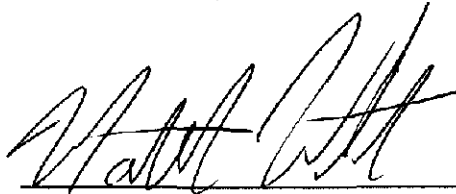
I hereby certify that a copy of the foregoing *Comments of The Kroger Co.* was served upon the following parties of record or as a courtesy, via electronic transmission or U.S. First Class mail, on February 23, 2010.

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