BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Commission's	)	
Review of Fuel Adjustment Clause	)	**Case No. 10-479-EL-UNC**
Guidelines	)	

REPLY COMMENTS OF THE DAYTON POWER AND LIGHT COMPANY

I. INTRODUCTION

On June 23, 2010, The Public Utilities Commission of Ohio ("Commission") issued an Entry seeking initial comments by July 14, 2010, and reply comments by July 28, 2010, on the Commission Staff's ("Staff") proposed Fuel Adjustment Clause Guidelines ("Proposed Guidelines"). The Dayton Power and Light Company ("DP&L") previously submitted its initial comments. These comments are submitted in reply to the initial comments filed by others.

II. GENERAL OBSERVATIONS

DP&L generally supports the comments that were submitted by Duke Energy Ohio ("Duke") and the joint comments submitted by AEP subsidiaries Columbus Southern Power and Ohio Power ("AEP"). These companies and DP&L did not always propose the same modifications, but there were some common themes. Duke, for example, made much the same point that DP&L made that several out-moded, pre-RTO era provisions of the old guidelines were carried over into the proposed guidelines.[1] AEP and DP&L both made proposed

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[1] Duke Initial Comments at 2; DP&L Initial Comments at 2-3.

modifications to ensure that the fuel clause auditor was focusing on items that affected fuel clause costs rather than some broader concern.[2]

DP&L does oppose certain aspects of the initial comments filed by Ohio Consumers' Counsel ("OCC"). In some instances, OCC is seeking modifications that would take an auditor far afield of the proper scope of a fuel audit. Such recommendations would increase the costs of audits substantially. Then, OCC compounds that problem by proposing a denial of recovery from customers of the costs of the audit. OCC's proposal is quite likely illegal; the incurrence of costs pursuant to a PUCO-mandated fuel audit is certainly a legitimate regulatory expense.

DP&L has also reviewed the Initial Comments of Eagle Energy, LLC. A key aspect of these comments appear to be contradictory in that it is first proposed that there may be no need for fuel audits anymore because of competitive pressures, then suggested that fuel audits could be waived if the utility agreed to fixed fuel prices, then suggested that a Fuel Adjustment clause be "set at least annually but would recommend a rate be set consistent with the term of the ESP."[3] Reliance on competitive pressures as a means to police fuel price fluctuations is inconsistent with the concept of establishing fixed fuel prices and it is not clear how one would simultaneously set fuel prices at least annually and also set them for the two or three year term of an ESP. DP&L also strongly objects to Eagle Energy's proposed use of the term "lowest practical price." As noted in DP&L's Initial Comments, that is now too narrow a term. Fuel procurement decisions need to be evaluated in a context that recognizes the existence of hedging instruments and other risk management strategies. DP&L proposed that a term used in some

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[2] E.g., both AEP and DP&L suggested that the reference in section II.A.(5)(d) to environmental compliance be clarified so that the auditor was reviewing emission allowance costs and retirements rather than an open-ended requirement to assess environmental compliance, which is more appropriately reviewed by the federal and state environmental agencies. AEP Initial Comments at 6-7; DP&L Initial Comments at 3-4.

[3] Compare Eagle Energy Initial Comments at 2 and 3.

parts of the proposed guidelines, "lowest reasonable overall cost," should be applied consistently throughout the guidelines.

III. SPECIFIC COMMENTS

A. Comments with Respect to AEP's Initial Comments.

AEP voiced concerns regarding the undefined use of the term "Economic Efficiency" in the proposed guidelines. AEP left that phrase alone in at least one instance, section II.A.6(d) new subsection (iv), but proposed revisions to the environmental section II.A.8 that avoided the use of that term, which was stated to be unclear.[4] DP&L had similar concerns, applicable to all uses of that term within the proposed guidelines, and therefore proposed in its Initial Comments at 3 that the PUCO define the term as follows:

> "Economic efficiency," in the context of a power purchase or sale or a fuel contract, means a transaction whose overall costs, based on information known at the time the transaction was entered into, appeared to be reasonable and lower than the overall costs of readily available alternatives, taking into consideration reliability of supply, the operating and environmental characteristics of fuel, and other relevant factors including counterparty past performance and financial stability.

DP&L supports AEP's proposal to delete certain references to "Company" so as to clarify when the guideline applies to an electric utility and when it is more broadly referring to a coal company or some other type of entity.[5] Similarly, the modifications proposed by AEP to Section I and II.A.(1) are useful clarifications. AEP proposes a substantive addition to Section II.A.(2) that would clarify that the objective of the audit includes consideration of securing reliable supplies delivered in a timely manner and managing risk. That proposal is consistent with DP&L's views expressed above in its proposed definition of Economic Efficiency. It is also consistent with DP&L's views that while the auditor should not seek to substitute his or her

[4] AEP Initial Comments at 10, 14.
[5] AEP Initial Comments at 2.

judgment of the specific mechanics of a utility's hedging and other risk management tools, the evaluation of the reasonableness of a utility's fuel procurement practices should recognize the existence and use of such tools.

DP&L and AEP also expressed similar positions with respect to section II.A.(6) that the fuel auditor should be focused on environmental issues that directly affect fuel costs, such as emission allowance transactions.[6] The fuel auditor should not be expected to be an environmental compliance expert who would substitute his or her judgment with respect to matters specifically delegated to the U.S. and Ohio Environmental Protection Agencies.

DP&L and AEP both proposed modifications in II.A.(6)(b) to focus the auditor on fuel cost-related matters.[7] The proposed guidelines include ambiguous language that could be interpreted as allowing the auditor to delve into areas such as transmission and distribution design and maintenance practices because it refers to the utility's ability to "procure fuel and provide reliable electric service." DP&L's proposal, the insertion of the word "generation" after reliable, is different from AEP's proposal which rewrites the provision more extensively. DP&L can support either approach.

AEP's substitution of the word "targets" in lieu of "limits" is a very positive suggestion in section II.A.(6)(d)(i). DP&L does not oppose the other changes proposed to that section by AEP.

AEP's proposed modifications to II.A.(6)(e) are generally supported by DP&L. With respect to subparagraph II.A.(6)(e)(vi), however, DP&L believes that AEP's proposal is an improvement over that which was proposed, but still wrongly implies that Ohio utilities should be evaluating and attempting to control coal companies' compliance with OSHA standards and

[6] AEP Initial Comments at 6-7; DP&L Initial Comments at 3-4.
[7] AEP Initial Comments at 7-8; DP&L Initial Comments at 4.

water quality standards. As noted in DP&L's initial comments as a technical point, the drafters of this language probably meant MSHA, the Mine Health and Safety Administration, rather than OSHA, whose jurisdiction is limited when another federal agency is given the specific authority to regulate employee safety practices in a particular area. The more substantive concern, however, is that DP&L is not in a position to make such evaluations and believes that there should be no implication that it is required to. The language in the guidelines previously in effect directed auditors to determine whether and how a utility evaluates the "performance and business respectability" of coal companies. That is still an ambiguous standard but appears to focus more on the matters that are within the realm of what a utility should be expected to evaluate; i.e., if a particular coal company has a business reputation of late shipments, non-conforming shipments, defaults on obligations, or strategically timed demands to renegotiate agreements, those are factors that a utility can evaluate and use in its consideration as to whether or not to execute an agreement with the coal company. In contrast, a utility has no special expertise or ability to weigh the implications of past coal company safety or environmental citations that the coal company may be disputing or may have resolved going forward. DP&L proposes that this subsection be reworded to state: "what checks are run and how coal companies' financial stability and past performance in meeting their contractual obligations are evaluated by the company."

DP&L strongly supports AEP's proposed deletion in section II.A.(8)(e), which as proposed would have imposed a duty on an auditor to consider "foregone" emission allowance transactions never made and perhaps not even contemplated. AEP correctly notes how burdensome and inefficient it would be to require proof of a "universal negative" as to why some potential transaction was not made. DP&L would add that such a standard is rife with the

potential for "Monday morning quarterbacking." As set forth in DP&L's proposed definition of Economic Efficiency, evaluations must be made based on what was known at the time a transaction was made.

B. Comments with Respect to Duke's Initial Comments

DP&L supports the two broad themes discussed in Duke's Initial Comments: 1) some aspects of the proposed Guidelines are from a pre-RTO era and should not have been carried forward from the Guidelines that were previously in effect;[8] and 2) the complexities of the current market are such that the "price" of fuel cannot be evaluated alone but must be evaluated in conjunction with the costs associated emission allowances, reagent costs and power purchase costs.[9]

C. Comments with Respect to OCC's Initial Comments.

DP&L cannot over-emphasize the degree to which it opposes OCC's concept that the fuel audit process be broad and far-reaching, that utilities should be charged for the privilege of being audited, and then utilities should be denied recovery through the fuel clause of these mandated fuel clause-related expense.[10] Utilities have the right to recover prudently incurred costs associated with providing standard offer service. In a regulatory structure where the PUCO is picking the auditor and approving the amount that we pay the auditor, such payments are unquestionably prudently incurred costs. An arbitrary and automatic denial of recovery such as that proposed by OCC is particularly offensive in the context of auditing fuel expenses on which the utility earns no return. OCC's proposal thus has the effect of ensuring an under-recovery and trapping legitimately and prudently incurred costs.

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[8] Duke Initial Comments at 2, 8-9.
[9] Duke Initial Comments at 3-6.
[10] OCC Initial Comments at 3 and citations therein.

The OCC's cited authorities appear to support only the front half of its proposal, i.e., that the Commission has in the past ordered that the costs of a particular audit be directly assessed to the audited utility. OCC's citations do not support the proposition that the utility should then be barred from recovery of the costs of the audit from ratepayers. In particular, OCC's reliance is misplaced on a 1999 order involving fuel clause audits and a 2002 order involving the costs of hiring a market research consultant for customer education during the transition to allowing retail electric choice. In the 1990s, DP&L was directly assessed the costs of fuel clause audits, but DP&L personnel involved in those cases have confirmed that those costs were then recovered through the fuel clause. Similarly, the costs of the market research consultant for consumer education were recoverable transition period expenses.[11]

OCC's comments with respect to the review of contract amendments seem to suggest that the fuel auditor should be looking today at the reasons why someone several years ago may have entered into a contract with a price escalator.[12] DP&L's view is that if an evaluation of utility personnel's' motivations and thought processes are to be undertaken, this provision should be limited to amendments made during the audit period and not include price adjustments that occur as the result of a contract provision entered into years ago (a.k.a. legacy contracts).

OCC's proposed additions to II.A.(6)(c) introduce an ambiguity. It appears that OCC is attempting to address concerns that it may have with respect to transactions between affiliates. As drafted, however, the language in subparagraphs (vi) and (vii) could be construed to imply

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[11] DP&L has no direct knowledge of the case cited by OCC relating to year 2000 audits of Ameritech Ohio, but would note that both cited orders in this case appear to involve audits that were ordered as the result of large numbers of customer complaints and a prior order where explicit findings had been made of inadequate service. *In the Matter of the Commission Ordered Investigation of Ameritech Ohio Relative to Its Compliance with Certain Provisions of the Minimum Telephone Service Standards*, Case No. 99-938-TP-COI, Entries of Oct. 18, 2000. No such findings are present here and the imposition of a penalty in the form of non-recovery of Commission-mandated costs in the absence of such findings could not be legally justified.

[12] OCC Initial Comments at 5.

that a non-regulated affiliate could be compelled to disclose its contracts made with third parties with the auditor making some sort of side-by-side comparison between terms and conditions of the non-regulated entity's contracts and the terms and conditions of a utility's contracts. If any aspect of OCC's proposal here is to be considered, the language should be modified to track more closely with its proposed subparagraph (viii), which does focus directly on those contracts that are between a utility and an affiliate.

DP&L does not support OCC's ambiguous language for a new section II.A.(6)(f) relating to a review of practices employed to manage fuel price volatility, including risk management and hedging practices.[13] As OCC has drafted this recommendation, it appears to invite an auditor to substitute his or her judgment as to the proper design and procedures of a hedging program. At most, this guideline should be rephrased to direct the auditor as follows: "review whether the utility followed its internal guidelines, processes and procedures relating to managing fuel price volatility, including risk management and hedging, and adequately documented and explained any deviations."

DP&L's initial comments with respect to II.A.(8) relating to environmental compliance were designed to refocus the scope of the fuel audit back to fuel-related costs, which in this context would include emission allowance transactions. OCC's proposals inappropriately broaden the scope even beyond that in Staff's proposed guidelines. In particular, DP&L would strike subparagraphs (f) and (g) of OCC's proposals.

OCC proposes revisions to section II.A.(10)(e) that would call for an auditor to evaluate managerial decisions not only in light of the information known to management, but also in light of information that the auditor subjectively believes "should have been known."[14] This kind of

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[13] OCC Initial Comments at 9.
[14] OCC Initial Comments at 12-13.

standard creates vast opportunities for litigation and opinion testimony regarding influences on prices whose significance may become apparent only after the fact. A utility should not have to defend against allegations that it should have been able to predict market price changes based on someone's subjective views of what management "should have known." While OCC claims that its reformulation is consistent with the way the Commission has defined prudence in the past, it cites only one case, which involved issues unique to the nuclear industry. OCC's reformulation is inconsistent with the standard that the Commission employed in its fuel clause review process as shown by the language of the prior guidelines which used the exact language reflected in the proposed guideline that OCC seeks to revise. Both the old and the proposed standard avoid the subjectivity of a "should have known" standard by requiring an evaluation based on "management decisions in light of the conditions, circumstances, and available information at the time the decisions were made."[15]

DP&L opposes OCC's insertion of the phrase "and sales for resale" into proposed guidelines II.B.(5)(e) and II.B.(9)(a) and vigorously opposes the rationale presented by OCC for such changes.[16] Sales for resale are not jurisdictional to this Commission. Apart from ensuring that the costs associated with sales for resale are not somehow subsidized by retail sales customers, the PUCO and the fuel auditor should have no further interest in them. OCC makes no attempt to hide its rationale for this modification – it explicitly is seeking an indirect approach to re-litigate an issue it already lost once in a recent AEP case where it argued that the Commission should credit the retail fuel clause by the revenues from off-system sales. While OCC mentions only AEP's Electric Security Plan proceeding, OCC's proposal and concept here is also completely at odds with the existing DP&L settlement, which provides explicit

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[15] See pre-existing guideline 4901:1-11, Appendix D, (L)(9).

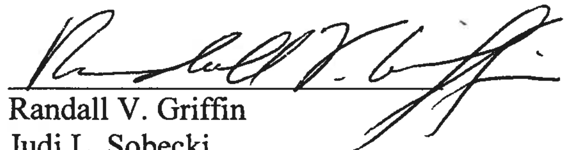
[16] OCC Initial Comments at 16.

mechanisms for allocating fuel costs and purchased power costs between wholesale and retail jurisdictions. In order to implement OCC's proposal, that settlement would need to be ripped up and replaced with an approach that begins with assigning 100% of fuel costs to retail customers. Such approaches were actually used at one time in the industry – back in the 1950s or so, an era when fuel clauses first became prevalent, when utilities were monopoly providers of generation service in designated service areas, and when off system sales were rare events done primarily to assist a neighboring utility that was caught short due to a forced outage. Such an approach makes no sense in the modern era where market based rates transacted through Regional Transmission Organizations are the norm.

IV. CONCLUSION

DP&L appreciates the opportunity to provide these comments relative to the Proposed Fuel Adjustment Clause Guidelines. DP&L urges the Commission to adopt the modifications suggested in DP&L's initial comments and in these reply comments.

Respectfully submitted,



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Summary: Reply Comments electronically filed by Mr. Randall V Griffin on behalf of The Dayton Power and Light Company