

FILE

BEFORE

THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Duke)
Energy Ohio for Approval of a Market)
Rate Offer to Conduct a Competitive)
Bidding Process for Standard Service) Case No. 10-2586-EL-SSO
Offer Electric Generation Supply,)
Accounting Modifications, and Tariffs for)
Generation Service.)

VOLUME II
TESTIMONY

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DIRECT TESTIMONY OF

BRIAN D. SAVOY

ON BEHALF OF

DUKE ENERGY OHIO, INC.

November 15, 2010

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BDS-1:	Projected Statements of Income
BDS-2:	Projected Balance Sheets
BDS-3:	Projected Sources and Uses of Funds

I. INTRODUCTION

1 **Q. PLEASE STATE YOUR NAME AND BUSINESS ADDRESS.**

2 A. My name is Brian D. Savoy, and my business address is 526 South Church Street,
3 Charlotte, North Carolina 28202.

4 **Q. BY WHOM ARE YOU EMPLOYED AND IN WHAT CAPACITY?**

5 A. I am employed by Duke Energy Business Services LLC (DEBS) as General
6 Manager of Corporate Financial Planning and Analysis. DEBS provides various
7 administrative and other services to Duke Energy Ohio, Inc. (Duke Energy Ohio
8 or the Company) and other affiliated companies of Duke Energy Corporation
9 (Duke Energy).

10 **Q. PLEASE BRIEFLY DESCRIBE YOUR EDUCATION AND**
11 **PROFESSIONAL EXPERIENCE.**

12 A. I earned a bachelor of business administration degree in accounting from Lamar
13 University in Beaumont, Texas. I am a certified public accountant in both Texas
14 and Ohio.

15 Prior to joining Duke Energy, I was a Manager with the international
16 accounting firm, Deloitte & Touche, based in Houston, Texas. During my tenure
17 at Deloitte & Touche, I served various energy clients through audit and consulting
18 services.

19 I joined Duke Energy in July 2001 as Manager of Technical Accounting in
20 Houston, Texas and, in December of that year, I was named Director of Risk
21 Management Accounting. In April 2004, I was promoted to Senior Director of
22 Risk Management Accounting and Analysis at Duke Energy North America in

1 Houston, Texas. In this role, I led the derivative accounting and trading control
2 functions for the energy trading and marketing activities of Duke Energy.

3 In April 2006, I was promoted to Vice President and Controller of the
4 Commercial Power unit of Duke Energy in Cincinnati, Ohio. In this role, I was
5 responsible for the financial accounting, reporting and internal controls of Duke
6 Energy's non-regulated generation and Duke Energy Generation Services
7 businesses.

8 In March 2009, I was appointed to my current position as General
9 Manager of Corporate Financial Planning & Analysis in Duke Energy's
10 headquarters in Charlotte, North Carolina. I am responsible for leading the
11 financial forecasting and planning for the corporation.

12 **Q. PLEASE DESCRIBE YOUR DUTIES AS GENERAL MANAGER OF**
13 **CORPORATE FINANCIAL PLANNING AND ANALYSIS.**

14 **A.** I lead and direct a team of approximately thirty professionals in the preparation
15 of the short- and long-term financial forecasts of earnings and cash flow of Duke
16 Energy, including each operating unit. This role also includes financial modeling
17 of sensitivities and strategic scenarios and evaluating the projected financial
18 impact of those alternatives. The primary deliverables from this group are
19 financial presentations to senior management and the board of directors as well as
20 financial targets for employee incentive compensation.

21 **Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THE PUBLIC**
22 **UTILITIES COMMISSION OF OHIO?**

23 **A.** No.

1 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS**
2 **PROCEEDING?**

3 A. The purpose of my testimony is to sponsor pro forma financial projections in
4 respect of the implementation of the Company's proposed competitive bidding
5 process (CBP) plan upon Duke Energy Ohio's generation rates for the first three
6 years under the MRO. The projections pertain to a three-year period, consistent
7 with the Company's expectation that it will transfer its legacy generating assets to
8 an affiliate on or before June 1, 2014.

II. DISCUSSION

9 **Q. WHAT ARE THE ATTACHMENTS FOR WHICH YOU ARE**
10 **RESPONSIBLE?**

11 A. I am sponsoring all or part of the items:

- 12 • BDS-1: Projected Statements of Income
- 13 • BDS-2: Projected Balance Sheets
- 14 • BDS-3: Projected Sources and Uses of Funds

15 **Q. PLEASE IDENTIFY AND DESCRIBE ATTACHMENT BDS-1.**

16 A. Attachment BDS-1 is the Projected Statements of Income for the period between
17 January 1, 2012, and May 31, 2014.

18 **Q. PLEASE IDENTIFY AND DESCRIBE ATTACHMENT BDS-2**

19 A. Attachment BDS-2 contains the Projected Balance Sheets for the years ending
20 December 31, 2012, December 31, 2013, and December 31, 2014.

21 **Q. PLEASE IDENTIFY AND DESCRIBE ATTACHMENT BDS-3.**

1 A. Attachment BDS-3 is the Projected Sources and Uses of Funds for the period
2 between January 1, 2012, and May 31, 2014.

3 **Q. HOW ARE THESE ATTACHMENTS AND SCHEDULES RELEVANT TO**
4 **THE COMPANY'S REQUEST FOR A MARKET RATE OFFER?**

5 A. As I have been informed, Ohio law allows for an electric utility company such as
6 Duke Energy Ohio to extend to its customers a market rate offer (MRO). In
7 seeking approval of such an offer, the Company must satisfy certain criteria.
8 Relevant to my testimony is the requirement that the Company provide pro forma
9 financial projections.

10 Specifically, I understand that Duke Energy Ohio must provide pro forma
11 financial projections, for the duration of the CBP plan, of the effect that
12 implementing a CBP has upon the Company's generation, transmission, and
13 distribution rates. I further understand that these projections must take into
14 consideration the required blending period during which the Company will
15 transition to having its entire standard service offer (SSO) load acquired via a
16 competitive auction.

17 **Q. DOES THE PROPOSED CBP PLAN HAVE ANY EFFECT UPON DUKE**
18 **ENERGY OHIO'S DISTRIBUTION RATES?**

19 A. No. As a result, I have not prepared pro forma financial projections concerning
20 distribution rates.

21 **Q. DOES THE PROPOSED CBP PLAN HAVE ANY EFFECT UPON DUKE**
22 **ENERGY OHIO'S TRANSMISSION RATES?**

1 A. No. Although the method of collection will change slightly due to the tariff
2 changes proposed by Company witness William Don Wathen Jr., the proposed
3 MRO will have no impact on the overall projected transmission revenue or on
4 projected transmission expense. As a result, I have not prepared pro forma
5 financial projections concerning transmission rates.

6 **Q. WHAT IS THE DURATION OF THE CBP PLAN THAT YOU USED FOR**
7 **PURPOSES OF DEVELOPING THE PRO FORMA FINANCIAL**
8 **PROJECTIONS ATTACHED TO AND A PART OF YOUR TESTIMONY?**

9 A. The pro forma financial projections attached to and a part of my testimony reflect
10 a CBP plan that culminates in a complete transition to market by the end of the
11 second year of the Company's MRO. For informational purposes, the second
12 year of Duke Energy Ohio's MRO covers the period between June 1, 2013, and
13 May 31, 2014, as discussed by Duke Energy Ohio witness James S. Northrup.

14 As explained by Duke Energy Ohio witness Wathen, there is a period of
15 transition for the Company, as it migrates from its current SSO price to an SSO
16 price that is derived solely from the auction process. This period of transition – or
17 blending period – is a function of the fact that the Company owned electric
18 generating facilities as of July 31, 2008. As I understand, the law proposes a term
19 for this transition period, during which the Company's SSO price is determined
20 with consideration to both the Company's most recent SSO price, as may be
21 adjusted, and the prospective market bid. The percentage of the Company's
22 SSO load that is subject to auction defines the percentages by which the SSO
23 price is blended.

1 Duke Energy Ohio is proposing here that its transition to market occur
2 over a three-year period such that, by year three, its entire SSO load is auctioned
3 and the SSO price is no longer influenced by the Company's most recent SSO
4 price. Duke Energy Ohio witnesses Wathen and Judah L. Rose provide the
5 support for this proposal. I have developed the pro forma financial projections
6 with reference to this proposal.

7 Once the Company's transition to market is complete, the generation
8 charges or standard service offer (SSO) charge resulting from the continued
9 execution of the CBP plan will be passed through to customers.

10 **Q. ARE THE SSO CHARGES THAT ARE REFLECTED IN THE PRO**
11 **FORMA FINANCIAL PROJECTIONS AFFECTED BY THE**
12 **COMPANY'S INTENTION OF TRANSFERRING ITS LEGACY**
13 **GENERATION ASSETS?**

14 **A.** For the following reasons, I do not believe so. Again, the Company is proposing
15 that the transition period conclude at the end of the second year of the MRO, after
16 which point all of the Company's load will be acquired through a competitive
17 auction. As described by Duke Energy Ohio witness Charles R. Whitlock, the
18 Company is further intending, subject to the appropriate approvals, to transfer its
19 legacy generating assets no later than this completed transition to market by year
20 three of the MRO. Thus, in year three of the Company's MRO, the Company's
21 continued ownership of generation assets is immaterial to the SSO charges
22 derived from the competitive auction process. Stated another way, there will be
23 no correlation between the generation assets and the generation charges derived

1 from an auction for all of the Company's load. Although the transfer of the
2 legacy generation assets will not affect the pro forma financial projections, the
3 transfer would function to eliminate any generation-related items from the income
4 statement (e.g., earnings, expenses, etc.) and balance sheet (e.g., plant, equity,
5 etc.).

6 **Q. WHAT IS THE IMPACT ON GENERATION CHARGES IF THE**
7 **COMPANY ELECTS TO TRANSFER ITS LEGACY ASSETS BEFORE IT**
8 **FULLY TRANSITIONS TO MARKET?**

9 A. If the Company were to transfer its legacy generating assets before the third year
10 of the MRO, it would have to procure power necessary to serve a portion of its
11 SSO load. And, should that circumstance arise, Duke Energy Ohio would enter
12 into a purchase power agreement (PPA) and the generation charges resulting from
13 that PPA would also be passed through to customers. But as there is some degree
14 of uncertainty in identifying a date – prior to the third year of the MRO – by
15 which the Company may transfer its legacy generation assets, I have prepared the
16 pro forma financial projections consistent with a transfer of assets and completed
17 migration to market occurring at the same time.

18 **Q. PLEASE EXPLAIN WHY YOU HAVE PROVIDED PRO FORMA**
19 **FINANCIAL PROJECTIONS THAT COVER THE THREE-YEAR,**
20 **TRANSITION PERIOD AS PROPOSED BY THE COMPANY.**

21 A. It is my understanding that the pro forma financial projections concern the
22 implementation of the CBP plan, which includes the blending period required
23 under R.C. 4928.142(D). As written, this particular provision advises that the

1 SSO price for the first five years of the MRO involve a blend between the
2 Company's most recent SSO price and the market bid price. Admittedly, the
3 Commission has discretion to determine the period of transition to full market and
4 Duke Energy Ohio has offered a slightly shorter period than that proposed in the
5 law. Accordingly, I have provided the pro forma financial projections consistent
6 with the Company's proposal. I would further note that, when the transition to
7 market is complete as of June 1, 2014, Duke Energy Ohio's financial statements
8 will not include generation revenues and expenses.

9 **Q. DID YOU INCLUDE IN YOUR PROJECTIONS A COMPARISON**
10 **BETWEEN THE PROJECTED ADJUSTED GENERATION SERVICE**
11 **PRICES UNDER THE CBP PLAN AND THE PROJECTED ADJUSTED**
12 **GENERATION SERVICE PRICES UNDER THE COMPANY'S**
13 **PROPOSED ELECTRIC SECURITY PLAN?**

14 **A.** No. The Company is not proposing an electric security plan in this application.
15 Consequently, this provision in O.A.C. 4901:1-35-03(B)(2)(j) is moot.

16 **Q. WHAT ASSUMPTIONS DID YOU MAKE FOR PURPOSES OF**
17 **DEVELOPING THESE PRO FORMA FINANCIAL PROJECTIONS?**

18 **A.** I made the following assumptions:

- 19 • The Company's transition to market is completed in the third year of the
20 MRO, with 100% of the SSO load acquired via the CBP plan beginning in
21 year three and continuing every year thereafter.
- 22 • Duke Energy Ohio's non-legacy generation assets are transferred to an
23 affiliate no later than January 1, 2011.

- 1 • Duke Energy Ohio's legacy generating assets are transferred to an affiliate
- 2 by the third year of the MRO, when the transition to market is complete.
- 3 • The most recent SSO price is 7.34 ¢/kWh.
- 4 • The most recent SSO price of 7.34 ¢/kWh is not adjusted for fuel,
- 5 purchased power, and environmental compliance costs during the first two
- 6 years of the Company's proposed MRO.
- 7 • All of the load in Duke Energy Ohio's service territory is served via the
- 8 Company's MRO.

III. CONCLUSION

9 **Q. WERE ATTACHMENTS BDS-1 THROUGH BDS-3 PREPARED BY YOU**
10 **OR PERSONS UNDER YOUR DIRECTION AND CONTROL?**

11 **A. Yes.**

12 **Q. DOES THIS CONCLUDE YOUR PRE-FILED DIRECT TESTIMONY?**

13 **A. Yes.**

Duke Energy Ohio
Legacy Generation Assets
Projected Statements of Income

Attachment BDS -1
Page 1 of 1

Line	Description	2012	2013	2014
1	Operating Revenues			
2	Sales of Electricity - Retail	1,452,526,000	1,412,400,000	568,034,000
3	Sales of Electricity - Wholesale	702,631,000	790,994,000	380,071,000
4	Other Operating Revenues	68,587,000	28,692,000	14,259,000
5	Total Electric Operating Revenues	2,223,744,000	2,232,086,000	962,364,000
6	Cost of Generation and Purchased Power			
7	Fuel Cost	508,865,000	546,268,000	253,953,000
8	Emission Cost	525,000	138,000	8,000
9	Purchased Power	1,075,090,000	1,069,468,000	462,493,000
10	Total Cost of Generation and Purchased Power	1,584,480,000	1,615,874,000	716,454,000
11	Gross Margin	639,264,000	616,212,000	245,910,000
12	Operating Expenses			
13	Operation and Maintenance	206,452,000	207,237,000	89,357,000
14	Depreciation and Amortization	109,594,000	109,139,000	45,146,000
15	Taxes Other Than Income Taxes	35,084,000	35,680,000	15,628,000
16	Total Operating Expenses	351,130,000	352,056,000	150,131,000
17	Operating Income	288,134,000	264,156,000	95,779,000
18	Interest Expense	63,155,000	63,155,000	26,315,000
19	Earnings Before Income Tax	224,979,000	201,001,000	69,464,000
20	Income Taxes			
21	Current Income Taxes	62,037,000	51,843,000	4,138,000
22	Deferred Income Taxes	22,240,000	22,648,000	20,765,000
23	Total Income Taxes	84,277,000	74,491,000	24,903,000
24	Net Income	140,702,000	126,510,000	44,561,000

Duke Energy Ohio
Legacy Generation Assets
Projected Balance Sheets

Attachment BDS - 2
Page 1 of 1

Line	Description	2012	2013	2014
1	ASSETS			
2	Gross Plant in Service	2,780,647,000	2,815,134,000	-
3	CWIP	20,040,000	37,614,000	-
4	TOTAL UTILITY PLANT	2,800,687,000	2,852,748,000	-
5	Accumulated Depreciation	215,482,000	270,701,000	-
6	NET UTILITY PLANT	2,585,205,000	2,582,047,000	-
7	CURRENT ASSETS			
8	Cash and Cash Equivalents	431,001,000	675,914,000	-
9	Receivables	211,552,000	220,252,000	-
10	Inventory	120,496,000	120,496,000	-
11	Other	46,342,000	46,342,000	-
12	TOTAL CURRENT ASSETS	809,391,000	1,063,004,000	-
13	Intangible Assets, Net	250,987,000	248,915,000	-
14	Other Non-current Assets	29,128,000	16,024,000	-
13	TOTAL ASSETS	3,674,711,000	3,909,990,000	-
14	EQUITY AND LIABILITIES			
15	Common Stock	379,315,000	379,315,000	-
16	Additional Paid-in Capital	2,270,352,000	2,270,352,000	-
17	Retained Earnings	(1,326,084,000)	(1,199,574,000)	-
18	Accumulated Other Comprehensive income (loss)	(28,037,000)	(28,037,000)	-
19	TOTAL EQUITY	1,295,546,000	1,422,056,000	-
20	LONG TERM DEBT	1,263,097,000	1,263,097,000	-
21	TOTAL CAPITAL	2,558,643,000	2,685,153,000	-
22	CURRENT LIABILITIES			
23	Accounts Payable	165,591,000	170,255,000	-
24	Notes Payable and Commercial Paper	-	-	-
25	Taxes Accrued	155,600,000	236,044,000	-
26	Interest Accrued	8,359,000	9,372,000	-
27	Other	45,043,000	45,043,000	-
28	TOTAL CURRENT LIABILITIES	374,593,000	460,714,000	-
29	DEFERRED CREDITS AND OTHER LIABILITIES			
30	Deferred Income Taxes	645,755,000	668,403,000	-
31	Asset Retirement Obligations	4,593,000	4,593,000	-
32	Other	91,127,000	91,127,000	-
33	TOTAL DEFERRED CREDITS AND OTHER LIABILITIES	741,475,000	764,123,000	-
34	TOTAL EQUITY AND LIABILITIES	3,674,711,000	3,909,990,000	-

Duke Energy Ohio
Legacy Generation Assets
Projected Sources and Uses of Funds

Attachment BDS - 3
Page 1 of 1

Line	Description	2012	2013	2014
1	SOURCE OF FUNDS			
2	Net Income	140,702,000	126,510,000	44,561,000
3	AFUDC	3,365,000	4,862,000	4,590,000
4	Depreciation / Amortization	109,594,000	109,139,000	45,146,000
5	Deferred Income Taxes	22,240,000	22,648,000	20,765,000
6	Changes in Working Capital	115,941,000	167,492,000	82,383,000
7		391,842,000	430,651,000	197,445,000
8	APPLICATION OF FUNDS			
9	Capital Expenditures	170,579,000	103,909,000	62,067,000
10	Dividends Paid	-	-	-
11		170,579,000	103,909,000	62,067,000