

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 IV

TESTIMONY

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DIRECT TESTIMONY OF

WILLIAM DON WATHEN JR.

ON BEHALF OF

DUKE ENERGY OHIO, INC.

November 15, 2010

TABLE OF CONTENTS

PAGE

I.	INTRODUCTION	1
II.	MRO STANDARD SERVICE OFFER PRICE STRUCTURE.....	2
III.	DISCUSSION OF RIDERS IN THE MRO.....	14
IV.	TRANSMISSION RIDERS	22
V.	OTHER NEW RIDERS.....	27
VI.	OTHER RIDER CHANGES	28
VII.	CONCLUSION	29

I. INTRODUCTION

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

2 A. My name is William Don Wathen Jr., and my business address is 139 East Fourth
3 Street, Cincinnati, Ohio 45202.

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 and Vice President of Rates, Ohio and Kentucky. DEBS provides
7 various administrative and other services to Duke Energy Ohio, Inc., (Duke
8 Energy Ohio or the Company) and other affiliated companies of Duke Energy
9 Corporation (Duke Energy).

10 **Q. PLEASE SUMMARIZE YOUR EDUCATION AND PROFESSIONAL**
11 **EXPERIENCE.**

12 A. I received Bachelor Degrees in Business and Chemical Engineering, and a Master
13 of Business Administration Degree, all from the University of Kentucky. After
14 completing graduate studies, I was employed by Kentucky Utilities Company as a
15 planning analyst. In 1989, I began employment with the Indiana Utility
16 Regulatory Commission as a senior engineer. From 1992 until mid-1998, I was
17 employed by SVBK Consulting Group, where I held several positions as a
18 consultant focusing principally on utility rate matters. I was hired by Cinergy
19 Services, Inc., in 1998, as an Economic and Financial Specialist in the Budgets
20 and Forecasts Department. In 1999, I was promoted to the position of Manager,
21 Financial Forecasts. In August 2003, I was named to the position of Director -

1 Rates. On December 1, 2009, I took the position of General Manager and Vice
2 President of Rates, Ohio and Kentucky.

3 **Q. HAVE YOU PREVIOUSLY TESTIFIED BEFORE THE PUBLIC**
4 **UTILITIES COMMISSION OF OHIO?**

5 A. Yes. I have presented testimony on numerous occasions before the Public
6 Utilities Commission of Ohio (Commission) and various other state, local, and
7 federal regulators.

8 **Q. PLEASE SUMMARIZE YOUR DUTIES AS GENERAL MANAGER AND**
9 **VICE PRESIDENT OF RATES, OHIO AND KENTUCKY.**

10 A. As General Manager and Vice President of Rates, Ohio and Kentucky, I am
11 responsible for all state and federal matters involving Duke Energy Ohio and
12 Duke Energy Kentucky, Inc.

13 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS**
14 **PROCEEDING?**

15 A. The purpose of my testimony is to support various components of Duke Energy
16 Ohio's proposed market rate option (MRO). I provide testimony regarding the
17 proposed standard service offer (SSO) price structure, its primary components,
18 and the transition from the current electric security plan (ESP).

II. MRO STANDARD SERVICE OFFER PRICE STRUCTURE

19 **Q. PLEASE DESCRIBE THE STATUTORY GUIDELINES FOR**
20 **ESTABLISHING DUKE ENERGY OHIO'S SSO PRICES UNDER THE**
21 **COMPANY'S PROPOSED MRO.**

1 A. Section 4928.142 of the Ohio Revised Code establishes the process to be used for
2 determining the SSO rates under an MRO (*i.e.*, the MRO Rules). Specifically, as
3 noted below, R.C. 4928.142(D) provides that the transition from an SSO price in
4 an ESP to the SSO price in an MRO be done over a period of time by “blending”
5 the SSO price from the ESP with a price derived from an auction of a share of the
6 load to be served.

7 The first application filed under this section by an electric distribution
8 utility that, as of July 31, 2008, directly owns, in whole or in part,
9 operating electric generating facilities that had been used and useful
10 in this state shall require that a portion of that utility’s standard
11 service offer load for the first five years of the market rate offer be
12 competitively bid under division (A) of this section as follows: ten per
13 cent of the load in year one, not more than twenty per cent in year
14 two, thirty per cent in year three, forty per cent in year four, and fifty
15 per cent in year five. Consistent with those percentages, the
16 commission shall determine the actual percentages for each year of
17 years one through five. The standard service offer price for retail
18 electric generation service under this first application shall be a
19 proportionate blend of the bid price and the generation service price
20 for the remaining standard service offer load, which latter price shall
21 be equal to the electric distribution utility’s most recent standard
22 service offer price, adjusted upward or downward as the commission
23 determines reasonable, relative to the jurisdictional portion of any
24 known and measurable changes from the level of any one or more of
25 the following costs as reflected in that most recent standard service
26 offer price:

- 27 (1) The electric distribution utility’s prudently incurred cost of fuel
28 used to produce electricity;
- 29 (2) Its prudently incurred purchased power costs;
- 30 (3) Its prudently incurred costs of satisfying the supply and demand
31 portfolio requirements of this state, including, but not limited to,
32 renewable energy resource and energy efficiency requirements;
- 33 (4) Its costs prudently incurred to comply with environmental laws
34 and regulations, with consideration of the derating of any facility
35 associated with those costs. In making any adjustment to the
36 most recent standard service offer price on the basis of costs
37 described in division (D) of this section, the commission shall
38 include the benefits that may become available to the electric

1 distribution utility as a result of or in connection with the costs
2 included in the adjustment, including, but not limited to, the
3 utility's receipt of emissions credits or its receipt of tax benefits
4 or of other benefits, and, accordingly, the commission may
5 impose such conditions on the adjustment to ensure that any such
6 benefits are properly aligned with the associated cost
7 responsibility. The commission shall also determine how such
8 adjustments will affect the electric distribution utility's return on
9 common equity that may be achieved by those adjustments. The
10 commission shall not apply its consideration of the return on
11 common equity to reduce any adjustments authorized under this
12 division unless the adjustments will cause the electric
13 distribution utility to earn a return on common equity that is
14 significantly in excess of the return on common equity that is
15 earned by publicly traded companies, including utilities, that face
16 comparable business and financial risk, with such adjustments
17 for capital structure as may be appropriate. The burden of proof
18 for demonstrating that significantly excessive earnings will not
19 occur shall be on the electric distribution utility. Additionally, the
20 commission may adjust the electric distribution utility's most
21 recent standard service offer price by such just and reasonable
22 amount that the commission determines necessary to address any
23 emergency that threatens the utility's financial integrity or to
24 ensure that the resulting revenue available to the utility for
25 providing the standard service offer is not so inadequate as to
26 result, directly or indirectly, in a taking of property without
27 compensation pursuant to Section 19 of Article I, Ohio
28 Constitution. The electric distribution utility has the burden of
29 demonstrating that any adjustment to its most recent standard
30 service offer price is proper in accordance with this division.

31 The subsequent paragraph, R.C. 4928.142(E), gives the Commission some
32 latitude to adjust the blending percentages in certain circumstances:

33 Beginning in the second year of a blended price under division (D) of
34 this section and notwithstanding any other requirement of this section,
35 the commission may alter prospectively the proportions specified in
36 that division to mitigate any effect of an abrupt or significant change
37 in the electric distribution utility's standard service offer price that
38 would otherwise result in general or with respect to any rate group or
39 rate schedule but for such alteration. Any such alteration shall be
40 made not more often than annually, and the commission shall not, by
41 altering those proportions and in any event, including because of the
42 length of time, as authorized under division (C) of this section, taken
43 to approve the market rate offer, cause the duration of the blending
44 period to exceed ten years as counted from the effective date of the

1 approved market rate offer. Additionally, any such alteration shall be
2 limited to an alteration affecting the prospective proportions used
3 during the blending period and shall not affect any blending
4 proportion previously approved and applied by the commission under
5 this division.

6 **Q. DOES THIS STATUTORY BLENDING REQUIREMENT APPLY TO**
7 **DUKE ENERGY OHIO?**

8 A. Yes. Because Duke Energy Ohio owned and operated "electric generating
9 facilities that had been used and useful in this state," the Company must apply the
10 "blending" requirement described in R.C. 4938.142(D) to its SSO. The period
11 during which the Company applies this blending requirement is referred to as the
12 "Blending Period" in my testimony.

13 **Q. HOW IS DUKE ENERGY OHIO PROPOSING TO COMPLY WITH THE**
14 **PROVISIONS OF REVISED CODE SECTION 4928.142?**

15 A. There are a number of provisions in R.C. 4928.142(D) that need to be addressed.
16 First, Duke Energy Ohio must establish the "*generation service price for the*
17 *remaining standard service offer load*" to be used in the blended rate. Second,
18 the Company must know the bid price resulting from the auction. Finally, Duke
19 Energy Ohio needs to know the proportion of each price to blend. It may be easier
20 to understand the calculation with a formula. The SSO price during the Blending
21 Period will be:

1 PTC-AAC), the capacity dedication rider (Rider SRA-CD), and the system
2 reliability tracker (Rider SRA-SRT) are being consolidated into a single SSO
3 generation price to be called Rider GEN; however, the rate structure, including
4 demand charges and any rate blocks, will continue. The only other component of
5 the generation price to be blended is the legacy of the current fuel tracker, Rider
6 PTC-FPP.

7 **Q. WHAT IS THE SOURCE OF THE BID PRICE?**

8 A. Ultimately, the "bid price" will be determined as a result of an auction for a share
9 of Duke Energy Ohio's load. The details of the auction or competitive bidding
10 process (CBP) are discussed in more detail in the testimony of Company
11 witnesses Robert J. Lee and James S. Northrup. As described in the testimony of
12 Duke Energy Ohio witness Bailey, the bid price resulting from the auction will be
13 converted into different components for customers to reflect differences in the
14 load patterns and seasonality. The end result will produce the "bid price"
15 component of the Blended SSO Price for each customer.

16 **Q. HOW DOES THE COMPANY PROPOSE TO CALCULATE THE**
17 **BLENDING PERCENTAGES TO BE USED FOR THE FIRST YEAR OF**
18 **THE MRO?**

19 A. R.C. 4928.142(D) explicitly states that 10% of the Company's SSO is to be
20 provided through an auction process in year one of the MRO. Consequently, the
21 Company's Blended SSO Price for year one of the Blending Period will be the
22 sum of 90% legacy ESP price and 10% of the winning bid price.

23 **Q. IS YEAR ONE OF THE MRO SIMPLY CALENDAR YEAR 2012?**

1 A. No. Because the Company will be a member of PJM Interconnection, LLC (PJM)
2 before the beginning of the MRO, it will be conducting the auction in the PJM
3 market for that share of the load being blended to create the Blended SSO Price.
4 As described more fully in the testimony of Duke Energy Ohio witness Kenneth J.
5 Jennings, the calendar in PJM's auction process is for the twelve month period
6 beginning June 1 and ending the following May 31. Therefore, Duke Energy
7 Ohio is proposing that year one of its MRO be defined as the seventeen-month
8 period beginning January 1, 2012, through May 31, 2013. With this adjustment,
9 each subsequent auction period used for providing SSO service to Duke Energy
10 Ohio's customers will coincide with the PJM market.

11 If the Commission determines that year one and subsequent years are
12 based on something other than the PJM calendar, the Company will accommodate
13 that mandate but it will require, at a minimum, additional complexity for all
14 involved in conducting auctions, establishing SSO rates, and administering tariffs.

15 Assuming the Commission accepts the Company's proposal to establish
16 year one as the period from January 1, 2012, through May 31, 2013, year two
17 would then be the twelve-month period ending May 31, 2014; year three would be
18 the twelve months ending May 31, 2015, and so on.

19 **Q. DESCRIBE THE BLENDING MECHANISM FOR THE YEARS AFTER**
20 **YEAR ONE IN THE MRO.**

21 A. Again, the MRO Rules dictate the extent to which blending is required. R.C.
22 4928.142(D) expressly recommends that the blending percentages to be used are
23 as follows:

Year	Percent of SSO Price from	
	Legacy ESP	Auction
1	90%	10%
2	80%	≤ 20%
3	70%	30%
4	60%	40%
5	50%	50%

1 Absent any other factors, the Company would follow the blending schedule
2 shown above; however, Section 4928.142(E) of the MRO Rules allows the
3 Commission to adjust these blending percentages beginning in year two of the
4 Blending Period. The rule expressly states the Commission may alter the
5 percentages 'prospectively' beginning in year two, thus providing that the first
6 year in which the blending percentages can be altered is year three of the MRO
7 period.

8 **Q. WILL THE BLENDED PRICES IN YEARS ONE AND TWO RESULT IN**
9 **SSO PRICES HIGHER OR LOWER THAN THE MARKET?**

10 A. Based on the Company's expectations of the market prices, current trends, and
11 current forward prices for the first two years of the MRO, the Blended SSO Price
12 is expected to be higher than the market price. But it will be lower than the SSO
13 price under the Company's current ESP. Furthermore, the fact remains that
14 customers have the right to choose alternative suppliers and, as the Company has
15 experienced in its ESP, customers do exercise that right.

16 At the time Amended Substitute Senate Bill 221 (S.B. 221) was being
17 formulated and approved, and even when the Company was seeking approval of
18 its ESP, Case No. 08-920-EL-SSO, *et al.*, in July 2008, market prices for power
19 were at or above the Company's expected ESP price. Since the date when the

1 Company's ESP was approved, however, market prices have been and are
2 expected to remain below the Company's SSO price established in its ESP. In
3 fact, as described in the testimony of Company witness Judah L. Rose, it is
4 expected that the retail market price will remain below the Company's blended
5 rate until 2014 when these prices are expected to converge, which would be the
6 third year of the Company's proposed MRO.

7 **Q. IS THE COMPANY PROPOSING THAT THE COMMISSION ADJUST**
8 **THE BLENDING PERIOD FROM THE SCHEDULE ESTABLISHED IN**
9 **R.C. 4928.142(D)?**

10 **A.** Yes. The blending requirement is a means of allowing the Commission to
11 gradually allow utilities' SSO rates to transition from the rates offered under an
12 ESP to a state where the SSO rates are 100% market-based. Once that transition
13 is achieved, the need for and rationale for further blending is obviated.

14 As discussed above, Company witness Rose provides testimony that the
15 market price and the existing ESP price will converge in the third year of the
16 MRO. Furthermore, as supported in the testimony of Duke Energy Ohio witness
17 Charles R. Whitlock, the Company is proposing to transfer its legacy generation¹
18 to an affiliate no later than the beginning of year three. For both of these reasons,
19 the Company proposes to end the Blending Period at the beginning of year three
20 and make available to its customers an SSO price based exclusively on the market

¹ "Legacy generation" refers to the generating assets currently owned by Duke Energy Ohio that were used and useful in providing generation service to Ohio retail customers before January 1, 2001.

1 price derived from an auction process. Similar to the table above, the Company's
2 blending proposal is as follows:

Year	Percent of SSO Price from	
	Legacy ESP ²	Auction
1/1/12-5/31/13	90%	10%
6/1/13-5/31/14	80%	20%
All Years after 5/31/14	0%	100%

3 **Q. IS THIS BLENDING PROPOSAL CONSISTENT WITH THE**
4 **STATUTORY REQUIREMENT FOR AN MRO?**

5 A. Yes. Not only is it consistent with the MRO Rules, R.C. 4928.142, it is consistent
6 with the objectives of S.B. 221 as it finally achieves an objective established by
7 the Ohio legislators when Senate Bill 3 was passed in 1999, promising Ohio
8 consumers unfettered full choice for their electric generation service. Any
9 provision that limits the ability of a utility to offer true market prices, such as the
10 blending requirement of the MRO rules, necessarily means that neither the
11 customer nor the utility is operating in the competitive environment envisioned by
12 Ohio lawmakers as much as twelve years ago. The Company's proposal
13 establishes a date that ensures that objective is finally realized.

14 **Q. DOES THE COMPANY'S INTENTION OF TRANSFERRING ITS**
15 **LEGACY GENERATING ASSETS AFFECT THE MRO PROCESS OR**
16 **THE BLENDING REQUIREMENT YOU DISCUSS ABOVE?**

17 A. The MRO Rules do not compel Duke Energy Ohio to retain ownership of its
18 generating assets during the Blending Period or, more generally, while operating

1 under an MRO. Rather, the MRO Rules only address whether the electric
2 distribution utility owned generation as of July 31, 2008, which is the case for
3 Duke Energy Ohio. Practically, however, the Blending Period must end when the
4 assets are transferred from Duke Energy Ohio, insofar as the electric distribution
5 utility can then only meet its SSO obligation through market purchases, the cost
6 of which would effectively be the basis for the SSO price. As described further in
7 the testimony of Company witness Whitlock, the timing of Duke Energy Ohio's
8 proposed transfer of its legacy generation assets is no later than the end of the
9 Blending Period.

10 **Q. WOULD YOU EXPAND ON YOUR RESPONSE THAT THE BLENDING**
11 **PERIOD MUST END WHEN THE LEGACY GENERATION IS**
12 **TRANSFERRED?**

13 **A.** Without generation, Duke Energy Ohio can only meet its SSO obligation via the
14 wholesale markets using auctions, bilateral contracts, or some other means of
15 acquiring capacity. This situation mirrors the current condition for First Energy
16 Corp. Its electric distribution utilities³ own no generation and must purchase all
17 of their load requirements via an auction and the result of the auction becomes the
18 SSO price available to their customers. Because the SSO load obligation is
19 competitively bid, it necessarily means that "market price" is the blended price so
20 any further "blending" would be superfluous. This situation is identical for Duke

(...continued)

² The "Legacy ESP" may also be referred to as the "ESP component" of the Blended SSO Price in this testimony.

1 Energy Ohio when it transfers its assets. Furthermore, R.C. 4928.142(D) provides
2 that a utility's SSO price can be adjusted for changes in the cost of purchased
3 power. Obviously, without owning generation, Duke Energy Ohio can only offer
4 SSO service by purchasing power from the market and, at the time of the transfer,
5 the Company's SSO rate would be comprised only of the price of its purchased
6 power, *i.e.*, the market price. Consequently, similar to the current situation for
7 FirstEnergy, the function of blending prices serves no purpose as the two prices
8 would both reflect market price and it is thus appropriate for the Commission to
9 terminate the Blending Period.

10 **Q. WILL THE ESP COMPONENT OF THE BLENDED PRICE BE**
11 **ADJUSTED DURING THE BLENDING PERIOD?**

12 A. Although the MRO Rules include provisions to adjust the ESP component for
13 changes in fuel, purchased power, and environmental costs, the Company is
14 proposing to make no adjustments during the two-year blending period. The
15 Company is willing to forgo these adjustments during the Blending Period as long
16 as the Blending Period ends before June 1, 2014. As noted above, however, after
17 year two, when the asset transfer is completed, the SSO price would be
18 exclusively based on the cost of market purchases for power to meet the SSO
19 obligation.

20 The Company's application includes placeholder tariffs for tracking
21 incremental fuel, purchased power, and environmental costs over the costs

(...continued)

³ First Energy's Ohio electric distribution utilities are Cleveland Electric Illuminating, Toledo Edison, and
(continued...)

1 included in the ESP rate used in the initial blended SSO price. The tariffs will not
2 be needed if the Commission accepts the Company's proposed two-year blending
3 period and the offer to freeze the ESP component of the blended SSO price for
4 that period. However, if the Blending Period is extended and the asset transfer
5 does not occur before June 1, 2014, these tariffs would be used to adjust the ESP
6 component on a quarterly basis beginning as early as year one depending on when
7 the Commission would make the determination to extend the Blending Period and
8 will last until the SSO Price is exclusively based on the auction price.

III. DISCUSSION OF RIDERS IN THE MRO

9 **Q. WILL YOU SUMMARIZE THE RIDERS AT ISSUE IN THE MRO?**

10 **A.** The following tables summarize the Company's riders being affected by the MRO
11 Application, showing new riders being proposed, riders being eliminated, and
12 riders being adjusted but not eliminated. All other existing riders in the
13 Company's tariffs will either be unchanged as a result of this Application or will
14 expire under existing terms and conditions.

(...continued)

Ohio Edison.

Table 1 - Existing Riders Being Modified		
Original Rider: New Rider	Description of Change	Avoidable?
Rider PTC-BG: Rider GEN	Original Price-to-Compare – Base Generation to be converted to Rider GEN by adding certain components from Table 3 below	Yes
Rider TCR: Rider RTO	Transmission Cost Recovery Rider becomes Rider RTO (Regional Transmission Organization).	Yes

Table 2 - New Riders		
Rider Name	Description	Avoidable?
Rider MRO	Market Rate Offer	Yes
Rider SCR	Supplier Cost Reconciliation	Yes
Rider AERR	Alternative Energy Recovery Rider	Yes
Rider BTR	Base Transmission Rider	No
Rider RECON	Reconciliation Rider for over-/under-recovery of eliminated ESP-era riders	No
Rider UE-GEN	Uncollectible Expense Rider for Generation	Yes

Table 3 – Existing Riders Being Eliminated		
Rider Description	Description	Basis for Elimination
Rider PTC-FPP	Price-to-Compare – Fuel and Purchased Power Tracker	Added to Rider GEN
Rider SRA-SRT	System Resource Adjustment – System Reliability Tracker	Added to Rider GEN
Rider SRA-CD	System Resource Adjustment - Capacity Dedication Rider	Added to Rider GEN
Rider PTC-AAC	Price-To-Compare - Annually Adjusted Component	Added to Rider GEN
Rider SC	Shopping Credit Rider	Obsolete

1 For the first two years of MRO, the Blended SSO Price available to all
 2 customers will be comprised of a base generation charge, Rider GEN, that will be
 3 blended with the auction price using the manner described above to produce the
 4 Blended SSO Price for customers who take generation service from Duke Energy
 5 Ohio. The rate for Rider GEN will be the base generation rate, Rider PTC-BG,
 6 applicable for 2011, combined with the 2011 rates for Rider PTC-AAC, Rider
 7 SRA-SRT (adjusted to remove any reconciliation adjustments), and Rider SRA-

1 CD. Rider GEN will also include the then most current Rider PTC-FPP rate (*i.e.*,
2 the rate effective from October 1, 2011, through December 31, 2011) also
3 adjusted to exclude any reconciliation adjustments and to eliminate cost recovery
4 of renewable energy credits that will now be recovered via the new Rider AERR,
5 which I will describe below. Company witnesses Bailey and Ziolkowski describe
6 the process for developing Rider MRO and the mechanism for applying Rider
7 MRO and Rider GEN to customers' bills to get the Blended SSO Price.

8 **Q. WILL THE RIDER GEN RATE BE SUBJECT TO ANY ADJUSTMENTS?**

9 A. No. As described above, Duke Energy Ohio is proposing to conditionally freeze
10 Rider GEN rates for the twenty nine months that less than 100% of its load is
11 supplied via the CBP auction process. If the Commission modifies the Blending
12 Period, the Company proposes to restore two trackers for its share of the Blended
13 SSO Price not taken from the auction. Specifically, the Company may implement
14 a tracker for incremental fuel and purchased power, and another tracker for
15 incremental environmental costs. 'Incremental,' in this case, would mean the
16 extent to which the then current cost would exceed the amount included in the
17 frozen Rider GEN rates. If it becomes necessary to make adjustments for changes
18 in the cost of fuel and purchased power, the Company will make quarterly filings
19 in a manner similar to its current Rider FPP⁴ filings with some minor changes to
20 accommodate the MRO proposal herein. Because Rider FPP would only reflect
21 the Company's share of resources used to provide SSO service (*i.e.*, the
22 percentage of SSO load not auctioned), this rider, if implemented, will not be

1 subject to the blending percentages. Instead, Rider FPP will be a bypassable
2 charge that will be added to the Blended SSO Price.

3 Similarly, if it becomes necessary to file adjustments for changes in
4 environmental costs during the blending period, as provided for in R.C.
5 4928.142(D)(4), Duke Energy Ohio proposes to implement an environmental
6 investment rider (Rider EIR) to adjust its environmental cost recovery in a manner
7 similar to the way the Rider PTC-AAC has worked in the past, except that (1) the
8 new rider, Rider EIR, will only track environmental costs whereas the Rider PTC-
9 AAC tracked environmental costs plus incremental Homeland Security costs and
10 incremental tax law changes and (2) the new rider will be updated quarterly
11 pursuant to the MRO Rules.

12 Finally, the Company is proposing to track its costs for complying with
13 Ohio's supply-side portfolio requirements (*e.g.*, costs for purchasing renewable
14 energy credits, or RECs) via Rider AERR and its demand-side portfolio
15 requirements will continue to be tracked via its existing Rider SAW-R (save-a-
16 watt Rider). I will discuss these two riders in more detail below.

17 **Q. DESCRIBE RIDER MRO SHOWN IN YOUR TABLE.**

18 A. Rider MRO is simply the rate to be used when determining the auction
19 component of the Blended SSO Price for a customer's bill. Using the
20 methodology described in the testimony of Bailey and Ziolkowski, Rider MRO
21 will be a tariff that includes a rate for each customer tariff that will be combined,

(...continued)

⁴ After its current ESP, the current Rider PTC-FPP will be known as Rider FPP.

1 using the blending percentages, with the Legacy SSO price, when computing
2 customers' bills.

3 **Q. WHAT IS THE PURPOSE OF THE RIDER SCR SHOWN IN YOUR**
4 **TABLE?**

5 A. Rider SCR provides a means of ensuring that the Company is able to recover from
6 non-switching customers no more and no less than the cost of acquiring the
7 portion of their SSO load served by the winning bidders in the auction. If all SSO
8 customers were to pay exactly the same price per MWh for the bidders' share of
9 their SSO load, then there would be no need to reconcile the revenue and the cost
10 for the auctioned load. As described more fully by Company witness Bailey, the
11 \$/MWh price received in the auction for the share of SSO load provided by the
12 winning bidders will be converted into different rates for certain customer classes
13 based on differences in loss factors and seasonality differences. Because the
14 auction price ultimately billed to customers in the blending process may differ
15 from the rate paid to the winning bidders, it is likely that the Company will
16 recover more or less revenue from customers attributable to the bidders' share of
17 the SSO price than it will owe the bidders. Rider SCR will only true-up any
18 difference and nothing in this proposed rider is intended to allow Duke Energy
19 Ohio to profit from its existence; rather, it is only intended to make the Company,
20 customers, and suppliers whole. Any balance of over- or under-recovery will
21 accrue a carrying charge equal to the electric distribution utility's weighted
22 average cost of long-term debt approved in its most recent retail rate case.

23 **Q. WILL RIDER SCR BE USED TO RECOVER ANY OTHER COSTS?**

1 A. Yes. Chapter 4901:1-35-3(B)(2)(l) of the Ohio Administrative Code allows the
2 Company to recover the cost of the CBP plan consultant. Rather than create a
3 new rider for recovery of this cost, Duke Energy Ohio is proposing to include this
4 cost in its Rider SCR. In the Company's opinion, there is a reasonable nexus
5 between this cost component and the overall objective of this rider.

6 Finally, net costs incurred by Duke Energy Ohio to provide SSO service in
7 case of default by a supplier and any other costs directly attributable to the auction
8 or interaction with suppliers will be eligible for recovery in Rider SCR.

9 **Q. WILL RIDER SCR BE A BYPASSABLE OR NON-BYPASSABLE**
10 **CHARGE?**

11 A. As Company witness Ziolkowski discusses further in his testimony, Rider SCR is
12 intended to be a bypassable charge; however, the Company is proposing that,
13 under certain conditions, the charge become a non-bypassable charge. In a
14 competitive environment, where customers are free to switch to alternative
15 suppliers, there is always the risk that some cost will be incurred during a period
16 when there was little switching that would need to be recovered in another period
17 when there was significant switching. As long as there is enough SSO load or as
18 long as the credits or charges to be flowed through Rider SCR are relatively small,
19 Rider SCR can remain bypassable. If the net credits/charges and/or switching is
20 above a certain threshold level, the Company is proposing to make Rider SCR
21 non-bypassable. This is necessary to mitigate the potential for having the
22 proverbial last non-switched customer have to pay for the all of the cost avoided
23 by the customers who have already switched.

1 **Q. DO YOU HAVE A PROPOSAL FOR THE THRESHOLD THAT WOULD**
2 **TRIGGER THIS RIDER BECOMING NON-BYPASSABLE?**

3 A. FirstEnergy has a similar rider and uses a threshold of 5% of the generation costs
4 being supplied under its SSO. That recommendation seems reasonable and the
5 Company proposes to use that threshold as well. It will also help the Commission
6 in maintaining consistency among the electric distribution utilities. Admittedly,
7 there is little chance that the threshold condition would be reached in the first two
8 years with only 10% and 20% of the SSO load being provided for via auction in
9 the first two years of the MRO. In other words, the SSO load provided for via the
10 auction in the first two years will only be a fraction of the overall cost of
11 generation and it is unlikely that any reconciliation of the revenue collected from
12 SSO customers and the amounts owed to auction suppliers would exceed 5% of
13 the overall cost of generation. However, when 100% of the SSO load is provided
14 for via auction, the potential for reaching that threshold is greater; thus, the need
15 to include it here.

16 **Q. WOULD RIDER SCR REMAIN A NON-BYPASSABLE CHARGE IF THE**
17 **THRESHOLD CONDITION IS MET?**

18 A. No. When the accumulated balance of over- or under-recovery falls back below
19 the 5% threshold for two consecutive quarters, Rider SCR will again be
20 bypassable only being charged or credited to SSO customers.

21 **Q. DESCRIBE THE NEW RIDER AERR SHOWN IN YOUR TABLE.**

22 A. Rider AERR is being proposed to recover the Company's share of the cost for
23 complying with the State's renewable energy requirements. Company witnesses

1 Andrew S. Ritch discusses the Company's plans for complying with the State's
2 alternative energy requirements as they relate to renewable energy. The rider will
3 be filed quarterly and will include true-up provisions. The responsibility for
4 procuring RECs generally follows the load obligation although the nexus is
5 slightly convoluted insofar as the REC obligation is based on the average of the
6 prior three years' of load rather than the current load obligation.⁵

7 Therefore, to the extent a Competitive Retail Electric Service (CRES)
8 provider is serving a portion of Duke Energy Ohio's retail load, that provider will
9 be responsible for acquiring a commensurate number of RECs and, consequently,
10 Rider AERR will be a bypassable charge.

11 **Q. ARE THERE ANY OTHER GENERATION-RELATED OR AUCTION-**
12 **RELATED RIDERS THAT ARE BEING PROPOSED?**

13 **A.** No. The riders that will comprise the generation- or auction-related components
14 of the SSO price are the following riders (1) GEN, (2) MRO, (3) EIR, (4) FPP, (5)
15 AERR, and (6) SCR. Rider GEN, Rider EIR, and Rider FPP will expire when the
16 Company reaches the point where 100% of its load is auctioned off. Rider SCR
17 will continue to be necessary to ensure that bidders are fully compensated and that
18 Duke Energy Ohio is made whole for the provision of generation services to its
19 SSO customers. Rider AERR will remain effective indefinitely as the Company's
20 obligation to secure RECs is independent of its generation ownership. The
21 generation rates proposed in the Company's MRO have two other important
22 characteristics: first, all of the charges except for Rider SCR are unconditionally

⁵ O.A.C. 4901:1-40-03(B)(1).

1 avoidable and, in most circumstances, Rider SCR is expected to avoidable as
2 well; and, second, residential and non-residential customers will no longer have
3 differences in how generation charges are applied. Generally speaking, the
4 generation rates should be easier for customers to understand which should add
5 some degree of transparency to the process for such customers to compare retail
6 market prices.

IV. TRANSMISSION RIDERS

7 **Q. DOES THE COMPANY PROPOSE TO RECOVER ITS TRANSMISSION**
8 **COSTS?**

9 **A.** Yes. Duke Energy Ohio's transmission service can be divided into two
10 components. The first is the network integrated transmission service (NITS) that
11 is required to provide energy to all retail customers, whether these customers have
12 switched or not. Currently, the Company recovers its NITS revenue requirement
13 from non-switched customers via its Rider TCR (Transmission Cost Recovery
14 Rider) and CRES providers effectively pay Duke Energy Ohio for the use of the
15 transmission system to provide their competitive retail service to their customers.
16 Included in its current transmission revenue requirement and included in Rider
17 TCR are charges incurred from the Midwest Independent System Operator, Inc.
18 (MISO) related to its Midwest Transmission Expansion Planning (MTEP).

19 The second broad category of transmission costs are the various costs
20 billed to Duke Energy Ohio from its regional transmission organization (RTO).
21 The RTO costs attributable to the electric distribution utility are generally a

1 function of how much retail load the Company, or a CRES provider, is serving.
2 These RTO costs are also currently recovered in the Company's Rider TCR.

3 All of the transmission costs for which Duke Energy Ohio is seeking
4 recovery are pursuant to FERC-approved tariffs.

5 **Q. HOW IS THE COMPANY PROPOSING TO RECOVER TRANSMISSION**
6 **COSTS BEGINNING JANUARY 1, 2012?**

7 A. In this filing, the Company is proposing to modify the manner in which it
8 recovers its transmission revenue requirement. The proposal is intended to
9 simplify the recovery method, better synchronize cost incurrence with cost
10 recovery, and enhance the competitive market. Specifically, the Company is
11 proposing to begin recovering its NITS revenue requirement directly from all
12 customers regardless of whether they have switched. This will relieve CRES
13 providers and participants in the SSO auction of the obligation to procure this
14 service from Duke Energy Ohio. This will also serve to keep the price-to-compare
15 (*i.e.*, the SSO price) for Duke Energy Ohio exclusively a 'generation' price rather
16 than a combined 'generation and transmission' rate. Because this revenue
17 requirement is for all retail load, it will be a non-bypassable charge. However,
18 because CRES providers must recover this cost from their customers as well, it is
19 essentially a non-bypassable charge today. The 'base transmission' rider (or
20 Rider BTR) will be based on the NITS revenue requirement for Duke Energy
21 Ohio as calculated pursuant to the FERC-approved formulas provided by the
22 RTO. Rider BTR will include all costs billed from either PJM and/or MISO

1 under FERC-approved tariffs except those costs billed from either RTO that are
2 recovered in other riders as I will discuss below.

3 **Q. WOULD RIDER BTR ALSO INCLUDE TRANSMISSION EXPANSION**
4 **PLANNING COSTS?**

5 A. Yes. To the extent Duke Energy Ohio is charged for these FERC- authorized
6 costs, these costs will be included in Rider BTR for recovery from retail
7 customers.

8 **Q. HAS THE COMMISSION STAFF OFFERED AN OPINION AS TO**
9 **WHETHER SUCH COSTS ARE RECOVERABLE?**

10 A. Yes. In its Post-Hearing Brief filed on April 30, 2010, in Case No. 10-388-EL-
11 SSO, at page 18, the Commission Staff refers to R.C. 4928.05 which states that
12 the Commission has the authority "to provide for the recovery, through a
13 reconcilable rider on an electric distribution utility's distribution rates, of all
14 transmission and transmission-related costs, including ancillary and congestion
15 costs, imposed on or charged to the utility by the federal energy regulatory
16 commission or a regional transmission organization, independent transmission
17 operator, or similar organization approved by the federal energy regulatory
18 commission."

19 Relying on that statute, the Commission Staff goes on to say that:

20 Pursuant to statute, transmission charges imposed by the FERC are
21 passed on to the ultimate consumer. This pass through is not
22 optional.

23 The Stipulation would change this and ratepayers would pay none
24 of the entrance or exit fees and would be shielded from RTEP costs
25 for five years. The Staff takes the position, and the record supports,

1 that, in the absence of the Stipulation, it is virtually certain that the
2 FERC would impose all these costs on ATSI. As noted above,
3 once these costs are imposed, they must be collected (in the
4 absence of the Stipulation).

5 To understand why these costs would be imposed by the FERC it is useful to look
6 at the problem from the perspective of the FERC. The FERC has approved both
7 the MISO and the PJM methods of administering RTOs, determining that both
8 result in just and reasonable rates. The entrance and exit fees are simply
9 components of these structures that the FERC has deemed reasonable. To imagine
10 that the FERC would determine that these charges, which would be reasonable for
11 anyone else, are not reasonable for [FirstEnergy], strains credulity. (emphasis
12 added)

13 **Q. IN THE FIRSTENERGY CASE YOU REFERENCE, DID THE**
14 **STIPULATION ALLOW THE COMPANY TO COLLECT ALL**
15 **TRANSMISSION EXPANSION PLANNING COSTS?**

16 **A.** No. As the Staff noted in its Post Hearing Brief in that case, the FirstEnergy
17 Companies reached a Stipulation in that proceeding and agreed to forgo recovery
18 of transmission expansion planning costs billed from PJM up to a maximum
19 amount. However, First Energy's agreement to forgo such costs was just one
20 component of a larger overall settlement that included a number of provisions that
21 were agreed to by the settling parties. Duke Energy Ohio is not in a comparable
22 situation inasmuch as there is no pending settlement in this proceeding, at least
23 not at the time of its filing; consequently, the Company is exercising its rights, as
24 fully supported by the Staff's comments in FirstEnergy's ESP case, to recover all
25 costs billed to the Company under FERC-approved tariffs.

1 **Q. DOES THE COMPANY HAVE A PROPOSAL TO RECOVER OTHER**
2 **COSTS BILLED FROM EITHER PJM OR MISO?**

3 A. Yes. Certain charges billed from the FERC-approved RTO are billed directly to
4 the entity serving the load whether it is Duke Energy Ohio or CRES provider. For
5 these RTO costs⁶, Duke Energy Ohio is establishing a separate rider, Rider RTO.
6 Because the Company will only incur RTO costs in proportion to its SSO load,
7 this rider will be bypassable and, thus, only recoverable from the Company's SSO
8 customers. CRES providers are and will continue to be charged RTO costs,
9 excluding NITS, in proportion to the load they are serving.

10 **Q. WILL EITHER OF THESE TWO RIDERS BE SUBJECT TO A TRUE-**
11 **UP?**

12 A. The RTO Rider and Rider BTR will be trued-up annually around June of each
13 year consistent with the current filing schedule for Rider TCR and the filing will
14 continue to be consistent with O.A.C. Chapter 4901:1-36. For Rider BTR, the
15 true-up will only reconcile the difference between costs actually billed by the
16 RTOs and the revenue collected.

17 **Q. WHY ARE YOU MAKING A DISTINCTION FOR THE TRUE-UP**
18 **PROVISIONS OF RIDER BTR?**

19 A. Since the inception of the Company's transmission cost recovery rider (Rider
20 TCR), there has been no true-up of the NITS revenue requirement because the
21 nexus between cost incurrence and cost recovery is not as clear as it is for RTO

⁶ Examples of these costs are administrative fees, ancillary services, revenue sufficiency guarantees, etc., per MISO's Transmission and Energy Markets Tariff (TEMT) or PJM's Open Access Transmission Tariff (PJM Tariff).

1 costs. For Rider RTO, costs and the revenue to recover that cost are easily
2 tracked and relate to the same period. In other words, if the Company pays \$1
3 million in costs for RTO fees, it will seek to recover no more and no less than \$1
4 million attributable to the costs incurred during that period. On the other hand,
5 for Rider BTR, most of the revenue requirement is not for 'out of pocket' (*i.e.*,
6 O&M, taxes, etc.) costs incurred during the collection period. Instead, most of the
7 revenue requirement is for return on and return of (*i.e.*, depreciation) its
8 investment in the transmission system. Generally, this type of cost is not 'trued
9 up' from period to period.

V. OTHER NEW RIDERS

10 **Q. IS THE COMPANY PROPOSING ANY OTHER NEW RIDERS IN THIS**
11 **FILING?**

12 **A.** Yes. Duke Energy Ohio is proposing two other new riders. The first new rider
13 being proposed by the Company to true-up the costs and revenue for certain riders
14 being eliminated or zeroed out as a result of the Company's proposed MRO.
15 Specifically, it is virtually impossible that the Company's current Rider PTC-FPP
16 or Rider SRA-SRT will have a \$0 balance of over- or under-recovery at the end of
17 the current ESP period, December 31, 2011. For those riders that will expire or
18 be zeroed out at the end of 2011, the Company is proposing a rider to either
19 collect or refund the collective balance of any over- or under-recovery. The
20 Company is proposing to make this rider, Rider RECON, non-bypassable and it
21 will exist for only the first year of the MRO as it is expected that the true-up can
22 be completed in that amount of time without significantly impacting retail rates.

1 This rider will be set at \$0 as of January 1, 2012. The Company plans to make a
2 filing no later than April 1, 2012, to set the amount to be charged or credited to
3 customers via Rider RECON.

4 For the other rider, Company is proposing to recover the cost of bad debt
5 associated with its SSO service using what will be called Rider UE-GEN. The
6 Company currently has an approved rider to recover costs of bad debt associated
7 with distribution service (Rider UE-ED⁷) and bad debt related to retail
8 transmission is a component of the FERC-approved formula rates for calculating
9 NITS revenue requirement recoverable in Rider BTR.

VI. OTHER RIDER CHANGES

10 **Q. ARE THERE ANY OTHER RIDER CHANGES YOU WOULD LIKE TO**
11 **DISCUSS?**

12 **A.** Yes. The Company currently has a shopping credit rider (Rider SC) that is
13 available to non-residential customers on the condition that these customers agree
14 not to return to the Company's SSO rate unless they are willing to pay a premium.
15 Rider SC was offered as an additional incentive to encourage shopping. This
16 rider was set at a rate to exactly offset the Company's Rider SRA-CD, which is
17 non-bypassable. The net effect of this rider is to make Rider SRA-CD avoidable
18 to those qualifying customers who agree to certain terms. The nature of an MRO
19 environment obviates the need to offer such an incentive; thus, the Company is
20 eliminating this rider beginning January 1, 2012.

⁷ "UE-ED" means "uncollectible expense – electric distribution."

1 Because Rider SRA-SRT and Rider SRA-CD are being combined into
2 Rider GEN, which is unconditionally avoidable, the Company will no longer have
3 any non-bypassable generation charges with the one exception being if the
4 threshold condition for Rider SCR is met.

5 **Q. IS THE COMPANY PROPOSING ANY CHANGES TO ITS COST**
6 **RECOVERY FOR MEETING ENERGY EFFICIENCY TARGETS IN**
7 **THIS CASE?**

8 A. Not at this time. Until further notice, the Company will continue to use its Rider
9 SAW-R (save-a-watt Rider) to recover the cost of complying with the State's
10 energy efficiency mandates.

11 **Q. IS THE COMPANY PROPOSING ANY CHANGES TO ITS ECONOMIC**
12 **COMPETITIVENESS FUND RIDER?**

13 A. No. Although the Company is not including any specific new proposals in this
14 MRO Application, the current Rider ECF (economic competitiveness fund rider)
15 should be continued to provide a mechanism for recovering some or all of the
16 costs of the Company providing for economic development. It is expected that
17 any costs recovered under this rider would have to meet the provisions of R.C.
18 4905.31 and O.A.C. 4901:1-38.

VII. CONCLUSION

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

20 A. Yes, it does.