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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 OFFER ELECTRIC GENERATION SUPPLY, ACCOUNTING MODIFICATIONS, AND TARIFFS FOR GENERATION SERVICE.	))))))))	CASE NO. 10-2586-EL-SSO

INITIAL BRIEF OF
<u>WAL-MART STORES EAST, LP, AND SAM'S EAST, INC.</u>

Wal-Mart Stores East, LP, and Sam's East, Inc., (collectively "Walmart") respectfully submit this initial brief pursuant to the direction of the Attorney Examiners. In support of its position in this docket Walmart states as follows:

INTRODUCTION

As will become evident in the discussion that follows, Walmart's approach to the application of Duke Energy Ohio ("DEO" or "the Company") in this docket is very focused. That is, Walmart does not oppose the Company's proposal in total. Rather, Walmart has focused on ensuring that the Company's proposal is fair to all customers, those remaining with the Company and those who choose to be supplied by competitive providers.

Walmart submitted the expert testimony of Mr. Steve Chriss in support of its position. *See* Direct Testimony Of Steve W. Chriss On Behalf Of Wal-Mart Stores East, LP, And Sam's East, Inc. (hereinafter "Chriss Direct"). Mr. Chriss' testimony was admitted without objection as Wal-Mart and Sam's Exhibit No. 1 (1/19/11 tr., p. 1139, ln. 22). In further support of its position in this docket Walmart submits the following arguments and authorities.

ARGUMENTS AND AUTHORITIES

I. WALMART DOES NOT OPPOSE THE COMPANY'S PROPOSAL TO USE A MARKET RATE OFFER FOR ITS STANDARD SERVICE OFFER OR ITS BLENDING PROPOSAL.

The Company's application proposes to fulfill its standard *service offering* ("SSO") obligation by means of a market rate order ("MRO"). As stated in the testimony of Mr. Chriss, Walmart does not oppose either the use of an MRO for the Company's SSO, or the Company's blending proposal. Chriss Direct p. 5, ln. 10-18.

Walmart believes that SSO rates based on market prices will benefit SSO customers by providing more transparent generation rates and improved price signals. The increased transparency can drive more informed consumption management decisions by customers. This can benefit the individual customer and the utility system as a whole. Additionally, the proposed structure of the market-based SSO rates provides price transparency for customers when shopping for a generation service supplier.

II. UTILITY RATES SHOULD BE BASED UPON THE COST TO SERVE, WHETHER IN A FULLY REGULATED, MONOPOLY MARKET OR IN A COMPETITIVE MARKET.

Walmart consistently advocates setting utility rates on the basis of the utility's cost to serve a particular customer or class of customer because it produces equitable rates that reflect cost causation to the utility, while also sending proper price signals and *minimizing price distortions to customers*. This is true whether dealing with a fully regulated, monopoly environment where utility customers have no choice as to their supplier, or in a competitive environment like that in Ohio where utility customers have the option of taking power from a competitive provider.

When rates are based on cost, each customer pays only what it costs the utility to serve them, no more and no less. In other words, when utility rates are based upon cost the "cost causer" pays for the costs that it imposes on the utility's system. This is inherently equitable. If rates are not based on cost, however, then some customers will contribute disproportionately to the utility's revenue requirement and provide contributions to the cost to serve other customers. This is inherently inequitable.

Moreover, cost-based rates send accurate price signals to customers so that customers can act rationally in managing their load. That is, if the price a customer or class of customers pays is less than it costs the utility to serve those customers, the customer class is receiving inaccurate pricing signals, i.e., that the power being consumed is less expensive or less valuable than it really is. This may cause the customers to be wasteful or inefficient in their use of electricity.

This, in turn, can produce a number of undesired effects. The utility may not recover all of its costs to serve that customer or class of customers, or other customers may be required to subsidize the usage of that customer class. Similarly, if enough customers are incentivized to use electricity inefficiently or wastefully, the utility may be forced to build additional generation facilities, facilities that may be unneeded, expensive and polluting.

In setting rates for a fully regulated utility whose customers have no choice of supplier the critical allocation of utility costs occurs between various classes of captive customers, e.g., residential, commercial and industrial. This is normally done in the cost allocation/rate design phase of a rate case in which the utility's revenue requirement is allocated between and within customer classes.

When setting rates in a competitive environment such as that existing in Ohio, however, there is another critical allocation of utility costs that must be made: between customers taking service from the incumbent utility and customers taking service from competitive suppliers. The same cost causation principles should apply. That is, the costs that an incumbent utility incurs in serving its own customer must be accurately allocated to those customers, while the costs that the utility incurs in serving the competitive market must be accurately allocated to that market. Failure to make such an allocation accurately can produce undesirable effects.

This principle is clearly articulated by Walmart's witness Steve Chriss:

> Charging competitively supplied customers for any part of DEO's generation-related costs misaligns cost causation and cost responsibility and results in inequitable rates as those customers [i.e., competitively supplied customers] will pay a cost for which they will receive no benefit.

Chriss Direct p. 8, ln. 10-14.

In other words, charging competitively-supplied customers for any part of the Company's generation-related costs for serving its SSO customers results in the competitively-supplied customers subsidizing the Company's SSO customers. This, in turn, may give the Company an unfair competitive advantage over competing suppliers.

Under the Company's proposed MRO, competitively-supplied customers are able to avoid paying for the Company's generation-related costs by simply "bypassing" the generation-related riders. The Company is proposing, however, a number of generation-related riders that cannot be bypassed by competitively-supplied customers. This lack of bypassability will cause competitively-supplied customers to pay for costs for which they receive no benefit

III. THE NON-BYPASSABLE RIDERS PROPOSED BY THE COMPANY SHOULD BE REJECTED. INSTEAD, THESE RIDERS SHOULD BE MADE BYPASSABLE TO ENSURE THAT COSTS ARE ACCURATELY ALLOCATED BETWEEN THE COMPETITIVE AND NON-COMPETITIVE MARKETS.

The Company has proposed two riders through which competitively supplied customers will unfairly bear revenue responsibility for the Company's generation-related costs: Rider RECON and Rider SCR. As discussed below, the Commission should reject both of these riders as proposed and, instead, make them bypassable.

A. Rider RECON should be bypassable by competitively-supplied customers.

The Company has proposed a new Rider RECON. The purported purpose of Rider RECON is to true-up the costs and revenue for existing generation riders that will be eliminated or zeroed-out as part of the Company's proposed MRO.

During cross-examination Company witness Wathen acknowledged that the existing generation riders being replaced by Rider RECON are currently bypassable by competitively-supplied customers. (1/13/11 tr., p. 610, ln. 25 – p. 611, ln. 18). This is appropriate. Since competitively-supplied customers do not take generation service from the Company they should not be forced to pay any portion of the costs of that generation.

And yet the Company is now proposing that Rider RECON – through which the costs currently being collected through bypassable generation riders will be collected –

cannot be bypassed by competitively-supplied customers. This is an inequitable result that violates a fundamental principle of cost allocation: costs should be allocated to the extent possible to the cost causer. The Company's proposed Rider RECON will impose generation-related costs on competitively-supplied customers who, by definition, do not take generation service from the Company.

Therefore, the Commission should reject the Company's proposal to make Rider RECON non-bypassable by competitively supplied customers.

Instead, the Commission might consider modifying the proposed Rider RECON in such a way as to accomplish the Company's stated purposes without violating cost causation principles. As explained in the direct testimony of Walmart witness Steve Chriss, there is one circumstance under which charging a competitively-supplied customer through Rider RECON does not violate cost causation principles:

> If, during the final period to be trued-up prior to implementation of the MRO, a competitively supplied customer takes SSO service from DEO or does not qualify to bypass Rider SRA-SRT, they will have caused the Company to incur some part of the amount to be trued-up. As such, it does not violate cost causation principles to apply Rider RECON to those customers.

Chriss Direct p. 9, ln. 9-17.

Mr. Chriss offers an alternative recommendation that does not violate cost causation principles:

> The Commission should reject Rider RECON as proposed. If, however, the Commission determines that Rider RECON should be approved, the Commission should also determine that the Rider is bypassable. If the Commission determines that the Rider is "non-bypassable," the rider should apply only to those competitively supplied customers who, during the final period to be true-up prior to the implementation of the MRO, take DEO SSO service, or who do not qualify

to bypass Rider SRA-SRT.

Chriss Direct p. 9, ln. 18 – p. 10, ln. 2.

B. Rider SCR should be bypassable by competitively-supplied customers.

The Company has also proposed another new rider that is non-bypassable in certain situations: Rider SCR. The Company's testimony indicates that Rider SCR is intended to serve two purposes.

First, Rider SCR is a true-up mechanism that reconciles the revenues recovered from SSO customers with the costs paid by the Company to the generation bidders for SSO load. Second, Rider SCR recovers the costs associated with "conducting, administering, and implementing the [competitive bidding] plan as well as the costs for any independent auction consultants" and costs the Company incurs as a result of supplier default that are not covered under the Master Service Offer Supply Agreement. *See* Direct Testimony of James E. Ziolkowski, page 8, line 23 to page 9, line 8.

The Company has proposed that, if the deferral balance for Rider SCR exceeds five percent of the SSO cost, the rider will become non-bypassable until the deferral balance drops below five percent. *Id.* page 9, line 16 to page 10, line 6. This proposal should be rejected by the Commission.

As acknowledged by Mr. Wathen during cross-examination, the costs flowing through Rider SCR include the costs paid by the Company to generation suppliers for supplying generation to serve the SSO load. (1/13/11 tr. p. 608, ln. 1-5). Pursuant to fundamental costing principles, those costs should be recovered from the cost-causer, i.e., from the SSO customers for whom the supply has been procured. However, when

Rider SCR becomes "conditionally non-bypassable" as proposed by the Company, those same costs will unfairly be passed through to competitively-supplied customers who had no part in causing the Company to incur those costs.

In addition, Rider SCR will also recover costs that the Company incurs as a result of supplier defaults not covered by the proposed Master Service Offer Supply Agreement. These costs are even more remote than the direct costs of procuring SSO generation. And yet these costs will also flow-through to competitively-supplied customers when Rider SCR becomes "conditionally non-bypassable." That is, competitively-supplied customers will bear costs related to the defaults of suppliers providing generation services for SSO customers. In effect, competitively-supplied customers will become involuntary guarantors of suppliers providing generation services for SSO customers.

The proposed condition inappropriately shifts risks that the Company, as a generation service provider, faces in a competitive environment, to customers that have chosen to take service from a competitor. The Company seems to focus on the risk of customer switching alone. However the rider also potentially protects DEO from a misalignment of the Company's rate-setting, collection, and generation contracting practices. Additionally, if the condition is triggered, it will inappropriately make competitively-supplied customers responsible for SSO-related competitive bidding and independent auction consultant costs.

For all these reasons, the Commission should reject Rider SCR as proposed by the Company. If, however, the Commission determines that Rider SCR should be approved, the Commission should also determine that the rider is completely bypassable by competitively-supplied customers under all conditions. If the Commission determines that the rider is non-bypassable, the Commission should determine that costs associated with "conducting, administering, and implementing the [competitive bidding] plan as well as the costs for any independent auction consultants" will not be collected through Rider SCR.

CONCLUSION

WHEREFORE, for all the above and foregoing reasons, Walmart respectfully requests that the Commission reject Rider RECON and Rider SCR as proposed by the Company.

In the case of Rider RECON, Walmart respectfully requests that the Commission determine that the rider is bypassable by competitively-supplied customers. In the alternative in the event the Commission determines that Rider RECON is not bypassable, Walmart respectfully request that the Commission determine that the rider applies only to those competitive-supplied customers that, during the final period to be trued-up prior to implementation of the MRO, either 1) take SSO service from the Company, or 2) do not qualify to bypass Rider SRA-SRT.

In the case of Rider SCR, Walmart respectfully requests that the Commission determine that the rider is bypassable by competitively-supplied customers. In the alternative in the event the Commission determines that Rider SR is not bypassable, Walmart respectfully requests that the Commission determine that costs associated with "conducting, administering, and implementing the [competitive bidding] plan as well as the costs for any independent auction consultants" will not be collected through the rider.

Respectfully submitted,

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The undersigned hereby certifies and affirms that on the 27th day of January, 2011, a true and correct copy of the foregoing instrument was served via electronic mail and/or first class mail, postage prepaid, to the following persons:

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