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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

REPLY BRIEF OF THE KROGER CO.

A. **<u>The Blended Price Period in Duke's MRO Application Must be at Least Five (5) Years Long as Mandated by R.C. 4928.142</u>**

As has been noted, Section 4928.142 of the Ohio Revised Code provides for special pricing requirements for an electric distribution utility, such as Duke, that is seeking its first market rate offering ("MRO") and which, as of July 31, 2008, directly owned operating electric generating facilities that were used and useful in Ohio. It is undisputed that Duke directly owned operating electric generating facilities that were used and useful in Ohio as of July 31, 2008. Duke's application for an MRO therefore must provide that a portion of the utility's SSO load will be competitively bid for the first five (5) years of the MRO, such that ten percent (10%) of the SSO load is competitively bid in year one, and <u>not more than</u> twenty percent (20%) of SSO load is competitively bid in year two (2), thirty percent (30%) in year three (3), forty percent (40%) in year four (4), and fifty percent (50%) in year five (5). Consistent with these percentages, the Commission is charged with determining the actual percentages for years one (1) through five (5).[1]

The "blended" SSO price is required to be part bid price and part generation service price for the SSO load; the "non-bid" portion being equal the electric distribution utility's most recent

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[1] R.C. 4928.142 and Kroger's Exhibit 1 at p. 5, lines 17-23 and p. 6, lines 1-3.

SSO price, adjusted upward or downward by the Commission to reflect the prudently-incurred costs of fuel, purchased power, supply and demand resource portfolio compliance and compliance with environmental laws and regulations.[2]

Duke is proposing that the mandatory blending period last only two (2) years, then be eliminated entirely. Under Duke's proposal, the bid price would constitute ten percent (10%) of the blended price in the first year of the MRO[3] and twenty percent (20%) in the second year. Starting in the third year, Duke proposes that one hundred percent (100%) of the SSO load be served through market rates.

R.C. 4928.142 does grant limited discretion to the Commission with respect to the blending proportions by permitting the Commission to <u>extend</u> the duration of the blending period from five (5) years to up to ten (10) years under a limited set of articulated circumstances. Duke claims that this discretion allows the Commission to eliminate the blending period after year two, as long as forecasted market rates and market rates "converge." The twisted logic necessary to reach this conclusion is described as "statutory interpretation."

As has been noted, the Commission's discretion in setting the blending proportions is addressed in two divisions of R.C. 4928.142. After enumerating the blending percentages, R.C. 4928.142(D) states that, "Consistent with those percentages, the commission shall determine the actual percentages for each year of years one through five." R.C. 4928.142(E) then goes on to provide that:

> Beginning in the second year of a blended price under division (D) of this section and notwithstanding any other requirement of this section, the commission may alter prospectively the proportions specified in that division **<u>to mitigate any effect of an abrupt or significant change in the electric distribution utility's</u>**

[2] Id.

[3] For the purposes of this filing, Duke requests that the "first year" actually be equal to 17 months.

<u>standard service offer price that would otherwise result in general or with respect to any rate group or rate schedule but for such alteration.</u>[4]

In justifying its proposal to eliminate the blending period, Duke cites to select portions of Division (E), above. However, Duke must engage in extreme word parsing and misrepresentation of the statutory language to conclude that as long as SSO price and market prices are forecasted to converge, the Commission may eliminate the blending period after two years and move to pure market rates.

Taken in context, the five (5) to ten (10) year blending period described in the statute clearly reflects a policy of gradual transformation to market pricing for SSO generation service when a first MRO is adopted for affected utilities. Duke's proposal to eliminate the blending period in two (2) years is recklessly inconsistent with that clear policy objective. The sort of price volatility that may result from an abrupt change to purely market rates is the sort of result that a conservative migration to full MRO pricing inherent in a five (5) to ten (10) year blending period expressly seeks to avoid.[5]

Duke's denial of the plain wording of Division (E) of R.C. 4928.142 to support elimination of the blending period runs counter to the clearly expressed logic in the first sentence of Division (E) itself. As previously noted, if the proportions specified in Division (D) are altered to mitigate any effect of an **<u>"abrupt"</u>** or **<u>"significant"</u>** **<u>prospective</u>** change **<u>in Duke's SSO price,</u>** the alteration can logically occur in only one direction: downward. This is because Division (D) specifies the percentages of the bid price in the blended price; the remaining portion of the blended price is essentially the status quo price. If abrupt or significant <u>changes</u> to the **<u>overall SSO price</u>** were expected to occur, it would have to be through the <u>new</u> bid price component, not the status quo component. Thus, mitigation of "abrupt" or "significant" changes

[4] Id. at lines 9-21.

[5] Kroger's Exhibit 1 at p. 8, lines 1-6.

in the SSO price by altering the proportion of the blended price could occur mathematically only by reducing the bid price component, not by increasing it (let alone to 100%) as Duke is proposing.[6]

Duke simply decides to ignore the words "in the electric distribution utility's standard service offer price" in Division (E). No explanation is given for this "oversight." However, skipping over an entire clause of a statute to determine its intent is unhelpful. Division E does not refer to any "abrupt" or "significant" change in the world generally, as Duke proposes. Rather, it specifies that the limited discretion granted the Commission should be used to mitigate the effect on customers of an abrupt or significant change **in the electric distribution utility's standard service offer price.** The only thing that can significantly or abruptly impact the SSO price is the amount of the bid price included in the blended SSO price.

Further, Duke fails to explain how a provision that does not appear to confer specific discretion to the Commission to act until 2013 can be exercised upon the approval of the MRO application. Duke also fails to explain why Division (D), which describes the proportions that must appear in the Company's MRO Application, can simply be ignored.[7]

It is also apparent from Duke's filing that Duke is applying an idiosyncratic, if not bizarre, grammatical interpretation to the first sentence of Division (D), which reads:

> The first application filed under this section by an electric distribution utility that, as of July 31, 2008, directly owns, in whole or in part, operating electric generating facilities that had been used and useful in this state shall require that a portion of that utility's standard service offer load for the first five years of the market rate offer be competitively bid under division (A) of this section as follows: ten percent of the load in year one, not more than twenty percent in year two, thirty percent in year three, forty percent in year four, and fifty percent in year five. [Emphasis added.]

[6] Id. at lines 7-19.
[7] Id. at p. 8, lines 20-23 and p. 9, lines 1-4.

According to Duke's apparent interpretation of this sentence, the phrase "not more than" modifies only "twenty percent," and not the thirty percent, forty percent, and fifty percent that follow.[8] In any reasonable understanding of the English language, the modifier "not more than" would apply to all items that follow it. Additionally, the very next sentence of this division states, *"Consistent with those **percentages**,* the commission shall determine the actual percentages for each year of years one through five." [Emphasis added][9]

Logically, for the Commission to determine *actual* percentages that are *consistent* with the enumerated percentages, some *range* of percentages would be implicit in the enumerated percentages. Yet, according to Duke's interpretation of Division (D), a range of percentages is indicated only for the second year of the MRO. The logical extension of Duke's interpretation of the first sentence of Division (D) is that the second sentence of Division (D) is relevant only to the second year, and not to the third, fourth, or fifth.

On the other hand, if Division (D) is interpreted as requiring that the proportionate weight given to the bid price for years three, four, and five of the MRO can be no more than thirty percent, forty percent, and fifty percent, respectively, then the Commission could adjust the bid price proportion in an amount up to the enumerated percentages, but not beyond. This more rational interpretation would rule out eliminating the status quo portion of the blended price in years three, four, and five as Duke is proposing.[10]

Therefore, Duke has not presented an MRO Application that complies with the requirements of R.C. 4928.142(D). Just as importantly, Duke's proposal is not compatible with

[8] This interpretation is evident in the table on page 9 of Mr. Wathen's direct testimony, in which the bid price proportion for the second year is shown as not more than 20 percent (i.e., $\leq$20%), whereas for years three, four, and five it is shown as equal to 30 percent, 40, percent, and 50 percent, respectively.
[9] Kroger Exhibit 1 at p. 9, lines 5-24.
[10] Id. at p. 10, lines 6-12.

a rational policy of gradual transformation to market pricing for SSO generation service. Duke's MRO Application must therefore be rejected as deficient.[11]

B. MRO Rate Design Should be Modified to Mitigate the Effect of the Design on High Load Factor Customers in Demand Based Rate Classes

As noted in the Initial Brief of the Kroger Co., currently a significant portion of Duke's ESP generation rate is comprised of demand charges for those rate schedules that are billed on a demand basis. This is an appropriate design for ensuring a proper alignment between capacity-related costs and like charges. Appropriately, Duke is proposing to retain this design in the ESP component of its blended price.[12] However, the bid price component of the proposed MRO is priced solely on a kilowatt-hour basis.[13] This abrupt and significant change in rates for customers on a demand billed rate schedule will be accompanied by a material impact on customer rates within each demand-billed rate schedule: higher-load-factor customers within each demand-billed rate schedule will see their rates negatively impacted, whereas lower-load-factor customers will receive a windfall benefit.[14]

[11] Id. at lines 13-17.

[12] Id. at lines 19-23, p. 13, lines 1 and 2.

[13] Kroger Exhibit 1 at p. 13, lines 3-11.

[14] Kroger's Exhibit 1 at p. 13, lines 3-11, and Transcript of Proceedings in Case Number 10-2586-EL-SSO, Volume III, dated January 13, 2011 at p. 566 – 573.

Kroger's witness Kevin Higgins ("Higgins") testified that he used the formulas in Duke's rate impact model provided in its work papers to examine the significant and rate impacts from Duke's proposed rate design change. For example, by the third year of the proposed MRO, an 80% load factor customer on the DP rate schedule would see its generation rates deteriorate by approximately 21% relative to a 30% load factor customer.[15] Similarly, a 90% load factor customer on the TS rate schedule would see its generation rates deteriorate by approximately 17% relative to a 50% load factor customer.[16] This type of rate impact is not reasonable.[17] These potential rate impacts are largely the result of Duke's rate design choice to eliminate retail demand charges for the bid price component of the SSO.

In response to Higgins findings that the rate design chosen by Duke will have dramatic negative impacts on high load factor customers in demand billed rate schedules, Duke merely states that there is no statutory requirement for Duke to submit a retail rate design that incorporates demand charges. "Thus, Duke Energy Ohio's proposed rate design satisfies the applicable requirements." [18] The fact that there is no specific statutory requirement for Duke to incorporate demand charges in a retail rate design is not sufficient reason to propose a rate design that dramatically and negatively impacts high load factor customers on existing demand based billing schedules. In fact, this is not even a serious attempt at support for such a drastic change. Further, The Kroger Co. did not suggest that the MRO application should be rejected in full for failure to incorporate demand charges. Rather, Mr. Higgins suggested that the application could easily be modified to mitigate the effects of Duke's suggested retail rate design on high load factor customers on demand based billing schedules, and that such mitigation and modification

[15] 4.20% to (-16.54%).
[16] Kroger's Exhibit 1 at p. 14, lines 1-17.
[17] Id. at p. 15, lines 1-5.
[18] Merit Brief of Duke Energy at 31-32.

was reasonable under the circumstances. Since Duke Energy has yet to offer any substantial reason, or really any reason at all, for ignoring the impact to high load factor demand based customers, the Commission should adopt the recommendations for modification suggested in Higgins' testimony in order to mitigate the abrupt rate impact such a fundamental change in rate design would cause to such customers.

CONCLUSION.

In summary, Duke's Application for an MRO currently pending before this Commission must not be approved as filed. Duke's Application fails to conform to the mandatory filing requirements for a first MRO related to the length of the blending period as well as the make-up of the blend percentages. Also, Duke's rate design unreasonably and unnecessarily has major negative impacts on high load factor customers in rate classes currently billed through demand rates. There is no principle or cost based reason for these significant negative impacts, and the Commission should modify this part of the Application to provide for the continuation of demand based rates.

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