

**BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO**

In the Matter Of The Application Of Duke)	
Energy Ohio, Inc. For Authority To Establish)	
A Standard Service Offer Pursuant To Section)	Case No. 14-841-EL-SSO
4928.143 Revised Code, In The Form Of An)	
Electric Security Plan, Accounting Modifications)	
And Tariffs For Generation Service)	
)	
In The Matter Of The Application Of Duke)	
Energy Ohio, Inc. For Authority To Amend)	Case No. 14-842-EL-ATA
Its Certified Supplier Tariff, P.U.C.O. No. 20)	

SIERRA CLUB’S REPLY BRIEF

Sierra Club urges the Commission to reject the proposed Price Stabilization Rider (“Rider PSR”). As demonstrated in the initial briefs filed by Sierra Club and other intervenors, Rider PSR will harm Duke’s customers by increasing costs and exposing them to risk without providing any benefit at all. Considering the overwhelmingly negative effect on customers, it should be no surprise that every intervenor aside from Ohio Energy Group (which has proposed to exempt its own members)¹ opposes Rider PSR.²

And the briefing in this case understates the opposition to Rider PSR. As the Commission is aware, 12 large businesses that together employ over 79,000 Ohioans have stated

¹ OEG Initial Brief at 15 (proposing that customers with 10 MW of load or more be permitted to avoid Rider PSR). OEG’s “support” for Rider PSR while proposing to exempt its own members speaks for itself. The Commission should discount OEG’s arguments accordingly.

² Staff Initial Brief at 2; OCC Initial Brief at 5; City of Cincinnati Initial Brief at 4; Constellation/Exelon Initial Brief at 2; Direct Energy Initial Brief at 11; ELPC Initial Brief at 5; IGS Energy Initial Brief at 17; IEU-Ohio Initial Brief at 2; Kroger Initial Brief at 8; ODSA Initial Brief at 7; OEC Initial Brief at 2; OMA Initial Brief at 5; OPAC Initial Brief at 7; RESA Initial Brief at 6; Universities Initial Brief at 6.

their opposition to the out-of-market subsidy proposed by the Ohio Power Company for its share of OVEC and "other similar programs that have been proposed in other pending proceedings."³ As these businesses—which employ at least an order of magnitude more Ohioans than do Duke or OVEC—have recognized, Ohio’s economic recovery and advancement are premised on the continued embrace of competitive markets and the relatively affordable energy these markets provide.⁴ Simply put, aside from those who have proposed to exempt themselves, all business and consumer stakeholders, as well as the largest city in Duke’s service area, oppose Rider PSR.

In response to this overwhelming opposition, Duke offers nothing but a dubious argument that Rider PSR might be permitted by one subsection of the electric security plan (“ESP”) statute and the observation that in a rising price environment, Rider PSR may benefit customers as a hedge. Neither argument is convincing. The Commission should protect customers from unnecessary rate increases and exposure to significant risk by rejecting Rider PSR.

I. Section 4928.143(B)(2)(d) Does Not Authorize Rider PSR Because Duke Has Not Shown that It Would Reduce Volatility for Ratepayers.

Even if Rider PSR were good for customers—which it is not⁵—the Commission could approve it only if a specific provision of the ESP statute authorized this proposed rider.⁶

³ Letter of Boston Market Corporation *et al.*, filed in docket 13-2385-EL-SSO on October 16, 2014, available at:

<http://dis.puc.state.oh.us/TiffToPDF/A1001001A14J17B23831F40292.pdf>.

⁴ *Id.* at 1-2.

⁵ Sierra Club Initial Brief at 5-20.

⁶ *In re Application of Columbus S. Power Co.*, 128 Ohio St. 3d 512, 520 (2011) (“if a given provision does not fit within one of the categories listed “following” (B)(2), it is not authorized by statute.”); *see id.* (the contrary interpretation “would remove any substantive limit to what an electric security plan may contain, a result we do not believe the General Assembly intended.”); *see also* Sierra Club Initial Brief at 3.

Contrary to Duke’s suggestion,⁷ subsection 4928.143(B)(2)(d) does not authorize Rider PSR because Duke has not shown that it would more likely than not have the “effect” of increasing price stability. A bare assertion that a certain ESP term is intended to achieve stability is not sufficient under the plain language of the statute. Instead, record evidence must demonstrate that a proposed term “would have *the effect* of stabilizing” prices.⁸ Here, because Duke has not met its burden to show that Rider PSR would have such effect, the Commission lacks authority to approve it.

At the very least, Rider PSR’s effect on volatility over the 25-year term of the proposal is highly uncertain, and Rider PSR would work as a counter-cyclical hedge under one scenario only: If energy and capacity prices increase substantially—and remain consistently high—while OVEC costs remain stable. Conversely, if OVEC costs increase just as much or more than market prices, there will be no hedging effect.⁹ Similarly, if Duke’s theory that energy and capacity prices will increase substantially proves incorrect, there will be no hedging effect at all.

As a preliminary matter, Duke has not provided a forecast of energy and capacity markets beyond 2024 and thus it has offered nothing more than speculation for the majority of the proposed term of Rider PSR.¹⁰ And, more fundamentally, accurately projecting costs and revenues over anything more than the near-term is essentially impossible.¹¹ In support of the purported hedging effect, Rider PSR has offered little more than speculation.

⁷ Duke Initial Brief at 18.

⁸ Ohio Revised Code § 4928.143(B)(2)(d) (emphasis added).

⁹ Hearing Transcript, Vol. I at 252; 11-19 (Henning Testimony) (acknowledging that if OVEC costs grow faster than market prices Rider PSR would increase volatility—not reduce it).

¹⁰ See OCC Exhibit 4.

¹¹ *E.g.*, Sierra Club Initial Brief at 16-17 (citing OCC Exhibit 43, Wilson Written Testimony at 8-9) (“Forecasts of costs and revenues necessarily rely on multiple unknown inputs, including energy and capacity price, fuel prices, environmental and other regulations” and therefore are “necessarily highly uncertain.”).

Further, the more persuasive record evidence shows that Rider PSR would in fact *increase* volatility for Duke’s customers because the OVEC units are likely to remain uneconomic. First, even under Duke’s own forecast, the OVEC units show negative cash flow during the first several years of the proposal, providing no hedge against rising prices. Second, Duke’s forecast likely understates OVEC costs while overstating revenues. As demonstrated in Sierra Club’s initial brief, Duke’s view of the energy and capacity markets is likely too optimistic—inflating the value of the OVEC plants in question.¹² For example, Duke’s speculation that capacity prices will increase in the future¹³ fails to account for basic economic theory. If, as Duke speculates, capacity prices do increase in the future, market forces would work to drive those prices down, as a sustained period of high prices would cause market participants to respond by adding capacity, which would tend to drive down prices. Similarly, as shown in Sierra Club’s initial brief, Duke likely understates the costs that will come to bear on the OVEC plants as they age over the next 25 years.¹⁴ More likely than Duke’s rosy projections, the OVEC plants will continue to show negative cash flow for years into the future, providing no hedge against rising prices (should such prices in fact rise).

In addition, Rider PSR would *increase* price instability because many of Duke’s customers are already protected by various hedge mechanisms, and this proposal would reduce their effectiveness.¹⁵ The twenty-three percent¹⁶ of Duke’s customers who are served via the SSO auctions are already insulated from rapid changes in market prices by the laddered and

¹² Sierra Club Initial Brief at 8-10.

¹³ Duke Initial Brief at 22.

¹⁴ Sierra Club Initial Brief at 10-15.

¹⁵ See RESA Initial Brief at 7-9 (describing how Duke’s SSO and CRES-served customers are already protected from market volatility).

¹⁶ Staff Exhibit 1, Choueiki Written Testimony at 10.

staggered auctions that are employed to service them.¹⁷ Further, the majority of customers in Duke’s service area receive service from CRES providers,¹⁸ and thus are already insulated from market price volatility by contract (to the extent they choose fixed-price contracts). These customers do not need a hedge mechanism imposed on them as they remain free to contract for one. For these customers, Rider PSR will “unravel the hedge that fixed price contracts provide.”¹⁹

Thus, to the extent Duke’s customers are subject to price volatility at all, Rider PSR would work to increase volatility—not reduce it. The Commission accordingly lacks statutory authority to approve Rider PSR.

II. Duke’s Interpretation of Subsection 4928.143(B)(2)(d) Is Not Plausible.

In addition to failing to show that Rider PSR would have the effect of increasing price stability for customers, Duke’s interpretation of subsection 4928.143(B)(2)(d) is not plausible for at least three reasons.

First, Duke suggests that this subsection—intended to reduce price instability—should be permitted to apply to a proposed cost-recovery mechanism that applies to *variable* costs over a 25-year period. If Duke’s proposed interpretation were adopted, there would be essentially no outer bound for the application of subsection 4928.143(B)(2)(d). Instead, the Commission should follow its precedent by holding that subsection 4928.143(B)(2)(d) permits approval of a hedge mechanism only where the proposal provides *fixed* rates or allows recover of *fixed* costs.²⁰

¹⁷ Sierra Club Initial Brief at 17; Staff Exhibit 1, Choueiki Written Testimony at 12-13.

¹⁸ Staff Exhibit 1, Choueiki Written Testimony at 10.

¹⁹ Direct Energy Exhibit 1 at 6.

²⁰ *In Re Columbus S. Power Co*, Pub. Util. Comm. No. 11-346-EL-SSO, Entry on Rehearing pg. 16 (January 30, 2013) (“the RSR promotes stable retail electric service prices by stabilizing base generation costs at their current rates, ensuring customers have certain and fixed rates going forward” and stabilization rates at the then-current level).

The Commission’s previous indication that this subsection should apply only to fixed rates or fixed costs is more plausible than Duke’s variable-cost interpretation.

Second, if the Commission were to approve Rider PSR, such approval would essentially remove subsection 4928.143(B)(2)(a) from the ESP statute. Subsection 4928.143(B)(2)(a) provides for “automatic recovery” for specified categories of cost (none of which apply here). The Commission must presume that “the entire statute is intended to be effective.”²¹ By granting “automatic recovery” for a category of cost not listed in subsection 4928.143(B)(2)(a), the Commission would render meaningless the Legislature’s intention to limit automatic-cost recovery to the specifically delineated categories of costs.

Third, Duke’s claim that 4928.143(B)(2)(d) authorizes any charge that is either bypassable or nonbypassable²² is nonsensical. Any proposed ESP term or charge could be labeled as such. If the Commission were to adopt Duke’s interpretation it would effectively rewrite the ESP statute to allow any term or charge so long as it could be shown to increase price stability. This would run counter to the Ohio Supreme Court’s holding that only specifically authorized terms or charges can be approved under the ESP statute.²³

III. Rider PSR Is Premised on a Future Breakdown of Competitive Markets and, If Approved, Would Contradict the Continued Development of Competitive Retail Electric Markets in Ohio.

Contrary to Duke’s assertion,²⁴ approval of Rider RSR would work to reverse the development of a competitive market for the provision of electric service in Ohio. Duke is correct when it concedes that the actual track record of Ohio’s competitive market in recent years

²¹ Ohio Revised Code § 1.47 (presumptions in statutory interpretation).

²² Duke Initial Brief at 18.

²³ See, above, *In re Application of Columbus S. Power Co.*, 128 Ohio St. 3d 512, 520 (Ohio 2011).

²⁴ Duke Initial Brief at 19.

has been to provide reliable electric service at low prices.²⁵ Against the backdrop of recent success, Duke offers pure speculation that future generation retirements *could* increase future prices. Duke's speculation defies basic capitalist theory, however, and the Commission should accord it no weight.

If supply of a commodity were suddenly reduced—by, for example, retirement of uneconomic production—competitive forces would send a strong signal to increase supply to meet demand. This prediction of the operation of a competitive market has in fact been borne out in PJM in recent years. After generation retirements threatened to reduce supply a few years ago, PJM experienced a wave of new generation offering into its markets:

As PJM reported, although changes in environmental rules have led to significant [unit] retirements, '[t]he announced generation retirements sen[t] a strong signal that there would be a need for new resources, and [the 2012] auction witnessed a record number of new generation offers.'²⁶

Should Ohio and PJM experience a similar shortfall in supply in the future—which as of today is pure speculation—Ohio should rely on market forces, instead of government fiat, to provide the required generation and to maintain reasonable prices. Contrary to Duke's suggestion, competitive-market theory and recent experience indicate that market forces will protect Ohio ratepayers from future high prices.

Further, Rider PSR would itself reverse Ohio's transition to competitive markets.²⁷ Ohio has chosen a de-regulated system to insulate customers from the performance or non-performance of individual units. By forcing the Duke's customers to accept Rider PSR, Duke's customers effectively become the owners of the units; however, they would get virtually none of the benefits of ownership, such as control over costs and strategic decisions, and would not be

²⁵ *Id.*

²⁶ *PPL EnergyPlus, LLC v. Hanna*, 977 F. Supp. 2d 372, 395 (D.N.J. 2013).

²⁷ Staff Initial Brief at 2-10; Sierra Club Initial Brief at 15-18.

entitled to the type of regulatory oversight that protects customers in a regulated system.²⁸

Duke's government fiat approach to long-term planning could lead to planning decisions that harm ratepayers over the long term. The free market approach is both mandated by Ohio law and flexible: Competitive markets, by design, allow for adjustment in the face of changing circumstances over the long term.

IV. Conclusion

A certain degree of price instability is inherent in any competitive market. The Ohio legislature should be presumed to be aware of this basic feature of capitalism when it endorsed competition as the best means to provide Ohioans with reliable, low-cost energy. Conversely, the Commission should rely on 4928.143(B)(2)(d) only where an applicant has demonstrated unusual or extreme volatility and proposed a mechanism that is guaranteed to reduce volatility at low cost to customers, without subjecting them to increased risk. Duke has not shown that any of these necessary conditions apply here. For all these reasons and those stated in Sierra Club's initial brief and the initial briefs of other intervenors, the Commission should reject Rider PSR.

Dated: December 29, 2014

Respectfully submitted,

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²⁸ Sierra Club Exhibit 4, Jackson Written Testimony at 5.

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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing Sierra Club's Reply Brief was served via electronic transmission upon the parties this 29th day of December, 2014.

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Case No(s). 14-0841-EL-SSO, 14-0842-EL-ATA

Summary: Reply Brief electronically filed by Mr. Christopher J. Allwein on behalf of SIERRA CLUB