BEFORE

THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Duke Energy Ohio, Inc., for Approval to Modify Rider PSR.	)))	Case No. 17-872-EL-RDR
In the Matter of the Application of Duke Energy Ohio, Inc., for Approval to Amend Rider PSR.	)))	Case No. 17-873-EL-ATA
In the Matter of the Application of Duke Energy Ohio, Inc., for Approval to Change Accounting Methods.	)))	Case No. 17-874-EL-AAM

APPLICATION OF DUKE ENERGY OHIO, INC.

Comes now Duke Energy Ohio, Inc., (Duke Energy Ohio or Company) and states as follows:

1. Duke Energy Ohio is an Ohio corporation engaged in the business of supplying electric generation, transmission, and distribution service to more than 700,000 customers in southwestern Ohio, all of whom will be affected by this Application. Duke Energy Ohio is a public utility, as defined by Ohio Revised Code (R.C.) 4905.02, and an electric light company, as defined by R.C. 4905.03, and is subject to the jurisdiction of the Public Utilities Commission of Ohio (Commission).

2. This Application is made pursuant to R.C. 4905.04, R.C. 4905.05, R.C. 4905.06, R.C. 4905.13, and R.C. 4909.18 and related sections of the Ohio Revised Code. The Company seeks the following:

a. An order from the Commission, under the authority of R.C. 4905.04, R.C. 4905.05, R.C. 4905.06, and R.C. 4909.18, establishing the initial tariff amounts applicable to the Company's existing Price Stabilization Rider (Rider PSR);

b. An order from the Commission, under the authority of R.C. 4905.04, R.C. 4905.05, R.C. 4905.06, and R.C. 4909.18, confirming the procedure pursuant to which Rider PSR will be periodically reviewed and adjusted;

c. An order from the Commission, under the authority of R.C. 4905.04, R.C. 4905.05, R.C. 4905.06, and R.C. 4909.18, amending Rider PSR to revise the effective period of said rider;

d. An order from the Commission, under the authority of R.C. 4905.13, authorizing Duke Energy Ohio to modify its accounting practices to establish a deferral, as of April 1, 2017, to account for the net costs[1] related to the Company's contractual entitlement in generating assets owned by the Ohio Valley Electric Corporation (OVEC); and

e. An order from the Commission, under the authority of R.C. 4905.13 and R.C. 4909.18, authorizing the recovery of such deferred amounts via Rider PSR.

PROCEDURAL BACKGROUND

3. By Opinion and Order dated April 2, 2015, the Commission authorized Duke Energy Ohio to establish a placeholder rider, Rider PSR, that would protect all retail customers

[1] As used herein, "net costs" shall refer to the revenues received by the Company in liquidating its output in the applicable wholesale markets less all costs incurred under the ICPA, where such amount may be either positive or negative.

"from price volatility in the wholesale market."[2] The Commission further authorized Duke Energy Ohio to institute a subsequent action for purposes of establishing initial tariff amounts applicable to Rider PSR.[3] Significantly, the Commission contemplated that "[a]ll of the implementation details with respect to the placeholder PSR [would] be determined by the Commission in that future proceeding."[4]

4. The Commission also identified several factors that Duke Energy Ohio is to address in connection with its request to adjust Rider PSR. In doing so, however, the Commission expressly stated that it would not be bound by such factors in assessing the Company's request.[5] The Commission further delineated additional elements to be incorporated into the request to adjust Rider PSR.[6]

OVEC CONTRACTUAL ENTITLEMENT

5. The Commission has already received substantial evidence on the Company's status as a counterparty to, and co-sponsor of, an intercompany power agreement (ICPA) with OVEC and other counterparties and has assessed such evidence in its decision in the ESP III proceeding. Duke Energy Ohio, therefore, does not intend to re-litigate issues concerning its co-sponsor status or the operation of the ICPA. Rather, the Company provides only a brief mention of OVEC so as to reiterate the significance of its request herein and stress the unique status of OVEC.

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[2] *In the Matter of the Application of Duke Energy Ohio, Inc., for Authority to Establish a Standard Service Offer Pursuant to R.C. 4928.143 in the Form of an Electric Security Plan, Accounting Modifications, and Tariffs for Generation Service*, Case No. 14-841-EL-SSO, *et al.*, Opinion and Order, at pp. 46-47 (April 2, 2015)(hereinafter ESP III).

[3] Id, at pg. 47.

[4] Id.

[5] Id. See also *In the Matter of the Application Seeking Approval of Ohio Power Company's Proposal to Enter into an Affiliate Power Purchase Agreement for Inclusion in the Power Purchase Agreement Rider*, Case No. 14-1693-EL-RDR, Second Entry on Rehearing, at pg. 66 (November 3, 2016)(Commission affirmed rider mechanism for Ohio Power that included only its contractual entitlement in OVEC, reiterating that, in evaluating the request, it would not be bound by the identified factors)(hereinafter AEP PPA Proceeding).

[6] ESP III, Opinion and Order, at pg. 47.

6. OVEC[7] was organized in 1952 for the purpose of meeting the power needs of uranium enrichment facilities operated by the Atomic Energy Commission (AEC). Notably, along with other entities, investor-owned utilities, including Duke Energy Ohio's predecessor, agreed to form OVEC for purposes of answering the nation's then-critical cold war needs. In 1952, OVEC and the AEC entered into a long-term agreement for the provision of power to these essential uranium enrichment facilities – an agreement that was, at the time, the largest single-customer contract in the history of the electric utility industry.[8] In order to support this long-term agreement and ensure that the substantial power requirements of the AEC were met, OVEC and OVEC's owners or their affiliates, together with affiliates of rural electric cooperatives then entered into the ICPA. OVEC's two generating facilities began producing power in 1955 and were, at the time, the largest power plants ever built by private industry and the most efficient, producing 1 KWH or electricity for every 0.7 pounds of coal. The AEC's successor, the Department of Energy (DOE), eventually assumed and extended the contractual obligations. However, in 2003, the DOE canceled the power agreement and all of the output of the OVEC-owned plants essentially reverted to the co-sponsors under the ICPA.[9]

7. The current ICPA to which Duke Energy Ohio is a counterparty has a term through June 30, 2040, as approved by the Federal Energy Regulatory Commission (FERC). The Company's entitlement approximates 200 MWs of the total generating capacity of the OVEC-owned assets.

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[7] OVEC and its subsidiary, Indiana-Kentucky Electric Corporation, own and operate two generating plants. For ease of naming convention, these entities are collectively referred to as OVEC.

[8] *The Portsmouth Story, Part 1 of 2*, The Atomic Energy Commission, at 1:54-2:02, https://www.youtube.com/watch?v=R7jUBak6mgI (accessed March 30, 2017). See also *New Power Plants Now Supplying Current to AEC Uranium Plant*, The Daily Times (New Philadelphia, Ohio), at page 14 (January 27, 1955).

[9] http://www.ovec.com/OVECHistory.pdf (accessed March 30, 2017). See also http://ovec.com/Clifty.php (accessed March 30, 2017), http://ovec.com/Kyger.php (accessed March 30, 2017).

8. "OVEC is different."[10] It cannot and should not be treated as analogous to those conventional generating stations constructed, operated, and maintained under a prior state regulatory framework. Indeed, it reflects an atypical arrangement undertaken in response to critical needs of the nation and it appropriately warrants individual consideration, as the Commission has recently recognized.[11]

RIDER PSR

9. Duke Energy Ohio proposes here to include in Rider PSR the net costs associated with its contractual entitlement in OVEC. Specifically, the full benefit of all revenues resulting from the Company's participation in the wholesale markets, with its contractual entitlement in OVEC, less all costs incurred under the ICPA, would flow through to customers on a nonbypassable basis under Rider PSR.

10. As required in the Commission's Opinion and Order in ESP III, Duke Energy Ohio proposes that Rider PSR be updated on a quarterly basis, with annual audits. For ease of administration, the Company proposes that, on a quarterly basis, it file updated amounts for inclusion in the rider. Such adjustments will automatically take effect thirty days subsequent to the Company's quarterly filing, thus allowing Staff a brief period of time to confirm the accuracy of the calculations underlying the updates. Because the FERC has approved the cost methodology incorporated into the ICPA, Duke Energy Ohio submits that any review of the costs factored into the overall Rider PSR rates must be limited to mathematical accuracy. Any further review risks invading the province of the FERC. In the course of the annual audit, however, the Commission would have the ability to fully review the revenues realized by the Company in connection with its contractual entitlement, including an analysis of managerial

[10] AEP PPA Proceeding, Second Entry on Rehearing, Concurring Opinion of Chairman Haque, at pg. 6 (November 3, 2016).
[11] Id, at pp. 5-6.

decisions related to participation in the wholesale markets. The annual audit will thus serve as an opportunity for the Commission, as it deems necessary, to assess the prudency of the Company's decisions in respect of monetizing its contractual share of the OVEC assets' output, based on the Company's submission of relevant information and data.

11. The wholesale markets in which Duke Energy Ohio participates in respect of its contractual entitlement are those administered by PJM Interconnection, L.L.C., (PJM) and include, for capacity, the Reliability Pricing Model market and, for energy, both the day-ahead and real-time energy markets. Effective with the 2020/2021 delivery year, PJM is requiring that all capacity resources qualify as Capacity Performance (CP). This transition to CP-only resources began with the 2016/2017 delivery year. CP resources are eligible for CP credits (bonuses) and at risk for CP charges (penalties).[12] Consistent with the Commission's requirement that the Company provide an alternate plan to allocate financial risk,[13] Duke Energy Ohio proposes herein that CP credits and charges be included in Rider PSR, which approach reconciles the rider with the economic realities of participating as a CP resource and thus properly aligns the interests of the Company and its customers.

12. As a complement to the above-mentioned alternate, or mitigation measure, Duke Energy Ohio further proposes to commit $1 million annually toward economic development initiatives in its southwest Ohio service territory, with such commitment beginning on June 1, 2018, and terminating simultaneous with Rider PSR. This commitment will be funded by shareholder dollars and is expressly conditioned upon the approval of all proposals included in the Application.

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[12] PJM Interconnection, L.L.C., FERC Docket No. ER15-623-000, *et al.*, Reforms to the Reliability Pricing Market ("RPM") and Related Rules in the PJM Open Access Transmission Tariff ("Tariff") and Reliability Assurance Agreement Among Load Serving Entities ("RRA"), PJM Initial Filing, at pg. 21 (December 12, 2014) and Order on Proposed Tariff Revisions, at pp. 10-11 (June 9, 2015).
[13] ESP III, Opinion and Order, at pg. 47.

13. In approving the placeholder Rider PSR, the Commission further instructed Duke Energy Ohio to include a severability provision that would allow for all other provisions of the current ESP to persist should its decision to establish a placeholder Rider PSR be declared invalid, in whole or in part, by a court of competent jurisdiction. Duke Energy Ohio submits that such a provision is likely moot at this time. Given that there is not a final, appealable order in ESP III as would be necessary to institute an appeal, recognizing the anticipated duration of an appeal to the Ohio Supreme Court, and conceding that the term of the current ESP expires in approximately fourteen months, the importance of a severability provision seems to have been tempered. Indeed, any future ruling as to the validity of any aspect of ESP III would be, at best, advisory in nature as the current ESP would have already ended and the provisions the Commission desired to preserve would have expired by their terms.

14. Duke Energy Ohio recognizes the Commission's expectation that Rider PSR be independent of the provisions included in an ESP. In furtherance of this expectation, the Company proposes a term for Rider PSR that aligns with the term of the ICPA. Perpetuation of Rider PSR beyond May 31, 2018, is consistent with established Commission precedent. Indeed, in the Company's two prior ESP proceedings, the Commission approved placeholder riders and subsequently authorized the riders to be adjusted via discrete proceedings, entirely independent

of any standard service offer (SSO) that might subsequently be advanced by the Company.[14]

15. Significantly, the Commission's authorization to adjust Rider PSR, as proposed herein, appropriately disassociates the rider proceeding from the ESP III proceeding and, consistent with established precedent, allows for future review of costs to be included in the rider on an independent basis, without regard to the Company's current or future SSOs. This disassociation represents a reasonable alternative to the severability provision as was contemplated by the Commission under different circumstances.

16. Perpetuation of Rider PSR beyond May 31, 2018, would enable customers to benefit from long-term stability. Given the admittedly volatile nature of the wholesale market and the uncertainties associated with CP, the full import of which cannot be realized prior to the 2020/2021 delivery year, it is undeniable that the price mitigation enabled by Rider PSR, as proposed herein, will benefit customers into the future. Additionally, perpetuation of the rider appropriately recognizes, and affords fair value for, the commitment Duke Energy Ohio made long ago in support of the nation's defense.

THE COMMISSION'S FACTORS

17. The Commission has determined that "any future cost recovery filing would not be limited to consideration of the factors."[15] Indeed, in recently approving a similar rider

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[14] See, *e.g.*, *In the Matter of the Application of Duke Energy Ohio, Inc., for Approval of an Electric Security Plan*, Case No. 08-920-EL-SSO, *et al.*, Opinion and Order, at pp. 17-18, 43 (December 17, 2008)(approving Rider DR-IM, initially set at zero, for future recovery, in a separate proceeding, of costs related to SmartGrid deployment) and *In the Matter of Duke Energy Ohio, Inc., for Authority to Establish a Standard Service Offer Pursuant to Section 4928.143, Revised Code, in the Form of an Electric Security Plan, Accounting Modifications, and Tariffs for Generation Service*, Case No. 11-3549-EL-SSO, *et al.*, Opinion and Order, at pp. 32-33, 51 (approving Rider UE-GEN, initially set at zero, for future recovery, in a separate proceeding, of costs related to generation uncollectible expense). See also *In the Matter of the Application of Duke Energy Ohio, Inc., to Adjust and Set its Gas and Electric Recovery Rate for 2010 SmartGrid Costs Under Rider AU and Rider DR-IM and Mid-Deployment Review of AMI/SmartGrid Program*, Case No. 10-2326-GE-RDR, Entry (October 27, 2010)(entry initiating review of grid modernization program previously established in an ESP) and *In the Matter of the Application of Duke Energy Ohio, Inc., to Adjust Rider DR-IM and Rider AU for 2012 Grid Modernization Costs*, Case No. 13-1141-GE-RDR, Application (June 28, 2013)(seeking adjustment to rider established in an ESP).

[15] AEP PPA Proceeding, Second Entry on Rehearing, at pg. 66 (November 3, 2016).

arrangement for Ohio Power Company, the Commission found considerations other than its previously identified factors to be persuasive, if not controlling. Consistent with the Commission's prior findings, Duke Energy Ohio submits that the factors, although addressed herein, are not determinative of its request to adjust Rider PSR.

18. As previously stated, Duke Energy Ohio is a counterparty to, and co-sponsor of, a FERC-approved ICPA. This agreement makes provision for the allocation of costs among the co-sponsors commensurate with their power participation ratio. It is undeniable that the costs incurred by OVEC, as the plants' owner and operator, will not change as a result of the Commission's approval of Rider PSR.[16] That is, OVEC will continue to have rights, and co-sponsors will continue to have obligations, as provided for in the ICPA, and an appropriate consideration, therefore, is the ability of any co-sponsor to fulfill those obligations.[17]

19. The OVEC generating assets represent approximately 2,400 MW of nameplate capacity in the PJM footprint. These coal plants represent one aspect of a diverse fuel source mix in PJM, which mix necessarily mitigates the impact of overdependence on any one fuel source.[18] It is indisputable that the plants are, and will continue to be, environmentally compliant.[19] Given the uncertainties now existing in respect of federal environmental regulation, it is imperative that properly maintained generating assets remain in operation. Indeed, premature closing of the OVEC generating plants would have an immediate adverse impact on the communities in which

[16] See *e.g.*, ESP III, Transcript of Hearing, Vol. XII, Cross examination of Staff witness Hisham Choueiki, at pg. 3457 (November 6, 2014).

[17] See, *e.g.*, AEP PPA Proceeding, Opinion and Order, Concurring Opinion of Chairman Haque (recognizing the impact of OVEC upon AEP Ohio and supporting its recovery of costs associated with an OVEC contractual entitlement).

[18] *Winter 2013-2014 Operations and Market Performance in RTOs and ISOs*, FERC Docket No. AD14-8-000, Presentation by FERC Staff, at pp. 2-3 (April 2, 2014)(2014 met with record high natural gas prices and depletion of U.S. natural gas storage) and *Polar Vortex 2014*, Presentation by Mike Kormos, Executive Vice President – Operations, PJM Interconnection, FERC Technical Conference, April 1, 2014 (gas plant outages and natural gas interruption represented almost half of the forced outages during the polar vortex).

[19] See, *e.g.*, ESP III, Transcript of Hearing, Vol. V, Cross examination of OCC witness John Brodt, at pp. 1322-1323 (October 28, 2014).

these plants are located.[20] And this harmful impact is likely to be long-term in nature, as significant job losses will not be easily remedied and individuals returned to a familiar way of life.

20. Ohio-based generating assets are retiring and will continue to retire. Indeed, one public utility in the state has committed, subject to certain conditions, to prematurely retire nearly 3,000MW of Ohio-based coal generation[21] it co-owns with a merchant generator. As the Commission observed, the parent company of another Ohio public utility is experiencing financial challenges not unlike other wholesale market participants[22] and has repeatedly acknowledged its intention to exit the competitive generation business.[23] The market is changing. More generating assets will retire,[24] with coal declining in the overall resource mix and individuals accustomed to working in coal plants becoming unemployed. Thus, although PJM provides assurances of a reliable supply,[25] it has not and cannot project the costs of achieving such an outcome.

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[20] See, *e.g.*, OVEC FERC Form 1(company paid over $6 million in property taxes alone in 2015).

[21] *In the Matter of the Application of The Dayton Power and Light Company for Approval of its Electric Security Plan*, Case No. 16-0395-EL-SSO, *et al.*, Testimony of Sharon R. Schroder in Support of the Stipulation and Recommendation, at pg. 21 (February 6, 2017); and The Dayton Power and Light Company's Memorandum in Opposition to the Motion to Intervene and Request for Leave to File Motion to Intervene Out of Time of Murray Energy Corporation, at pg. 5 (admitting the potential for generating plants to close as a part of a settlement). See also, DP&L Media Statement - Retirement of J.M. Stuart and Killen Stations in Ohio (March 20, 2017).

[22] *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Authority to Provide for a Standard Service Offer Pursuant to R.C. 4928.142 in the Form of an Electric Security Plan*, Case No. 14-1297-EL-SSO, Fifth Entry on Rehearing, Concurring Opinion of Chairman Haque, at pp. 3-4 (October 12, 2016)(remarking on the consequence of downgrades and the desire for healthy regulated utilities)(hereinafter FE ESP IV).

[23] See, *e.g.*, "FirstEnergy Takes Steps Towards Exiting Merchant Generation; Credit Neutral Overall," *Moody's Investor Service*, December 8, 2016 (www.moodys.com/research); "CEO: FirstEnergy will Exit Competitive Electricity Business," *The Washington Times*, November 9, 2016 (CEO Chuck Jones opining that some merchant generation units get sold while others shutdown).

[24] *2015 State of the Market Report for PJM*, Prepared by Joseph Bowring, Monitoring Analytics, at pp. 42-45, MC Special Session, March 31, 2016 (summary of PJM unit retirements by fuel, zone, and geographic location)(www.monitoringanalytics.com).

[25] See, PJM's Mission and Vision, February 2, 2017 ("…to ensure the safety, reliability, and security of the bulk electric power system")(www.pjm.com).

21. Rider PSR, as proposed herein, is directly tied to existing, coal-fired generation. The continued operation of that generation promotes resource diversity and economic development, criteria significant to the Commission.[26] Additionally, it is noteworthy that the Commission's approval of Rider PSR will not adversely affect wholesale competition or run afoul of state policy. Indeed, the Commission has found that Rider PSR is not an illegal subsidy[27] or an impermissible transition revenue.[28] Consequently, Rider PSR, as proposed herein, cannot be portrayed as unfairly favoring one competitive generator to the exclusion of all others. Rather, Rider PSR appropriately recognizes the unique nature of the Company's contractual entitlement, undertaken in response to national security, and enables a moderate financial hedge.

DEFERRAL REQUEST

22. Duke Energy Ohio respectfully requests that the Commission authorize it to: (i) defer net costs associated with its contractual entitlement as of April 1, 2017, and (ii) to recover such costs via Rider PSR in the same manner as proposed herein.

23. R.C. 4905.13 authorizes the Commission to establish systems of accounts to be kept by public utilities and to prescribe the manner in which these accounts shall be kept. The FERC has established a Uniform System of Accounts for electric utilities. This system of accounts is applicable to Ohio's regulated electric utilities only to the extent it has been adopted by the Commission, which adoption is found in O.A.C. 4901:1-9-05.

24. Duke Energy Ohio requests that the Commission authorize Duke Energy Ohio to modify its current accounting procedures and permit Duke Energy Ohio to defer income statement recognition of its net costs incurred under the ICPA effective as of April 1, 2017. The

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[26] FE ESP IV, Fifth Entry on Rehearing, at pp. 46-47 (rejecting revised rider arrangement, described as a "virtual hedge," that did not support resource diversity or economic development).
[27] ESP III, Opinion and Order, at pg. 48 (April 2, 2015).
[28] AEP PPA Proceeding, Second Entry on Rehearing, at pp. 98-100 (November 3, 2016).

recovery of the deferred amount will be addressed consistent with the process proposed herein, with such deferral included in the first Rider PSR adjustment. Duke Energy Ohio proposes to record all costs as a regulatory asset on its balance sheet in a separate account under FERC Account 182.3, Other Regulatory Assets.

Respectfully submitted,

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