

proposal.⁵

The Office of the Ohio Consumers' Counsel ("OCC") urges the PUCO to reject Duke's application. Use of avoided costs is an inappropriate basis for rates charged to residential customers. Further, Duke has not shown that the \$3 million is an ordinary and necessary expense associated with providing service to its customers. And Duke has not met the PUCO's standard for establishing deferrals.

II. RECOMMENDATIONS

A. **The PUCO should not create a regulatory asset that will be used for a charge to residential customers that is based on avoided costs.**

Duke asks the PUCO for authority to create a regulatory asset that is based solely on its alleged avoided costs of relocating a pipeline. Because the regulatory asset will eventually be used to create a charge for residential customers, basing the charge to customers solely on avoided costs is inappropriate.

Charges based on avoided costs have historically been used only for wholesale and commercial customers.⁶ For retail customers, avoided costs are generally used as one of many factors considered in determining a rate.⁷ And they are used to reduce the amount customers pay, not increase it. But here, Duke asks that costs it avoided paying be the basis for a charge to customers.

⁵ Entry (October 24, 2017) at 2.

⁶ See, e.g. *Application of Cincinnati Gas & Electric Co.*, Case No. 95-656-GA-AIR, Entry on Rehearing (February 12, 1997), 1997 PUC Lexis 106 [*16] (it may be appropriate to base the interruptible transmission rate on avoided costs). See also Ohio Adm. Code 4901:1-7-21(D)(2) (resale rates for telephone).

⁷ See, e.g., *Investigation into Impacts of Demand-Side Management Programs and Power Purchases on Profitability of Electric Utilities*, Case No. 90-723-EL-COI, Entry on Rehearing (April 4, 1991), 1991 PUC Lexis 468 [*24] (lost revenue calculation includes applicable tariff rate net of costs avoided).

Duke's proposal to create a regulatory asset based on avoided costs is inappropriate. The PUCO should reject it.

B. The application fails to show that the \$3 million is an expense that is ordinary and necessary to provide service to Duke's customers.

Duke's application provides scant information regarding the cost of the retaining wall and whether that cost is ordinary and necessary in the provision of utility service. For a cost to be ordinary and necessary, the utility needs to "clearly demonstrate a direct, primary benefit to its customers."⁸

Duke states that the landslide has affected a 20-inch pipeline that feeds about 50 service lines.⁹ But Duke does not discuss what types of customers are served by the pipeline and the service lines. This information would be important in determining whether the pipeline is a "vital and integral part" of Duke's system, as Duke asserts,¹⁰ and whether it is necessary to provide service to Duke's customers.

In addition, the pipeline is along the Ohio River,¹¹ so it may help serve Duke customers in Kentucky or Indiana. Not only would this call into question whether it is ordinary and necessary for Ohio customers, it would raise jurisdictional issues and questions about who should be responsible to pay.

Further, we have only Duke's allegation that the gas pipes were endangered by the landslide.¹² Duke has offered no photographs or independent analysis to support this

⁸ *City of Cleveland v. Public Utilities Commission of Ohio*, 63 Ohio St.2d 62, 406 N.E.2d 1370 (1980), citing *Re Iowa Pub. Serv. Co.*, 96 P.U.R.3d 1, 1972 WL 297730 (1972).

⁹ Application at 2.

¹⁰ *Id.*

¹¹ *Id.*

¹² *Id.* at 2.

claim. As the applicant in this case, Duke has the burden of showing that the \$3 million it has agreed to pay the City is ordinary and necessary to provide service to its customers. Duke has failed to meet that burden. The PUCO should deny the application.

C. Duke’s request for deferral authority in this case does not meet the long-standing PUCO standards for granting deferrals.

Duke seeks authority to defer the \$3 million, plus interest at its long-term debt rate, for collection from its customers. Duke offers no reasons why any collection from customers should be deferred if the PUCO approves Duke’s voluntary contribution to the City’s wall as a legitimate cost (which it should not because Duke has not shown it is an ordinary and necessary cost to provide service). Duke also does not reveal how long it intends to defer collection from customers. The PUCO should reject Duke’s request.

Deferrals needlessly add to the amount consumers pay for utility service. Duke’s long-term debt rate is 5.32 percent.¹³ A deferral would mean that customers would pay at least an additional \$159,600 for every year collection of the \$3 million is deferred. The PUCO should not allow this to happen.

In its review of utility applications seeking approval to defer capital costs or related expenses, the PUCO has determined that granting deferral authority is a *discretionary matter* within the PUCO’s authority.¹⁴ However, the PUCO has ruled that deferrals are not the standard mechanism for collecting costs. Instead, the PUCO has held that deferral accounting is an exception to utility ratemaking:

¹³ See Case No. 12-1682, Opinion and Order (May 1, 2013) at 6, 11.

¹⁴ *In the Matter of the Joint Application of Ohio Edison Company, The Cleveland Electric Illuminating Company and The Toledo Edison Electric Company for Approval of a Generation Charge Adjustment Rider*, Case No. 05-704-EL-AAM, Opinion and Order (January 4, 2006) at 8. (“FirstEnergy Deferral Order”).

Standard application of public utility ratemaking and accounting principles would require that ordinary expenses incurred by a regulated public utility must be recovered, if at all, through annual revenues.¹⁵

The PUCO has established clear criteria that must be met before permitting a utility to defer expenses for future collection:

We believe that to approve such a measure *requires* that we find there to be *both exigent circumstances and good reason* demonstrated before such amounts should be treated differently from ordinary utility expenses.¹⁶

These requirements have been recognized and confirmed by the Ohio Supreme Court.¹⁷ Thus, utilities requesting deferral authority – like Duke – must demonstrate that both exigent circumstances and good cause or reason exist why the expenses should be treated differently from ordinary utility expenses.¹⁸ Furthermore, the costs in question must be subject to review before they are incorporated into rates, ensuring that the costs

¹⁵ *Id.*

¹⁶ *Id.* at 8-9 (emphasis added).

¹⁷ *Elyria Foundry Co. v. Pub. Util. Comm. of Ohio* (2007), 114 Ohio St.3d at 310-312, 2007-Ohio-4164.

¹⁸ While the Supreme Court of Ohio recognized that FirstEnergy had not demonstrated exigent circumstances for approval of deferral, it found that current rates are not affected by the accounting deferrals and other parties could challenge the recovery of deferred distribution expenses in FirstEnergy's next distribution rate cases. The Supreme Court emphasized that "[t]he commission made it clear that 'deferred amounts will be reviewed before they are incorporated into future rates' and thus the 'commission's accounting order was not conclusive for ratemaking purposes.'" *Id.*, citing *Cincinnati v. Pub. Util. Comm.*, 63 Ohio St.3d 366, 588 N.E.2d 775 (1992) (no prejudice resulting from an accounting order having a ratemaking effect where rate proceeding was still pending and appellant had a right of appeal). The Court also emphasized that the commission provided "a process to ensure that the deferred expenses for improvements to and maintenance of its infrastructure are in fact necessary costs related to improving the reliability of its distribution system." The Court stated that the "commission will scrutinize these deferred expenses to determine whether the 'costs to be deferred are reasonable, appropriately incurred, clearly and directly related to specifically necessary infrastructure improvements and reliability needs of [FirstEnergy], and in excess of expense amounts already included in the rate structures of each of the [FirstEnergy] Companies.'" Among other things, the Court noted that the commission required FirstEnergy to establish separate accounts for each project for which they proposed to defer expenses and that commission staff would then review the reasonableness and necessity of the deferred expenses in those accounts annually.

are reasonable, appropriately incurred, and clearly and directly related to the exigent circumstances for which they were authorized.¹⁹

In addition to these two requirements, the PUCO also noted that the deferral must apply only to expenses that exceed amounts already included in the utility's base rates and that the expenses are necessary to maintain the utility's financial or service reliability integrity:

We are mindful that such deferrals must be scrutinized to assure that the costs to be deferred are reasonable, appropriately incurred, clearly and directly related to specific and necessary infrastructure improvements and reliability needs of the Companies, *and in excess of expense amounts already included in the rate structure of each of the Companies.*²⁰

The PUCO must review Duke's application with these standards in mind. Duke fails to show that its request to defer the "avoided cost" meets the standards discussed. The PUCO should reject Duke's request.

D. The PUCO should not authorize Duke to create a regulatory asset that may be charged to consumers.

It seems that Duke was not required by the City to contribute to the cost of building the retaining wall. In its application, Duke stated: "Because the Company and its natural gas customers benefitted from the construction of the retaining wall, it is reasonable and prudent to contribute to its cost."²¹

¹⁹ FirstEnergy Deferral Order at 8-9.

²⁰ *Id.* at 9 (emphasis added).

²¹ Application at 3.

Apparently, the offer to contribute to the cost of the wall came solely from Duke, without the City requiring Duke to do so. If there was no obligation for Duke to pay for the wall, then it should not be considered a cost of providing service to Duke's customers.²²

Duke's customers should not be charged for any wall-related costs that the City did not require Duke to pay for. If Duke's intent in agreeing to contribute \$3 million towards building the retaining wall is to promote corporate good will, any contribution should be made by the utility's shareholders, not its customers. This would be akin to public relations or image advertising spending that the PUCO has not required jurisdictional customer to pay.²³

III. CONCLUSION

Duke's application does not show that the \$3 million costs related to the retaining wall are ordinary and necessary to serve Duke's customers. In addition, Duke's application inappropriately bases a charge to customers on avoided costs. Additionally, the application does not meet the PUCO's standards for deferrals. The PUCO should deny the application.

²² *East Ohio Gas Co.*, Case No. 80-769-GA-AIR, Opinion and Order (August 12, 1981) at 17-18 (holding that East Ohio had no obligation to pay the assessment on the intrastate volumes and that East Ohio would not pay the assessment on the intrastate volumes if the Commission did not allow it to do so).

²³ *See, e.g., Application of Ohio Bell Telephone Co.*, Case No. 83-300-TP-AIR, et al., Opinion and Order (January 31, 1984), 1984 Ohio PUC Lexis 61 [*135]; *Application of Cleveland Electric Illuminating Co.*, Case No. 85-675-EL-AIR, Opinion and Order (June 24, 1986), 1986 PUC Lexis 53 [*128]; *Application of Cleveland Electric Illuminating Co.*, Case No. 86-2025-EL-AIR, Opinion and Order (December 16, 1987), 1987 PUC Lexis 28 [*186].

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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing Comments was served on the persons stated below via electronic transmission this 21st day of November 2017.

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