

**BEFORE  
THE PUBLIC UTILITIES COMMISSION OF OHIO**

In the Matter of the Review of Duke                     )  
Energy Ohio, Inc.'s Distribution                     ) Case No. 19-1287-EL-RDR  
Capital Investment Rider.                     )

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**COMMENTS  
BY  
THE OFFICE OF THE OHIO CONSUMERS' COUNSEL**

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The distribution capital investment rider (“Rider DCI” or “Rider”) enables Duke Energy Ohio, Inc. (“Duke”) to charge customers for a return on and of its distribution infrastructure investments.<sup>1</sup> This Rider also allows Duke to charge customers sooner than under traditional ratemaking and without the benefit of a full regulatory review of all revenues and expenses under a traditional rate proceeding.<sup>2</sup> The Public Utilities Commission of Ohio (“PUCO”) has required that Duke’s Rider be audited annually for accounting accuracy, prudence, and compliance with PUCO orders. This audit involves a review of capital spending during the period July 1, 2018 through June 30, 2019 (“review period”).

Rehmann Consulting (“Rehmann” or “Auditor”) performed the audit and detailed the findings in an audit report filed with the PUCO.<sup>3</sup> The Auditor identified many issues concerning the unreasonable amount of Rider DCI charges collected from customers

<sup>2</sup> R.C. 4909.18.

<sup>3</sup> See Case No. 19-1287-EL-RDR, Compliance Audit of the July 1, 2018 to June 30, 2019 Distribution Capital Investment Rider (“Rider DCI”) Duke Energy Ohio at 2 (December 13, 2019) (The review included November 1, 2018 quarterly filings up to and including the August 1, 2019 filing) (“Audit Report”).

during the audit period and a significant number of “defects” in Duke’s process, procedure, and policies that should be corrected. Some of these defects have also been identified in prior audit reports and yet Duke has made little progress in resolving the defect. The Auditor also made several recommendations that will reduce the costs that were inaccurately recorded under Rider DCI by \$13,611,269 and lower the ongoing Rider DCI revenue requirement paid by customers by \$880,052 during the audit period, accordingly.<sup>4</sup>

The purpose of these comments filed by the Office of the Ohio Consumers’ Counsel (“OCC”) is to recommend that the PUCO adopt all of the Auditor’s recommendations, along with some additional recommendations by OCC to further protect consumers from being overcharged through the Rider.

## II. COMMENTS

### A. **The PUCO should adopt recommendations made by the Auditor to remove improperly included transmission plant, operations and maintenance expenses, and incentive pay expenses from the distribution Rider so that customers are not overcharged.**

The purpose of Rider DCI as approved by the PUCO is to allow Duke to proactively modernize its distribution infrastructure in order to improve reliability for customers.<sup>5</sup> The PUCO ordered that only distribution plant could be included in the distribution improvement rider. The PUCO did not approve the collection of

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<sup>4</sup> See *Id.* at 38, Report Table 11.

<sup>5</sup> See *In re 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., Finding and Order at 71-72 (April 2, 2015).

transmission plant under Rider DCI.<sup>6</sup> Nor did the PUCO authorize tree trimming expenses or incentive compensation expenses , which are not distribution plant, to be capitalized and collected through the distribution investment rider. Duke's inclusion of such costs for collection from customers results in those customers being overcharged. Improper Rider DCI charges from transmission plant, tree trimming, and incentive compensation should be disallowed as the Auditor recommended because they are not PUCO-approved charges.

The Auditor found that Duke incorrectly classified \$198,254 (as part of an invoice for \$1,494,878) in transmission plant as distribution plant subject to collection from customers under Rider DCI and recommended that the improper transmission plant costs be removed from Rider DCI.<sup>7</sup> The Auditor also recommended that the revenue requirement be reduced by \$67,787 for nine months.<sup>8</sup> OCC agrees with this recommendation because transmission plant is not permitted to be collected as part of the distribution rider

Similarly, the Auditor found that Duke incorrectly capitalized \$11,538 in vegetation management expenses for collection under Rider DCI, when they should have been treated as operations and maintenance ("O&M") expenses, and recommended their removal from the Rider.<sup>9</sup> The Auditor further recommended that the revenue requirement be reduced by \$2,692 for 12 months.<sup>10</sup> The Auditor's recommendation should be adopted

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<sup>6</sup> *Id.*

<sup>7</sup> *Id.*

<sup>8</sup> *Id.*

<sup>9</sup> *Id.* at 7.

<sup>10</sup> *Id.*

because vegetation management is an operations and maintenance expense, and is not related to distribution infrastructure investment. Therefore, it is not an appropriate cost that should be collected from customers under Rider DCI.

Finally, the Auditor recommended that capitalized incentive pay was improperly captured and offset in Rider DCI. Duke was required to capture capitalized incentive pay accrued since July 1, 2016 and offset the amount to Distribution Rate Base in future Rider DCI filings.<sup>11</sup> The total offset through the June 30, 2019 Rider DCI is \$1,090,193.<sup>12</sup> Rehmann reviewed a sample of 15 work orders that were field visited, to determine whether each was offset in the Rider DCI filings (with 30% earnings related incentives in 2018 and 35% earnings related incentives in 2019).<sup>13</sup> The Auditor found incentive pay included in Retirement Work in Progress since July 1, 2016 totaled \$212,475 and determined a 30% and 35% earnings component results in a net \$66,361 of additional incentive pay offset.<sup>14</sup> The Auditor recommended that the revenue requirement be reduced for the incentive pay offset overcharges by \$19,527 over a year.<sup>15</sup> Additionally, the Auditor recommended that the Rider filing for September 30, 2019 be amended to reflect an adjustment to the incentive pay calculation by adding \$66,361 to the cumulative total of gross plant incentives and \$69,240 to the incentive pay offset total adjustment.<sup>16</sup> The PUCO should adopt the Auditor's recommendations to remove incentive payments from Rider DCI, and to reduce the applicable revenue requirement,

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<sup>11</sup> *Id.* at 13.

<sup>12</sup> *Id.*

<sup>13</sup> *Id.*

<sup>14</sup> *Id.*

<sup>15</sup> *Id.*

<sup>16</sup> *Id.*

because these payments are not appropriate costs to collect from customers under Rider DCI.

**B. The PUCO should adopt recommendations made by the Auditor to remove Contributions in Aid of Construction from the Rider to protect customers from paying for a return on non-investor supplied capital.**

Contributions in Aid of Construction (“CIAC”) is properly treated as an offset to plant in service because the CIAC is not investor supplied capital. Moreover, it is established regulatory precedent that utilities, such as Duke, should not earn a return on plant that its investors did not fund. For this reason, it is important to properly account for and segregate CIAC charges so that customers do not pay a return on non-investor supplied capital. To do otherwise is contrary to long-standing case precedent.<sup>17</sup>

Unfortunately for Duke’s customers, Duke did not properly bill and collect CIAC from customers during this audit period.<sup>18</sup>

The Auditor recommended a reduction to the revenue requirement of \$562,933 for the missing or untimely CIAC entries for four quarters (the length of time the overcharge went undetected).<sup>19</sup> The Auditor further recommended that \$296,024 be

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<sup>17</sup> See *In re the Matter of the Application and Complaint and Appeal of Columbus and Southern Ohio Electric Company for Authority to Amend and Increase Certain of its Rates and Charges for Electric Service*, Case No. 77-545-EL-AIR, Opinion and Order at 54 (March 31, 1978)) (“the Commission is of the opinion that a rate base deduction to reflect customer advances for construction is proper and that the staff recommendation should be adopted. Section 4909.05(I) Revised Code provides that the rate base should be reduced by any amounts a utility has received as total or partial defrayal of the cost of its property. Customers advances clearly fall within this category.”); See *In re the Matter of the Application and Complaint and Appeal of Columbus and Southern Ohio Electric Company for Authority to Amend and Increase Certain of its Rates and Charges for Electric Service*, Case No. 78-1438-EL-AIR, Opinion and Order at 14 (December 17, 1975) (“As we pointed out in our decision in Case No. 77-545-EL-AIR, customer advances clearly fall within amounts received as total or partial defrayal of the cost of the company’s property, which must be deducted from the rate base...”).

<sup>18</sup> Audit Report at 12.

<sup>19</sup> *Id.*

removed from Rider DCI for CIAC overcharges.<sup>20</sup> And to prevent this issue from recurring, the Auditor recommended a separate detailed audit for any CIAC postings unrecorded in work orders and Rider DCI from July 1, 2018 to June 30, 2019, and that any unrecorded CIAC should be quantified in a report for the revenue requirement impact and applied to the December 31, 2019 Rider DCI filing.<sup>21</sup>

Notably, it is not the first time that Duke's lax accounting of CIAC has created overcharges to customers. This same issue was raised in the previous audit of the DCI rider. In fact, to resolve that audit, Duke agreed, as part of a settlement, to implement enhanced controls to ensure that CIAC is billed on a timely, complete, and accurate basis by January 1, 2020. In its follow-up here, the Auditor found that out of 25 work orders it sampled, more than half of them (13) were improperly charged to customers or not recorded at all.<sup>22</sup> This indicates that there continues to be a serious problem with Duke's accounting controls for the recording of CIAC.

In addition to correcting the revenue requirement impact of the CIAC, as recommended by the Auditor, the PUCO should also disallow in this audit, and any future audits, any CIAC that has not been properly recorded. This will ensure that the Rider DCI is not collecting costs from customers that result in a return on non-investor supplied capital. By not reflecting the proper CIAC amounts, the amount Duke charges its customers is overstated and customers are charged more than is just and reasonable.

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<sup>20</sup> *Id.*

<sup>21</sup> *Id.*

<sup>22</sup> *Id.*

**C. To protect consumers, the PUCO should adopt recommendations made by the Auditor to remove improper expenses such as depreciation expense lag from unposted retirements and ineffective cost controls for estimating projects resulting from Duke's inefficient accounting practices from the Distribution Improvement Rider.**

The Auditor discovered several issues with Duke's accounting practices such as inconsistencies in the accumulated depreciation balances between Duke's Federal Energy Regulatory Commission ("FERC") Forms and its Rider DCI filing,<sup>23</sup> ineffective budgeting planning and follow-up controls.<sup>24</sup>

The Auditor identified a \$311,135 revenue requirement reduction for the depreciation expense impact of the lag in unposted retirements and an increase of \$109,064 for the accumulated depreciation impact of the lag in on top entries<sup>25</sup> for a year.<sup>26</sup>

The Auditor also found that Duke has problematic procedures for estimating projects to ensure their accuracy.<sup>27</sup> Rehmann sampled 25 work orders and found that at least eight varied from estimates by -117% to 2,065%.<sup>28</sup> For a third year in a row, a PUCO appointed auditor was unable to determine the effectiveness of Duke's budgeting process and follow-up controls.<sup>29</sup> At Duke's request, the Auditor even re-estimated three of the 25 work orders that had significant overages from original estimated costs.<sup>30</sup>

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<sup>23</sup> *Id.* at 5.

<sup>24</sup> *Id.* at 8-9.

<sup>25</sup> Securities and Exchange Commission, Accounting and Enforcement Release, SEC Docket, Vol. 93, Part 1, page 69 (April 2008) ("On top" entries generally refer to the accounting practice of recording large, unsupported entries after the close of each quarter).

<sup>26</sup> Audit Report at 8-9.

<sup>27</sup> *Id.*

<sup>28</sup> *Id.*

<sup>29</sup> *Id.*

<sup>30</sup> *Id.* at 9.

The Auditor also recommended that an operational audit of contractor charges be completed to determine whether competitive bids are being obtained, contractors are complying with their bid specifications, contract terms are being adhered to, duplicate payments are not made, and contractor time sheets and equipment hours are being closely monitored by Duke.<sup>31</sup> Further, any detected overcharges and operational improvements should be quantified in a report for the revenue requirement impact and the impact applied to the March 31, 2020 Rider DCI filing.<sup>32</sup> Finally, the Auditor recommended that when a contractor's estimated hours needed to complete the work exceeds the estimated hours, then Duke should evaluate whether or not to approve a contract change order for the overage.<sup>33</sup>

But Duke has shown that it cannot be relied on to do this. Therefore, OCC recommends that the *Auditor* for the next DCI Rider audit review disallow for the overrun portion of any sampled work orders any final costs that exceed the original budget by more than 25% if Duke fails to verify the reasonableness of the cost overruns. The Auditor should also increase the sample size of the work orders that are audited if more than 20% of the sampled work orders are over-budget by more than 25%. In selecting work orders that should be added to the original sample, the auditor should select a minimum of 25 additional work orders based on criteria including total work order costs.

The PUCO should implement the Auditor's recommendations, but it should also go further to protect consumers. The OCC previously filed comments filed in Cases 17-

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<sup>31</sup> *Id.*

<sup>32</sup> *Id.*

<sup>33</sup> *Id.*

1118-EL-RDR and 18-1036-EL-RDR, recommending that the continuing significant cost overruns show that Duke's implementation and management of Rider DCI are inadequate. Given that Duke has failed to implement sufficient management and accounting controls in the Rider DCI budget planning and implementation process for a third time, the PUCO must act now to protect consumers by imposing more stringent requirements before more DCI Rider costs are collected from customers. Requiring customers to pay charges in the DCI Rider for significant cost overruns that continue is not just and reasonable. The additional scrutiny OCC is requesting should (hopefully) incent Duke to adequately manage the programs and costs that it seeks to collect from consumers through Rider DCI.

**D. The PUCO should enforce its previous orders and adopt recommendations made by the Auditor so that Duke's Unitization and Retirement Work in Progress backlogs are eliminated, and consumers are protected from unreasonable charges.**

Timely unitization is important because it detects errors resulting from charging expenditures to distribution plant, charging incorrect work orders, or charging incorrect FERC accounts.<sup>34</sup> Duke previously agreed that the un-unitized plant backlog would be caught up within one year from October 23, 2019.<sup>35</sup> Accordingly, as part of this audit, Rehmann was directed to assess Duke's efforts to timely unitize plant including efforts to eliminate the Plan Unitization and Retirement Work in Progress backlogs.

The Auditor found that while Duke has made progress on its backlog of un-unitized work orders from in-service year 2017 and older, there are still significant un-

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<sup>34</sup> Case No. 18-1036-EL-RDR, Compliance Audit at 10 (December 7, 2018).

<sup>35</sup> *Id.*, Stipulation and Recommendation at 6 (June 10, 2019).

unitized work orders that are over one year old from in service date.<sup>36</sup> The Auditor also discovered an increase in Retirement Work in Progress from \$53,465,525 to \$77,939,478.<sup>37</sup> Rehmann also noted that an accumulating balance delays the unitization of cost of removal and salvage to FERC Plant Accounts 360-374, which are critical components of establishing depreciation rates at individual FERC Plant Accounts 360-374.<sup>38</sup> Rehmann also explained that while Rider DCI has authorized depreciation rates, it would be difficult to establish new authorized rates, which are representative of current depreciation expense, without the \$77,939,478 unitized.<sup>39</sup>

These overcharges should be eliminated. but Duke has not complied with its previous commitment to get caught up on this work order backlog. There should be enforcement consequences for Duke's repeated failure to get caught up on the backlog of unitization.<sup>40</sup> It is wrong for Duke's customers to pay unjust and unreasonable Rider DCI charges caused by Duke's failure to timely and properly unitize or error-check its accounting. The PUCO should enforce its previous orders. At a bare minimum, the PUCO should (again) adopt the Auditor's recommendations to require Duke to catch up this backlog within one year of the PUCO's Order adopting the settlement in Case No. 18-1036-EL-RDR (October 23, 2019).

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<sup>36</sup> Audit Report at 9.

<sup>37</sup> *Id.*

<sup>38</sup> *Id.*

<sup>39</sup> *Id.*

<sup>40</sup> Case No. 18-1036-EL-RDR, Direct Testimony of James D. Williams at 12-13 (July 8, 2019).

### III. CONCLUSION

By law, consumers are entitled to be charged only what are just and reasonable rates for adequate and reliable utility service. Accordingly, the PUCO should adopt the auditor recommendations along with OCC's additional recommendations that are directed at removing improper costs from the distribution improvement rider so that the charges are just and reasonable.

Respectfully submitted,

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### **CERTIFICATE OF SERVICE**

I hereby certify that a copy of these Comments was served via electronic transmission upon the following parties of record this 28th day of February 2020.

/s/ Ambrosia E. Logsdon

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