BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Review of the Reconciliation Rider of Duke Energy Ohio, Inc.	))	Case No. 20-167-EL-RDR

INITIAL COMMENTS
BY
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I. INTRODUCTION

The PUCO ordered a prudence audit of the charges that 637,000 Duke Energy of Ohio ("Duke") consumers have paid to subsidize Duke's interest in two coal power plants (one located in Ohio and the other in Indiana. Duke's customers pay an amount based on Duke's ownership share of the plants. Because these dirty old plants are uneconomic, Duke's customers pay a subsidy to the extent the costs for the two coal plants exceed any revenues Duke derives from bidding the power produced by the plants into PJM markets. To minimize charges to consumers, therefore, it is essential that the two power plants be operated prudently and efficiently and that Duke act prudently and reasonably in bidding its energy and capacity into the competitive PJM markets.

In 2019, Duke's customers were forced to pay a subsidy of at least \$23.6 million. [1] Overall, OVEC's 2019 total revenues from selling energy and capacity were about \$300 million less than its cost to produce power from these plants. Through the so-called Price Stabilization Rider ("OVEC subsidy charge" or "PSR") (approved by the PUCO in Case Nos. 14-841-EL-SSO and 17-1263-EL-SSO), Duke charged its consumers this \$23.6 million above-market subsidy starting April 2019.[2]

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1 Audit Report at 26, Figure 8.

2 Audit Report at 7.

The PUCO engaged an outside auditor, London Economics International LLC, to audit the OVEC subsidy charge for calendar year 2019. As stated in the Audit Report, the purpose of the audit is to "establish the prudency of all the costs and sales flowing through the PSR, and to investigate whether DEO's[Duke's] actions were in the best interest of its retail ratepayers."[3] The Attorney Examiner allowed parties to provide comments on the Audit Report.

The Office of the Ohio Consumers' Counsel ("OCC") respectfully requests that the PUCO consider the following consumer-protection comments and recommendations regarding the findings of the Auditor and charges to consumers under the OVEC subsidy Rider.

II. BURDEN OF PROOF

When the PUCO approved the Settlement that established Duke's OVEC rider, it ordered that the rider would be subject to an annual prudency review.[4] This Settlement does not describe the prudency review process in detail. Instead, the Settlement notes that two other utilities have a similar OVEC rider and that the PUCO should approach the prudency determination for all three utilities in a similar manner. The Settlement states:

> The Stipulating Parties acknowledge that two other Ohio electric distribution utilities are Sponsoring Parties pursuant to the ICPA and, as such, the Signatory Parties recommend that the Commission approach the determination of prudently incurred costs and the reasonableness of the generation revenue for all three jurisdictional electric distribution utilities in a uniform manner, pursuant to controlling law, which affords parties of interest with due process.[5]

The first utility OVEC rider (also referred to as "Power Purchase Agreement Rider" or "PPA Rider") the PUCO approved was AEP's. The PUCO's order in AEP's ESP case ruled that

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[3] Audit Report at 7.

[4] *In re Duke ESP, Case* No. 17-1263-EL-SSO (Stipulation and Recommendation at 19) (Apr. 13, 2018).

[5] *Id.*

the utility has the burden of proof in the annual prudence reviews. The PUCO declared that : "AEP Ohio will bear the burden of proof in demonstrating the prudency of all costs and sales during the review, as well as that such actions were in the best interest of retail ratepayers."[6] Likewise, the PUCO ruled that "[r]etail cost recovery may be disallowed as a result of the annual prudency review if the output from the units was not bid in a manner that is consistent with participation in a broader competitive marketplace comprised of sellers attempting to maximize revenues."[7]

Accordingly, consistent with the PUCO ruling that the standards for the prudence review shall be the same for all three utilities, Duke has the burden of proof to show that all actions related to the OVEC plants were prudent and in consumers' best interests.

III. CONSUMER PROTECTION RECOMMENDATIONS

A. The PUCO should protect Duke's customers by disallowing the additional costs Duke incurred from its voluntary purchase of FirstEnergy's OVEC share (a purchase from FirstEnergy that AEP did not make), which was not in the best interests of customers.

Duke is already charging customers for its own share of the above market costs for the OVEC plants. That, in itself, is a travesty of justice that the PUCO and the Ohio Supreme Court has sanctioned. But to add insult to injury, Duke unilaterally chose, on behalf of its customers, to take on more of the OVEC liability when it voluntarily bought FirstEnergy's share of the OVEC output. As discussed below, AEP did not purchase an additional share from FirstEnergy and as we understand, it is not seeking to charge its customers for an additional share of OVEC.

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[6] *In re Ohio Power PPA Rider,* Case No. 14-1693-EL-RDR (Opinion & Order at 89) (Mar. 31, 2016) (the "OVEC Order") (also stating, "AEP Ohio will bear the burden of proof in demonstrating that bidding behavior is prudent and in the best interest of retail ratepayers."). This March 31, 2016 Order related to AEP's PPA Rider, which, at the time, included more than just OVEC. The rider was subsequently modified to be for OVEC only. *See* Case No. 14-1693-EL-RDR (Second Entry on Rehearing) (Nov. 3, 2016). This modification does not impact the burden of proof in this audit proceeding.

[7] *Id.*

Duke's charges for purchasing an additional share of OVEC is unreasonable and imprudent and not in the best interest of customers.

Duke co-owns OVEC with several other entities, including public utilities. One of the co-owners, FirstEnergy Solutions, filed for bankruptcy on March 31, 2018. After FirstEnergy Solutions filed for bankruptcy, it stopped buying its share (or "entitlement") of OVEC's electricity and capacity. As a result, each of the OVEC co-owners received the opportunity to buy part of FirstEnergy Solutions' entitlement to OVEC's output, in proportion to their own ownership share in OVEC.

Duke inexplicably decided to double down on the above-market cost of the OVEC generation and voluntarily buy its share of the FirstEnergy Solutions entitlement during 2019. Specifically, the Audit Report noted that "[i]n the meantime, however, as noted by OVEC '*Per the ICPA… OVEC made available to all other Sponsoring Companies FES's entitlement to available energy under the ICPA*.' DEO purchased a portion of FES's entitlement, as discussed in Section 4."[8]

There is no evidence that Duke is required to purchase this additional FirstEnergy Solutions entitlement or that such a purchase would benefit Duke's retail customers. To the contrary, this voluntary purchase by Duke has increased the 2019 OVEC costs (paid by Duke's customers) by $700,033.[9]

AEP had the same opportunity to purchase a share of the FirstEnergy Solutions OVEC entitlement, but apparently declined to do so. This is discussed at pages 16-17 of the Audit Report in the AEP OVEC Rider case.[10] AEP's apparent decision to decline this purchase

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8 Audit Report at 14.

9 Audit Report at 26, Figure 8, Column G.

10 *In Re Ohio Power Co. OVEC Rider*, Case No. 18-1759-EL-RDR (Audit Report) (September 17, 2020).

suggests that Duke could have done so too. The PUCO should protect consumers by denying Duke any collection of additional charges for the share of OVEC that Duke purchased from FirstEnergy.

The PUCO should stop Duke from charging an additional $700,033 in OVEC subsidies related to Duke's purchase of FirstEnergy Solutions' OVEC entitlement. Duke has not demonstrated that it needed to purchase this electricity and capacity or, more importantly, that it was prudent to do so. Duke's decision to buy the FirstEnergy entitlement was imprudent and the PUCO should disallow this item.

B. To protect consumers and consistent with the best interests of customers, the PUCO should disallow Duke's request to collect OVEC costs from customers because OVEC's commitment of the plants into PJM as must-run units was not prudent.

A prudent decision is defined as:

> One which reflects what a reasonable person would have done in light of conditions and circumstances which were known or reasonably should have been known at the time the decision was made. The standard contemplates a retrospective, factual inquiry, without the use of hindsight judgment, into the decisionmaking process of the utility's management.[11]

The PUCO adopted an even higher standard for the prudence review in the OVEC rider cases – the utility has the burden of proof to establish that the plants were operated "in the best interest of retail ratepayers."[12]

The Audit Report identified a problem – OVEC operates the plants (except one unit) as "must-run" units in the PJM energy markets[13] – meaning that the plants are designated to run at all times, except when shut down for scheduled maintenance or unexpected outages. But, during

[11] *Cincinnati v. Pub. Util. Comm.*, 67 Ohio St. 3d 523, 530, 620 N.E.2d 826, 830 (1993).

[12] *See* footnote 7, *supra.*

[13] Audit Report at 38.

2019, it made no economic sense to run the plants continuously because the plants lost money a great deal of the time. The plants operated at a loss much of the time because the variable operating costs often exceeded the market value of their capacity and energy. The auditor reported:

> Because the OVEC plants are offered into the PJM DA [Day Ahead] market as "must run," there were times during which the PJM DA prices did not cover the variable cost of running the plants. LEI [London International Economics, LLC] examined all twelve months in 2019; on a monthly average basis, PJM prices at the Duke Energy Ohio-Kentucky ("DEOK") hub were slightly lower than OVEC energy charges in April, May, June, August, and December.[14]

The auditor's statement that the PJM prices were only "slightly lower" than the OVEC prices during these five months provides no comfort because OVEC sold several million MWhs of electricity into the PJM market during these months. So even though OVEC's costs were only slightly higher than PJM's prices, this matters a great deal to consumers because every minute operated at a loss contributed in part to Duke's total $23.6 million subsidy charge to its customers from its OVEC entitlement during the audit period.

The prudent course of action is clear – if a plant is losing money so much of the time, don't run it when the plants' variable operating costs exceed the PJM market price. This is an obvious recommendation from industry experts who have reviewed the situation. For example, MISO operates a forward energy market similar to the PJM market used by the OVEC plants. The MISO Independent Market Monitor ("IMM") did a comprehensive review of coal plant

[14] Audit Report at 53 (Citations omitted).

dispatch patterns in a recent report.[15] The report covered all MISO coal plants during 2016-2019. The report noted that most utilities operate their plants in an economic manner.

The report concluded, however, that there were three utilities, like OVEC, with coal plants that had negative net operating revenues in 2019. The report concluded that the reason these three utilities lost money was likely due to dispatching their plants on a must-run basis rather than on an economic basis. The report states:

> The five least efficient owners of coal resources accounted for almost 80 percent of the inefficient losses incurred by coal resources among all integrated utilities. For these least efficient utilities, the inefficient losses were almost half of the total efficient net operating revenues they earned in 2019. Three of these five utilities actually incurred negative net operating revenues overall in 2019. In other words, the inefficient losses were larger than the aggregate efficient net operating revenues. *This generally indicates that there is substantial room for improvement for these companies in how they commit and dispatch their coal-fired resources.*[16]

The report also noted that merchant operators of coal plants routinely dispatched their plants on an economic basis and, as a result, their operations were much more profitable than the coal plants operated by vertically integrated utilities. The report explained that this resulted from the fact that merchant companies operate in a competitive market and are not guaranteed a return, unlike monopoly utilities. The report notes:

> Coal resources operated by merchant utilities differ from those operated by MISO's integrated utilities, *which underscores the fact that regulatory incentives can weaken the natural discipline of the competitive markets.*[17]

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15 Potomac Economic, *A Review of the Commitment and Dispatch of Coal Generators in MISO* (September 2020), available at: https://cdn.misoenergy.org/20201008%20MSC%20Item%2004%20IMM%20Coal%20Dispatch%20Study481336.pdf

16 *Id.* at 11 (Emphasis added).

17 *Id.* at 1 (Emphasis added).

The Southwest Power Pool ("SPP") also has a forward energy market similar to PJM's. The SPP IMM made a similar finding to the MISO report. The SPP wholesale market uses the term "self-commitment" to mean the same thing as "must-run" in PJM and MISO. The SPP report stated: "In order to improve price formation and market efficiency, we recommend SPP and stakeholders work to reduce the incidence of self-commitments."[18]

The U.S. Energy Information Administration studied this trend of uneconomic coal plants changing from "must-run" to economic dispatch, and reported the following:

> Seasonal differences in capacity factor have become more pronounced during the past two years, largely because coal has been displaced by cheaper generation from natural gas and renewable energy during the shoulder months. In April and May 2020, the coal fleet operated less than 30% of the time. As a result, coal plants sometimes assert that they are unable to operate for enough hours to produce enough annual revenue to cover costs.
>
> In an effort to improve the economics of coal plants, owners are evaluating plans to run plants on a seasonal basis, when electricity demand allows for steadier operation. Under these plans, coal plants would only operate during periods of higher electricity demand, from December to February (winter) and from June to August (summer). The expectation is that completely shutting down plants when electricity demand is low will limit financial losses.
>
> So far in 2020, four large coal-fired plants announced plans to operate on a seasonal basis. Two of the plants, totaling 1,193 megawatts (MW), are in Minnesota. The other two are a 793 MW plant in Arizona and a 645 MW plant in Louisiana. The two units in Minnesota will run during the summer and winter. The plants in Arizona and Louisiana will only operate during summer because they are located in warmer climes.

[18] Southwest Power Pool Market Monitoring Unit, *Self-Committing In SPP Markets: Overview, Impacts and Recommendations* at 2 (December 2019), available at: https://assets.documentcloud.org/documents/6573451/Spp-Mmu-Self-Commitment-Whitepaper.pdf

> Whether or not seasonal operation sufficiently improves the economics of coal plants remains to be seen. In 2018, owners of a plant in Wisconsin and a plant in Texas switched to seasonal operation. However, the practice lasted for less than a year because both facilities were completely shut down shortly thereafter.[19]

When consumers confronted Duke's Indiana utility about this issue, Duke agreed to stop operating its Indiana coal plants as must-run, and agreed to only dispatching them when it was economic to do so. The issue arose in a Fuel Adjustment Cause case for Duke Energy Indiana several years ago. In that case, customer groups opposed Duke Energy Indiana's practice of designating its coal plants as "must-run." As a result of opposition from customer groups, Duke voluntarily agreed that, going forward, it would only dispatch the plants into MISO when it would be economic to do so, as discussed below:

> **A. Assignment of Generation Resources Committed by the RAC [Reliability Assessment Commitment] Process.** The Industrials and OUCC [Indiana Office of Utility Consumer Counselor] took issue with the Company's practice of assigning generating units committed by the Midwest ISO as a part of its RAC process to native load by treating them as must-run units.
>
> In FAC66, the Company presented unopposed testimony related to this practice which the Commission approved therein. Company witness Ms. Pashos testified in her June 19, 2006, pre-filing in this proceeding that Duke Energy Indiana's thinking on this issue had evolved as it gained experience in the Midwest ISO Day 2 energy markets. She proposed on a going forward basis for Duke Energy Indiana to economically stack units assigned in the RAC process and for the Make Whole payments associated with the units to follow the allocation of the unit. Duke Energy Indiana implemented this proposal beginning in FAC70 filed with the Commission on October 30, 2006.[20]

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[19] EIA, *As U.S. Coal-fired Capacity and Utilization Decline, Operators Consider Seasonal Operation* (September 1, 2020), available at: https://www.eia.gov/todayinenergy/detail.php?id=44976

[20] *In re PSI Energy, Inc. Fuel Cost Adjustment Clause*, Cause No. 38707 FAC 67 51, 2007 Ind. PUC LEXIS 258 (2007) at 59-60 (citations omitted).

Duke Indiana apparently reverted back to designating its uneconomic coal plant as must-run units because the issue was litigated in a more recent Fuel Adjustment Clause case, which is awaiting a ruling from the Indiana Commission.[21] The Minnesota and Missouri Commissions also have open dockets where they are monitoring this issue.[22]

The auditor in this case concluded that Duke handled the issue of must-run commitments in a reasonable manner, but the Audit Report does not support this finding. The auditor described how Duke prepares a 21-day price forecast and shares this with the OVEC operations committee to decide whether the OVEC plants will be profitable during the next few weeks.[23] The auditor gave an example of how Duke showed that the plants would be unprofitable during a 21-day period in April 2020 because energy market prices were depressed due to the Covid-19 pandemic.[24] The auditor noted how this caused the OVEC operations committee to recommend a change to the OVEC operating committee.[25] The auditor does not describe what this new policy was, or how it might affect OVEC's practice of committing the plants as must-run. The other sections of the Audit Report addressed whether OVEC operated the plants prudently, in areas such as capital expenditures, maintenance practices and fuel purchases. This section of the Audit Report, however, only addressed whether Duke acted prudently by recommending that OVEC change its policy of designating the plants as "must-run." The Audit Report does not

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21 *In re Duke Energy Indiana, Inc. Fuel Adjustment Clause,* Cause No. 38707 FAC 124, 2020 Ind. PUC LEXIS 260 (June 29, 2020).

22 *In the Matter of the Review of the 2016-2017 Annual Automatic Adjustment Reports for all Electric Utilities*, Docket No. E-999/AA-17-492, 2019 Minn. PUC LEXIS 38 (February 7, 2019); Mo. Pub. Serv. Comm'n, *PSC Opens Electric Working Docket* (June 7, 2019), available at: https://psc.mo.gov/Electric/PSC_Opens_Electric_Working_Docket

23 Audit Report at 44.

24 *Id.*

25 *Id.*

address whether OVEC itself acted prudently by continuing this practice, despite Duke's recommendation to the OVEC operating committee to change the policy.

The importance of prudent plant operations cannot be understated especially when the utility has captive customers to absorb the operating losses (through above-market subsidy charges). A major point for the Ohio 1999 deregulation law was its shifting of the generation risk from consumers to the plant owners. But the subsidy culture at the PUCO continues to unjustifiably harm consumers by allowing utility risks to be shifted to consumers. The independent auditor should be making recommendations that call out imprudent utility decisions and actions. In turn, the PUCO should adopt measures (such as cost disallowances) to protect consumers from bearing the risk of Duke and OVEC acting imprudently.

As noted earlier, the PUCO placed the burden of proof on utilities to show that the OVEC costs are reasonable. The Ohio utilities, taken together, own a major share of OVEC. While the Audit Report notes that Duke raised the must-run issue at an operations committee meeting, the Ohio utilities should have collectively required the OVEC operating committee to change the practice of running the plants on a "must-run" basis. The Auditor's Report fails to show that committing the OVEC plants as must-run was prudent. The MISO and SPP studies show that plants that are uneconomic can reduce their losses by changing from must-run status to economic dispatch. Duke Energy Indiana agreed to change over to economic dispatch when consumers raised the issue there. Duke has failed to meet its burden of proving that it was reasonable to run the OVEC plants as must-run units; therefore, the PUCO should bar Duke from recovering OVEC costs.

C. The PUCO should require Duke to use more accurate billing data to prevent customer over-charges, consistent with the best interests of customers.

The Audit Report noted that Duke bills customers for OVEC charges based on the volume of annual customer sales dating from a 2017 rate case.[26] The actual sales in 2019 have been higher than the 2017 rate case sales and this means the 2019 OVEC subsidy rates were too high and collected too much from customers.[27] Even though the cumulative over/under collection balance may even out eventually over time, the auditor recommended that using more recent annual sales data for these billings would result in more accurate billing. This would benefit both Duke and its customers through fewer over-collections and under-collections that are now occurring by using inaccurate sales data for the billings.[28] OCC agrees with the auditor's recommendation and asks the PUCO to require the use of more recent annual sales data in establishing the OVEC charges to consumers.

D. To protect consumers, the PUCO should require Duke Energy, consistent with the best interests of customers, to provide a final report on whether the OVEC plants should participate in PJM's ancillary services markets to maximize revenues.

The Audit Report explains that OVEC is continuing to evaluate whether the plants should participate in PJM's ancillary services markets, particularly the market for regulating reserves.[29] The Audit Report notes that OVEC is preparing a study on this subject, and that the report will be completed by the end of 2020.[30] This topic has been debated in past OVEC proceedings, but no data has ever produced. It would be prudent for the OVEC owners to evaluate whether the

[26] Audit Report at 36.

[27] *Id*.

[28] Audit Report at 37.

[29] Audit Report at 52-54.

[30] Audit Report at 53.

OVEC plants should participate in these markets. OCC recommends that: (1) Duke file such a report in this docket by February 1, 2021; and (2) the OVEC plants should participate in the PJM ancillary services markets to maximize revenues, thus lowering the overall subsidy being charged to consumers.

E. To protect consumers, and consistent with the best interests of customers, the PUCO should direct Duke to improve OVEC's poor fuel management practices and disallow any additional fuel costs resulting from poor fuel management.

The Audit Report identified situations where OVEC maintained higher coal inventory levels than needed and also used a higher quality of coal (higher heat rate) than needed for the plants.[31] Both practices caused OVEC to incur unreasonably higher costs. The auditor recommended at page 76 that OVEC should improve its inventory management processes and examine the process it uses to create its coal burn outlook and its policy on taking deliveries of coal.[32] The auditor also recommended that OVEC should negotiate with coal suppliers to obtain future delivery of coal with acceptable quality at more competitive prices, and should also conduct an annual internal fuel procurement audit.[33]

These actions to reduce the cost of fuel would be expected of plants owners managing plants in the competitive market. But in this case, with consumers paying the utility for its losses, the plant owners have no skin in the game and thus no need to minimize costs.

OCC agrees with these auditor recommendations and requests that Duke and OVEC be required to implement these practices. OCC further recommends that the PUCO require the auditor to calculate the cost of this -- or any imprudent decision(s) like this one -- and

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[31] Audit Report at 55-76.

[32] Audit Report at 76.

[33] Audit Report at 71.

recommend a disallowance of at least three times the cost. Merely pointing out imprudent decision-making does not eradicate it unless the Duke is made to feel a consequence from its imprudent decisions.

IV. CONCLUSION

Given the lack of market discipline for these OVEC power plants whose losses are subsidized by Ohioans, the PUCO should closely scrutinize all subsidy charges to Ohio consumers for the plants. Duke had to prove in this case that the subsidy charges were prudent, that its actions were in the best interests of customers, and that all charges comply with the various limitations set forth in the PUCO Orders approving the OVEC Subsidy charge. As explained above, Duke did not meet its burden of proof in several respects. OCC respectfully requests that the PUCO disallow the collection of OVEC costs from Duke's consumers and implement the recommended practices as discussed in these comments.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that a copy of these Initial Comments were served on the persons stated below via electric transmission this 18th day of December 2020.

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The PUCO's e-filing system will electronically serve notice of the filing of this document on the following parties:

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