COMMONWEALTH OF KENTUCKY
BEFORE THE PUBLIC SERVICE COMMISSION

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In the Matter of:

Duke Energy Kentucky, Inc.'s Application for Approval to Transfer Functional Control of Certain Transmission Assets from the Midwest Independent Transmission System Operator to the PJM Interconnection Regional Transmission Organization and Request for Expedited Treatment	Case No. 2010-00203

Post-Hearing Brief of the Midwest ISO

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Midwest Independent Transmission System Operator, Inc. ("Midwest ISO"), an intervenor in this proceeding, hereby presents its post-hearing brief in opposition to the realignment with PJM Interconnection Regional Transmission Organization, L.L.C. ("PJM") as proposed by Duke Energy Kentucky, Inc. ("DEK"), a wholly-owned subsidiary corporation of Duke Energy Ohio, Inc. ("DEO"). This brief supports its points by citation to authorities and reference to the DEK Application initiating this proceeding ("Application"), prefiled testimony,[1] responses to data requests,[2] hearing testimony,[3] and other materials filed in this proceeding. By a separately-filed supplement to this brief, accompanied by a petition for confidential treatment, the Midwest ISO discusses information contained only in material subject to a Confidentiality Agreement between the parties and to which the Commission has granted confidential treatment.[4]

INTRODUCTION

In this proceeding, DEK requests the Commission to approve the transfer of control of certain of its transmission assets from the Midwest ISO Regional Transmission Operator ("RTO") to the PJM Interconnection, LLC ("PJM") RTO. These transmission assets consist of

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[1] Reference to prefiled testimony — all by witnesses on behalf of DEK and filed on July 6, 2010 — is to the witness's last name and page/line numbers, *e.g.*, SWEZ 5/18–6/2 or JENNINGS 6/2-5.

[2] Reference to a data request response is to the first or supplemental set, a short form for the requesting party, the number and, if relevant, subpart of the request, *e.g.* 1 PSC Staff 3. If there is a *confidential* version of a response as well as a *public* one, the distinction is italicized. Unless otherwise noted, the most recently-filed response — supplemental, clarifying, etc. — is the one referenced. Post-hearing data responses that DEK recently filed (mis-identified as responses to Midwest ISO hearing requests) are referenced as "PHDR #."

[3] Reference to hearing testimony is to the Video Transcript ("VT") of the 11/3/10 hearing, including the beginning time and the witness's last name, *e.g.*, 11/3/10 VT 16:53:54 (Swez)

[4] Some such information is provided in *confidential* text responding to data requests, for which there is also a redacted, *public* version. This category also includes the confidential portion of the 11/3/10 Video Transcript (17:43:35—18:23:55) and memos or spreadsheets attached as *confidential* data responses to 2 MISO 7(c) & 7(d), as supplemented and clarified. These attachments are referred to herein by descriptors available from the public record: DEK Analysis (the 2 MISO 7(c) printout and Excel file, provided as a supplement on 9/28/10 and 10/28/10, respectively); Swez Study (the 2 MISO 7(c) Sept. 2009 emails with printed out attachments); PJM Simulation (the 2 MISO 7(d) Attachment #1 spreadsheet); and, Corporate Memo (the 2 MISO 7(d) Attachment #2 document) The last three were provided as clarifying, supplemental responses on October 28, 2010.

eighteen 138 kV connections that connect DEK's distribution system to the transmission system of its parent, Duke Energy Ohio, Inc. ("DEO"). DEO's transmission system currently provides DEK's only direct interconnection with the Midwest ISO.

In support of its transfer-of-control application, DEK states that realignment of its transmission facilities to PJM is "appropriate" because DEO intends to realign from the Midwest ISO to PJM effective January 1, 2012, which would leave DEK without a direct interconnection with the Midwest ISO. (Application pp. 1, 3). DEK claims generally that the proposed realignment would "avoid potential inefficiencies, operational complexities and costs," (*Id.* p.4), and would enhance generation capacity revenue. (*Id.* pp. 9, 14). DEK, however, has failed to offer competent proof that realignment as proposed is other than for the pecuniary benefit of DEO, or that the proposed realignment would be in the public interest. Evidence produced at the hearing, in fact, demonstrates that DEK failed to research alternatives to the proposed realignment, or to adequately study the effects of the proposed realignment on DEK, its ratepayers, or the regional transmission grid. For this reason, and in light of the uncertainties inherent in realignment, the Midwest ISO opposes the transfer of control of DEK's eighteen 138 kV connections to PJM as proposed by DEK. The Midwest ISO also provides for the Commission's consideration possible alternatives to DEK's proposal that would assure that DEK and its corporate parent and sole shareholder, DEO — and not DEK's ratepayers, current members of the Midwest ISO, or other Kentucky utilities — bear the burdens and risks of any realignment.

ARGUMENT

DEK's proposed transfer of functional control of its transmission facilities — from the Midwest ISO to PJM — falls within the purview of KRS 278.218, by which Commission approval must be obtained prior to the transfer of control of a utility's assets with a value of

$1,000,000 or greater. The prerequisites for Commission approval are that the control change "is for a proper purpose and is consistent with the public interest."[5] The latter requirement has been interpreted as follows:[6]

> [A]ny party seeking approval of a transfer of control must show that the proposed transfer will not adversely affect the existing level of utility service or rates <u>or</u> that any potentially adverse effects can be avoided through the Commission's imposition of reasonable conditions on the acquiring party. The acquiring party should also demonstrate that the proposed transfer is likely to benefit the public through improved service quality, enhanced service reliability, the availability of additional services, lower rates or a reduction in utility expenses to provide present services. Such benefits, however, need not be immediate or readily quantifiable.

The same criteria apply in determining whether the transfer of functional control to an RTO satisfies the "public interest" standard, although the burden of persuasion remains with the utility (rather than the "acquiring" RTO).[7]

The Commission has detailed the public-interest analysis required by KRS 278.218 as follows: "This standard establishes a two-step process: first, there must be a showing of no adverse effect on service or rates; and, second, there must be a demonstration that there will be some benefits."[8] Significantly, the Commission in past RTO alignment cases has made clear that an applicant cannot satisfy the first step with vague and unsupported claims that a proposed transfer is not likely to have an adverse impact rates and services, but rather must produce utility-

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[5] KRS 278.218(2).

[6] 5/30/02 Order, at p.7, Case No. 2002-00018, Application for Approval of the Transfer of Control of Kentucky-American Water Company to RWE Aktiengesellschaft and Thames Water Aqua Holdings GmbH.

[7] *See, e.g.*, 11/1/10 Order, at pp. 4, 9-10, Case No. 2010-00043, Application of Big Rivers Electric Corporation for Approval to Transfer Functional Control of its Transmission System to Midwest Independent Transmission System Operator, Inc.

[8] 8/25/03 Order, at pp. 4-5, Case No. 2002-00475, Application of Kentucky Power d/b/a American Electric Power, for Approval, to the Extent Necessary, to Transfer Functional Control of Transmission Facilities Located in Kentucky to PJM.

specific cost/benefit analyses that compare the costs and benefits of the proposed course of action with those of the status quo and other viable alternatives.[9]

Because DEK has failed to establish in this proceeding that the proposed transfer of functional control satisfies either the "proper purpose" or "public interest" standard, the Commission should disapprove the transfer as proposed by DEK. The Midwest ISO respectfully suggests that there are reasonable alternatives to simply denying DEK's Application or postponing a decision thereon to provide DEK a further opportunity, subject to the necessary regulatory scrutiny and cross-examination/rebuttal, to make the required showing. The options include approving the exit from the Midwest ISO and entrance into PJM as of a date no earlier than January 1, 2014. Another option would be to approve realignment on the date proposed (1/1/2012), but explicitly condition approval on: (1) DEK's shareholder bearing the costs and risks of realignment; and (2) the ratepayers being secured an appropriate participation in the projected, possible benefits.

I. DEK has not provided evidence to show that there will not be adverse effects on service or rates or that there is any likely public benefit.

In its Application (at p.1), DEK refers to the transfer as "appropriate" because DEO (DEK's direct parent and shareholder)[10] is leaving the Midwest ISO and joining PJM, taking with it the transmission delivery system by which DEK is currently interconnected. The Midwest

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[9] *See* 7/17/03 Order, at pp. 14-17, Case No. 2002-00475, Application of Kentucky Power (finding "no merit" in applicant's assertion that cost/benefit analysis is required only where there are alternative courses of action to joining an RTO, and rejecting as insufficient a multi-state study). *See also* 11/1/10 Order, at p. 5, Case No 2010-00043, Application of Big Rivers (approving application of Big Rivers to transfer control of transmission system to MISO where Big Rivers conducted "extensive research of the potential options" and presented analysis that "compared the benefits and costs" of the options); and 5/31/06 Order, at p.10, Case No. 2003-00266, Investigation into the Membership of the Louisville Gas and Electric Company and Kentucky Utilities Company in the Midwest Independent Transmission Operator, Inc. (finding applicants' request to transfer control of transmission facilities from MISO was for proper purpose and in the public interest based on applicants' "economic analyses" comparing costs and benefits of various courses of action).

[10] Application pp. 2, 7 (¶4); 11/3/10 VT 10:56:58 (Wathen).

ISO recognizes the voluntary nature of RTO participation and fully supports its members' rights to exercise the right to pursue realignment. The contractual right to realign, however, is not the issue presented in this proceeding. Rather, DEK was required to demonstrate that the proposed transfer is in the public interest and will have no adverse effects relative to the *status quo* or possible alternatives. Because DEK clearly failed to establish that it fully considered alternatives, the transfer as proposed by DEK should be denied, conditioned, or delayed.

A. Ohio is the focus and intended beneficiary of realignment with PJM.

Ohio — referring both to the state and DEO — is the driver of the proposed transfer of functional control to PJM. Realignment of DEO is the sole, "but for" cause for proposing to move DEK from the Midwest ISO to PJM.[11] The "many benefits" claimed for DEO in realigning (Application p.8) are specifically described to include the strengthening of DEO's existing high degree of integration with current PJM members[12] and "improved efficiencies in Ohio's competitive retail and wholesale markets."[13] In addition, all of Ohio will then be in a single RTO (PJM) — a result purportedly sought by the Ohio PUC.[14]

The particular attraction appears to be the opportunity to offer generation into the capacity market conducted by PJM through RPM auctions.[15] A Midwest ISO estimate of the annual capacity payments that could be garnered under PJM's RPM auctions suggests that DEO could

[11] DEK's realignment "will come about because its parent, DEO has elected to leave the Midwest ISO and join PJM." Application p.2. For similar statements that the DEO decision is the effective cause for DEK's realignment, *see id.* pp. 8-9 (¶9); GAINER 14/14-17; WATHEN 12/3-5; 7/7-10; 2 MISO 7(b) *public*; 2 PSC 9(a).

[12] Application p.7 (¶8); GAINER 6/16-21; 1 PSC 2(a); Corporate Memo pp. 2-3.

[13] Application p.7 (¶8); GAINER 6/20-21; 1 PSC 2(a); Corporate Memo p. 2.

[14] Application p.7 (¶8); GAINER 6/7-14; 1 PSC 2(a); Corporate Memo pp. 3, 6.

[15] Application p. 4; SWEZ 6/15-18; WATHEN 11/18-20; GAINER 10/11-13; JENNINGS 3/7-12; Corporate Memo p. 3.

receive approximately $325 million per year.[16] DEK has criticized this estimate,[17] but not shown it to be invalid or substantially different from the Duke entities' own projection for DEO.[18] Whatever the precise amount of anticipated increased profits to DEO, from Duke corporate's perspective, they are sufficient to support a decision to move DEO from an RTO geared toward vertically-integrated utilities (the Midwest ISO) to one that better accommodates utilities operating in an environment of active wholesale and retail competition (PJM).[19] The decision to realign DEO was antecedent to consideration of DEK's realignment,[20] and in no way depends on whether DEK is also realigned.[21]

There was no independent decision about DEK. Two earlier decisions from higher up the corporate chain — DEO's realignment and DEK's transmission dependence — were taken as fixed, given situations.[22] Consideration of whether DEK should realign <u>began</u> with a

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[16] DEK estimates its pro rata share of realignment costs to be 15% of the total for it and DEO. Application p.12 (¶15); Corporate Memo p. 4; supplemental, clarifying 2 MISO 7(c) #2 *confidential*; PHDR 2 Attachment. The $325 million estimate for DEO is derived by applying 85% to the $353 million annual total referenced in the 2 PSC Staff 9 request.

[17] 2 PSC Staff 9(c) *public* (contending that DEK had "not be able to recreate the Midwest ISO's estimates").

[18] Projections/estimates for DEO are redacted from the version of the Corporate Memo produced in this case (*see id.* pp.1, 3-4). Although DEK protested that a combined analysis of DEK/DEO would be inappropriate, 2 PSC Staff 9, it appears that there is no barrier to a Duke person on the <u>regulated</u> assets side of things (where DEK is) to review or be privy to quantitative information about DEO. 11/2/10 VT 14:44:57 (Burner; testifying that he had reviewed a completely unredacted version of the Corporate Memo).

[19] Application p.8 (¶8); 6/25/10 letter filed in ER10-1562, p. 7; Corporate Memo pp. 2-3, 6.

[20] 2 PSC Staff 9(a) *public*; GAINER 14/16-17.

[21] 2 PSC Staff 9(a) *public*; GAINER 14/13-14.

[22] 2 MISO 7(b) *public*; 2 PSC 9(a) *public*; GAINER 21/19-21. DEK's transmission dependence is an artifact of decisions made by the corporate parent of ULH&P/DEK to transfer to it generation assets with highly-limited transmission facilities connecting DEK's load and generation <u>only</u> to CG&E/DEO. 12/5/03 Order, Appendix, Case No. 2003-00252, Application of The Union Light, Heat and Power Company for A Certificate of Public Convenience and Necessity to Acquire Certain Generation Resources and Related Property; For Approval of Certain Purchase Power Agreements; For Approval of Certain Accounting Treatment; and For Approval of Deviation From Requirements of KRS 278.2207 and 278.2213(6).

presumption that DEK should follow DEO wherever it went,[23] and the only evidence presented in this matter of any Kentucky-specific analysis consisted of conclusory and unspecific conjecture as "described in the direct testimony of John D. Swez, James B. Gainer, and William Don Wathen Jr."[24] When pressed at the hearing, Mr. Swez offered a non-technical, vague regurgitation of the unsupported assertion in DEK's Application[25] that it is complicated for DEK to remain in the Midwest ISO, as opposed to DEI, and that there *may* need to be additional metering installed.[26] The details and costs associated were never provided, nor examined.

Curiously, a contrary decision was reached to have Duke Energy Indiana, Inc. ("DEI"), remain in the Midwest ISO.[27] In describing the decision that DEI would remain in the Midwest ISO, DEO and DEI stated in their initial FERC RTO Realignment filing that: "The Midwest ISO is a robust, well-run RTO that is well suited to the needs of a vertically integrated utility, such as DEI."[28] DEK offers no explanation why similar reasoning would not apply if a truly independent decision were made for DEK.

There was also no independent decision by DEK. In response to 2 MISO 7(a) *public*, James B. Gainer claims that "DEK's decision to realign its RTO affiliation was based on the interests of DEK." However, it was not DEK's decision at all. Instead, as Mr. Gainer admitted at the hearing, an executive group at Duke Energy Business Systems ("DEBS") made the decision about DEK.[29] DEBS is not a direct or indirect corporate parent of DEK; it is an affiliate

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[23] 1 MISO 21; SWEZ 9/18-20; 2 MISO 7(b) *public*; GAINER 14/14-16.

[24] 2 MISO 7(b) *public*.

[25] DEK Application, p.15 (¶24).

[26] 11/3/10 VT 13:33:30 (Swez).

[27] GAINER 5/5-6; 2 MISO 10; 1 PSC 3; 6/25/10 ltr pp. 8-9.

[28] Initiating FERC RTO Realignment filing of DEO and DEK, by letter dated June 25, 2010, at p. 8.

[29] The DEBS executive group was comprised of Mark Manly, Lynn Good, Keith Trent, and Jim Turner. 11/3/10 VT 13:36:00 (Gainer).

corporation that provides various services to DEK and other utilities within the Duke corporate family.[30] None of the four individuals in that DEBS "executive management team" is an officer of DEK or DEO,[31] and none of them provided testimony in support of DEK's application or performed such "analysis" as is claimed to have been done about DEK. They may have seen the analysis described in 2 PSC 9(a) *public* or a summary thereof, but the only effects considered therein relate to forecasts of capacity sales and energy sales.[32] Nothing supports the claim that the decision was DEK's or that it was made based on only DEK's interests; as a matter of fact, the decision to realign DEK was made to serve Duke corporate interests as a whole.

B. Uncertainties overwhelm what little information has been given about alternatives to and effects of DEK's proposed realignment.

In its Application, DEK asserts that it considered alternatives to realignment (pp. 15-16 (¶24)) and that there are no adverse changes and some greater off-system sales expected from realignment (pp. 13-15). When asked for some quantification, projections, or other evidence of systematic study to support these assertions and its avowed expectations about the net effect of realignment, DEK repeatedly stated that it had not performed such analysis or had no estimates to give.[33] It is as though DEK did not want to look too closely at the risks and burdens created by DEO's realignment or the array of public interest effects due to DEK's shifting from the Midwest ISO to PJM.[34]

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[30] 11/3/10 VT 13:36:10 (Gainer); *see also* GAINER 1/5-6; JENNINGS 1/6-9.

[31] *Compare* list in fn. 29 *with* the most recent Annual Report available through the Kentucky Secretary of State's website, <www.sos.ky.gov>.

[32] 2 PSC Staff 9(a), (c) *public*; 11/3/10 VT 17:44:48 (Swez); Corporate Memo p.4; DEK Analysis p.1.

[33] *See, e.g.*, SWEZ 12/8-10; 1 MISO 13(b); 1 MISO 14; 1 MISO 15 (c); 1 MISO 16 (f)(iii); 1 MISO 17 (a); 11/3/10 VT 17:02:28 (Swez).

[34] What analysis that has surfaced, provided as *confidential* attachments to 2 MISO 7(c) and Attachment #1 to 2 MISO 7(d), is limited in scope and is outdated (having been prepared in September 2009 — January 2010 and not updated with more current information). *See* 2 PSC Staff 9(a), (c) *public*; 11/3/10 VT 16:56:25, 17:02:28 (Swez); *id.* 14:56:39 (Burner).

Such "analysis" that was performed turns out to consist of unstructured musings and qualitative descriptions of possible effects. For example, Mr. Swez states that the possibility of DEK's being its own balancing authority was considered but it "quickly became apparent that this alternative is unworkable;"[35] however, this "consideration" involved no discussion, study, or documented analysis, just "quite a lot" of thinking about it on his part.[36] Furthermore, there is a professed lack of expertise of those considering the effects and providing testimonial evidence about it in this proceeding.[37] For example,

- ratepayer effects are left to someone who considered the financial effects (on DEK) not rate effects (Wathen),[38]
- claimed complexities and problems of not following DEO's transmission assets into PJM end up with someone who by his own description is not an expert about transmission (Swez),[39] and
- how DEK might function within PJM is explained by someone who cannot be told specifics about DEK's operations and will not be the liaison for DEK within PJM (Jennings).[40]

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[35] SWEZ 12/16–13/3, echoing Application p.16 (¶26).

[36] 11/3/10 VT 16:44:04 (Swez) (only considered from the market perspective, not regarding reliability). Given that the consideration started "with the basic proposition that [DEK] is too small to operate on an economically efficient basis as its own balancing area authority," Application p.16 (¶25), it is hardly surprising that the conclusion was that "this alternative is unworkable."

[37] Apparently, PJM would perform studies for the Duke companies on request, as with the PJM Simulation. 11/3/10 VT 13:50:30 (Gainer). However, other than the PJM Simulation (the results of which were not considered particularly significant, *see* Corporate Memo p. 3), no such request appears to have been made. DEK even neglected to propound a data request to PJM to gather information about near-term RTEPP. *Compare with* 1 DEK 8-10 (data requests to the Midwest ISO about MTEP).

[38] *Compare* WATHEN 3/5 – 6/16, 9/21 – 11/20 *with* 11/3/10 VT 11:34:42 (Wathen).

[39] *Compare* SWEZ 10/4-12 and 1 MISO 17 (d), (g)(i) *with* 11/3/10 VT 16:53:54 & 17:23:32 (Swez).

[40] *Compare* JENNINGS 2/7-17 *with* 11/3/10 VT 15:42:18 (Jennings).

The cursory nature of such consideration, combined with inexpert opinion about purported effects, is not sufficient to establish that the transfer of functional control from the Midwest ISO to PJM is in the public interest.

The lack of supporting information, and resulting uncertainties, are particularly egregious as to the following three important issues:

1. Remaining in the Midwest ISO

DEK's avowed "plan and preference is to move to PJM with DEO,"[41] and so it has neither studied all the ways it might maintain the status quo by remaining in the Midwest ISO, nor assessed in an unbiased manner the relative benefits to Kentucky ratepayers of doing so. Instead, DEK's lack of independence has led it to treat <u>following DEO into PJM</u> (rather than the *status quo* of remaining in the Midwest ISO) as the baseline for the public interest inquiry. Thus, in DEK's distorted world-view:

> If Duke Energy Kentucky were to choose to remain integrated with the Midwest ISO after Duke Energy Ohio's transmission assets are transferred to PJM, any cost or risks incurred would be the result of <u>Duke Energy Kentucky's</u> business decision.

1 MISO 20 (emphasis added). Little wonder then, that the only arrangement for remaining in the Midwest ISO after DEO left to which DEK gave <u>any</u> consideration (pseudo-tying) is one in which such additional costs or risks incurred are easily allocable to DEK and its ratepayers.

a. pseudo-tying

In its Application (p.15 (¶24)), DEK contends, without support, that to "preserve, in virtual form, some mode of DEK participation in the Midwest ISO" would "translate into additional costs to customers" (*i.e.*, ratepayers). "Although it is technically possible to pseudo-

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[41] 1 MISO 16(f)(iii) (Swez; explaining why DEK had made no assessment of additional resources/costs it claimed were needed to operated under a pseudo-tying arrangement); 11/3/10 VT 14:31:19 (Burner).

tie [DEK's] load *through* PJM to the Midwest ISO, and to further pseudo-tie [DEK's] generation *from* PJM to the Midwest ISO, ... the pseudo-tie arrangements will add unnecessary complexity and costs" – allegedly requiring additional metering and other equipment and "personnel to complete additional scheduling functions."[42] These protestations of complexity and costs are not supported with facts or analysis, and are belied by existing arrangements that have worked for many years for DEO/DEK generation that has been physically located in PJM, as well as the decisions related to DEI to allow the Vermillion generation plant to continue to remain in the Midwest ISO. Furthermore, there appears to have been no consideration of the possible savings and benefits from DEK's staying in the Midwest ISO with its vertically-integrated regional affiliate, DEI, while its competitive retail markets focused parent (DEO) joins the similarly oriented PJM.

At the 11/3/10 hearing, DEK witnesses testified that pseudo-tying is too complex and risky and they did not know how well it would work.[43] This is simply not credible. The Duke corporate family plans to make use of such arrangement for DEI's Madison generating facility after DEO realigns.[44] Furthermore, as noted above, similar arrangements may need to be made after DEO's realignment for its Vermillion generating plant, which will remain part of the Midwest ISO even after the rest of DEO's assets and load shift to PJM.[45] In addition, pseudo-tying is used <u>today</u> to link DPL's ownership share of DEK's East Bend generating facility from the Midwest ISO to PJM.[46]

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[42] Application p.15 (¶24); *see also* SWEZ 11/6–12/13; 1 MISO 16 (a).

[43] 11/3/10 VT 16:46:08 (Swez); *see also* SWEZ 12/10-13.

[44] 2 MISO 11(a); 6/25/10 letter to FERC pp. 8-9.

[45] 2 MISO 10. The Vermillion plant is located in Indiana and is connected to the bulk transmission system via a circuit owned by DEI. *Id*; 1 MISO 16(c).

[46] Revised and clarifying supplemental 2 MISO 12(b)–(e). "This dual RTO situation has not caused any significant issues thus far...." SWEZ 9/15-16.

There is similarly nothing to support the claims of increased costs (let alone any basis for insisting that such costs caused by DEO's realignment with PJM be potentially borne by Kentucky ratepayers); DEK appears to think that it is sufficient to hypothesize that there could be such costs that could be "avoided if [DEK] realigns with PJM at the same time."[47] Repeated requests have yielded no detail, quantification, estimates, or analysis.[48] DEK could not identify any additional tasks or marginal costs beyond those needed for DEI that would arise from DEK's also remaining in the Midwest ISO, although it flatly denied that there were efficiencies of scale or scope in having personnel fulfill the relevant functions for DEK as well as DEI.[49] In fact, these are not functions performed by DEK, but by DEBS's Regulated Portfolio Optimization ("RPO") group on behalf of DEK, DEI, and other regulated generation-owning Duke utilities; the RPO group will continue to perform these functions for DEK regardless of whether DEK realigns.[50] A separate such DEBS group performs those functions for DEO and other unregulated generation-owning Duke utilities.[51] Separating the midwestern Duke utilities between the Midwest ISO (DEK and DEI) and PJM (DEO) will reinforce and sustain the required separation between personnel in the two groups.[52]

b. other options

The Midwest ISO, in membership discussions regarding EKPC, has previously identified options that would permit EKPC to join the Midwest ISO as a contiguous member system, even

[47] Application pp.15-16 (¶24). *See also* SWEZ 11/20-22 ("Depending upon the arrangement..., the Company may have to allocate additional labor resources...."), 12/1-2 (DEK "may need to install ... equipment"); 1 MISO 16 ("Additional undesirable coordination, scheduling and metering would be required to move DEK load and resources from PJM to MISO...."), 1 MISO 17 (a).

[48] 1 MISO 16; 2 MISO 11; 11/3/10 VT 16:47:10 (Swez).

[49] 1 MISO 16(f).

[50] 2 MISO 10; 2 MISO 11; 11/3/10 VT 14:32:18 (Burner).

[51] 2 MISO 11.

[52] 2 PSC 9(a); 11/3/10 VT 15:35:07 (Jennings).

after DEO realigns with PJM. DEO could provide (*e.g.*, by shifting capacity from one affiliate to another through a joint ownership arrangement between DEO and DEI) nominal transmission capacity from the Miami Fort substation to the DEO interconnection point at the Buffington substation. Alternatively, DEO could guarantee a contract path from DEI to EKPC without specifying the transmission path or the amount of capacity, effectively holding EKPC harmless as a result of the proposed realignment. Pursuant to Section 6.5 of the Joint Operating Agreement ("JOA") between Midwest ISO and PJM, these paths would permit PJM and Midwest ISO to share the transmission capacity between these two points, without the need to reserve additional capacity, or to pseudo-tie loads or generation into the Midwest ISO or out of PJM.

In the case of DEK, the path already exists in the form of DEO's transmission connections to DEI, and there is no need to transfer capacity between Duke affiliates. Under the JOA, once the path exists, sharing is an option even though one party "loses" its physical connection (in fact, one of the primary benefits of this provision is that service is uninterrupted during a line outage that causes one RTO to be separated from its load):[53]

> **6.5 Sharing Contract Path Capacity.** If the Parties have contract paths to the same entity, the combined contract path capacity will be made available for use by both Parties. This will not create new contract paths for either Party that did not previously exist. PJM will not be able to deal directly with companies with which it does not physically or contractually interconnect and the Midwest ISO will not be able to deal directly with companies with which it does not physically or contractually interconnect.

Joint Operating Agreement, Midwest ISO FERC Rate Schedule No. 5, PJM Rate Schedule No. 38, Section 6.5.

Thus, the Joint Operating Agreement provides much simpler alternatives to pseudo ties that will allow DEK to continue its membership in the Midwest ISO, with its affiliate, DEI.

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[53] *See Alliance Companies, et al.,* 100 FERC ¶ 61,137, at P 53. The same result would apply if EKPC were to join before DEO's departure. There would be no need to create additional paths if EKPC were to be physically connected as a member before DEO's realignment.

There will be no change in transmission service or energy market dispatch, no exit fees or overlapping transmission expansion obligations, and DEK will have the ability to offer surplus generation into the PJM capacity auction.[54]

2. FRR vs. non-FRR participation

The expectation of benefits to DEO and DEK in realigning with PJM relies heavily on the perceived opportunities presented by participation in the PJM capacity market, with its Reliability Pricing Model ("RPM") and Base Residual and Incremental Auctions.[55] There is, however, "an alternate way to participate in PJM's capacity construct which is essentially an opt-out provision called the Fixed Resource Requirement (FRR)."[56]

> The FRR alternative ... allows [a Load Serving Entity (LSE)] to match its reliability requirement to its own generation while still being permitted to sell some or all of its excess supply into RPM auctions up to the FRR Limit.

JENNINGS 4/18-23 (emphases added). The FRR option thus resembles the traditional model, in which a vertically-integrated utility self-supplies its own load and offers any excess capacity for sale to third parties.[57] In marked contrast, non-FRR LSEs "merely allow PJM to procure capacity on their behalf,"[58] and are obligated to offer their capacity into the RPM auctions — with the market-clearing price and accepted offers being determined by an administratively determined

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[54] Because membership does not affect deliverability, DEK generation that would be deliverable after DEO joins PJM, must be deliverable whether or not DEK also joins PJM. *See also* 2 MISO 9 (stating that generating resources internal to the PJM footprint are fully deliverable within PJM).

[55] In his prefiled testimony (3/3–4/15), Kenneth J. Jennings describes the PJM capacity market. The expected benefits from participation in the capacity market — particularly for DEO — are discussed or asserted throughout DEK's case. *See, e.g.*, Application pp. 7-8 (¶8); GAINER 9/21–10/1-13; JENNINGS 6/14-21; SWEZ 6/3-9; DEK Analysis p.1; Swez Study p.7; Corporate Memo pp. 3-4. In fact, the request for expedited treatment of DEK's Application is based on a stated desire to participate in the early 2011 Auctions relating to the 2014-15 delivery year. Application p.4.

[56] JENNINGS 4/16-18; *see also* 11/3/10 VT 14:33:50 (Burner).

[57] 2 PSC Staff 6; 11/3/10 VT 14:34:28 (Burner); JENNINGS 5/21-23 (describing risks avoided by electing the FRR option).

[58] JENNINGS 6/7-8.

demand curve.[59] Any offered capacity sold in the RPM auctions requires that the corresponding energy be offered into the PJM daily energy market.[60]

Despite the far-reaching and critical differences it would make, DEK has steadfastly refused to say whether it will elect to be FRR or non-FRR.[61] Nor does there appear to be any effort at systematic analysis projecting what might happen under the two options, even though the election must be made with PJM by the end of 2010.[62] This suggests the decision has already been made for DEK, and all available evidence points to an intent for DEK to be an FRR LSE only for a limited transitional period,[63] and then be a full-on, non-FRR, RPM participant.[64]

Such a shift to buying all needed capacity and selling all available capacity through the RPM auctions raises issues in addition to the fit between such a competitive-markets model with a traditionally-regulated utility enjoying an absolute monopoly within a defined territory. Because electing non-FRR status commits a utility to serve its load through capacity procured by PJM and to employ its generation capacity only through sales to a third parties (usually, PJM through accepted Auction offers), that election itself arguably constitutes a transfer of "ownership of or control, or the right to control" utility assets and a utility function that requires prior approval under KRS 278.020(5) and 278.218(1). Offers into the RPM Auctions are for one-year periods, and although an offer might not be accepted (and so no transfer effected), the utility cannot be sure of that when making the offer and so must have Commission approval already in

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[59] 2 PSC Staff 6; JENNINGS 4/9-15. Both PJM and suppliers can use the Incremental Auctions to balance their respective capacity positions.

[60] 2 PSC Staff 6. There is a similar obligation on FRR LSEs to offer energy. *Id.*

[61] 11/3/10 VT 14:36:10 (Burner); 1 MISO 5(a).

[62] 1 PSC Staff, 2 PSC Staff 6; 11/3/10 VT 14:36:24 (Burner).

[63] 6/25/10 FERC letter pp. 11, 21-22. The request to have FRR status for a period of approximately 2.5 years would be unnecessary if it were the Duke companies' intent to make the usual FRR commitment of 5 years.

[64] *See, e.g.*, Application p.4; 11/3/10 *confidential* VT 18:05:48 (Burner).

hand. DEK has not sought prior approval to be a non-FRR LSE, and cannot participate as one until it has that separate Commission approval.

3. MTEP/RTEPP overlap

A third important issue on which DEK has created uncertainty is with respect to the division between DEK's ratepayers and shareholder (*i.e.*, DEO) of costs allocated to DEK related to PJM's regional transmission expansion planning process (RTEPP) and the Midwest ISO's transmission expansion plan (MTEP). As explained by Mr. Wathen in his pre-filed testimony (8/6–9/20), at the time of realignment, DEK will be obligated for MTEP costs for projects approved before its exit from the Midwest ISO and will become obligated on a going-forward basis for an allocation of RTEPP costs (including previously approved projects) from the date of its entrance into PJM; thus, for a period after realignment, DEK will be subject to costs for both MTEP and RTEPP projects. In its Application (p.12 (¶15)), DEK commits that "in its next electric base rate case, [it] will not seek to recover from customers transmission costs for both RTEPP and MTEP assessments for the same time periods."[65] The meaning of "costs for both RTEPP and MTEP assessments for the same time periods" is a bit obscure[66]; however, DEK clarified at the evidentiary hearing that each month of a base rate case test year may include costs relating to RTEPP <u>or</u> MTEP (but not both).[67]

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[65] *See also* GAINER 11/21-22 – 12/1-4; WATHEN 9/16-18 (DEK "will not seek to double recover in its base rates both RTEPP and METP [sic] costs that may be assessed for overlapping time periods").

[66] The post-exit MTEP "assessment" is of a fixed sum negotiated between the Midwest ISO and the exiting member(s), the payment of which may be negotiated to occur over a period of time. *See* DEK 7; PHDR 3. Thus, the periods in which the respective plans' expansion project costs are incurred, the allocated costs are assessed, and payment is made may all be different.

[67] 11/3/10 VT 11:18:40 (Wathen); *see also* WATHEN 9/18-20, 10/13-22.

DEK has provided an estimate of what the at-exit MTEP assessment might be for it and DEO combined, and has revised that estimate (downward) to $36 million.[68] Although the division of the assessment between DEK and DEO is within the Duke companies' control, DEK has only estimated its share at 15% of the total "[b]ased upon initial discussions with Duke Energy Ohio."[69] Beyond that, DEK claims that it has no data and has not studied or analyzed what its RTEPP assessment might be at the time of entry into PJM, how long costs might be incurred for MTEP projects approved prior to its exit from the Midwest ISO, etc.[70] DEK has also steadfastly refused to provide any indication of how it might implement the "no overlap" commitment — not providing any formula, factors, or considerations it would employ,[71] creating additional uncertainty and further departing from the known status quo alternative. Once again, DEK is reserving for itself the maximum flexibility for cost recovery (or profit maximization) by leaving the Commission in the dark about the effects of the proposed transfer of control.

C. Burdens, risks, and costs are being shifted to third parties.

1. Ratepayers

DEK's "public interest" case for the proposed realignment has three main elements: (1) an assertion that nothing much will change when it follows DEO into PJM; (2) projection of additional net revenues from off-system sales of capacity and energy, to be *split* (for an indefinite period)[72] with ratepayers through the Rider PSM; and, (3) a partial commitment not to pass along to ratepayers most of the costs due to realignment *per se*. These elements, however, do not meet the basic standard of no adverse effect on the existing level of utility service or rates (or avoid-

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68 PHDR 3; *see also* 11/3/10 VT 11:17:29 (Wathen). The Midwest ISO provided data about MTEP projects approved or pending/targeted for approval, in response to 1 DEK 8-10.

69 Application p.12 (¶15); 11/13/10 VT 11/28/57 (Wathen).

70 Supplemental, clarifying 2 MISO 6(a); initial 2 MISO 6; 11/3/10 VT 11:28:57 (Wathen).

71 Application p.5.

72 11/3/10 VT 11:50:50 (Wathen); Application pp.12-13 (¶¶15-16); WATHEN 10/1–11/8; 1 PSC Staff 4.

ance of potentially adverse effects through reasonable conditions). This failure is traceable to DEK's studious avoidance of even contemplating any risks or possible costs associated with a switch to PJM.

a. "sharing" market-driven off-system results

DEK projects that the "profits" component of its Rider PSM is likely to be greater with membership in PJM vis-à-vis membership in the Midwest ISO and, if so, ratepayers may see a reduction in their overall electric bill.[73] A "public interest" focus on rates should be on <u>base</u> rates rather than on a highly variable temporary rider dependent on market-driven results for off-system transactions; properly construed, "utility service" does not include a forced "opportunity" to participate in off-system ventures, with "investment" returns credited on one's electric bill. Moreover, DEK has not shown that any increase in such profits is likely or sustainable or that realignment's effect will always be positive.

The only possible enhancement to DEK's ability to engage in off-system sales mentioned in the Application (p.14 (¶20)) is the prospect of selling capacity in the RPM Auctions. There was some — flawed — analysis undertaken to estimate increases to capacity sales revenues that might result from realignment,[74] but DEK disclaims <u>any</u> analysis of associated enhanced revenue streams or cost reductions associated with "more opportunities to sell energy in [the] PJM market."[75] The other "profit" component of Rider PSM — transactions in ancillary services — gets no analysis beyond a statement that DEK "participates in these ancillary service markets in the Midwest ISO and intends to do the same in the PJM ancillary service markets."[76]

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[73] Application p.14 (¶20).

[74] *See confidential* Supplement filed November 19, 2010, with a Petition for Confidential Treatment.

[75] 1 MISO 13. Mr. Swez apparently would not put the Swez Study in that category.

[76] SWEZ 7/8-10.

Furthermore, the limited analysis that was undertaken or relied upon in making the decision to realign DEK[77] depends upon projected averages in which DEK is a net seller in off-system capacity and energy transactions. An average, of course, conveys nothing about the variability (and consequent risk) associated with market-determined prices, or about the worst-case scenario when a decision made about a period three years into the future proves to be very wrong. DEK's reported experience under the Rider PSM shows that there are months[78] and quarters[79] in which these off-system transactions yielded negative profits. DEK has provided no evidence that any projected increase in profits related to off-system sales in one area will not be reduced or negated by negative results in another.

The possible adverse effects are not only that there could be negative profits for off-system transactions, but that the overall profits allocable to ratepayers through the Rider PSM will be <u>less</u> than those that would have been achieved within the Midwest ISO or even than <u>have</u> been achieved in the past.[80] For its projection that there will be increased revenues in PJM, DEK relies mostly on data indicating that capacity/energy prices in PJM are (on average) greater than comparable prices in the Midwest ISO.[81] This is obviously an advantage only to the seller (not a buyer), and DEK has been and will continue to be a net <u>buyer</u> of energy at times[82] and will be

[77] DEK Analysis; Swez Study; Corporate Memo.

[78] MISO Hearing Exhibit #1 schedule 2, lines 8 & 18. The Off-System Sales Margin (line 18) was negative for April–June and September–November 2009. The ASM component was negative for March and July–November 2009, due to DEK <u>purchases</u> in these months. *Id.* schedules 2, 5; 11/3/10 VT 10:44:07 (Wathen)

[79] 1 MISO 12(d) Attachment. ASM was negative for Q2 and Q3 2009; overall profits and energy sales profits were negative for Q2–Q4 2009.

[80] *See* MISO Hearing Exhibits #1 (schedule 2) and #2 (schedule 2). The $1 million threshold (for which 100% of the profits are allocated to ratepayers) has always been met and exceeded.

[81] Application pp.8-9 (¶9); SWEZ 6/4-9; 1 MISO 13(a); Swez Study pp. 2-8; DEK Analysis pp. 2-3; Corporate Memo p.4

[82] SWEZ 8/19-21.

obligated to be a purchaser (as well as a seller) as a non-FRR LSE in PJM.[83] Finally, the average price differences for energy sales in the Midwest ISO and PJM markets have narrowed over time,[84] as should occur in open, competitive markets. Absent artificial barriers, competitive forces also should both moderate the capacity prices presently observed in the RPM Auctions[85] and reduce or eliminate any difference between PJM and the Midwest ISO.[86] Any existing "premium" for PJM markets is not likely to provide a sustained increase to Rider PSM profits.

b. on-system risks and costs unexamined

Effects on base rates and risks to reliability and service are left unexamined by DEK. To the extent that the Application mentions them at all, it is only to assert that there will be no change after realignment[87] and that inquiry about rate effects should wait until it files its next electric rate case.[88] These are not matters on which DEK (or the Commission) may "wait and see." The "public interest" standard requires a showing that the proposed transfer <u>will not</u> adversely affect rates or that potential adverse effects can be avoided through imposition of reasonable conditions by the Commission in <u>this</u> case.[89] DEK has glossed over issues affecting reliability, *e.g.*, whether capacity procurement is to be turned over to PJM (see part I.B.2 above)[90]

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[83] *See* part I.B.2 above.

[84] *See, e.g.*, Swez Study pp. 2-6.

[85] For example, though inducing new construction and demand response, as described in Mr. Jennings prefiled testimony (3/7-15). *See also* DEK Analysis p.3.

[86] *See, e.g.*, DEK Analysis p.3.

[87] *E.g.*, Application pp. 13 (¶19), 14 (¶22); *see also* 1 PSC Staff 9.

[88] *E.g.*, Application pp. 5-6; *see also* supplemental, clarifying 2 MISO 6(a).

[89] *See* 5/30/02 Order, at p.7, Case No. 2002-00018 (KAWC transfer); 8/25/03 Order granting Rehearing, at pp. 4-5, Case No. 2002-00475, Application of Kentucky Power d/b/a American Electric Power, for Approval, to the Extent Necessary, to Transfer Functional Control of Transmission Facilities Located in Kentucky to PJM.

[90] In responding to a request about a PJM scarcity-pricing, DEK explicitly relied on <u>PJM's</u> maintenance of "sufficient energy and capacity resources for DEK customers." 2 PSC Staff 10.

or inconsistency between PJM and Commission-ordered reserve margin standards (*see* part I.C.2, below), thereby completely failing to establish that there will be no negative effects.

The only base rate cost elements expressly discussed by DEK are RTO administrative and membership fees and transmission expansion plan costs.[91] As with the RTEPP costs — which will be a continuing obligation after realignment[92] — DEK is relatively specific about the analogous Midwest ISO fee or cost, but provides no estimate, projection, or analysis for PJM.[93] Instead of a direct comparison between such Midwest ISO and PJM cost elements, DEK either asserts that the costs will be substantially equivalent[94] or suggests a calculation or metric that puts the PJM cost in a relatively favorable light.[95] Neither approach shows that there will not be an adverse effect on rates, as is required by Commission precedent to establish that the proposed transfer will be in the public interest.

In addition, supplying native load through the RPM capacity Auctions as a non-FRR LSE will present different costs and risks than those for self-supply from DEK-owned generation.[96] DEK has turned away every question about the risks and possible increase in costs to ratepayers with a statement that it is DEK's <u>intent</u> to have capacity charges fully offset by revenues received from the RPM Auctions.[97] DEK has not shown that such perfect hedging is possible (or likely), or otherwise that there will be no adverse effect on rates.

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[91] *See, e.g.*, Application p. 12(¶15); SWEZ 14/4-10.

[92] Initial 2 MISO 6(a).

[93] *Compare* WATHEN 3/11/15 1 MISO 15(a),(b); *with* 1 MISO 15(c); supplemental, clarifying 2 MISO 6(a).

[94] *See, e.g.*, Application pp. 8 (¶8), 15 (¶23); 1 MISO 15.

[95] *See, e.g.* 1 MISO 15(c).

[96] 1 MISO 7(a). There might be similar base-rate (or FAC) effects due to changes in energy sales/ purchases through PJM markets. *See* WATHEN 11/11-12; Swez Study p.7.

[97] 2 PSC 6; 1 MISO 7(b),(c); 1 MISO 11(b); 2 MISO 8.

c. ill-defined commitments

Non-recurring costs due to the realignment itself (exit from the Midwest ISO, entry into PJM) are generally dealt with by commitments not to seek to recover them in base rates.[98] There is, however, no comprehensive commitment to hold ratepayers harmless against adverse base rate (or FAC) effects from increases (or increased variability) in recurring costs. There is also no commitment that DEK and its shareholder, DEO, will not recover all those non-recurring re-alignment costs by delaying any rate case filing and thereby retaining cost savings or additional revenues that would otherwise reduce its revenue requirement. Finally, there is no commitment that net-negative months regarding off-system capacity or energy sales or other relatively unfavorable results in the PJM markets will not reduce the ratepayers' Rider PSM share below what it would have been in the Midwest ISO.

The stated commitment about the MTEP/RTEPP overlap is so imprecise as to provide no assurance that potentially adverse effects of the proposed transfer will not be borne by rate-payers. In contrast to the MTEP/RTEPP commitment here, DEK made a very <u>specific</u> commit-ment when it applied to amend Rider PSM to include ASM revenues:[99] that it would absorb the loss for any month in which total costs of purchasing ASM services for load exceeded any revenues from ASM sales and not flow this negative amount through the Rider PSM.[100] None-theless, negative amounts were flowed through the Rider PSM in March and July-November 2009, reducing the profits allocated to ratepayers.[101] DEK acknowledged and corrected this error

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[98] Application pp. 2, 5; 1 MISO 3(b); PHDR 8. The exception is the assessment to close out DEK's obligation for MTEP costs, which is covered by the more-partial commitment about MTEP-RTEPP overlap.

[99] The expansion of Rider PSM to include ASM revenues was approved in the final Order, dated 1/30/99, in Case No. 2008-00489. *See* clarifying, supplemental 2 MISO 2(b)(iii).

[100] Supplemental, clarifying 2 MISO 2(d)(i) (citing DEK's Case No. 2008-00489 Application).

[101] *Id.* & Attachment; MISO Hearing Exhibit #1.

only after the Midwest ISO insisted on supplementation and clarification of DEK's responses to its data requests on the matter.[102] Given that DEK failed to implement a straightforward commitment correctly and the error went unnoticed for over 18 months, the more-complicated pledges expressed by DEK in this case may be of little practical benefit to ratepayers.

DEK has not made the same "no negative months" commitment regarding capacity revenues as it made for ASM revenues. Contrary to its position that "expand[ing] Rider PSM <u>in any way</u> would require an application before the Commission" and that it "must seek Commission approval to ... include possible future market opportunities as they develop, even for existing facilities,"[103] DEK <u>unilaterally</u> incorporated capacity sales revenues into Rider PSM in mid-2009, after the Midwest ISO's implementation of monthly Voluntary Capacity Auctions.[104] Sharing half of these net revenues with the ratepayers may seem generous, but not by comparison to the ASM commitment or the Rider PSM provision for crediting ratepayers with 100% of the net margins on sales of emission allowances.[105] In avoiding Commission review, DEK forestalled any need to make a stronger commitment or to justify such a departure from typical ratemaking treatment (*i.e.*, requiring ratepayers to split off-system sales profits with shareholders).[106]

2. Externalities

DEK treats burdens, risks, and costs of realignment that do not fall directly on it as mere (negative) externalities and, as economic theory would predict, neither takes them into account nor accepts responsibility for them. Thus, DEK has not studied and presented no information

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[102] 11/3/10 VT 10:44:10 (Wathen).

[103] Clarifying, supplemental 2 MISO 2(b)(iii) (citing Case No. 2008-00489 to include ASM revenues as an example).

[104] 1 MISO 12(d) Attachment; MISO Hearing Exhibit #1 (schedule 2); 2 MISO 1(c)(i).

[105] 2 MISO 2g; 1 MISO 12(a) (Rider PSM Tariff (page 1/2)).

[106] 2 MISO 2c; *see* 12/5/03 Order, at p.19, Case No. 2003-00252.

about the effects of realignment on other Kentucky transmission owners.[107] Similarly, while acknowledging that realignment will cut the tie that East Kentucky Power Company (EKPC) now has to the Midwest ISO, DEK contends that it should not have to pay the costs of a transmission path to the Midwest ISO[108]; instead, any such increased costs resulting from the change in the status quo should be borne by someone else.

Negative externalities,[109] however, demonstrate that the proposed transfer of functional control is not consistent with the public interest and should not be approved as proposed. The EKPC issue is particularly instructive. EKPC is exploring the possibility of joining the Midwest ISO.[110] There presently are upgrades planned (or underway) for EKPC's interconnection with Duke company facilities that are part of MTEP, with the costs being borne by EKPC.[111] To maintain the status quo as part of the southeastern edge of the Midwest ISO despite DEO's exit, DEK could negotiate a transmission path through PJM to the Midwest ISO — aided by JOA §6.5 and the pre-existence of a physical link through its transmission-owning parent/shareholder, DEO.[112] Then, EKPC would still have the option of directly linking to DEK (and its transmission path) in order to be able to join the Midwest ISO, and could invoke JOA §6.5 to maintain a path even if DEK subsequently switched to PJM. DEK, however, has not fully explored its options for remaining in the Midwest ISO based on its own self-interest (considered

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[107] 1 PSC Staff 10.

[108] 2 PSC 5(a).

[109] The only positive externalities mentioned in the Application are alleged to flow from DEO's realignment and relate to all of Ohio belonging to one RTO. Application pp.7-8 (¶8); *see also* 1 PSC Staff 2(a); 2 PSC Staff 1; Corporate Memo p.2.

[110] 2 PSC Staff 5; 1 DEK 19; Midwest ISO's 7/26/10 comments, filed in FERC Docket ER-10-1562-000, p.34 (referenced in 2 PSC Staff 5).

[111] 2 MISO 5(b); *see also* Appendix A to the DEBS-EKPC Interconnection Agreement attached to 1 PSC Staff 6.

[112] *See* part I.B.1.b, above.

independently of benefits to DEO), let alone considered any positive externalities that would be lost by realigning alongside DEO.

The effects on EKPC are not the only burdens and risks imposed on neighboring transmission owners and other third parties by realignment. The boundary of the PJM footprint on the transmission grid is an artificial line,[113] given an inflated effect with respect to PJM's RPM capacity market. Although external generators may in theory participate, they must demonstrate firm deliverability in order to do so — and such deliverability is not available across the PJM boundary.[114] The Duke companies would erase their PJM deliverability problem by realigning to be within PJM.[115] However, in eliminating this artificial constraint on them and adding their generation and load to the pool to be served internally, they exacerbate the real deliverability constraints within PJM and delay the day when firm deliverability is a practical possibility for external generators.

Another negative externality is possible interference with Kentucky reliability planning, particularly if DEK elects to be a non-FRR (fully exposed RPM) LSE. The PJM planning reserve standard is different from the 15% used by DEK in its latest IRP.[116] None of the DEK witnesses at the 11/3/10 hearing appeared to know what the Kentucky standard was or take it

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[113] *See also* 1/4/06 Letter from PUCO (p.2), FERC Docket AD05-13-000, attached to 2 MISO 1 ("[T]he RTO choices made by Ohio utilities ... have resulted in a lack of geographic scope that produces artificial barriers to commerce with neighboring utilities, particularly if those neighbors are located in a different RTO.").

[114] 1 MISO 17(g)(i); 2 PSC Staff 7; 2 MISO 9; 11/3/10 VT 16:51:20 (Swez).

[115] 1 MISO 17(g)(i); 2 MISO 9: 11/3/10 VT 16:52:20 (Swez).

[116] The Commission Staff did not recommend any change in this margin. *See* 4/22/10 Staff Report, pp. 5 ("DEK believes that a reserve margin target of 15 percent should be maintained."), 22-23 (reliability criteria), Case No. 2008-00248, The 2008 Integrated Resource Plan of Duke Energy Kentucky, Inc. This Commission's 5/11/10 Order found that the 4/22/10 Staff Report represented final substantive action in the case.

into account.[117] Furthermore, there is no testimony or other evidence that PJM would allow DEK to substitute (*e.g.*, for planning or in procuring capacity and modeling demand) the reliability standard approved by this Commission for the PJM standard, which presently is the case under the Midwest ISO planning reserve construct. The consequence of conflicting standards is just one more problem that DEK leaves for someone else to bear.

II. The transfer should be denied as proposed.

Because DEK has failed to provide competent evidence that its proposed realignment from the Midwest ISO to PJM will not adversely affect the existing level of rates and services, it is appropriate for the Commission to simply deny DEK's Application.[118] While an outright denial is justified in this matter due to the lack of evidence and analysis, there are other procedural and substantive tools at the Commission's disposal, which the Midwest ISO submits may better serve all involved. One set involves postponement of the earliest date for DEK's realignment; another, the imposition of true hold-harmless conditions on DEK, so as to avoid adverse effects on Kentucky rates and services and improve the likelihood of public benefit from the transfer of functional control.

A. Postponement of approval or of the transfer date approved would reduce the uncertainties and risks related to DEK's realignment.

One option to outright denial would be to postpone the final decision to a later date, giving DEK the opportunity to conduct thorough, comprehensive cost-benefit analyses and otherwise address the KRS 278.218 public interest standard. Approval could still be requested for realignment as of January 1, 2012, and DEK could proceed with notifying the Midwest ISO of an intent to withdraw as of that date, to participate in the 2014-15 supply year RPM Auction,

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[117] *See, e.g.*, 11/3/10 VT 14:06:20 (Gainer), 15:15:15 (Jennings); 11/3/10 *confidential* VT 18:07:03 (Burner); DEK Analysis p.2.

[118] *See* 7/17/03 Order denying Approval, at pp.14-17, Case No. 2002-00475 (Kentucky Power).

and to otherwise ready itself for realignment as of 2012. DEK would do so, however, at its risk that if the transfer is not approved, expenditures for realignment might not be recoverable and it might also have incurred obligations or commitments that are difficult or costly to unwind.[119]

Approving a postponed effective date of realignment to no earlier than January 1, 2014, would offer several benefits while preserving the status quo and protecting Kentucky ratepayers. Specifically, delay would permit the necessary level of study by DEK and the Commission of the costs and benefits of the proposed realignment, including whether the move would degrade the service and cost benefits already shown to exist through Midwest ISO membership. Delaying the effective date of realignment also would allow the Commission to observe the actual consequences of DEO's move into PJM, and to fine-tune any conditions placed on approval of DEK's application based on this experience. And providing for a January 1, 2014 realignment would permit DEK to proceed with plans/expenditures necessary to achieve full integration in time for participation in the RPM Base Residual Auction for the 2014-15 supply year.[120] A delay in realignment also would provide EKPC two years in which it would have to take advantage of dual access to PJM and the Midwest ISO (*see* part I.C.2. above).

Another significant benefit of postponing DEK's realignment would be to improve DEK's independence from DEO. Separating DEK's move from that of its parent and sole shareholder, DEO, would require DEK's transfer of control to stand on its own merits. An exit by DEO in 2012, and then by DEK in 2014, would enable a more objective, arms-length determination of the respective MTEP charges and exit fees for the two Duke companies.[121]

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[119] *See* Application p.4; PHDR 5.

[120] Application p.4; *see also Confidential* Supplement point #1.

[121] *Compare with* Application p.12 (¶15) (allocation shares being set by internal discussions between DEK and DEO).

Furthermore, for the two years that they are in different RTOs, DEK will gain practical experience with the alternatives it has (*see* part I.B.1) to following DEO wherever it goes.

B. Reasonable conditions on the transfer would reduce the risk of adverse effects and make it more likely that there will be public benefit.

Risks and burdens created by realignment should be clearly placed on DEK (and its parent) so that the decision to go forward is made with due consideration of the risks. Other conditions could directly reduce uncertainty by limiting the range of outcomes or magnitude of potential adverse effects. The Midwest ISO suggests consideration of the following as reasonable conditions:

exit/entrance costs: Ratepayers should be held harmless from all nonrecurring costs due to realignment — including the closing out of DEK's MTEP obligation. This would eliminate the possibility of any "overlap" or "double recovery" of the ongoing RTEPP charges, and thus end any difficulties in enforcing DEK's proposed "no overlap" commitment.[122]

capacity markets participation: For its initial five years in PJM, DEK should be limited to participating as an FRR LSE. Self-supply for native load and stricter standards about what is "excess capacity" that can be offered into the RPM Auctions significantly reduce the risks to a vertically-integrated utility (and its ratepayers) of operating in market adapted to retail competition. It also avoids possible negative effects on rates and reliability, as well as the issues regarding prior approval for FRR election or must-offer participation in an RPM Auction.[123]

capacity revenues: All, not half, of excess capacity sales revenue should redound to the benefit of the ratepayers. DEK has admitted that it is not critical to the business decision to realign

[122] *See* parts I.B3 and I.C.1.c, above; *Confidential* Supplement point #3.

[123] *See* parts I.B.3, I.C.1.b, and I.C.2, above.

that such revenue be split with its shareholder.[124] At the least, the rule should be that negative capacity revenue months not be included in the Rider PSM calculation (as is now true for ASM transactions). Or perhaps, any participation in the PJM long-term capacity market should be conditioned on seeking separate Commission approval therefor — with consideration of whether there should be a reduction in the rate base or a flow-through of revenues to ratepayers.

externalities: EKPC may be a afforded a two-year period (through a postponement of DEK's realignment date, *see* part II.A, above) in which to make its decision about joining the Midwest ISO in a context approaching the status quo. If not, the Commission should consider ways in which this externality of the realignment decision may be mitigated for EKPC or internalized for the Duke entities.[125]

CONCLUSION

WHEREFORE, the Midwest ISO respectfully suggests that the Commission deny the transfer of functional control as proposed, and employ the procedural and substantive options available to it to secure a result consistent with the public interest.

Respectfully submitted,

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124 2 MISO 2f.

125 *See, e.g.*, parts I.B.1.b and I.C.2, above.

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CERTIFICATE of FILING and SERVICE

I hereby certify that on this the 19th day of November, 2010, the original and ten (10) copies of the foregoing were hand-delivered to the Commission for filing, and a copy was served, via U.S. Mail, first-class, postage prepaid, on each person at the address shown on the attached Service List.

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