**UNITED STATES OF AMERICA**
**BEFORE THE**
**SECURITIES AND EXCHANGE COMMISSION**

In the Matter of the Application of Cinergy Corp. ) File No. 070-10254

# REPLY BY THE OFFFICE OF THE OHIO CONSUMERS' COUNSEL TO RESPONSE OF CINERGY CORP. TO MOTION TO INTERVENE AND PROTEST, AND IN THE ALTERNATIVE, MOTION FOR HEARING OF THE OFFICE OF THE OHIO CONSUMERS' COUNSEL

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In the Matter of the Application of Cinergy Corp. ) File No. 070-10254

**REPLY BY**
**THE OFFFICE OF THE OHIO CONSUMERS' COUNSEL**
**TO**
**RESPONSE OF CINERGY CORP.**
**TO MOTION TO INTERVENE AND PROTEST,**
**AND IN THE ALTERNATIVE, MOTION FOR HEARING OF THE OFFICE OF THE OHIO CONSUMERS' COUNSEL**

## I. INTRODUCTION

### A. History of the Above-Captioned Case

On September 30, 2004, Cinergy Corp. ("Cinergy"), parent company to the Cincinnati Gas & Electric Company ("CG&E") and The Union Light, Heat & Power Company ("ULH&P;" collectively with CG&E and Cinergy Corp., the "Company" or "Applicant") filed a request ("Application") that was later supplemented on January 19, 2005 ("Supplement").[1] The Company requested that the Commission allow CG&E to sell, pursuant to Section 12(d) of PUHCA and Commission Rule 44, its ownership interests in three electric generating facilities to ULH&P at net book value.[2] The Company's Application and Supplement are only supported by statements regarding the effects of the transaction on Kentucky customers.

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[1] Form U-1 Declaration ("Application"); Form U-1/A ("Supplement").

[2] Application, Item 1.A. ("at net book value"); also Supplement, Item 1.C.

On February 14, 2005, the Office of the Ohio Consumers' Counsel ("OCC") moved to intervene in the above-captioned case ("Motion"). The Motion brought into focus the harm caused by the transaction to the approximately 600,000 residential customers served by CG&E in Ohio.

On March 4, 2005, the Company submitted its Response to OCC's Motion ("Response").[3] The Response mischaracterizes the OCC's Motion as an effort to "overturn or reconsider statutes enacted by the Ohio legislature and decisions by the Public Utilities of Ohio ('PUCO') on these very matters."[4] In this Reply, the OCC emphasizes the *actual* outcome of cases before the Public Utilities Commission ("PUCO" or the "Ohio Commission") and the PUCO's *actual* interpretations of Ohio statutes.

This Reply pierces the Company's misapplication of Ohio law, use of Company testimony as a substitute for legal authority (such as decisions by the Ohio Commission), and use of case law out of its proper order. Afforded with a more complete context of the PUCO's decisions, the Commission can better render a fair decision regarding the proper value for the proposed sale involving the Company's affiliates. The proposal should be denied as presently structured.

### B. History of Proceedings Before the Ohio Commission

The sequence of the PUCO's decisions and the words actually used by the PUCO should guide the Commission's actions in the above-captioned case. The OCC's attachments to its Motion include two important decisions that involve CG&E: an August

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[3] Form U-1, Amendment No. 2, Exhibit H ("Response").

[4] Motion at 2.

31, 2000 Order in the electric transition plan case ("ETP Case")[5] and a November 23, 2004 Entry on Rehearing in a post market development period case ("Post-MDP Case").[6] The ETP Case set rates and conditions for service, including CG&E's corporate separation requirements, for the MDP period that ended on December 31, 2004 for nonresidential customers and will end on December 31, 2005 for residential customers. The Post-MDP Case has not yet been fully litigated,[7] but the PUCO's latest word regarding rates and terms of service for the period ending December 31, 2008 is contained in the Entry on Rehearing issued in November 2004.[8] That Entry on Rehearing approved, in principal part, a post-order proposal by CG&E and supersedes the PUCO's original Order dated September 29, 2004.

In the ETP Case, the PUCO unbundled rates from those in effect for vertically integrated service and delayed CG&E's corporate separation requirements until the end of 2004. The PUCO's Order in the ETP Case states: "CG&E notes that its corporate separation financing plan provides for a program to complete the transfer of its generating assets to an EWG [exempt wholesale generator] by December 31, 2004 ..."

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[5] *In re CG&E Electric Transition Plan*, PUCO Case No. 99-1658-EL-ETP, *et al.*, Opinion and Order (August 31, 2000), attached to Motion as Attachment No. 4.

[6] *In re CG&E Post Market Development Period Service*, PUCO Case No. 03-93-EL-ATA, *et al.*, Entry on Rehearing (November 23, 2004); attached to Motion as Attachment No. 1.

[7] Although rates under the Post-MDP Case have gone into effect for non-residential customers, the Commission has yet to rule on a matter upon which it granted rehearing. *Post-MDP Case*, Case No. 03-93-EL-ATA *et al.*, Second Entry on Rehearing (January 19, 2005). Residential rates are scheduled to increase on January 1, 2006. The OCC submitted its Notice of Appeal on March 18, 2005.

[8] The Commission issued its Second Entry on Rehearing on January 19, 2005. However, the Second Entry on Rehearing did not make any substantive changes to the PUCO's November Entry on Rehearing.

and that the PUCO would conduct a "periodic Commission review of the interim separation plan ...."[9]

The Post-MDP Case set forth a system by which rates for CG&E's generation service would be determined through the end of 2008. The PUCO's September 2004 Order in the case modified the terms of a partial stipulation that CG&E filed in the case.[10] In response, CG&E proposed a new generation rate plan that adopted five previous PUCO directives and otherwise laid out new plan components. Those components included an infrastructure maintenance fund ("IMF") charge "to compensate CG&E for committing its generation capacity"; a system reliability tracker ("SRT") charge "to flow though those actual costs [from purchase power to cover peak and reserve capacity requirements] on a dollar-for-dollar basis"; a fuel and economy purchased power ("FPP") component to cover "fuel and economy purchased power [including recovery of emission allowances]"; and an annually adjusted component ("AAC") based on CG&E's tariffed generation charges ("little g").[11] The PUCO's November 2004 Entry on Rehearing approved CG&E's new generation rate plan without a hearing, clarifying that, "in its consideration of CG&E's expenditures in these categories, [the PUCO] will continue to consider the reasonableness of expenditures."[12]

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[9] *In re CG&E Electric Transition Plan*, PUCO Case No. 99-1658-EL-ETP, *et al.*, Opinion and Order at 46-47 (August 31, 2000); cited in Motion at 7.

[10] *In re CG&E Post Market Development Period Service*, PUCO Case No. 03-93-EL-ATA, *et al.*, Entry on Rehearing at 2, ¶(6) (November 23, 2004); attached to Motion as Attachment No. 1.

[11] *Id.* at 8-9.

[12] *Id.* at 10.

The November Entry on Rehearing in the Post-MDP Case also addressed CG&E's obligation regarding the disposition of its generating plants.

> The Commission's approval of CG&E's proposed *delay* in the implementation of its corporate separation remains conditional, being now conditioned on CG&E's acceptance of the Commission's modifications and clarifications set forth in this entry on rehearing.[13]

Therefore, the PUCO's last statement on the matter of CG&E's ownership of generating plants delayed CG&E's obligations, but did not change them in such a manner that the plants could be sold to a regulated affiliate such as UHL&P.

## II. ARGUMENT

### A. Ohio Retail Generation Rates Are Determined Based on the Cost of CG&E's Power Plants Under A CG&E Proposal that was Approved by the Ohio Commission[14]

#### 1. Ohio Law and The Results of Proceedings Before the Ohio Commission Regarding Corporate Separation Are Misrepresented in the Company's Response.

The OCC seeks to apply the results from cases before the Ohio Commission rather than "re-litigate issues of Ohio state law and regulation."[15] While asserting that the sale of plants to ULH&P was "specifically contemplated[d]" by previous PUCO

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[13] *In re CG&E Post Market Development Period Service*, PUCO Case No. 03-93-EL-ATA, *et al.*, Entry on Rehearing at 16 (November 23, 2004) (emphasis added); attached to Motion as Attachment No. 1.

[14] In the CG&E Post-MDP Case and elsewhere, the OCC has advocated for a result that would not permit generation prices in Ohio to be set based upon costs associated with CG&E's generation plants "because generation is a competitive service in Ohio." Response at 3, title to Section A. However, as shown in this Reply and documented in the attachments to the Motion, the Ohio Commission adopted a CG&E plan that bases generation prices on costs associated with CG&E's generation plants. CG&E should not benefit from legal arguments before the SEC that are contradicted by its proposals in Ohio and that are contradicted by the current state of administrative case law in Ohio.

[15] Response at 2.

decisions,[16] the Company also states that the "*argument between CG&E and the PUCO* [regarding corporate separation obligations] is not at issue in this proceeding."[17]

The first argument in the Response renews CG&E's previously failed argument before the PUCO that Ohio Rev. Code Ann. §4928.17(E) provides "Ohio utilities ... sole discretion and control over the retention or divestiture of their generation assets."[18] As stated in the Motion, the PUCO rejected that argument in the Entry on Rehearing:

> [CG&E] claims that Section 4928.17(E), Revised Code, permits CG&E to determine whether it will, or will not, divest its generation assets.
>
> * * *
>
> We find no merit to this assignment of error. Clearly the [Ohio] Commission has the statutory authority to require CG&E to implement a corporate separation plan.[19]

As stated previously, the PUCO has required the transfer of CG&E's generating assets to an exempt wholesale generator. This requirement is violated by the sale of generating plants to ULH&P.

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[16] Response at 4.

[17] *Id.* (emphasis added)

[18] Response at 3.

[19] *In re CG&E Post Market Development Period Service*, PUCO Case No. 03-93-EL-ATA, *et al.*, Entry on Rehearing at 15; attached to Motion as Attachment No. 1. This portion of the Entry on Rehearing was previously quoted at length. OCC Motion at 8. The PUCO has jurisdiction "to determine whether an electric utility has failed to implement ... a transition plan ...." Ohio Rev. Code Ann. §4928.36 (Anderson 2000). The PUCO also has jurisdiction "to determine whether an electric utility or its affiliate has violated any provision of section 4928.17 of the Revised Code...." Ohio Rev. Code Ann. §4928.18 (Anderson 2000). Both statutes provide remedies.

### 2. CG&E's Generation Costs Are Integral to Retail Rate Setting in Ohio Under A Plan Submitted by CG&E and Approved by the Ohio Commission.

The Company falsely asserts that Ohio customers will not be affected by the sale to ULH&P because of limited PUCO regulation of retail rates after "the Ohio legislature deregulated generation service...."[20] That assertion is contradicted by CG&E's applications to the Ohio Commission and the resulting decision in the Post-MDP Case. As set forth above, CG&E proposed a rate plan to the Ohio Commission regarding generation rate setting through 2008 based on previously tariffed generation rates ("little g") and IMF, SRT, FPP, and AAC charges that are all based on CG&E's generation costs or the cost of purchased power in the absence of sufficient CG&E generating capacity. The generation rate increases will be subject to PUCO review and approval.[21] Contrary to the Company's assertion in its Response, CG&E's cost of generation remains an integral part of rate setting for its Ohio customers.

To the extent that the Company has any complaint, it has its own proposal before the PUCO and the Ohio Commission's approval of that proposal to blame. The Company should not benefit before this Commission as the result of its misrepresentation of Ohio case law.

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[20] Response at 4.

[21] *In re CG&E Post Market Development Period Service*, PUCO Case No. 03-93-EL-ATA, *et al.*, Entry on Rehearing at 10; attached to Motion as Attachment No. 1.

### B. The PUCO Has Not Found That Ohio Consumers Are "Held Harmless" by the Proposed Sale of Generating Assets.

The last reference in the Response to Ohio consumers being "held harmless" is the title to its argument, Section B.[22] Thereafter, the Company relies upon CG&E's testimony[23] in the Post-MDP Case instead of legal authority regarding the effect of the sale of generating assets to ULH&P. The PUCO's last word in the Post-MDP Case in November 2004 -- including the first imposition of a "SRT" charge -- was decided without a hearing and not based on CG&E's testimony or that of any other party.

CG&E's more recent response to the OCC's discovery requests (in the docket before the Ohio Commission regarding CG&E's proposal to purchase or build additional generation capacity to serve Ohio) is informative on the issue of whether Ohio consumers are "held harmless." CG&E states that it "did not prepare any scenarios for its SRT [cost recovery] application which contemplated that it would retain the 1,077 MW for these plants beyond April 1, 2005."[24] Thus, any Company statement regarding the potential harm to Ohio consumers is entirely speculative. As a disputed fact, such matters should be the subject of a hearing as requested in the OCC's Motion.[25]

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[22] Response at 5.

[23] Response at 5 ("testimony of CG&E witness, Mr. Steffen"). The Company also asserts that Ohio consumers "may actually benefit," again citing only CG&E's testimony. Response at 7. The Company's discussion is limited to speculation concerning a single component of generation costs, environmental costs.

[24] *In re New CG&E Power Plant*, PUCO Case No. 04-1811-EL-AAM *et al.*, Response to Interrogatory No. 2 (attached).

[25] Motion at 10.

The Company never quotes a PUCO decision in which the Ohio Commission states that Ohio consumers are "held harmless," either as the result of CG&E's initial proposal to the PUCO or as that package was modified by the PUCO. The Company has not established that Ohio consumers will not be harmed by the proposed sale, either to the PUCO or to the Commission.

### C. A Sale at Net Book Value Is Not in the Public Interest

The Company's plans are anti-competitive and designed to shift costs between state jurisdictions. Instead of transferring plants to an EWG that could bid on the load in Ohio and Kentucky,[26] the Company plans to provide ULH&P with its first power plants to keep that load from being served by alternative suppliers.[27] The Company argues that "ULH&P customers have paid the contract rate approved by the FERC and the KPSC"[28] and notes that the FERC "has accepted for filing or cancellation certain agreements between CG&E and ULH&P relating to the Proposed Transfer."[29] The FERC reviewed the power sales agreements according to the requirement that transactions between

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[26] As stated in the OCC's Motion, the Kentucky Commission was deeply concerned about the less-than-arm's-length relationship between ULH&P and its affiliated wholesale supplier" and sought an alternative to the situation. Motion at 9, citing *In the Matter of the Application of the Union Light, Heat and Power Company for Certain Findings Under 15 U.S.C. §79Z*, KPSC Case No. 2001-058, Order at 13 (May 11, 2001) (attached to Motion as Attachment No. 5).

[27] The Company states: "The OCC alleges that Ohio law requires such a [competitive bid] process. It does not. Ohio law requires CG&E to offer a competitive bid process for retail consumers to choose or reject a retail price resulting from the competitive bid." Response at 9. This view of Ohio law is too inscrutable to permit the OCC to reply.

[28] Response at 8.

[29] *Id.* at 4, footnote 4.

affiliated companies reflect market rates.[30] The review did not consider whether the contemplated *sale of power plants* is anti-competitive.

The sale of plants to ULH&P is anti-competitive even though cancellation of previous power sales contracts, and any acceptance of new contracts, may meet a FERC test that is not designed to test the effect of plant sales. In this case, the Company seeks to circumvent the FERC's review regarding sales at market rates *by selling entire generating units below market value*. This, in essence, provides the purchasing utility with a long-term flow of electric generation at below market rates. The sale of generating plant in this case falls under the Commission's review regarding the sale price of generating facilities and the effect of such a sale on competitive conditions. The strategy is anti-competitive, and the Commission should deny the Company's proposals under Section 12(d) of PUHCA to maintain competitive conditions to protect consumers.

## III. CONCLUSION

The approximately 600,000 residential customers in southern Ohio should not be asked to pay for increased purchased power costs or for expensive, new generating facilities while the depreciated plants paid for by Ohioans are sold to serve Kentucky customers at lower costs. The Application should be rejected.

The OCC respectfully requests that its Motion to Intervene in this proceeding be granted, and that the Company's requested sale of CG&E's generating facilities to ULH&P be rejected as filed.

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[30] *Union Light, Heat and Power Company and The Cincinnati Gas & Electric Company*, Docket No. ER04-1248-000, ER04-1248-001, and ER04-1247-000, Order Accepting Filing, 110 FERC ¶61,212 at 4 (March 3, 2005); citing *Boston Edison Co. Re: Edgar Electric Energy Co.*, 55 FERC ¶61,382 (1991).

Respectfully submitted,

The Office of the Ohio Consumers' Counsel

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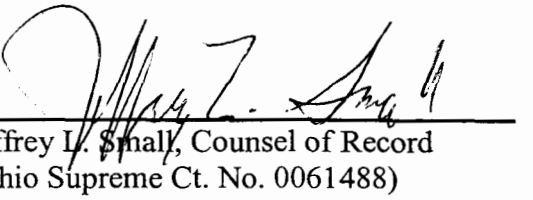
Consumers' Counsel



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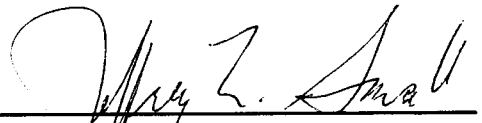
## CERTIFICATE OF SERVICE

I hereby certify that a copy of the OCC's *Reply to Response of CG&E* was served on the person(s) stated below via first class U.S. Mail, postage prepaid, this 25th day of March 2005.



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# ATTACHMENT

*In re New CG&E Power Plant*, PUCO Case No. 04-1811-EL-AAM, *et al.*, Response to Interrogatory No. 2 (Response February 21, 2005).

**Ohio Consumers' Counsel First Set Interrogatories**
**CG&E Case No. 04-1811-EL-AAM et al.**
**Date Received: February 1, 2005**
**Response Due: February 21, 2005**

**OCC-INT-01-002**

**REQUEST:**

2. In the Application at page 4, CG&E states: "For the summer of 2005, CG&E anticipates that forward reliability purchases will provide approximately 20% of its peak load capacity needs." What percentage of CG&E's peak load would need to be purchased if the 1,077 MWs from East Bend, Miami Fort 6 and Woodsdale remained with CG&E?

**RESPONSE:**

Objection. CG&E objects to this interrogatory pursuant to OAC 4901-1-16(B), on the grounds that it seeks information that is inadmissible and not reasonably calculated to lead to the discovery of admissible evidence. The information sought is objectionable because CG&E decided to transfer these plants to ULH&P in 2003, and the transfer is presently scheduled for an effective closing date of April 1, 2005. CG&E prepared its System Reliability Tracker (SRT) application for 2005 based on this assumption. Assuming that the 1,077 MW for these plants would remain with CG&E is irrelevant and not reasonably calculated to lead to the discovery of admissible evidence, because the plants will not remain with CG&E. If the effective date of the transfer is changed and this impacts CG&E's system reliability purchases, CG&E will provide such information to OCC at that time.

Additionally, CG&E did not prepare any scenarios for its SRT application which contemplated that it would retain the 1,077 MW for these plants beyond April 1, 2005. Given that CG&E did not perform such calculation for its SRT application, CG&E objects to OCC's request that CG&E should do so now, on the grounds that it is unduly burdensome for OCC to request that CG&E should now perform additional modeling for different types of scenarios, which CG&E did not consider for the SRT application, merely for purposes of OCC's attempt to support its own position in this case.

**WITNESS RESPONSIBLE: TBD**