PUBLICATIONS

Commission Approves Stipulation and Duke Energy's Request to Recover Environmental Remediation Costs

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On November 13, 2013, the Public Utilities Commission of Ohio (PUCO) issued an order in the Duke Energy Ohio, Inc. (Duke) natural gas distribution rate case. The result involved no change in distribution revenues but does enable Duke to recover environmental remediation expenses related to two manufactured gas plants (MGPs). [1]

In July 2012, Duke filed an application with the PUCO for approval of an increase in natural gas rates and related applications for tariff approval, an alternative rate plan, and to change accounting methods. In total, Duke sought a revenue increase of approximately $44.6 million or approximately 18.09 percent over its current revenue. Duke also sought to recover approximately $62.8 million for the cleanup of two former MGPs in accordance with the federal Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA).

In April 2013, most intervening parties in the case entered into a stipulation to address all of the issues in the case, except those issues related to Duke's request for cost recovery associated with remediation of the former MGP sites. Provisions of the stipulation included: no increase in current base rates, continued recovery of costs associated with Duke's SmartGrid deployment for its gas distribution business, the resetting of certain riders, $350,000 per year through shareholder contributions to be used for low-income weatherization in Duke's service territory, and the establishment of a 9.84 percent return on equity. While the stipulation did not address

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Duke's request for cost recovery associated with remediation of the former MGP sites, the stipulation did establish how any PUCO-approved cost recovery should be allocated among customer classes, with the majority of costs allocated to residential customers. As part of the order, the PUCO adopted the stipulation.

With the PUCO's adoption of the stipulation addressing Duke's distribution rate and tariffs, the majority of the order was devoted to the PUCO's consideration of Duke's request for recovery of MGP-related costs. At issue was the recoverability of costs incurred by Duke for the environmental investigation and remediation associated with two former MGP sites that were owned and operated by two of Duke's predecessor companies. For over a century, until the mid-1960s, MGPs were used for the production of commercial grade gas from the combustion of coal, oil, and other fossil fuels for use with lighting, heating, and cooking. Residuals from the production process included tar and sulfur residues, and, in some instances, ammonia and naphthalene residues, which were often disposed of at the MGP site.

According to Duke, it commenced environmental investigations of the two MGP sites at issue in 2007 and 2010 due to changing conditions at the sites that could have led to new exposure pathways. Duke asserted, in its application, that it then acted prudently to address the impacted sites. Costs incurred by Duke included environmental consultants, construction management, site security, landfill disposal, and audits throughout the remediation process.

The PUCO's Staff (Staff) disagreed with Duke's request to recover $62.8 million for the environmental investigation and remediation associated with the MGP sites. Staff primarily argued that the majority of the remediation work was done in sections of the sites not used for gas distribution, and, therefore, the remediation efforts were not associated with "used and useful" facilities as required by Ohio Revised Code (R.C.) 4909.15. Instead, Staff recommended that Duke only be permitted to recover $6.3 million, limiting remediation cost recovery to portions of the MGP sites with actual gas distribution infrastructure. A number of interveners to the case also disputed Duke's request. For example, the Ohio Manufacturers' Association

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recommended that the PUCO adopt the Staff's recommendation, while the Ohio Consumers' Counsel argued that shareholders, and not ratepayers, should be responsible for the costs.

In the decision, the PUCO permitted Duke to recover costs, minus carrying charges, related to environmental remediation at the two MGP sites over a five-year period. The PUCO noted that, under CERCLA, Duke is under a statutory mandate to remediate MGP residuals from the sites, and, therefore, the "used and useful" standard under R.C. 4909.15 was not applicable when considering whether Duke may recover the costs associated with its investigation and remediation of the MGP sites. Instead, the PUCO determined that R.C. 4905.15(A)(4), providing that the PUCO, when fixing just and reasonable rates, shall determine "[t]he cost to the utility of rendering the public utility service for the test period," was relevant to its determination. The PUCO then determined that Duke supported its claim that the remediation costs incurred were a cost of providing utility service. In this determination, the PUCO noted that remediation costs were a necessary cost of doing business as a public utility in response to a federal law: "Not only is Duke legally obligated to remediate these sites as the owner and operator of these sites, but it is undisputed on the record that Duke has the societal obligation to clean up these sites for the safety and prosperity of the communities in those areas and in order to maintain the usefulness of the properties; therefore, these costs are a current cost of doing business."

The PUCO's decision was not unanimous. Commissioners Lesser and Haque issued a joint dissent, arguing that Duke's remediation is not a "cost to the utility of rendering the public utility service" under R.C. 4905.15(A)(4). Additionally, the dissent argued that Duke "failed to demonstrate the nexus between the remediation expense and its distribution service."

Footnote

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1. PUCO Case No. 12-1685-GA-AIR