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BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO 2008 MAR 31 PM 4:25

PUCO

In the Matter of the Application of The East Ohio Gas Company d/b/a Dominion East Ohio for Authority to Increase Rates for its Gas Distribution Service.	)	Case No. 07-829-GA-AIR
In the Matter of the Application of The East Ohio Gas Company d/b/a Dominion East Ohio for Approval of an Alternative Rate Plan for its Gas Distribution Service.	)	Case No. 07-830-GA-ALT
In the Matter of the Application of The East Ohio Gas Company d/b/a Dominion East Ohio for Approval to Change Accounting Methods.	)	Case No. 07-831-GA-AAM
In the Matter of the Application of The East Ohio Gas Company d/b/a Dominion East Ohio for Approval of Tariffs to Recover Certain Costs Associated with a Pipeline Infrastructure Replacement Program Through an Automatic Adjustment Clause, And for Certain Accounting Treatment.	)	Case No. 08-169-GA-UNC

REPLY TO DEO'S MEMORANDUM CONTRA OCC'S MOTION TO DISMISS
BY
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I. SUMMARY

This cycle of pleadings began with a Motion by the Office of the Ohio Consumers' Counsel ("OCC") to dismiss Dominion East Ohio Gas Company's ("DEO") application to collect $2.5 billion from northern Ohio consumers, for the reason that DEO has not complied with the procedures and standards established by the Ohio General

Assembly for such an application to collect the costs of pipeline replacement.[1] DEO argues that its pipeline infrastructure application was appropriately filed under R.C. 4929.11.[2] In this regard, DEO asserts that its application amounts to an automatic adjustment mechanism that would permit DEO's rates to fluctuate in accordance with changes in specific costs.[3] DEO opines that the Commission need only determine if the proposal is "just and reasonable," and that determination is a matter for hearing and not proper grounds for dismissal.[4]

Secondly, DEO argues that the rider application does not amount to an application for an increase in rates and is not an alternative rate plan application that is governed by R.C. 4929.05.[5] Alternatively, DEO argues that if the application is to be considered an alternative rate plan, R. C. 4929.05 does not require that the application be filed as a rate case.[6]

Notwithstanding the arguments presented by DEO, OCC's Motion to Dismiss should be granted. DEO's application is an alternative rate plan, and thus must comply with the statutory requirements of R.C. 4929.05, which include that the application must be filed as part of a R.C. 4909.18 application and must be noticed. Since DEO has failed to meet these requirements, the Commission is without jurisdiction to rule upon the

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[1] OCC also filed a Memorandum Contra DEO's motion to consolidate its $2.5 billion application with its pending rate case.

[2] DEO Memorandum Contra at 2.

[3] DEO Memorandum Contra at 3-4.

[4] DEO Memorandum Contra at 3.

[5] DEO Memorandum Contra at 6.

[6] DEO Memorandum Contra at 6.

alternative rate application. DEO's application does not qualify as an automatic adjustment mechanism under R.C. 4929.11 because the costs under the infrastructure replacement program are not costs that "fluctuate automatically in accordance with changes in specified cost or costs." Even if the Commission determines that DEO's application qualifies as an automatic adjustment mechanism under R.C. 4929.11, it should nonetheless determine it is not just or reasonable and should deny it. Further, DEO's application, if approved, will increase rates to customers and thus, must comply with the statutory mandates of R.C. 4909.18. DEO's application should thus be dismissed. These arguments will be addressed in detail below.

A. Because DEO failed to file its alternative rate plan as part of a rate case application, the Commission has no jurisdiction to entertain the application.

DEO asserts that even if its application is considered to be an alternative rate plan under R.C. 4929.05, it need not be filed as part of a rate case.[7] DEO believes that the wording of R.C. 4929.05 is permissive in this respect because the statute refers to the fact that a natural gas company "may" request approval of an alternative rate plan. DEO argues that OCC's interpretation is inconsistent with the language and policy of Chapter 4929 and should be rejected. Finally DEO argues that if the Commission determines that the application is governed by R.C. 4929.05, it "will not be difficult to bring its filing into compliance." [8]

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[7] DEO Memorandum Contra at 11.

[8] DEO Memorandum Contra at 12.

R.C. 4929.05 provides that the Commission is permitted to use the alternative rate making method for gas companies only when considering an application "filed pursuant to section 4909.18 of the Revised Code." The statute reads as follows:

> (A) **As part of an application filed pursuant to section 4909.18** of the Revised Code, a natural gas company may request approval of an alternative rate plan.

R.C. 4929.05 (emphasis added).

R.C. 1.42 provides that "words and phrases shall be read in context and construed according to the rules of grammar and common usage." When the language [of a statute] ***clearly expresses the legislative intent, the court need look no further [,]" because "at that point the interpretative effort is at an end, and the statute must be applied accordingly."[9] Under R.C. 4929.05, the Commission is permitted to use alternative rate-making methods to set rates for gas companies only "as part of an application filed pursuant to section 4909.18 ***." Any other interpretation defies the express language and clear intent of the General Assembly. Thus, if the utility is to seek alternative rate making methods as it "may" it may only do so when it files the alternative rate application as part of an application filed under R.C. 4909.18.

In *Time Warner v. Pub. Util. Comm.*, 75 Ohio St. 3d 229 (1996), the Ohio Supreme Court addressed this very issue in the telephone alternative regulation statute. In that case, the statute in question was R.C. 4927.04(A). R.C. 4927.04(A) contains almost identical prefatory language as that contained in R.C. 4929.05.

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[9] *Time Warner v. Pub. Util. Comm.*, 75 Ohio St.3d 229, 237 (1996), citing *Provident Bank v. Wood*, 36 Ohio St.2d 101 (1973) *et. al.*

R.C.4927.04(A) states that:

> **In considering an application pursuant to section 4909.18,** the rates and charges for basic local exchange service * * * may be established by the Commission * * * by a method other than that specified in section 4909.15 of the revised code * * *

Time Warner challenged the Commission's approval of telephone alternative rate plan, filed under R.C. 4927.04, instead of R.C. 4909.18.

The Ohio Supreme Court reversed the Commission's decision, and found that the Commission was only permitted to use the alternative regulation statutes when the applicant was seeking to increase rates, pursuant to R.C. 4909.18:

> It follows that Ameritech's application did not trigger the commission's use of alternative rate treatment under R.C. 4927.04(A) and the commission exceeded the scope of its authority when it used non-traditional rate setting methods to set Ameritech's rates. Accordingly, the commission's exercise of authority under R.C. 4927.04(A) was unlawful and its opinion and order should be reversed.
>
> * * *
>
> Absent a change in the statutory framework, the commission is constrained, as we are, to apply the existing statutory framework to all applications for an alternative form of regulation. Accordingly, the commission erred when it attempted to bypass the General Assembly and use alternative regulation in setting basic local exchange service rates for Ameritech in a case not requesting an increase in basic local exchange service rates.[10]

Time Warner is directly applicable to the case at hand. Here, as in *Time Warner*, DEO asks that the Commission exceed the scope of its authority by approving a mechanism under the alternative gas regulation statute when DEO has not filed its application as part of a request for a rate increase under R.C. 4909.18. This is not permitted under the Supreme Court's decision in *Time Warner*.

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[10] *Time Warner* at 241.

DEO claims that if the Commission determines that the application is governed by R.C. 4929.05, dismissal is not required because if any part of DEO's filing is non-compliant, it can be fixed.[11] In particular, DEO contends that it has already complied with notice requirements of R.C. 4929.05 by sending a letter (DEO Memo Contra Exhibit A) to public officials (listed on DEO Memo Contra Exhibit B).

Notice is a crucial mandatory component to the alternative regulation process. It is the statutory prerequisite to the Commission's considering an application under R.C. 4929.05(A) -- "after notice, investigation, and hearing * * *." The fact that the notice required under R.C. 4929.05(A) is the same notice required under R.C. 4909.18 is axiomatic. R.C. 4929.05 begins with "[a]s part of an application filed pursuant to R.C. 4909.18 of revised code * * *."

An application filed under R.C. 4909.18 must be noticed at the time the application is filed and must be substantial, as expressed in R.C. 4909.19: "[u]pon the filing any application for increase provided for by section 4909.18 of the Revised Code the public utility shall forthwith publish the substance and prayer of the application * * *." R.C. 4909.19 directs notice to the customers who will be affected by the rate increase. Under this statute the Company must give notice by publishing the gist of the application, for three consecutive weeks in newspapers generally circulated throughout the utility's service territory.

There are also other notice requirements associated with an R.C. 4909.18 filing as well. R.C. 4909.43(B) pertains to notice that must be given to municipalities, before the rate application is filed, if the rate increase affects the municipality. Under R.C.

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[11] DEO Memorandum Contra at 12.

4909.43(B):

> [n]ot later than thirty days prior to the filing of an application pursuant to section 4909.18 or 4909.35 of the Revised Code, a public utility shall notify, in wiring, the mayor and legislative authority of each municipality included in such application of the intent of the public utility to file an application, and the proposed rates to be contained therein.

Thus, to properly consider the application as an alternative regulation plan, the Commission must determine whether the notice provisions have been satisfied. They have not.

The company failed to provide notice to the municipalities affected, as required by R.C. 4909.43(B), thirty days before its February 22, 2008 application. Instead eight days after the application was filed, it sent Exhibit A to public officials listed in Exhibit B. Under R.C. 4909.43(B) the notice must be given prior to the rate application filing. It was not. It must fail as the mandatory language of the statute clearly requires the filing *prior* to the application being filed.

Notice to the public was not made either, at the time of the application, as required under collect $2.5 billion from customers over a twenty-five year period.

DEO has failed to satisfy the notice requirements of R.C. 4929.05. These are statutory requirements that cannot be waived. Thus, the Commission is without jurisdiction to entertain the alternative regulation plan -- because a mandatory perquisite -- notice, has not been met.

B. DEO's application does not qualify as an automatic adjustment mechanism under R.C. 4929.11 because the costs under the infrastructure replacement program are not costs that "fluctuate automatically in accordance with changes in specified cost or costs."

DEO argues that its application to approve collection of $2.5 billion from its customers for proposed pipeline infrastructure replacement is an appropriate filing under R.C. 4929.11 and should not be dismissed.[12] DEO asserts that raising this issue now is premature, and that whether the application is "just and reasonable" or passes some other test, is a matter for hearing and not proper grounds for dismissal.[13]

DEO submits that its application functions as an "automatic adjustment mechanism" that will allow its rates to "fluctuate automatically" due to changes in costs. DEO argues that the costs to be recovered under its pipeline infrastructure program will "change constantly" as DEO replaces infrastructure over the 25 year period.[14] Further, DEO asserts that the annual spending will not be stable or predictable over the entire time span.[15] DEO claims it has "no control over the costs."[16] Additionally, according to DEO, its current rates cannot cover the costs of the proposed projects.[17]

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[12] DEO Memorandum Contra at 3-6.

[13] DEO Memorandum Contra at 6.

[14] DEO Memorandum Contra at 5-6.

[15] Id.

[16] Id. at 6.

[17] Id.

Despite these claims, Revised Code 4929.11 states:

> Nothing in the Revised Code prohibits, and the public utilities commission may allow, **any automatic adjustment mechanism or device** in a natural gas company's rate schedules rate schedules that allows a natural gas company's rates or charges for a **regulated service or goods to fluctuate automatically in accordance with changes in a specified cost or costs.** (Emphasis added)

It is well settled that the Commission is a creature of statute and may exercise no power, authority, or jurisdiction beyond that conferred upon it by statute.[18] The jurisdiction of the Commission is limited by the language contained within the confines of R.C. Chapter 4929 -- the gas alternative regulation provisions. Accordingly, attention must be paid to the plain language of the statute, R.C. 4929.11.

The statutory language of R.C. 4929.11 is clear -- automatic adjustments may be permitted only where the costs being tracked fluctuate on the same automatic basis. DEO would essentially eliminate the General Assembly's statutory definition by arguing that automatic fluctuation in cost occurs whenever there is any change in cost measured over the long term (for example, 25 years of the program). Under the definition that DEO would substitute for the General Assembly's, there is no cost that would not fit its definition of a fluctuating cost, as most any cost could fluctuate over a 25-year period. But the General Assembly has stated in R.C. 1.47 that, in "enacting a statute," the "entire statute is intended to be effective...."

While DEO urges a broad and expansive interpretation of the statutory terms of R.C. 4929.11, the Ohio Supreme Court's precedent suggests that it is more appropriate to

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[18] See for example, *Cincinnati v. Pub. Util. Comm.*, 96 Ohio St. 270, 275 (1917); *Ohio Central Tel. Corp. v. Pub. Util. Comm.*, 166 Ohio St. 180, 182 (1957); *Penn Central Transportation Co. v. Pub. Util. Comm.*, 35 Ohio St. 2d 97, 99 (1973).

strictly construe the statutory terms of R.C. 4929.11. While not directly ruling upon this statute, the Court nonetheless has, in the past, strictly construed other automatic adjustment provisions of Title 49.[19]

In such instances the Court's rationale has been that the automatic adjustment provisions should be construed strictly, otherwise the regulatory framework of R.C. 4909.15 will be compromised.[20] *Pike Natural Gas Company v. Pub. Util. Comm.*[21] is the seminal case where the Court emphasized the need to maintain the integrity of the General Assembly's ratemaking formula. In *Pike Natural Gas*, the Court rejected a single automatic adjustment to one component of customers' rates -- excise taxes. There the utility sought approval of an automatic adjustment clause to recover the gross receipts tax levied on its revenues. The Court found that the only statute that authorized an adjustment clause, R.C. 4905.302, allowed for adjusting customers' rates due to "fluctuations" in the price of gas to a utility.[22] Thus, the Court did not allow the

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[19] *See for example, Montgomery County Board of Commissioners v. Pub. Util. Comm.*, 28 Ohio St. 3d 171 (1986) (Court reversed PUCO order which permitted the utility to recoup percentage of income payment arrearages in an expedited manner (through electric fuel component rate) where the expenses were not acquisition and delivery costs under R.C. 4901.191; *Pike Natural Gas Company v. Pub. Util. Comm'*, 68 Ohio St. 2d 181 (1984) (R.C. 4905.302 provides solely for adjustment clause that reflect fluctuations in the price of gas to a utility and use of an excise tax adjustment clause was not permissible under R.C. 4905.302 or under R.C. 4905.31).

[20] Additionally, there are public policy reasons that the Commission should consider before it determines to allow a rider to go into effect, beyond those enunciated by the Supreme Court. Automatically approving the infrastructure expenditures will diminish the incentives of the Company to keep the costs of its program down and may lead to customer confusion and misunderstanding. See for example the PUCO holding *In re Columbia Gas of Ohio, Inc. (Martins' Ferry)* Case No. 77-1428-GA-AIR, where the Commission determined not to allow automatic pass-through of excise taxes -- "to do so diminishes the incentive for the company to avail itself of the least expensive source of supply. Customer confusion and misunderstanding might well result if this new adjustment or surcharge were to appear on individual bills. Customer acceptance is, after all, a recognized principle in establishing rate design." Opinion and Order (May 24, 1979) (cited in *Pike Natural Gas* at footnote 5).

[21] 68 Ohio St.2d 181 (1984).

[22] Id. at 183.

Commission to flow through the excise taxes incurred by a utility.[23]

Additionally, the Court dismissed arguments that R.C. 4905.31 would sanction such a clause. Noting that it had never interpreted that statute to allow an adjustment clause, the Court wisely recognized the difficulty it would encounter if it permitted an automatic adjustment for one discrete utility expense:

> it would be difficult to deny adjustment clauses for any operating expenses, for just as excise taxes may increase, other non-fuel costs will increase. This could eliminate the regulatory framework, contained in R. C. 4909.15, that rates are to be based upon historic costs. We are unwilling to proceed down this 'slippery slope' under the guise of interpreting R. C. 4905.31. (citation omitted)[24]

The Court also rejected the regulatory lag arguments raised by the utility. It concluded that regulatory lag -- the lag between the time costs increase and the recovery of such costs in a rate case -- is not a question for the Commission or for the Court to address. Rather the Court advised that its resolution is for others to make -- in particular, the legislature.[25]

But under DEO's approach, the term "automatic adjustment mechanism" and costs that "fluctuate automatically with changes in specified costs" is so broadly defined, that Ohio consumers would go careening down the slippery slope that the Ohio Supreme Court chose to avoid. In this case there will be severe consequences for the 1.1 million DEO customers who are subject to DEO's proposal to increase rates by $2.5 billion.

Under any construction, loose or strict, DEO's expenses that it seeks to recover

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[23] Id. at 184.

[24] Id. at 186.

[25] Id.

here do not fit the definition of automatically fluctuating costs under R.C. 4929.11. And, because DEO's application fails to meet R.C. 4929.11, the Commission is without jurisdiction to rule upon the justness and reasonableness of the application. Thus, DEO's claim that this issue is a matter for hearing and not properly the grounds for dismissal must be rejected.

C. Even if the Commission determines that DEO's application qualifies as an automatic adjustment mechanism under R.C. 4929.11, it should nonetheless find that the application is not just or reasonable.

OCC has argued that DEO's application does not meet the statutory definition of R.C. 4929.11. Even if the Commission disagrees, it should find that DEO's application is not just or reasonable. Not only is DEO's interpretation of the statute inconsistent with the Ohio Supreme Court precedent, but it is also inconsistent with standards the PUCO has adopted in evaluating automatic adjustment riders.

Although the Commission has approved riders in the past[26], including riders for Percentage of Income Payment Plan arrearages, excise taxes, and uncollectibles (bad debt expense), approval of these riders have turned upon the **common characteristics not found in the DEO application.**[27] The Commission has approved riders where the expenses in question have been extremely volatile and are beyond the Company's control.[28]

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[26] Not all the PUCO Commissioners have endorsed the Commission's use of riders. Both Commissioner Mason and former Commissioner Jones have filed dissenting opinions in a number of bad debt rider cases, objecting to the use of a rider since it permits single issue rate collection outside of a rate case. Commissioner Mason's dissent in an East Ohio Gas rider case explains this: "This case examines a single issue and rules in favor of the company. Perhaps there are other issues that the Commission should examine that the company has not brought to our attention. That is why we have rate cases. The company has not shown us that the uncollectibles dropped the company below its authorized rate of return. The record is void of sworn testimony and a complete review of the company's books and records has not occurred." *In the Matter of the Application of the East Ohio Gas Company, Pursuant to Revised Code Section 4909.18 of a Payment Matching Program and Other Matters,* Case No. 01-2592-GA-UNC, Dissent from *Opinion and Order* at 1 (Oct. 24, 2001).

Commissioner Jones echoed this concern in a dissent filed in the 2006 *Ohio Gas Company* uncollectible rider case, Case No. 06-706-GA-UEX. See *In the Matter of the Application of Ohio Gas Company for Approval of an Adjustment to the Uncollectible Expense Rider,* Opinion and Order (June 6, 2006) "The current policy of allowing bad debt riders, at least as it is currently implemented, is seriously flawed. Before we consider bad debt riders, I believe we need full-blown rate cases where all applicable facts would be presented and debated. After all, this commission has not reviewed Ohio Gas Company's base rate and expenses in a number of years and has no information to analyze the impact of recent increases in uncollectible expenses. Only through the hearing process could the Commission determine whether the rates are just and reasonable. Without all the facts before me and without a compelling rationale for selectively adjusting uncollectible expenses (apart from other company expenses), I cannot approve this entry."

These dissents emphasize the one-sided nature of single issue adjustments that are being endorsed by the PUCO outside of rate cases. Such adjustments, including the rider in this case, destroy the balance between utilities and consumers that the General Assembly achieved in R.C. 4909.15, and tilt the scales in favor of utilities.

[27] Whether these characteristics equate to a test, as asserted by OCC, or whether they are factors that underlie the Commission's precedent is not the issue, DEO's arguments notwithstanding.

[28] Another factor the commission has looked at is whether the current rates are sufficient to cover the expenses in question. While OCC would concede that current rates would not cover expenses associated with the company's ramped up infrastructure program, current rates are set to include the ordinary level of infrastructure investment taking place on a non-accelerated basis.

For instance, the Commission has on a number of occasions allowed uncollectible expenses to be recovered in riders when the utilities have been subject to extreme volatility in gas prices.[29] In the 2003 Uncollectibles Application case, six gas companies, including the four largest in Ohio, filed for rider approval claiming they were experiencing volatile and high gas prices that were expected to continue into the future. The Commission noted that these uncollectible expenses were driven largely by gas costs and could not have been avoided altogether or been extensively mitigated.[30] Additionally weather contributed to the large uncollectible expenses, which was clearly unpredictable and not within the gas companies' control.[31]

In a similar vein, the Commission has allowed gross receipts tax to be recovered from automatic adjustment riders on the basis that such taxes fluctuate directly as GCR rates fluctuate.[32] The Commission has noted that for gross receipts taxes there is no conceptual difference from these and other fluctuating recovery mechanisms.[33]

In sharp contrast with these exceptions is DEO's application where there is a conceptual difference setting its application apart -- the costs related to its infrastructure

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[29] *In the Matter of the Applications of the East Ohio Gas Company d/b/a Dominion East Ohio, Columbia Gas of Ohio, Inc., Vectren Energy Delivery of Ohio, Northeast Ohio Natural Gas Corp., and Oxford Natural Gas Company for Approval, Pursuant to Revised Code Section 4929.11, of Tariffs to Recover Uncollectible Expense Pursuant to an Automatic Adjustment Mechanism*, Case No. 03-1127-GA-UNC, Application May 7, 2003) ("2003 Uncollectibles Application case").

[30] *In the Matter of the Applications of the East Ohio Gas Company d/b/a Dominion East Ohio, Columbia Gas of Ohio, Inc., Vectren Energy Delivery of Ohio, Northeast Ohio Natural Gas Corp., and Oxford Natural Gas Company for Approval, Pursuant to Revised Code Section 4929.11, of Tariffs to Recover Uncollectible Expense Pursuant to an Automatic Adjustment Mechanism*, Case No. 03-1127-GA-UNC, *Finding and Order* at 10-11 (Dec. 17, 2003).

[31] Id.

[32] Id,

[33] Id.

replacement program are not costs that fall within the definition of R.C. 4929.11. Moreover they do not have the characteristics of prior Commission approved automatic adjustment mechanisms -- the costs are not volatile, nor are they beyond the Company's control.

DEO cites to the recently stipulated Columbia Gas Riser Case, Case No. 07-478-GA-UNC, as precedent against OCC's argument here.[34] This citation is improper and must be ignored. The Columbia case is by its very nature not precedent and DEO's attempt to use it here should be rejected. Citing to a Stipulation is contrary to the notion of a stipulation and indeed contrary to the very terms of the stipulation. The Columbia Stipulation and Recommendation states:

> Except for enforcement purposes, neither this Stipulation nor the information contained herein or attached, shall be cited as precedent in any future proceeding for or against any Party, or the Commission itself, if the Commission approves the Stipulation and Recommendation, other than a proceeding to enforce the terms of this stipulation. (footnote omitted).[35]

Stipulations may not be used for such purposes because each settlement contains a fundamental quid pro quo that is not present in a case such as this, where there is no agreement.

In any event it is not relevant whether OCC has or has not endorsed R.C. 4929.11 filings in other stipulated cases. The Commission need not approve every rider

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[34] DEO Memorandum Contra at 4.

[35] *In re the Application of Columbia Gas of Ohio, Inc. for Approval of Tariffs to Recover Through an Automatic Adjustment Clause Costs Associated with the Establishment of an Infrastructure Replacement Program and for Approval of Certain Accounting Treatment*, Case No. 07-478-GA-UNC, Amended Stipulation & Recommendation at 2 (Dec. 18, 2007).

application before it. The Commission may determine that in certain cases the rider is not reasonable and should not be approved. The Commission should draw that conclusion here and now. The Commission should find DEO's application to be unjust and unreasonable and should deny it.

D. DEO's application, if approved, will increase rates to customers and thus, the application must comply with the statutory mandates of R.C. 4909.18.

DEO argues that the requirements of R.C. 4909.18 do not apply to its $2.5 billion rider.[36] DEO believes the rider is not a rate increase because the proposed tariff sheet filed with the application is set at zero, and "rates simply will not increase upon approval of this application."[37] DEO claims that a "later rate impact" does not transform a rider application into a rate case. DEO offers two Ohio Supreme Court cases to support its premise: *Ohio Consumers' Counsel v. Pub. Util. Comm.*[38] and *River Gas Co. v. Pub. Util. Comm.*[39]

Under the Company's view, a request to book $2.5 billion in infrastructure investments as deferrals -- for future collection from customers -- does not constitute a request for a rate increase for customers simply because the Company set the initial rider at zero (for the time being). This argument ignores the fact that consumers will be forced to pay higher rates to recover these costs, regardless of what the Company calls them. Moreover, once the Company has received approval of the rider (even at zero), DEO

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[36] DEO Memorandum Contra at 6-9.

[37] DEO Memorandum Contra at 7.

[38] 69 Ohio St. 2d 509 (1982).

[39] 110 Ohio St. 3d 394, 2006-Ohio-4706.

would then insist that parties could not oppose the rate increase until the rider is ready to be imposed on customers, even though the accounting, the regulatory framework, the concepts for recovery, review, and approval have all been determined by its application (in a process bereft of any procedure, by DEO's own admissions). Thus, consumers get no notice of the $2.5 billion increase until after they begin receiving bills that reflect this increase. Such a process would totally circumvent due process and the notice of Ohio's ratemaking statutes. Moreover, such analysis strains legal reasoning.

At this time, DEO is seeking approval of the rider concept plus the accounting authority needed to allow it to defer for financial accounting purposes $2.5 billion in expenses for the infrastructure replacement. Although these expenses are not yet being incurred, they will be incurred over the next twenty-five years and will be in turn collected from customers on an annual basis though the rider mechanism proposed by DEO here. Moreover, the magnitude of this request makes any prior Ohio gas utility request under this statute pale in comparison, and warrants even greater scrutiny by the Commission.

Under accounting standards, DEO can only defer these expenses on its books if it has "regulatory assurance," that the expenses will be collected from customers. Financial Accounting Standard ("FAS") 71 provides guidance to utilities in preparing financial statements.[40] FAS 71 allows regulated utilities to adopt accounting treatment of assets and liabilities that would otherwise be improper according to the Financial Standards

[40] Statement of Financial Accounting Standards 71, Financial Accounting Standards Board of the Financial Accounting Foundation (1982).

Accounting Board[41] -- where "*regulation provides assurances that incurred costs will be recovered in the future.*"[42] "Regulation," in the form of a PUCO's order being sought by DEO, will provide this assurance of later recovery of these expenses from customers that DEO needs to defer the expenses in its financial statements.[43]

In a recent appeal to the Ohio Supreme Court regarding authorization of an accounting deferral for regional transmission organization expenses by the Commission, the Court rejected similar arguments presented here by DEO -- that orders were not final because rate changes associated with the order would not be implemented until later.[44] Instead the Court found to the contrary: "The PUCO orders were final and appealable."[45]

The Court found that the accounting orders (similar to what DEO is seeking here) were in fact final appealable orders, because customers had already been harmed by the Commission's actions:

> The fact that subsequent orders may result in more direct effects does not mean that the orders allowing accounting procedure changes are not final. Thus the Consumers' Counsel may argue in these appeals that customers have already been harmed by PUCO actions that she claims were unreasonable or unlawful.[46]

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[41] FAS 71, *"This statement may require that a cost be accounted for in a different manner from that required by another authoritative pronouncement."* at 2. (Emphasis added).

[42] Id. at 1. (Emphasis added).

[43] In cases where the independent auditors disagree with the company on whether there is assurance by the regulatory body that costs will be recovered in the future, and the level of costs is material, this disagreement is disclosed by the independent auditors in the company's financial reports. Rule 203, 204 of the Rules of Conduct of the Code of Professional Ethics of the American Institute of Certified Public Accountants.

[44] The Court's opinion relates to two consolidated cases, each raising accounting issues.

[45] Id. at 15.

[46] Id. at ¶ 25.

The Court's decision in the *FirstEnergy* cases recognized the reality of PUCO ratemaking -- customers end up paying in rates what PUCO accounting orders allow to be booked, as expenses in this case, -- in regulatory accounting adjustments pursuant to FAS 71. In the *FirstEnergy* appeal, the Commission pressed for the continuation of earlier rulings where the Court distinguished accounting from ratemaking and declined to find that rates are affected by such accounting.[47] The Court was not persuaded. Instead, in *FirstEnergy,* the Court identified the connection between accounting and rates:

> To be sure, as Consumers' Counsel contends, FirstEnergy and Dayton Power and Light, having secured the accounting changes, will likely ask the PUCO for permission to raise their customers' rates after the market development period to cover the costs that the PUCO has allowed the companies to defer during that period.[48]

Through *FirstEnergy* the Court recognized that when the PUCO creates a regulatory asset, or permits deferral of expenses in an accounting case, there is an inextricable "influence"[49] on future rates.

Like the deferral of expenses in the *First Energy* case, the expenses to be sought from DEO's customers in this case are real, not theoretical, and amount to billions of dollars. OCC need not wait, as urged by DEO, for the later rate impact to befall its clients. Rather, if OCC were to wait, consumers will have already begun to pay the costs before any review occurs. Even then, the review will be cursory and the burden of proof

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[47] See *e.g. Ohio Consumers' Counsel v. Pub. Util. Comm.* (1983), 4 Ohio St.3d 111, 115; 4 OBR 358, 447 N.E.2d 749 (where the Court permitted the utility to amortize the balance of four terminated nuclear units over a fifteen year period for book purposes only); *Ohio Consumers' Counsel v. Pub. Util. Comm.* (1983), 6 Ohio St.3d 377, 6 OBR 428, 453 N.E.2d 673 (where the Court upheld the PUCO ruling allowing DP&L to change its accounting procedures to extend the period of time in which it could capitalize AFUDC).

[48] *Ohio Consumers' Counsel v. Pub. Util. Comm.* (2006), 111 Ohio St.3d 384, 2006-Ohio-5853, 856 N.E.2d 940, at ¶ 35.

[49] *Ohio Consumers' Counsel v. Pub. Util. Comm.* (1983), 6 Ohio St. 3d 377, 380, (Locher, R.S., dissenting) (where Justice Locher recognized that the purpose of an accounting change is to "influence rates").

will have been effectively switched from the Company to OCC and other intervenors to prove that the costs were imprudent. OCC's customers will be harmed if the Commission approves this rider.

DEO cites to *Ohio Consumers' Counsel v. Pub. Util. Comm.*[50] as authority for the proposition that even if this case is an application to increase the rates customers must pay, it is not necessarily an R.C. 4909.18 application. While OCC agrees that there are other limited exceptions under the Code that permit rate increases to be granted outside of R.C. 4909.18, including R.C. 4905.26, DEO has not shown how its application fits into any of these limited exceptions. It does not, and so DEO must comply with R.C. 4909.18.

DEO also argues that the Ohio Supreme Court has held that automatic adjustment mechanisms "similar in operation to the one proposed here" do not constitute ratemaking, citing to *River Gas Co. v. Pub. Util. Comm.*[51] However, DEO fails to recognize the inherent distinction between the pervasive purchased gas adjustment statutes of R.C. 4905.302, and the extraordinary and limited regulatory exception embodied in R.C. 4929.11. In *River Gas*, the expenses in issue were those of gas supplier refunds linked to gas costs, which are clearly defined in great detail by statute and whose automatic recovery is permitted solely through R.C. 4905.302. Calling the difference between gas costs and infrastructure replacement a "distinction without a difference," ignores the fundamental separation that is embodied in the separate and distinct regulatory schemes set in R.C. 4905.302 and Chapters 4909 and 4929.

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[50] 110 Ohio St. 3d 394, 2006-Ohio-4706.

[51] DEO Memorandum Contra at 7-8, citing *River Gas Co. v. Pub. Util. Comm.*, 69 Ohio St.2d 509 (1982).

Here however, there is no such clear designation of the infrastructure replacement costs as the type of costs designated for recovery under a limited exclusion to traditional ratemaking. In fact these costs are costs of service that would otherwise be includable as expenses related to the cost of serving customers under R.C. 4909.15. The difference in cost is, contrary to DEO's assertions otherwise, a distinction that is significant, and cannot be ignored.

Moreover, the Ohio General Assembly has specifically addressed automatic adjustment mechanisms outside of the context of alternative rate plans and limited those mechanisms to specific proceedings such as the gas cost recovery proceedings. The Ohio General Assembly, however, has not seen fit to establish an automatic adjustment mechanism for infrastructure replacement. The Commission should not permit DEO to do so either.

E. DEO's Application is an alternative rate plan that must comply with the statutory requirements of R.C. 4929.05, including being filed as part of an R.C. 4909.18 application and properly noticed under R.C. 4909.19 and 4909.43(B). Since DEO has failed to meet these requirements, the Commission lacks jurisdiction to rule on the alternative rate application.

DEO argues that its application is not for an alternative rate plan.[52] DEO believes that automatic adjustment mechanisms are authorized by R.C. 4929.11 and that R.C. 4929.11 does not require that such applications be filed as alternative rate plans or otherwise approved under R.C. 4929.05. R.C. 4929.11 is a "stand alone" mechanism "that exists independently from an alternative rate plan."[53]

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[52] DEO Memorandum Contra at 9.

[53] DEO Memorandum Contra at 10.

DEO's argument belies the fact that Revised Code section 4929.11 was created as part of House Bill 476 and became effective September 17, 1996. Statutes that are in pari materia must be harmonized unless they are "'irreconcilable and in hopeless conflict."[54] Statutes are considered in pari materia if they pertain to the same subject matter.[55] Clearly, R.C. 4929.11 and 4929.05 are in pari materia, as both were promulgated as part of the same House Bill, and pertain to natural gas alternative rate regulation, as the regulatory scheme was set forth as Chapter 4929 of the Ohio Revised Code.

A statute, such as R.C. 4929.11, cannot be examined in a vacuum[56], as suggested by DEO. It must be viewed as part of Chapter 4929. R.C. 4929.11 should be read in the context in which it was passed. R.C. 4929.11 should be construed in connection with the other statutes and sections of Chapter 4929. According to the rules of statutory construction, all such sections and statutes are to be compared with reference to the entire system of which all are parts.[57]

The purpose of H.B. 476 was to enable natural gas companies to apply for alternative rate regulation and R.C. 4929.11 is squarely couched in this context. As part of these alternative rate plans, natural gas companies could seek to establish automatic rate adjustment mechanisms.[58] To establish an alternative rate plan, however, a natural

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[54] *Hughes v. Registrar, Ohio Bureau of Motor Vehicles*, 79 Ohio St.3d 305, 308 (1997).

[55] The Latin translation of in pari materia is "in the same matter," and Black's Law Dictionary defines the term as "on the same subject, relating to the same matter." (8th ed. West 2004).

[56] 85 Oh Jur Statutes 176, citing *State ex rel Quirke v. Patriarca*, 100 Ohio App.3d 367 (11th Dist. Lake County 1995).

[57] 85 Oh Jur Statutes 176, *citing Nadler v. New Amsterdam Cas. Co.*, 25 Ohio N.P. 572, 3 Ohio L. Abs. 752 (C.P. 1925), *rev'd on other grounds*, 115 Ohio St. 472 (1926).

[58] See R.C. 4929.01(A).

gas company must undergo an application procedure that affords the public notice, the opportunity for comment, and a hearing. This is the very least that can be said for an application that seeks to extract $2.5 billion from DEO's customers over the next 25 years. And whether the rate increase is sought through an automatic adjustment or an R.C. 4909.18 application, it has the same end result -- customers' rates can increase, and in this alternative rate application that increase amounts to a whopping $2.5 billion.

Otherwise, if R.C. 4929.11 is a stand alone provision as DEO argues, there is no procedural process delineated for it. This would suggest that the General Assembly believed it appropriate to permit rate increases under R.C. 4929.11 in derogation of R.C. 4929.05 and 4909.18. Such a conflict could not have been intended by the General Assembly.[59]

Although DEO is correct in pointing out that the Commission has ruled that some applications filed under R.C. 4929.11 are not subject to the procedural requirements of R.C. 4929.05, OCC believes such decisions were ill-advised. OCC encourages the Commission to revisit the issue here in light of the arguments proposed by OCC and the sheer magnitude of DEO's proposal.

A more appropriate and statutorily consistent approach was utilized recently in the Vectren decoupling rider case.[60] There Vectren filed its application in 2005, seeking authority to obtain authority under R.C. 4929.11 for a demand side management program

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[59] See *Canton v. Imperial Bowling Lanes, Inc.*, 16 Ohio St.2d 47, 53 (1985) concluding that '[t]he General Assembly will not be presumed to have intended to enact a law producing unreasonable or absurd consequences."(citation omitted).

[60] *In the Matter of the Application of Vectren Energy Delivery of Ohio, Inc. for Approval, Pursuant to Revised Code Section 4929.11 of a Tariff to Recover Conservation Expenses and Decoupling Revenues Pursuant to Automatic Adjustment Mechanisms and for Such Accounting Authority as May be Required to Defer Such Expenses and Revenues for Future Recovery through Such Adjustment Mechanisms*, Case No. 05-1444-GA-UNC.

and a favorable ratemaking mechanism (rider) called "decoupling." By Attorney Examiner Entry, the Company's request was determined to be "a request for an alternative rate plan as described in Section 4929.01(A), Revised Code" and Vectren was directed to follow the process found under R.C. 4929.05.[61] No party, including Vectren, filed an interlocutory appeal of the Attorney Examiner's opinion. The Commission in its subsequent *Opinion and Order*, approved, but significantly modified a joint stipulation between OCC, OPAE, and Vectren, as a gas alternative rate regulation plan under R.C. 4929.05.[62] Subsequent applications for rehearing, appeals, and a torturous and mangled process ensued, but through it all the Commission remained firm that the R.C. 4929.11 application should be governed by R.C. 4929.05.[63]

II. CONCLUSION

For the reasons stated above, DEO's Application must be dismissed because DEO has not met the statutory requirements of an alternative rate regulation filing under Chapter 4929. DEO's Application also fails to meet the statutory requirements of Chapter 4929 because, as filed, it fails to qualify as an alternative rate plan under R.C. 4929.11. Additionally, even if the Commission determines that the application qualifies under R.C. 4929.11 as an automatic adjustment mechanism, it should find that, given the underlying circumstances, it is not just and reasonable to approve it. Moreover, the

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[61] Id. *Entry* (Feb. 7, 2006).

[62] *In the Matter of the Application of Vectren Energy Delivery of Ohio, Inc. for Approval, Pursuant to Revised Code Section 4929.11 of a Tariff to Recover Conservation Expenses and Decoupling Revenues Pursuant to Automatic Adjustment Mechanisms and for Such Accounting Authority as May be Required to Defer Such Expenses and Revenues for Future Recovery through Such Adjustment Mechanisms*, Case No. 05-1444-GA-UNC, *Opinion and Order* at 8-10 (Sept. 13, 2006).

[63] See *Supplemental Opinion and Order* at 9-11 (June 27, 2007).

Company failed to file the "alternative rate plan" as part of its R.C. 4909.18 application and failed to properly give notice to the public and public officials regarding the application, as required by R.C. 4929.05.

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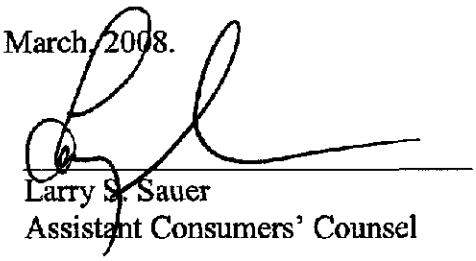
CERTIFICATE OF SERVICE

I hereby certify that a copy of the Office of the Ohio Consumers' Counsel's forgoing *Reply to DEO's Memorandum Contra OCC's Motion to Dismiss by the Office of the Ohio Consumers' Counsel* was provided to the persons listed below via first class U.S. Mail, postage prepaid, this 31st day of March, 2008.



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