

FILE

BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

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In the Matter of the Application of The)
East Ohio Gas Company d/b/a Dominion)
East Ohio to Adjust its Pipeline) Case No. 09-458-GA-UNC
Infrastructure Replacement Program Cost)
Recovery Charge and Related Matters.)

REPLY BRIEF
BY
THE OFFICE OF THE OHIO CONSUMERS' COUNSEL

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November 12, 2009

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TABLE OF CONTENTS

	Page
I. INTRODUCTION	1
II. ARGUMENT	2
A. Capital Additions Placed In-Service After The Date Certain Should Be Excluded From PIR Cost Recovery.	2
B. The Costs Of Curb-To-Meter Service Lines Serving New Customers Should Be Excluded From PIR Cost Recovery.	6
C. Incremental Operation And Maintenance Expenses Should Be Excluded From PIR Cost Recovery.	7
D. The PIR Cost Recovery Charge Should Be Calculated With Appropriate Savings Relative To A Baseline Level Of Expenses For Customers.	11
E. The PIR Cost Recovery Charge Should Not Be Overstated Due To A Delay In Reporting Retirements.	14
III. CONCLUSION	16

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I. INTRODUCTION

On November 2, 2009, the Office of the Ohio Consumers' Counsel ("OCC") filed its Initial Post-Hearing Brief ("OCC Brief") in the above-captioned matter, to protect the interests of approximately 1.1 million residential consumers from an unjust and unreasonable Pipeline Infrastructure Replacement Program Cost Recovery Charge by East Ohio Gas Company d/b/a Dominion East Ohio's ("DEO" or "the Company"). The Staff ("Staff") of the Public Utilities Commission of Ohio ("PUCO" or "Commission") filed a brief ("Staff Brief") that similarly addressed the issues OCC raised in this case as follows:

First, DEO should not be allowed recovery from customers for plant additions that were not placed in service as of June 30, 2009, the date certain in this case.

Second, DEO should not be allowed recovery from customers for installation of new service lines that are associated with new customer growth because it disregards the fact that new customer growth generates new revenues.

Third, DEO should not be allowed recovery from customers for incremental operation and maintenance (“O&M”) expenses.

Fourth, DEO has failed to reduce what it is asking customers to pay by an amount that reflects the cost savings that result from being allowed to use an alternative method to collect costs sooner from customers than under traditional regulation.

In addition on November 2, 2009, the Company filed its brief (“DEO Brief”) in opposition to the positions advocated by OCC and Staff.

The history of the case is incorporated herein as presented in OCC’s Brief.

II. ARGUMENT

A. Capital Additions Placed In-Service After The Date Certain Should Be Excluded From PIR Cost Recovery.

It is an undisputed fact that DEO has sought recovery of costs incurred for projects which were not in-service as of June 30, 2009, the date certain in this case.¹ In an attempt to circumvent legal precedent that would deny cost recovery for projects not in service as of the date certain, DEO relies on inappropriate authority for arguing that such costs should be recoverable.²

DEO fails to include any citation to Ohio law in support of its argument. In contrast, both OCC and Staff argue that recoverability of the costs associated with the plant additions not in service on date certain is unlawful pursuant to R.C. 4909.15.³ The

¹ DEO Brief at 13; OCC Brief at 8-10, Staff Brief at 12-17.

² DEO Brief at 11-17 (DEO cites to the PIR Staff Report (Staff Ex. No. 2), Stipulation (DEO Ex. No. 7), Rate Case Staff Report (Staff Ex. No. 3), and The Blue Ridge Consulting Services, Inc. Report (DEO Ex. No. 8).

³ OCC Brief at 9; See also, Staff Brief at 13.

concept of including the costs of capital additions as of date certain within rates for cost recovery is fundamental to rate making and Ohio law. R.C. 4909.15(A)(1) states:

(A) The public utilities commission, when fixing and determining just and reasonable rates, fares, tolls, rentals, and charges, shall determine:

(1) The valuation as of the date certain of the property of the public utility used and useful in rendering the public utility service for which rates are to be fixed and determined. * * *.

There is no dispute regarding the status of these various projects as of date certain in this case. As of June 30, 2009, the projects in question were not in service, and they were not used and useful; therefore, the associated costs should be excluded from capital additions in order to develop lawful rates that customers will pay. The only dispute is whether the law should be applied. As such the PUCO is a creature of statute⁴ and lacks the authority to ignore the law.

DEO has also failed to cite any case law that supports its position that would result in DEO including in rate base and recovering costs associated with facilities that are not used and useful. There is case law; however, that supports the proposition that “the test of whether the value of any given property shall be included in the rate base of the public utility is whether it is used and useful in supporting the commodity or service that the utility has undertaken to furnish.”⁵ Given that DEO does not dispute the fact that these projects were not in-service by date certain in this case, it is axiomatic that they are not used and useful. Therefore, the Commission should deny DEO recovery through the PIR Cost Recovery Charge for costs associated with projects that are not in-service as of June 30, 2009, the date certain in this case.

⁴ *Canton Storage and Transfer Co. v. Public Util. Comm.* (1995), 72 Ohio St.3d 1, 5, 647 N.E.2d 136.

⁵ *Office of Consumers' Counsel v. Public Utilities Commission of Ohio*, (1979) 58 Ohio St. 2d 44.

Instead of reliance on the law to make its case, DEO looks to documents in the case to support its unlawful position. DEO states that pursuant to the Stipulation and Recommendation (“Stipulation”) from DEO’s Rate Case in 07-829-GA-AIR, et al.⁶ and the PIR Staff Report,⁷ neither contained language regarding plant additions * * * or set forth a recommendation regarding the determination of DEO’s PIR rate base.”⁸ DEO further reaches outside of the PIR case documents, and looks to the Rate Case Staff Report, about which DEO states: “[the Rate Case Staff Report] did address the specific components DEO is to use in its rate base calculations.”⁹ DEO states that in particular the Rate Case Staff Report relied on a Blue Ridge Consulting Services (“Blue Ridge”) Report that conducted a financial review of DEO’s rate case application.¹⁰

However, any attempt by DEO to suggest that processes that were deemed appropriate by Blue Ridge for establishing plant additions in the DEO rate case should also be appropriate for the PIR program is unfounded. The reason is that there is no record evidence in this case that demonstrates that the Commission ever approved the inclusion of property that was not used and useful in rates even if DEO included it in its rate application.¹¹ In this case; however, there are specific identified projects for which DEO seeks recovery associated with these projects in plant additions that were not in-service, and hence not used and useful, as of the June 30, 2009 date certain, in this case.

⁶ DEO Ex. No. 7.

⁷ Staff Ex. No. 2.

⁸ DEO Brief at 12.

⁹ DEO Brief at 12.

¹⁰ DEO Brief at 12-13.

¹¹ Staff Brief at 16-17.

The Commission should exclude the costs for those projects from DEO's PIR Cost Recovery Charge.

Further, DEO has unreasonably argued that its treatment of plant additions is consistent with the Federal Energy Regulatory Commission ("FERC") system of accounts.¹² DEO relies on 18 C.F.R. 201 at Gas Plant Instructions, (11) Work Order and Property Record System Required, subpart (B)]." According to DEO, that section states,

Each utility shall keep its work order system so as to show the nature of each addition to or retirement of gas plant, the total cost thereof, the source or sources of costs, and the gas plant account or accounts to which charged or credited. Work orders covering jobs of short duration may be cleared monthly.¹³

DEO's reliance on accounting recognition that a project is closed is unreasonable because such accounting recognition does not mean that from an engineering standpoint the facilities are actually in-service, used and useful, and that gas is flowing through the facilities serving customers.¹⁴ DEO witness Friscic, under cross-examination, admitted that such accounting treatment "has nothing to do with placing plant facilities in-service."¹⁵ Therefore, the Commission should adhere to the statutory requirement that DEO facilities must be used and useful in order for DEO to collect costs on its investments from customers. These facilities were not used and useful as of date certain and the Commission should exclude the associated costs from the PIR cost recovery charge in this case, so that customers are not charged for such costs.

¹² DEO Brief at 16.

¹³ DEO Brief at 16.

¹⁴ OCC Brief at 10; See also Staff Brief at 16.

¹⁵ Tr. Vol. I (Friscic) at 156 (October 16, 2009).

For all the reasons stated above, the Commission should deny DEO recovery of all costs associated with projects that were not in-service by June 30, 2009, the date certain in this case, because the plant additions were not used and useful. Therefore, it would be contrary to Ohio law to include such costs for recovery through DEO's PIR Cost Recovery Charge.

B. The Costs Of Curb-To-Meter Service Lines Serving New Customers Should Be Excluded From PIR Cost Recovery.

The Commission should exclude cost recovery through the PIR Cost Recovery Charge for curb-to-meter service lines to serve new customers. OCC and Staff relied on the Company's own rate case testimony on the issue of inclusion of costs of Company investment to serve new customers.¹⁶ In the rate case, DEO witness Murphy stated:

Q25. Does DEO propose to include mainline extensions needed to serve new customers in the PIR program costs to be recovered?

A25. No. DEO will recover revenues from those mainline extensions in the base rates charged to those *new customers*. In order to avoid duplicative recovery, DEO will not include the costs associated with revenue-generating mainline extensions or other revenue-generating infrastructure investments in the amounts to be recovered by the PIR Cost Recovery Charge.¹⁷

DEO argues to the contrary "that new service lines are neither [revenue-generating or infrastructure investments].¹⁸ It is unclear what they are if indeed they are not revenue-generating or infrastructure investments. DEO unfortunately does not elaborate. These

¹⁶ OCC Brief at 12-13, Staff Brief at 18.

¹⁷ Staff Ex. No. 5 (Attachment IS-2, *PIR Rate Case*, Case No. 07-828-GA-AIR, et al., Supplemental Direct Testimony of Jeffrey A. Murphy) at 12 (May 30, 2008) (emphasis added).

¹⁸ DEO Brief at 18.

are the words in Mr. Murphy's testimony, and the Company should not be permitted to retreat from that position now.

It is OCC's position that the PIR program is intended to address replacement of aging infrastructure.¹⁹ It is not to provide the Company with an alternative cost recovery mechanism for other single ratemaking issues. Therefore, the Commission should deny DEO recovery of costs associated with curb-to-meter service lines serving new customers, through the PIR Cost Recovery Charge.

C. Incremental Operation And Maintenance Expenses Should Be Excluded From PIR Cost Recovery.

Resolution of this issue should be straightforward for the Commission. The Parties to the Stipulation agreed that "the Staff Report's recommendations with regard to the [PIR] Application in Case No. 08-169-GA-ALT shall be adopted * * *."²⁰ The Staff has been unwavering in terms of its stated intention, based upon the language that was used in the Staff Report, to disallow DEO to recover incremental O&M expenses from the PIR Cost Recovery Charge.²¹ Nearly five-hours and 100 pages of transcribed DEO cross-examination of Staff witness Adkins did not elicit a hint of a doubt about Staff's position on this issue.²² DEO's arguments contained in its brief are merely an attempt to obfuscate this issue, and reinterpret the Staff Report in a self-serving manner that supports DEO's position.²³ The Commission should disregard DEO's unreasonable

¹⁹ OCC Ex. No. 2 (Supplemental Direct Testimony of Vicki Friscie) at 5, See also DEO Ex. No. 13 at 1-2.

²⁰ DEO Ex. No. 7 at 8.

²¹ Staff Ex. No. 1 (Comments) at 9-10; See also Staff Brief at 18-25.

²² Tr. Vol. II (Adkins) at 40-144 (October 19, 2009).

²³ DEO Brief at 19-25.

arguments because the Staff is in the unique position to authoritatively and with assurance explain what it intended within the PIR Staff Report.

DEO unreasonably argues that incremental O&M expenses are included as part of a regulatory asset that was proposed in DEO's PIR Application.²⁴ Staff witness Soliman explained the accounting for a regulatory asset as follows:

[a] regulatory asset is the object of the amortization and not depreciation expense. * * * When the amortization [depreciation] is recorded in the income statement, it becomes depreciation expense, and when the amortization is deferred and recorded in the balance sheet, it becomes a regulatory asset. The deferral creates the asset.²⁵

DEO has not deferred the incremental costs in question, but instead has proposed the immediate expensing of these costs in the year they were incurred; therefore, the incremental costs in question could not become part of the regulatory asset as DEO argued.

Further, DEO has improperly argued that OCC did not oppose the recovery of incremental O&M expenses.²⁶ DEO bases its argument on OCC's Comments²⁷ and withdrawal of one comment²⁸ that were filed by OCC in this case.²⁹ However, on cross-examination, DEO witness Friscic stated that OCC had not expressed to her its position on incremental O&M expenses:

²⁴ DEO Brief at 19.

²⁵ Staff Brief at 7-8.

²⁶ DEO Brief at 20.

²⁷ OCC EX. No. 2 (Comment) at 8.

²⁸ OCC Ex. No. 3 (Withdrawal of One Comment).

²⁹ DEO Brief at 20.

- Q. Ms. Friscic, if you would turn to page 2 of your [supplemental] testimony -- And in your answer No. 5 there was some discussion of OCC's comments; do you see that?
- A. Yes, I do see that.
- Q. And your understanding of OCC's comments is speculation, is it not?
- A. It is DEO's view of OCC's comments and what they mean.
- Q. And no one from OCC has told you that was their position.
- A. Correct.
- Q. And if you would turn to page 10 of your [supplemental] testimony, lines 7 to 10. Are you there?
- A. I am.
- Q. In there you are making a comment about OCC's Comments, are you not?
- A. I am. It's DEO's view that OCC's failure to recommend the exclusion of incremental O&M can be interpreted as support for inclusion of the O&M.
- Q. And no one from OCC has told you that was their position, have they?
- A. That's correct.
- Q. And if you would turn to page 16 of your [supplemental] testimony, your question and answer 31 through 33.
- A. Yes.
- Q. You're addressing OCC comment No. 4 in there, are you not?
- A. I am.
- Q. And your answer 33 is a statement regarding whether or not the Envista expenses should have been included in incremental O&M; is that the issue?

A. That's true. In the answer to 33 we're stating our support for why Envista subscription service should, in fact, be included in incremental O&M. Since it's incremental, it would not have been incurred but for the PIR program.

* * *

Q. You've stated that OCC has agreed to the recovery of incremental expenses as part of the stipulation underlying the PIR cost recovery charge, the last statement in lines 16 through 18.

A. That's correct.

Q. And no one from OCC has said that to you, have they?

A. Correct, no one from OCC has said that,

* * *

DEO has provided no evidence to support its speculation as to OCC's position.

Moreover, even assuming that DEO's position has merit, this does not establish the burden of proof necessary to support DEO's position. Rather, DEO's claim regarding the OCC position is nothing more than a poor attempt to obfuscate the lack of proof that the Company has presented. Therefore, the PUCO should accept OCC's position as set forth in its brief, and any attempt by DEO to suggest otherwise should be disregarded by the PUCO.

OCC's position as stated in its brief on this issue is that the Commission should disallow recovery of the \$1.1 million in incremental O&M expenses through the PIR cost recovery charge that customers pay.³⁰ As a subordinate proposal, OCC recommended that, if and only if the PUCO determined that these incremental costs should be

³⁰ OCC Brief at 14-19.

authorized for recovery, then the incremental costs should be capitalized rather than expensed.³¹

D. The PIR Cost Recovery Charge Should Be Calculated With Appropriate Savings Relative To A Baseline Level Of Expenses For Customers.

The PIR Program is a generous program in which the Company is rewarded with more timely recovery of its costs thus dramatically reducing the regulatory lag. Without the benefit of the PIR program, DEO would be forced to confront the financial implications of this capital program in another manner (e.g. seek rate relief in the form of rate case filings pursuant to R.C. 4909.18 and R.C. 4009.19). However, this claim flies in the face of the fact that in the 13 years between 1994 and 2006, DEO incurred distribution plant additions of approximately \$629 million, in total, or averaged about \$48 million each year since the last rate case.³² The Company managed the regulatory lag without filing for rate relief during that 13-year period. That best summarizes what the PIR Program offers DEO; however, what is in it for DEO's customers?

Customers were promised the opportunity of significant O&M expense savings as a result of the implementation of the PIR Program. In the Company's 08-169 Application, DEO cited the \$8.5 million in O&M savings to date that Duke's customers have realized, and stated: "DEO also anticipates *significant benefits from a reduced incidence of leak repair expenses*, and like Duke will credit savings in avoided O&M

³¹ OCC Brief at 19-20.

³² DEO Ex. No. 8 (Blue Ridge Consulting Report) at 78.

costs to customers.”³³ The issue before the Commission is how best to calculate the savings to assure customers achieve the benefit promised.

The Company suggests that in exchange for the recovery of and recovery on the \$90.3 million in plant additions in this case, customers should be satisfied with approximately \$85,000 in O&M savings.³⁴ DEO’s proposed calculation nets the result of the baseline expense level of the four identified components to the test year expense level of these same components.³⁵ OCC finds this level of savings to be meager at best.

Staff has proposed a calculation of baseline savings that will enhance the level of O&M savings to approximately \$550,000.³⁶ In part, the Staff’s methodology is in response to a concern that the Company is unable to more definitively testify as to when recognition of anticipated baseline savings will be achieved.³⁷ The Staff’s argument is that DEO’s inability to articulate when savings will be achieved runs counter to a fundamental premise underlying both the Company’s annual PIR applications and the Commission’s approval of PIR recovery (i.e., that the accelerated replacement of aging infrastructure would reduce leaks and corrosion problems thereby generating O&M savings that would benefit customers and partially offset the costs of the program).³⁸ The Staff’s savings calculation was described as follows:

Rather than performing an overall netting of the cost accounts as DEO has done, which again would allow an increase in costs in one category to swallow up savings in the other expense categories, Staff witness Adkins has proposed that each of the

³³ DEO Ex. No. 13 (08-169 Application) at Paragraph 6, page 3 (emphasis added) (February 22, 2008).

³⁴ DEO Brief at 25-29.

³⁵ DEO Brief at 26-27.

³⁶ Staff Brief 29-30.

³⁷ Staff Brief at 28; See also, Staff Ex. No. 1 (Comments) at 11.

³⁸ Staff Brief at 28; See also, Staff Ex. No. 1 (Comments) at 11.

accounts be considered individually and, where test year costs in any amount exceed the agreed-upon baseline cost, that that account simply be set at zero. The Staff's approach is superior because it maximizes customer savings, and in this case, results in a revised cost savings calculation of \$554,300 for the test year. This is the amount of savings that Staff advocates be passed on to customers for this review period.³⁹

Therefore, the Staff's methodology for calculating the baseline O&M savings more appropriately balances the recognition of such savings taking into account the control that the Company has in determining the timing and magnitude of these savings. The Staff's approach more appropriately protects consumers from the potential eventuality that a single component of test year expense could dwarf the other baseline expense components when netted against each other resulting in no customer savings.

Additionally, DEO's decision to place transmission projects ahead of the distribution projects (that would have the greatest impact on leak reductions) directly influenced and reduced the amount of baseline savings that DEO could pass back to consumers. Despite the fact that DEO stated in testimony, during the rate case proceeding, its transmission and distribution system was deemed safe today and would be safe tomorrow,⁴⁰ the Company nevertheless decided to replace the transmission facilities ahead of distribution facilities for safety reasons. Such action by the Company is yet another factor that negatively impacted the resulting savings calculation proposed by DEO. Therefore, the Commission should adopt the Staff's proposal for calculating savings in this case, and in DEO's future PIR Cost Recovery Cases.

³⁹ Staff Brief at 29-30.

⁴⁰ *In re DEO Rate Case*, Tr. Vol. II (McNutt) at 60-71 (August 6, 2008).

E. The PIR Cost Recovery Charge Should Not Be Overstated Due To A Delay In Reporting Retirements.

OCC raised a concern, in its Comments, regarding a potential lag in the process by which DEO recognizes certain plant retirements.⁴¹ Timely reporting of plant retirements is important to residential customers because retirements reduce the costs in rate base and thus should reduce what customers would pay in rates. DEO argued on brief as follows:

Similarly, DEO's PIR Cost Recovery Charge implements the same methodology for retiring assets that DEO used in calculating its base rates. Again, however, despite the fact that Staff raised no objection to the use of this methodology in the rate case. Staff and OCC now speculate that the methodology is somehow flawed and improperly delays retirements (although neither Staff nor OCC placed any evidence in the record regarding the alleged amount of improper delay). Having already approved DEO's treatment of blanket work orders and retirements, *Staff and OCC are wrong to now seek to collaterally attack their, and the Commission's, prior approval of these methodologies.*⁴²

To the extent that DEO relies on its arguments made in the plant additions Section A of the Reply Brief supra, those same arguments will not be revisited here. However, contrary to DEO's argument on brief, OCC is not collaterally attacking the Commission's prior approval of methodologies.

What has transpired is that OCC noted an approximately \$600,000 discrepancy between the plant retirements reported in the Company's Notice of Intent and in its PIR Application.⁴³ DEO witness Friscie filed supplemental testimony on October 9, 2009, offering the following explanation:

⁴¹ OCC Ex. No. 2 (Comments) at 9 (emphasis added).

⁴² DEO Brief at 11-12.

⁴³ OCC Ex. No. 2 (Comments) at 9.

DEO disagrees with OCC Comment [regarding a delay in reporting plant retirements] because DEO's Notice of Intent was intended as an estimate. DEO's PIR Cost Recovery Charge Application included actual expenses and adjustments, including plant retirements. DEO's Application has been the subject of extensive investigation and audit. OCC has not suggested that it has uncovered any accounting error that would delay the recognition of retirements. DEO does not believe that a systematic accounting problem exists. DEO, however, committed to cooperate with OCC by addressing its concerns regarding the timely processing of retirements associated with the PIR program with its Operations and Accounting departments.⁴⁴

DEO's explanation might appear plausible in a vacuum. However, Staff witness Soliman, in his Testimony filed on October 14, 2009, included the following question and answer.

Q. Does the Staff have any other concerns?

A. Yes. It appears that additional PIR plant retirement should be recognized in the calculation of the final PIR rates. The Staff received information on October 6, 2009 after the issue of its comments indicating that additional retirements related to the date certain PIR projects were not included in the Company's application. The Staff recommends that the Company provides the additional retirements data as soon as possible to the Commission Staff for the final determination of the PIR rates.⁴⁵

The information that Staff was provided appears to conflict with the Company's assurances contained in DEO witness Friscie's testimony. It is OCC's position that the Commission should assure that DEO is required to properly record the plant retirements in the calculation of its PIR Cost Recovery Charge.

⁴⁴ DEO Ex. No. 2 (Supplemental Direct Testimony of Vicki Friscie) at 17.

⁴⁵ Staff Ex. No. 5 (Prefiled Testimony of Ibrahim Soliman) at 9.

Therefore, OCC recommended on brief that the Commission order DEO to finalize the analysis of plant retirements in this case, and provide all interested parties with the analysis, additional time to review the analysis including discovery if needed, and if necessary, reopen the proceedings prior to the effective date of the PIR cost recovery charge.⁴⁶ Such a process will assure that all interested parties have an opportunity to be heard on this issue.

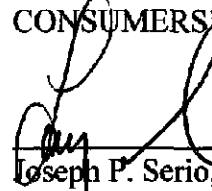
III. CONCLUSION

The Commission should reduce the PIR Cost Recovery Charge in accordance with the preceding arguments. To accomplish this result, the Commission should deny DEO the authority to include the costs associated with plant additions for projects that are not in-service, or for facilities built to serve new customers from whom DEO obtains additional revenues. The Commission should also deny DEO the authority to recover incremental O&M expenses. In addition, the Commission should adopt the Staff's methodology for calculation of the baseline savings in order for customers to achieve the benefits from the PIR Program that were promised. Finally, the Commission should preclude DEO from delaying the booking of plant retirements. Should the Commission adopt OCC's recommendations, in this case, that will reduce DEO's proposed PIR Cost Recovery Charge, and thereby reach a just and reasonable result.

⁴⁶ OCC Brief at 29-33.

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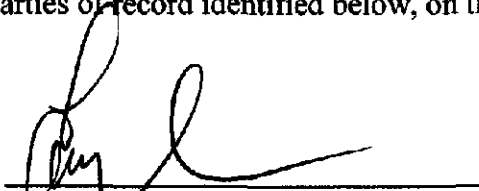
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CERTIFICATE OF SERVICE

I hereby certify that a copy of the Office of the Ohio Consumers' Counsel's *Reply Brief* was served via electronic mail, to the parties of record identified below, on this 12th day of November 2009.



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