BEFORE THE
PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company and The Toledo Edison Company for Authority to Provide for a Standard Service Offer Pursuant to R.C. 4928.143 in the Form of an Electric Security Plan	Case No. 14-1297-EL-SSO

POST-REHEARING BRIEF OF OHIO EDISON COMPANY, THE CLEVELAND ELECTRIC ILLUMINATING COMPANY, AND THE TOLEDO EDISON COMPANY

TABLE OF CONTENTS

Page

TABLE OF CONTENTS
(continued)

Page

I. INTRODUCTION

The Commission already has approved, with modifications, the fourth Electric Security Plan ("ESP IV") of Ohio Edison Company ("Ohio Edison"), The Cleveland Electric Illuminating Company ("CEI") and The Toledo Edison Company ("Toledo Edison") (collectively, the "Companies").[1] The ESP IV, as modified and approved by the Commission, provides customers:

- reliable, reasonably priced electric service;
- the benefits of market-based pricing while avoiding the full effect of market risks;
- the benefits of economic development; and
- the wise use of our natural resources through increased energy efficiency, use of renewable power and reduced emissions from power plants.

One important component of ESP IV is the Retail Rate Stability rider ("Rider RRS"), which the Commission found would "protect consumers against rate volatility and price fluctuations by promoting rate stability."[2]

The Companies sought rehearing of the March 31 Order because, in part, the Commission's modifications to Rider RRS were unreasonable. Yet, in an effort to save all the time and effort of the parties and the Commission in this proceeding to date, the Companies proposed in their Application for Rehearing to modify the calculation of the costs and revenues that flow through Rider RRS (the "Proposal"). Several intervenors took a contrary path, urging that Rider RRS be eliminated altogether and thereby putting the entirety of ESP IV at risk.[3] The

---

[1] *See* March 31, 2016 Opinion and Order ("March 31 Order").

[2] March 31 Order, p. 79.

[3] *See*, *e.g.*, PJM Power Providers Group and Electric Power Supply Association (collectively, "EPSA") AFR, pp. 22-23, 71-75; Dynegy, Inc. ("Dynegy") AFR, pp. 2-6; Ohio Consumers' Counsel and Northwest Ohio Aggregation Coalition ("OCC/NOAC") AFR, pp. 28, 39, 45; Northeast Ohio Public Energy Council ("NOPEC") AFR, p. 18; Environmental Law and Policy Center, Ohio Environmental Council, and Environmental Defense Fund

Commission found sufficient reason to grant all applications for rehearing, and it held rehearing to consider the Companies' Proposal and alternatives to the Proposal.[4] Thus, the scope of rehearing is limited. On rehearing, the Commission must address the merits of the Proposal, as well as the Staff's alternative proposal of a Distribution Modernization Rider ("Rider DMR") and associated conditions (the "Staff Proposal").

The Commission should approve the Companies' Proposal. By adopting the Proposal, the Commission will allow ESP IV, as modified, to provide all the rate stabilization benefits recognized in the March 31 Order. This will preserve the benefits of ESP IV as previously determined by the Commission, without reliance on a purchase power agreement ("PPA") or any other contractual arrangement or involvement of FirstEnergy Solutions Corp. ("FES").[5] By eliminating the PPA from the calculation, the Proposal moots many of the concerns raised by intervenors in their applications for rehearing.[6] Importantly, the Commission and all interested parties already spent much time and effort over many months in prior hearings to approve an ESP with many substantial benefits for customers and the state of Ohio. The Proposal is a simple solution that ensures the Commission can preserve all the benefits of ESP IV without revisiting the entire ESP process.

Additionally, by fixing the cost side of the hedge, Rider RRS as modified by the Proposal "will have fewer moving parts and, thus, will present less risk to customers."[7] And because the

---

(collectively, "ELPC") AFR, pp. 3-12; The Ohio Manufacturers' Association Energy Group ("OMAEG") AFR, pp. 26-30; The Retail Energy Supply Association ("RESA") AFR, pp. 22-26, 89-90.

[4] *See* May 2, 2016 Entry on Rehearing, pp. 2-3 ("First Entry on Rehearing"); July 6, 2016 Third Entry on Rehearing, ¶¶ 25, 30 ("Third Entry on Rehearing").

[5] Rehearing Testimony of Eileen M. Mikkelsen ("Mikkelsen Rehearing Test."), pp. 4, 6.

[6] *See* note 3, *supra*.

[7] Mikkelsen Rehearing Test., p. 4.

hedging function will be provided by the Companies, they will be able to use Rider RRS revenues to support other ESP IV initiatives, including: modernizing the Companies' distribution grid through advanced metering infrastructure, distribution automation, and Volt/VAR controls; investing in battery resources; and investing in new Ohio renewable resources.[8] The Proposal is a win-win for customers and the state of Ohio.

The rehearing record also showed that Rider DMR, if properly designed, would also benefit the public.[9] According to Staff witness Choueiki, Rider DMR is intended to assist the Companies receive more favorable terms when accessing the capital market, which will enable the Companies to procure funds to jumpstart their distribution and grid modernization initiatives or to evaluate and possibly integrate battery technology into their distribution system.[10] Grid modernization "will benefit customers and competitive suppliers by enabling an array of innovative products and services."[11] In order for Rider DMR to have its intended effect, however, the calculation of the annual Rider DMR revenue amount should be modified to include: (1) a 15 percent target for Cash Flow from Operations pre-Working Capital ("CFO") to Debt; (2) a three-year average from 2012-14; (3) a pre-tax gross up; and (4) an allocation factor for the Companies of 40 percent.[12] The Commission also should modify the Rider DMR revenue amount to properly reflect the economic development and job retention conditions associated with the FirstEnergy

---

[8] Mikkelsen Rehearing Test., pp. 5, 12.

[9] Rehearing Rebuttal and Surrebuttal Testimony of Eileen M. Mikkelsen ("Mikkelsen Rehearing Rebuttal Test."), p. 5.

[10] Rehearing Testimony of Hisham M. Choueiki ("Choueiki Rehearing Test."), p. 15; Mikkelsen Rehearing Rebuttal Test., p. 5.

[11] Mikkelsen Rehearing Rebuttal Test., p. 6.

[12] Mikkelsen Rehearing Rebuttal Test., pp. 9-13.

Corp. corporate headquarters and nexus of operations proposed by Staff.[13] The annual Rider DMR revenue amount should be $558 million to provide credit support, plus an additional amount determined by the Commission to reflect the economic development value of the rider.[14] Although Rider RRS provides the greatest benefit to customers,[15] the Staff Proposal, with these improvements, has merit.[16]

Therefore, the Commission should determine on rehearing that the Companies' Proposal is beneficial for customers and approve the proposed modifications to Rider RRS. In the alternative, it would not be unreasonable for the Commission to approve a properly designed Rider DMR.

II. DISCUSSION

A. The Commission Should Approve the Companies' Proposal.

1. The Proposal maintains the Commission-approved hedge and modifies the calculation of the costs and revenues reflected in Rider RRS.

Under the Proposal, the Companies will use record evidence already relied on by the Commission in this case to modify the cost, output and cleared capacity assumptions in the Rider RRS calculation.[17] In particular, replacing actual costs with the cost assumptions currently in the record ensures that Rider RRS contains only the costs that the Commission relied on in determining that Rider RRS was reasonable. The assumed costs are representative proxies for

---

[13] *See* Mikkelsen Rehearing Rebuttal Test., p. 13-15. In addition to the economic development and job retention benefits associated with these conditions, Rider DMR provides additional benefits related to spending on human resources and equipment, having a modernized grid, and reduced outages and improved reliability. Rehearing Tr. Vol. X, p. 1818 (Mikkelsen Redirect).

[14] Mikkelsen Rehearing Rebuttal Test., pp. 14-15.

[15] Rehearing Tr. Vol. X, p. 1698 (Mikkelsen Cross) ("The Companies looked at the Proposal in the context of the entirety of the ESP and all of the provisions of the ESP, and concluded that the Proposal was more beneficial to the Companies, customers and the state of Ohio than Rider DMR.").

[16] Mikkelsen Rehearing Rebuttal Test., pp. 4, 5.

[17] *See* Mikkelsen Rehearing Test., pp. 5, 8.

fuel-diverse baseload generation in the region.[18] The EDU team did extensive due diligence on the costs and concluded that the costs are representative of nuclear and coal plant costs.[19] The costs are known and fixed for the eight-year term of ESP IV.[20] This modification addresses a number of stakeholder concerns by removing the variability that was inherent in the original hedge proposal. Moreover, the modification makes Rider RRS a more reliable hedge insomuch as it focuses only on actual changes in energy and capacity prices.[21]

Actual generation output (MWhs) will be replaced with the previously-projected proxy generation output, and actual capacity (MWs) cleared in the PJM capacity market will be replaced with the proxy capacity projected to clear.[22] Both inputs are already evidence of record and relied upon by the Commission in this case.[23] The capacity projected to clear for the first three years is cleared capacity shown in Figure 5 of the Companies' Reply Brief, and for the remaining years of ESP IV is the projections included in the case.[24] In contrast to Rider RRS as originally proposed, Rider RRS charges and credits under the Proposal will not be based on the generation output of specific generating plants.[25] This reduces certain potential risks that could have arisen by any differences between actual and assumed values. Under the Proposal, the projected performance of the proxy generation will be locked in.

---

[18] Rehearing Tr. Vol. I, pp. 161-62 (Mikkelsen Cross).

[19] Rehearing Tr. Vol. I, p. 162 (Mikkelsen Cross). *See* Direct Testimony of Jay Ruberto, p. 5 (Aug. 4, 2014); Hearing Tr. Vol. XIII, pp. 2773-74, 2887-88 (Ruberto Cross); Sierra Club Ex. 37C.

[20] *See* Rehearing Tr. Vol. I, pp. 54-55 (Mikkelsen Cross), and Sierra Club Ex. 89.

[21] Rehearing Tr. Vol. II, p. 127 (Mikkelsen Cross).

[22] Mikkelsen Rehearing Test., pp. 5, 8.

[23] Mikkelsen Rehearing Test., p. 5.

[24] Rehearing Tr. Vol. I, pp. 193-94 (Mikkelsen Cross).

[25] Rehearing Tr. Vol. I, pp. 50, 162 (Mikkelsen Cross); Mikkelsen Rehearing Test., pp. 5-6.

Also, there will be no need to reconcile costs included in Rider RRS; they will not change from the projections in the record.[26] Nor will reconciliation of capacity revenues be necessary, since both the MWs of capacity cleared and the capacity price will be known at the time the annual Rider RRS charge or credit is set.[27] Other than reconciling actual sales and billing demands with projected amounts, only energy revenues will need to be reconciled to actual energy pricing in the quarterly true-up required by the Commission's March 30 Order.[28] Again, this further reduces risk by locking in the projected costs of the proxy generation.

2. The Proposal does not modify any of the provisions the Commission relied upon in making its decision that ESP IV is more favorable than an MRO.

The Proposal maintains the benefits of the Commission-approved Rider RRS. While the Proposal consists of a few modifications to the calculation of the charges and credits included in Rider RRS,[29] the purpose of Rider RRS has not changed – to protect customers during periods of higher prices, with the understanding that Rider RRS will be a charge if market prices are low.[30] And, because the Proposal is designed to produce the same or very similar retail price stability results for customers, the Proposal does not affect the Commission's prior determination that "Rider RRS will generate $256 million in net revenue [*i.e.*, net credits to customers] over the

---

[26] Mikkelsen Rehearing Test., p. 8.

[27] Mikkelsen Rehearing Test., p. 8.

[28] Mikkelsen Rehearing Test., pp. 7, 8. *See* March 31 Order, p. 90. Rider RRS initially would be set each year using average monthly on-peak and off-peak energy forwards for the AEP-Dayton ("AD") Hub posted on the Intercontinental Exchange. Mikkelsen Rehearing Test., p. 8. The Companies would reconcile energy revenues on a quarterly basis using the actual monthly average on-peak and off-peak day-ahead locational marginal prices at the AD Hub. *Id.*, p. 7. The Commission also could decide that this reconciliation occur annually. *See* Direct Testimony of Joanne M. Savage, p. 3 (Aug. 4, 2014) ("Rider RRS will be updated and reconciled on an annual basis.").

[29] Rehearing Tr. Vol. I, pp. 159, 160 (Mikkelsen Cross).

[30] Rehearing Tr. Vol. I, p. 128 (Mikkelsen Cross). *See* March 31 Order, p. 118 ("the evidence in the record demonstrates that Rider RRS will promote rate stability by providing a credit if and when energy prices increase").

eight-year term of ESP IV."[31] Moreover, all five qualitative benefits of ESP IV relied upon by the Commission in its March 31 Order remain unchanged.[32] Because the quantitative and qualitative factors the Commission relied upon to approve ESP IV have not changed, it is not necessary for the Commission to reconstruct the ESP v. MRO analysis from whole cloth. The Commission can simply find that ESP IV, as modified by the Proposal, continues to be more favorable in the aggregate compared to the expected results of an MRO.[33]

a. Rider RRS will continue to protect customers against rate volatility and retail price increases.

In approving Rider RRS in the March 31 Order, the Commission found that: (1) the Companies' customers are exposed to market risk tied to the volatility and fluctuation in retail electric prices;[34] and (2) Rider RRS will promote rate stability by protecting customers against that rate volatility and price fluctuations.[35] These findings, which were based on the Commission's view of energy and capacity price forecasts, are unaffected by the Proposal for the simple reason that the modifications to Rider RRS included in the Proposal have no impact on energy and capacity prices. Instead, the Proposal simply sets three Rider RRS inputs – cost, generation output and cleared capacity – at the levels relied upon by the Commission in approving Rider RRS.[36]

---

[31] March 31 Order, p. 118; Mikkelsen Rehearing Test., p. 18.

[32] March 31 Order, p. 119. Staff witness Turkenton agreed that the qualitative benefits of ESP IV relied on by the Commission have not been changed by the Companies' Proposal. Rehearing Tr. Vol. II, p. 479.

[33] Mikkelsen Rehearing Test., pp. 18-21. *See* Hearing Tr. Vol. X, p. 1682 (Mikkelsen Cross) ("All of the qualitative and quantitative benefits relied upon by the Commission in reaching its determination about the ESP versus MRO test remain intact under the Companies' Proposal.").

[34] March 31 Order, pp. 79-83; *id.*, p. 83 ("The Commission does not believe that the evidence supports OCC and NOPEC's prediction that we have entered a period of energy price utopia"); Rehearing Tr. Vol. II, p. 372 (Baron Cross) (customers are exposed to market risk).

[35] March 31 Order, pp. 78-79, 118.

[36] Mikkelsen Rehearing Test., pp. 5-6.

By fixing these inputs, as OEG witness Baron calculated, Rider RRS "essentially provides a fixed price for the generation component for 40 percent of a customer's usage."[37] Put another way, Rider RRS provides "a scheduled fixed price for the eight years" of ESP IV.[38] In Mr. Baron's rehearing testimony, he calculated the stable costs of Rider RRS for each year of ESP IV against which energy and capacity prices are hedged.[39] These costs already were reviewed by the Commission in its March 31 Order when approving Rider RRS and determining that it would provide a $256 million benefit to customers.[40] Thus, the Commission's findings with regard to the purpose and benefits of Rider RRS are unaffected by the Proposal.

b. All other factors the Commission relied upon in approving ESP IV as more favorable than an MRO are unaffected by the Proposal.

In addition to the benefits attributed to Rider RRS by the Commission – rate stability and $256 million in net credits over the eight-year term of ESP IV[41] – all other benefits relied upon by the Commission in approving ESP IV will be maintained under the Proposal.[42] The Order recognized an additional $51.1 million in quantitative benefits from shareholder funding for economic development, low-income customers and a customer advisory agency, all of which are

---

[37] Rehearing Tr. Vol. II, p. 352.

[38] Rehearing Tr. Vol. II, p. 371. *See also id.*, p. 398.

[39] Rehearing Testimony of Stephen J. Baron ("Baron Rehearing Test."), p. 7, Figure 3; Rehearing Tr. Vol. II, p. 394.

[40] March 31 Order, pp. 78, 80-81; Mikkelsen Rehearing Test., p. 6; Rehearing Tr. Vol. II, p. 385 (Baron Cross).

[41] March 31 Order, p. 118. Although the Commission also had before it evidence showing that Rider RRS would provide transmission cost, resource diversity and economic development benefits, the Commission expressly disclaimed reliance on that evidence when approving ESP IV. *Id.*, p. 87. The Commission approved Rider RRS solely as a retail hedge based upon retail ratemaking authority under state law. *Id.*, p. 86. The Commission made no mention of these additional benefits when conducting its ESP v. MRO test. March 31 Order, pp. 118-20.

[42] All of these ESP IV benefits are flowing to customers today, with the Proposal designed to provide the equivalent value to customers as envisioned by the Third Supplemental Stipulation. *See* Third Supp. Stip. ¶ V.B.3.c.

unchanged under the Proposal.[43] Thus, the Proposal does not alter the Commission's finding that ESP IV, on a quantitative basis, is \$307.1 million more favorable than an MRO.[44] Notably, Staff's rehearing testimony did not present any quantitative analysis that suggests the Companies' Proposal changed the Commission's prior quantitative analysis of the ESP v. MRO test.[45]

The Proposal also does not affect the five qualitative benefits recognized by the Commission in its March 31 Order: (1) continuation of the distribution rate increase freeze until June 1, 2024; (2) continuation of multiple rate options and programs to preserve and enhance rate options for various customers provided in previous ESPs; (3) establishment of a goal to reduce CO2 emissions by FirstEnergy Corp. with periodic reporting requirements; (4) reactivation and expansion of energy efficiency programs previously suspended by the Companies, with a goal of saving 800,000 MWh of energy annually; and (5) programs to promote the use of energy efficiency programs by small businesses pursuant to state policy set forth in R.C. 4928.02(M).[46] Staff witness Turkenton agreed that none of the qualitative factors relied on by the Commission have been changed by the Companies' Proposal.[47] Indeed, as Company witness Mikkelsen testified, the Proposal enhances the qualitative benefits of ESP IV by providing even greater rate stability to customers.[48] That rate stability, in turn, has economic development benefits "which

---

[43] March 31 Order, pp. 118-19; Mikkelsen Rehearing Test., p. 19.

[44] March 31 Order, p. 119.

[45] Rehearing Tr. Vol. II, pp. 478-79 (Turkenton Cross).

[46] March 31 Order, p. 119. Company witness Mikkelsen testified that nothing in the Proposal changes the base distribution rate freeze included in ESP IV. Rehearing Tr. Vol. I, p. 201.

[47] Rehearing Tr. Vol. II, p. 479. *Accord* Mikkelsen Rehearing Test., pp. 19-20 ("the modified Rider RRS calculation does not impact any of the other qualitative benefits of Stipulated ESP IV relied upon by the Commission in its Order").

[48] Mikkelsen Rehearing Test., p. 19.

will contribute to the overall vibrancy of our service territory."[49] Thus, the Proposal does not alter the Commission's finding that ESP IV, including its pricing and all other terms and conditions, is more favorable in the aggregate than would otherwise apply under an MRO.[50]

Indeed, all other elements of ESP IV, as modified by the March 31 Order, remain unchanged by the Proposal, including the Commission-ordered mechanism limiting average customer bills. As explained by Ms. Mikkelsen:

> The Companies will remain obligated to fulfill the remaining terms, conditions, and commitments set forth in Stipulated ESP IV, as approved. And the multiple quantitative and qualitative benefits of Stipulated ESP IV remain unaffected, such as the $100 million risk sharing mechanism, the grid modernization and resource diversification initiatives, the base distribution rate freeze, programs to preserve and enhance rate options for customers, and support for retail competition. Moreover, the Commission-ordered mechanism limiting average customer bills will provide additional customer protections.[51]

There also are no proposed changes to the rate design or the timing of the annual Rider RRS filing.[52] All benefits of ESP IV relied upon by the Commission continue in place under the Proposal.

c. The Commission's directives regarding review of Rider RRS will continue to apply.

The Commission directed that Rider RRS be subject to rigorous review, primarily because its charges and credits would depend in part on a PPA with an affiliate.[53] Under the Proposal, the Commission's concern is largely moot because Rider RRS no longer depends upon a PPA with

---

[49] Rehearing Tr. Vol. X, p. 1699 (Mikkelsen Cross).

[50] March 31 Order, p. 120.

[51] Mikkelsen Rehearing Test., p. 7. *See also id.*, p. 13 ("Rider RRS must be maintained to ensure all of the economic benefits and components of the Commission-approved Stipulated ESP IV remain intact.").

[52] Mikkelsen Rehearing Test., p. 7.

[53] March 31 Order, pp. 88-91.

FES. Staff nevertheless will have the opportunity to perform a rigorous review of Rider RRS under the Proposal.[54] Staff will be able to conduct its initial review of the annual Rider RRS filing for mathematical accuracy, consistency with approved rate design and incorporation of any prior audit findings.[55] Staff also will be able to conduct an annual audit of Rider RRS following completion of the final reconciliation filing.[56]

Because the Proposal simplifies Rider RRS, Staff's review also will be simplified. Staff already had the opportunity to review the plant costs filed with the case. Moreover, given that it is no longer part of the case, Staff will not need to review actual plant costs, conduct annual prudence reviews, or request information regarding the FES fleet.[57] Nor will Staff need to examine whether early retirement costs are included in the Rider RRS calculation,[58] because no retirement costs were included in the as-filed costs that will be used for Rider RRS under the Proposal.[59] In addition, the Proposal, if approved, will render moot the Commission's concerns expressed in the March 31 Order regarding bilateral affiliate transactions, jurisdictional boundaries, and market offers.[60] While the Proposal will make Staff's and the Commission's job easier, it does not alter in any way the authority of the Commission and Staff to review Rider RRS.

---

[54] Mikkelsen Rehearing Test., pp. 16-17.

[55] Mikkelsen Rehearing Test., pp. 16-17

[56] Mikkelsen Rehearing Test., p. 17.

[57] Mikkelsen Rehearing Test., p. 17.

[58] *See* March 31 Order, p. 92.

[59] Mikkelsen Rehearing Test., p. 17.

[60] March 31 Order, pp. 86-87, 90, 91-92.

3. Commission approval of the Proposal will provide substantial benefits to customers and Ohio.

a. The Proposal will result in timely implementation of all aspects of the Commission-approved ESP IV.

An obvious benefit of the Proposal is that it avoids the delay resulting from FES obtaining approval from the Federal Energy Regulatory Commission ("FERC") of the PPA under 18 C.F.R. § 35.39(b).[61] Any such proceeding would require a lengthy time period to come to conclusion.[62] By modifying how Rider RRS charges and credits are calculated in a manner that eliminates reliance on the PPA or any other contractual arrangement or other involvement of FES, the Proposal ensures that the entire economic value of the Commission-approved ESP IV is made available in a timely manner to the Companies and their customers.[63]

b. The Proposal provides funds to the Companies that could be used to implement ESP IV provisions.[64]

Under the Proposal, revenues from Rider RRS charges will go to the Companies.[65] The Companies will be solely responsible for implementing Rider RRS.[66] The Companies intend to use Rider RRS dollars collected for their operations, *e.g.*: investments in advanced metering infrastructure, distribution automation, Volt/VAR control; investment in battery resources; investment in renewable resources; or other business purposes such as funding the pension or other operations.[67] If the Proposal is approved, then the Companies also are committed to going

---

[61] *See* Mikkelsen Rehearing Test., p. 4.

[62] Mikkelsen Rehearing Test., p. 4.

[63] Mikkelsen Rehearing Test., pp. 2, 4, 13.

[64] Mikkelsen Rehearing Test., pp. p. 5, 7, 12.

[65] Mikkelsen Rehearing Test., pp. 6-7, 11.

[66] Mikkelsen Rehearing Test., p. 11.

[67] Rehearing Tr. Vol. I, p. 58 (Mikkelsen Cross); Mikkelsen Rehearing Test., p. 12.

forward with whatever grid modernization/SmartGrid programs are authorized by the Commission.[68]

The Companies recognize that payment of credits under Rider RRS are forecasted for future years. However, because those future years also will include multiple other revenue sources, any future reduction in the revenues from Rider RRS will not affect the Companies' ability to fulfill their grid modernization commitments.[69] Revenues received by the Companies from Rider RRS could be used to fund the SmartGrid. Those investments will then generate dollars from revenue requirements arising from the SmartGrid investment (*i.e.*, return on and of those investments).[70] The Companies will also receive additional revenue from Rider DCR, shared savings, lost distribution revenue, and other elements of ESP IV.[71] Additionally, to the extent necessary, FirstEnergy Corp. (as history has shown) could provide equity to the Companies in order to maintain their investment grade status.[72]

c. The Proposal provides economic development benefits.

As Company witness Mikkelsen explained at hearing, the Companies "have always been very, very vested, very interested in the economic vitality of their service territories, . . . and that very much was an underpinning and continues to be an underpinning of the Companies' proposal."[73] Rider RRS promotes economic development by mitigating future price increases and

---

[68] Rehearing Tr. Vol. I, p. 70 (Mikkelsen Cross). Pursuant to the Third Supplemental Stipulation, the Companies already have filed their Smart Grid Modernization Business Plan with the Commission for review and consideration. *See* Case No. 16-481-EL-UNC.

[69] Rehearing Tr. Vol. I, pp. 80-81 (Mikkelsen Cross).

[70] Rehearing Tr. Vol. I, pp. 80-81 (Mikkelsen Cross).

[71] Rehearing Tr. Vol. I, pp. 81, 85 (Mikkelsen Cross).

[72] Rehearing Tr. Vol. I, p. 85 (Mikkelsen Cross).

[73] Rehearing Tr. Vol. I, pp. 255-56. *See* Mikkelsen Rehearing Test., p. 12.

volatility.[74] "Price stability is an important consideration in site location and expansion as well as large capital investments and employment decisions."[75] As Ms. Mikkelsen explained, this predictability and certainty may have tertiary effects on existing generating plant operations, as it "may provide more certainty that customers would remain situated in our service territory or perhaps grow their load in our service territory. And to the extent that happens, I think that that may help to ensure the generation assets in the area continue to operate."[76] Thus, approval of the Proposal will contribute to the economic vitality of the region.[77]

d. By eliminating the PPA and fixing certain inputs of the Rider RRS calculation, the Proposal addresses intervenors' concerns and results in a superior Rider RRS.

The Proposal renders moot intervenors' concerns that the original Rider RRS would create unnecessary risks for customers because of the connection between Rider RRS charges and credits and a PPA. The Proposal eliminates the PPA associated with Rider RRS.[78] Under the Proposal, Rider RRS "will be solely the responsibility of the Companies."[79] The Proposal is not designed to transfer regulated revenues to FES; and, in fact, there is no mechanism within the Companies' organization that would allow them to share dollars with FES or transfer revenues or expenses to FES.[80] In addition, FirstEnergy Corp. has indicated that it is not going to make any more investments in FES going forward.[81] Thus, intervenors lack any factual basis for arguing that

---

[74] Mikkelsen Rehearing Test., p. 12.

[75] Mikkelsen Rehearing Test., p. 12.

[76] Rehearing Tr. Vol. I, pp. 51, 263.

[77] Mikkelsen Rehearing Test., p. 12.

[78] Rehearing Tr. Vol. I, p. 227 (Mikkelsen Cross); Mikkelsen Rehearing Test., pp. 4, 6, 11.

[79] Mikkelsen Rehearing Test., p. 11. *See* Rehearing Tr. Vol. I, p. 227 (Mikkelsen Cross).

[80] Mikkelsen Rehearing Test., p. 11; Rehearing Tr. Vol. I, pp. 226-27 (Mikkelsen Cross).

[81] Rehearing Tr. Vol. I, p. 158 (Mikkelsen Cross).

Rider RRS, as modified by the Proposal, violates various provisions of federal or Ohio law or will have adverse market impacts.[82]

In contrast to Rider RRS as approved, the Proposal will use the cost assumptions and generation/capacity output assumptions fixed at the levels that already are in the record.[83] As approved, the Commission's estimated $256 million benefit of Rider RRS depended in part on plant cost, generation output (MWh) and cleared capacity (MW) forecasts that would be reconciled to actual values. This created some uncertainty in the unlikely event the actual costs or output levels varied significantly from the forecast. In contrast, the Proposal sets those costs, MWhs and MWs at the levels relied upon by the Commission in approving Rider RRS.[84] Because these cost and revenue proxies are not dependent on the actual operational or market characteristics of any particular generating facilities, intervenors can no longer argue that:

- The projected costs are subject to unexpected cost pressures, such as from higher-than-anticipated environmental compliance costs or operational issues, that could be passed through Rider RRS;
- The projected generation output could be lower because of extended outages or other operational performance concerns; or
- The projected cleared capacity could be lower, because of the effect of offer strategies, performance penalties, failure of generating units to clear, or other market performance concerns.[85]

---

[82] *See, e.g.*, EPSA AFR, pp. 22-25, 71-75; Dynegy AFR, pp. 2-6, 14-16; OCC/NOAC AFR, pp. 28, 39, 45; NOPEC AFR, p. 18; ELPC AFR, pp. 3-12; OMAEG AFR, pp. 26-31, 47-51; RESA AFR, pp. 22-28, 89-90; Sierra Club AFR, p. 21; CMSD AFR, pp. 21-25

[83] Mikkelsen Rehearing Test., pp. 5-6, 8. *See* Co. Ex. 24 (OVEC costs, MWh and MW); Co. Ex 25 (Sammis and Davis-Besse costs, MWh and MW); Sierra Club Ex. 89 (aggregate costs); Figure 5 and fn. 328 in Companies' Post Hearing Reply Brief (Feb. 26, 2016) (summarizing capacity MW and revenues for 2016/17, 2017/18 and 2018/19 Planning Years).

[84] Mikkelsen Rehearing Test., pp. 5-6.

[85] Mikkelsen Rehearing Test., pp. 5-6.

Because the only components of Rider RRS that will be subject to change are day-ahead energy prices and actual capacity prices (starting with the 2020-2021 Delivery Year), the Proposal provides customers the hedge benefits recognized in the March 31 Order without bearing the risk of changes in generating costs, operating levels, or any other operational or market performance risk.[86] As modified and improved by the Proposal, Rider RRS should provide a more reliable hedge against increasing market prices.[87]

e. Multiple customer groups support the Proposal.

The Proposal is supported by nearly all of the Signatory Parties to Stipulated ESP IV: Ohio Power Company; Ohio Energy Group ("OEG"); City of Akron; Council of Smaller Enterprises; Cleveland Housing Network; Consumer Protection Association; Council for Economic Opportunities in Greater Cleveland; Citizens Coalition; Nucor Steel Marion Inc.; Material Sciences Corporation; The Association of Independent Colleges and Universities of Ohio; the International Brotherhood of Electrical Workers – Local 245; Ohio Partners for Affordable Energy; EnerNOC; and Interstate Gas Supply, Inc.[88] Of the remaining Signatory Parties, The Kroger Co. does not oppose the Proposal, and Staff is recommending that the Commission deny the Proposal in favor of an alternative.[89] The Companies discussed the Proposal with Signatory Parties prior to its filing and shortly thereafter, and they largely were in

[86] Mikkelsen Rehearing Test., p. 6. OCC witness Wilson agreed that the Proposal eliminates certain risks inherent as part of the original Rider RRS design, such as the risks of costs increasing beyond the forecasted costs. Rehearing Tr. Vol. IV, p. 892.

[87] Mikkelsen Rehearing Test., pp. 5, 19.

[88] *See* Co. Ex. 198 (May 4, 2016 letter stating that Signatory Parties support the Proposal).

[89] Co. Ex. 198, p. 1; Choueiki Rehearing Test., pp. 13-15.

support and were anxious to expeditiously move forward with the Proposal in order to bring closure to the ESP IV proceeding.[90]

f. Staff's opposition to the Proposal is unreasonable.

Staff's belated opposition to the Proposal is surprising, given that Staff supported Stipulated ESP IV with the original Rider RRS and that the Proposal provides equivalent value within the spirit of Stipulated ESP IV.[91] Staff witness Choueiki offered two reasons for Staff's opposition, but neither holds water. First, he stated that the removal of a PPA as support for Rider RRS eliminates the resource diversity and economic benefits that the Commission "highlighted" in the March 31 Order.[92] This ignores the Commission's express statement that its decision "does not turn on such issues."[93] While the Commission may have mentioned certain ancillary benefits of Rider RRS in its order (to say they were "highlighted" is an overstatement), it made clear that its approval of Rider RRS was based on its retail ratemaking authority to approve a hedge in order to promote retail rate stability.[94] Staff's change of heart ignores that the Commission did not mention the resource diversity or economic benefits of Rider RRS as part of its ESP v. MRO analysis.[95] Thus, Staff's first reason for opposing the Proposal lacks any reasonable basis.

Staff also opposed the Proposal because Staff believed that Rider RRS, as modified, "may potentially be construed as a transition charge."[96] Notably, Staff did not construe Rider RRS, as approved, to be a transition charge. In fact, Staff strongly supported the original Rider RRS as in

---

[90] Rehearing Tr. Vol. I, p. 239 (Mikkelsen Cross).

[91] *See* Rehearing Tr. Vol. II, p. 476 (Turkenton Cross).

[92] Choueiki Rehearing Test., p. 13.

[93] March 31 Order, p. 87.

[94] March 31 Order, pp. 86-87, 118.

[95] March 31 Order, pp. 118-20.

[96] Choueiki Rehearing Test., p. 14.

the public interest and not contrary to any important regulatory principle or practice.[97] Given that Staff did not believe that the original Rider RRS was a transition charge, Staff's contention that Rider RRS as modified by the Proposal could be a transition charge has no basis.

A hedge for market prices – with its potential for charges and credits – has no relationship to "transition revenues" authorized under R.C. 4928.38.[98] The "transition revenues or any equivalent revenues" referenced in R.C. 4928.38 allowed EDUs transitioning to market-based rates while separating their generating assets to recover the difference between their actual generating plant costs and the forecasted market value of those costs.[99] The Companies completed this transition many years ago. They transferred their generation assets in 2005 and have been offering market-based SSO pricing to their customers since 2009.[100] To the extent Rider RRS is projected to be a charge, it is not recovering the costs of any generating plants. Plainly, the Companies have no such costs to recover.

Rider RRS also is not designed to protect the Companies from the financial harm of transitioning to market rates.[101] Rider RRS does not involve any type of "transition" and does not seek to recover the Companies' generating plant costs (as none exist).[102]

Not only does Rider RRS have no potential of recovering transition costs, but its actual purpose already has been clearly defined by the Commission in the March 31 Order. Rider RRS

---

[97] Post-Hearing Brief Submitted on Behalf of the Staff of the Public Utilities Commission of Ohio, pp. 6-12 (Feb. 16, 2016); Reply Brief Submitted on Behalf of the Staff of the Public Utilities Commission of Ohio, pp. 3-12 (Feb. 26, 2016).

[98] *See* R.C. 4928.31(A) and 4928.38-.40.

[99] *See* R.C. 4928.39.

[100] Mikkelsen Rehearing Rebuttal Test., pp. 3-4.

[101] Rehearing Tr. Vol. X, p. 1697 (Mikkelsen Cross).

[102] *See* Mikkelsen Rehearing Rebuttal Test., p. 4; Rehearing Tr. Vol. V, p. 1252 (Staff witness Choueiki agreeing that the Companies do not own generation and do not have generation costs to recover through Rider RRS).

will promote rate stability by generating a $256 million net benefit for customers during ESP IV.[103] Rider RRS "will operate as a form of rate insurance," with the amount of credits customers receive increasing the more energy market prices rise.[104] When Rider RRS is a charge, customers pay the cost of the hedge, not the cost of out-of-market generating plants owned by the Companies while the Companies transition to market and separate their generating assets. And because Rider RRS is projected to be a net credit to customers over the ESP IV term, it is not recovering any costs at all – transition or otherwise – during ESP IV.[105]

The fact that Rider RRS is "a generation rider"[106] means nothing. There are many generation riders that are not transition charges: *e.g.*, the Generation Service Rider ("Rider GEN"), Generation Cost Reconciliation Rider ("Rider GCR"), Alternative Energy Resource Rider ("Rider AER") and Non-Distribution Uncollectible Rider ("Rider NDU"). Simply because a transition charge is generation related does not mean that all generation riders are transition charges. Staff's concern that Rider RRS "may potentially be construed as a transition charge" lacks any evidentiary support in the record,[107] is inconsistent with Staff's prior support of Rider RRS under the Third Supplemental Stipulation, and simply cannot be taken seriously.

---

[103] March 31 Order, pp. 78-79, 118.

[104] March 31 Order, p. 80.

[105] Rehearing Tr. Vol. X, p. 1688 (Mikkelsen Cross).

[106] Choueiki Rehearing Test., p. 14.

[107] *See* Choueiki Rehearing Test., p. 14. Notably, OCC submitted the Rehearing Direct Testimony of Kenneth Rose in an attempt to create a record that Rider RRS will collect transition revenues. But his testimony is devoid of fact. *See* OCC Ex. 45.

g. The Proposal could help the Companies avoid a credit downgrade.[108]

Collection of revenues under the Proposal would improve some of the credit metrics for the Companies, including Funds from Operations ("FFO") to debt and CFO to debt.[109] If the Companies cannot maintain credit metrics adequate for investment grade ratings, a negative rating action could result in the Companies falling below investment grade.[110] Under the Proposal, cash received in the early years would have a positive impact on the Companies' credit rating.[111] Looking at the Proposal with all other ESP IV components as a whole over eight years, the Companies expect to remain above investment grade.[112]

If the Companies fall below investment grade, it could have negative effects on the Companies and their customers, including:

- Constrained, limited and speculative access to capital markets;
- Increased borrowing costs, higher interest rates and more onerous terms and conditions;
- Collateral provisions would require additional cash calls;
- Suppliers and counterparties may enact more stringent terms; and

---

[108] Sierra Club Ex. 98 (Staff Data Request 35).

[109] Rehearing Tr. Vol. I, p. 76 (Mikkelsen Cross); *See* Rehearing Tr. Vol. III, p. 520 (Buckley Cross). Although credit support was not intended as a benefit of the Proposal, Staff has identified credit support as a concern. *See* Rehearing Testimony of Joseph P. Buckley ("Buckley Rehearing Test."), pp. 4-5.

[110] Mikkelsen Rehearing Rebuttal Test., p. 7.

[111] Rehearing Tr. Vol. I, p. 90 (Mikkelsen Cross).

[112] Rehearing Tr. Vol. I, pp. 90-91 (Mikkelsen Cross).

- Overall higher cost of doing business; much more challenging to be competitive with peers.[113]

The cost of doing business goes up, which has negative consequences for customers.[114] In contrast, because the Proposal would help the Companies maintain an investment grade credit rating, it would have a positive impact on customers.

4. Rider RRS revenues and expenses should be excluded from SEET.

Rider RRS as originally proposed was intended to be revenue neutral to the Companies and, thus, would have no impact on the Significantly Excessive Earnings Test ("SEET").[115] While the Proposal is not revenue neutral to the Companies on an annual basis, the impact of Rider RRS revenues and credits should be excluded from the SEET. Exclusion is necessary in order for the Proposal to continue to provide the balance of benefits included in the Commission-approved ESP IV.[116]

R.C. 4928.143(F) directs the Commission to consider whether "adjustments" in an ESP

> resulted in excessive earnings as measured by whether the earned return on common equity of the electric distribution utility is significantly in excess of the return on common equity that was earned during the same period by publicly traded companies, including utilities, that face comparable business and financial risk, with such adjustments for capital structure as may be appropriate.

The SEET statute also requires the Commission to give consideration "to the capital requirements of future committed investments in this state."[117] An "earned return on common equity" generally

[113] Buckley Rehearing Test., p. 6; Sierra Club Ex. 98; Mikkelsen Rehearing Rebuttal Test., pp. 7-8.

[114] Mikkelsen Rehearing Rebuttal Test., p. 8.

[115] Mikkelsen Rehearing Test., p. 18.

[116] Mikkelsen Rehearing Test., p. 18.

[117] R.C. 4928.143(F).

is calculated by dividing a company's net income, after applying appropriate exclusions, by shareholder's common equity. Thus, the Commission determined in its Finding and Order in the Generic SEET Proceeding, Case No. 09-786-EL-UNC (the "09-786 Order"), that, for purposes of the SEET calculation, "the earned return will equal the electric utility's profits after deduction of all expenses, including taxes, minority interest, and preferred dividends, paid or accumulated, *and excluding any non-recurring, special, and extraordinary items*."[118]

Rider RRS credits and charges should be excluded from "earned return" as a special item.[119] As Company witness Mikkelsen explained, Rider RRS credits and charges in each of the years of ESP IV are a special item because they are not related to (or only incidentally related to) typical utility operations.[120] Moreover, including Rider RRS revenues in the SEET calculation would defeat the purpose of the hedge – the hedge is symmetric in providing charges and credits, while the SEET asymmetrically increases the Companies' risk of a SEET refund during years when Rider RRS is a charge while providing no downside protection during years when Rider RRS is a credit.[121] Indeed, OCC witness Kahal agreed that excluding the cost of Rider RRS credits from the SEET calculation could make customers better off.[122] Including Rider RRS in the SEET calculation would retroactively alter the cost of the hedge itself, since customers would

[118] 09-786 Order, p. 18 (June 30, 2010) (emphasis added).

[119] Mikkelsen Rehearing Test., p. 18.

[120] Mikkelsen Rehearing Rebuttal Test., p. 21.

[121] Mikkelsen Rehearing Rebuttal Test., p. 21. *See* Rehearing Tr. Vol. V, p. 1166 (EDF/OEC witness Finnigan agreeing that SEET is asymmetrically applied to Rider RRS because the Companies are exposed to a SEET adjustment if Rider RRS is a charge but not provided with any protections if Rider RRS is a credit).

[122] Rehearing Tr. Vol. V, pp. 1107-08.

receive all credits but may not have to pay all charges.[123] Thus, the full value of the hedge would not be realized.[124]

Moreover, excluding Rider RRS revenues from the SEET enables the Commission to conduct a valid comparison required by statute of the Companies' return on equity to that of other comparable companies. Under the SEET statute, the Companies' return on equity must be compared to "the return on common equity that was earned during the same period by publicly traded companies, including utilities, that face comparable business and financial risk."[125] Other comparable companies would not have a hedge mechanism similar to Rider RRS and, thus, would have a different business and financial risk from the Companies.[126] Thus, in order for the comparison to be apples-to-apples, Rider RRS charges and credits must be excluded from the SEET calculation.

Although OCC witness Duann opined that Rider RRS revenues should be included in the SEET calculation,[127] his testimony proves the opposite. Dr. Duann's reading of the specific language of the 09-786 Order at issue – "non-recurring, special, and extraordinary items" – supports the exclusion of Rider RRS revenues and expenses from the SEET calculation. He agreed that any item deemed nonrecurring, special or extraordinary may be excluded from net income for purposes of the SEET.[128] He also testified that these words, as adopted by the

---

[123] Mikkelsen Rehearing Rebuttal Test., p. 21.

[124] Mikkelsen Rehearing Rebuttal Test., p. 21.

[125] R.C. 4928.143(F).

[126] Mikkelsen Rehearing Rebuttal Test., pp. 21-22. EDF/OEC witness Finnigan agreed that he knows of no comparable utility that has a stability hedge like Rider RRS that is not backed by a PPA or physical generation. Rehearing Tr. Vol. V, pp. 1164-65.

[127] Rehearing Direct Testimony of Daniel J. Duann ("Duann Rehearing Test."), p. 3.

[128] Rehearing Tr. Vol. IV, pp. 919-21.

Commission in the 09-786 Order, do not have a technical economic meaning.[129] To the contrary, he testified that each has a common meaning: (1) "non-recurring" means an item that does not happen regularly or happens one time; (2) "special" means one-of-a-kind or not ordinary; and (3) "extraordinary" means out-of-the-ordinary, not ordinary or unusual.[130] Using Dr. Duann's own definitions, the Commission should exclude Rider RRS revenues/costs from the SEET calculation because these items will not happen regularly, are not ordinary, and are unusual.

B. Staff's Proposal Could Benefit Customers If Properly Designed.

Although the Companies' Proposal is the superior option because it provides rate stability to customers, a properly designed Staff Proposal could have merit.[131] Staff witness Choueiki testified that the Staff Proposal would provide credit support to the Companies through Rider DMR revenues that "will assist the Companies in receiving more favorable terms when accessing the capital market. Accessing the capital market, in turn, will enable the Companies to procure funds to jumpstart their distribution grid modernization initiatives."[132] The Staff Proposal anticipates that Rider DMR revenues will enable the Companies to implement whatever grid modernization plan is approved by the Commission in Case No. 16-481-EL-UNC, as well as other grid modernization initiatives.[133]

---

[129] Rehearing Tr. Vol. IV, p. 921.

[130] Rehearing Tr. Vol. IV, pp. 924-27.

[131] Mikkelsen Rehearing Rebuttal Test., pp. 4-5.

[132] Choueiki Rehearing Test., p. 15.

[133] Choueiki Rehearing Test., pp. 15-16; Rehearing Tr. Vol. IV, p. 1007; Rehearing Tr. Vol. V, pp. 1210-12; *id*., pp. 1221-23 (Staff witness Choueiki explaining that initiatives to be incentivized included all grid modernization provisions in ESP IV, including AMI, battery storage and Volt/VAR); Rehearing Tr. Vol. X, pp. 1727, 1729 (Ms. Mikkelsen explaining that Dr. Choueiki's vision for grid modernization could include, among other things, investments in battery technologies, a self-healing distribution system, and incremental investments in SCADA technologies.).

However, to be effective, Rider DMR must be properly designed and must represent the value of the conditions included in the Staff Proposal. If properly designed, Rider DMR would jumpstart grid modernization and recognize the significant economic development and job retention benefits of Staff's condition that FirstEnergy Corp. maintain its corporate headquarters and nexus of operations in Akron for the entirety of ESP IV.[134] Indeed, in addition to the economic benefits attributable to this headquarters condition, Rider DMR would provide other economic development benefits, including: (1) benefits arising from dollars spent on human resources and equipment; (2) benefits arising from having a modernized grid, which will help customers better control and manage their energy spend; and (3) benefits from reduced outages and improved reliability.[135] As such, Rider DMR would be suitable for inclusion in ESP IV under R.C. 4928.143(B)(2)(h) as a provision regarding the Companies' distribution service[136] and under R.C. 4928.143(B)(2)(i) as a provision under which the Companies implement economic development and job retention programs.

---

[134] Mikkelsen Rehearing Rebuttal Test., pp. 9, 13-14.

[135] Rehearing Tr. Vol. X, p. 1818 (Mikkelsen Redirect).

[136] OCC witness Williams agrees that provisions related to grid modernization are permissible in an ESP. Direct Testimony of James D. Williams, p. 16 (Dec. 22, 2014). R.C. 4928.143(B)(2)(h) authorizes any provisions in an ESP "regarding the utility's distribution service." Those provisions may include, but are not limited to, provisions regarding single-issue ratemaking or any incentive ratemaking. R.C. 4928.143(B)(2)(h). Rider DMR, among other things, relates to single-issue ratemaking and incentive ratemaking. Mikkelsen Rehearing Rebuttal Test., p. 5.

1. The Staff Proposal, properly modified, could be beneficial.

a. The Staff Proposal, properly modified, would enable the Companies to procure funds to jumpstart their distribution grid modernization initiatives.

The Companies believe that a properly designed Rider DMR would benefit the public.[137] The Companies need to undertake significant investments in technologies and equipment in order to prepare their distribution system for integration with advanced technologies.[138] Given the age of the existing system, the Companies cannot move directly to "one of the most intelligent grids" envisioned by Staff witness Choueiki.[139] To begin modernizing the distribution system, the Companies could face significant investments to rehabilitate urban area network systems, replace underground cable, and upgrade overhead circuits and substation equipment.[140] These projects will benefit the Companies' customers in terms of reliability, safety and customer satisfaction.[141] In addition, to prepare the distribution system for integration with advanced technologies, the Companies need to undertake significant investments related to distribution circuits, network technologies, advanced distribution management systems, and other information technology processes.[142] The completion of such projects will allow for full utilization of advanced technologies.[143]

Both the Signatory Parties and many non-signatory parties support grid modernization. The Signatory Parties, of course, support investigation of the many grid modernization initiatives

---

[137] Mikkelsen Rehearing Rebuttal Test., p. 5.

[138] Mikkelsen Rehearing Rebuttal Test., p. 6.

[139] *See* Rehearing Tr. Vol. IV, p. 967; Mikkelsen Rehearing Rebuttal Test., pp. 5-6.

[140] Mikkelsen Rehearing Rebuttal Test., p. 5.

[141] Mikkelsen Rehearing Rebuttal Test., p. 5.

[142] Mikkelsen Rehearing Rebuttal Test., p. 6.

[143] Mikkelsen Rehearing Rebuttal Test., p. 6.

included in Section V.D. of the Third Supplemental Stipulation.[144] In addition, RESA witness Crockett-McNew agreed that encouraging the deployment of smart meters would be an important policy objective for the Commission.[145] She further opined that the widespread deployment of SmartGrid in the Companies' territories would cause more competitive providers to enter and offer more products to retail customers.[146] She also testified that widespread deployment of smart meters would promote the use of net metering and behind-the-meter generation.[147] Likewise, ELPC/OEC/EDF witness Rábago has actively advocated in favor of SmartGrid, supports grid modernization efforts, and believes there are many grid modernization opportunities that would benefit the Companies and their customers.[148] Exelon/Constellation witness Campbell also supports grid modernization initiatives.[149] The Staff Proposal, properly modified, would position the Companies to implement these projects for the benefit of the Companies' customers.

b. The funds received from Rider DMR would help the Companies receive more favorable terms when accessing the capital market.

Rider DMR would provide credit support to the Companies to access capital markets and, in turn, modernize the grid.[150] Staff's goal for Rider DMR is to provide the Companies sufficient funds to engage in a distribution modernization program.[151] Of the three scenarios presented for the Companies' grid modernization business plan filed in Case No. 16-481-EL-UNC, full

---

[144] *See* Hearing Tr. Vol. XXXVI, pp. 7624-25 (Mikkelsen Cross).

[145] Rehearing Tr. Vol. IV, p. 846.

[146] Rehearing Tr. Vol. IV, pp. 844-45.

[147] Rehearing Tr. Vol. IV, p. 845.

[148] Hearing Tr. Vol. XXXVIII, pp. 8168, 8180.

[149] Second Supplemental Testimony of Lael Campbell, p. 12 (Dec. 30, 2015).

[150] Rehearing Tr. Vol. II, pp. 426, 433 (Turkenton Cross).

[151] Rehearing Tr. Vol. II, p. 482 (Turkenton Cross).

deployment will not occur at the earliest until 2026 and at the latest until 2033.[152] The substantial investments that will be required over this extended timeline require cash. Rider DMR would jumpstart the Companies' ability to fund these investments, either through capital support or through access to capital markets under more favorable terms.[153] By being able to access the capital markets more efficiently and effectively, the Companies will "have the money to actually invest in the distribution modernization."[154] Indeed, Rider DMR, properly constructed, would serve as a form of incentive ratemaking to incentivize grid modernization.[155] The Companies are committing that they intend to use Rider DMR funds for purposes within the Companies' operations, such as jumpstarting grid modernization.[156]

The Companies need access to capital markets for a number of reasons, "including to meet cash needs for debt redemption requirements, which exceed one billion dollars through 2024, and to fund capital expenditure programs such as distribution grid modernization initiatives."[157] One challenge the Companies face when accessing capital markets is maintaining financial metrics adequate for investment grade ratings from Moody's Investor Services ("Moody's") and Standard & Poor's ("S&P").[158] S&P currently rates FirstEnergy Corp. and the Companies as BBB-, one

---

[152] Mikkelsen Rehearing Rebuttal Test., p. 15.

[153] Mikkelsen Rehearing Rebuttal Test., p. 5; Choueiki Rehearing Test., p. 15.

[154] Rehearing Tr. Vol. II, p. 463 (Turkenton Cross).

[155] Rehearing Tr. Vol. II, p. 426 (Turkenton Cross).

[156] Rehearing Tr. Vol. X, pp. 1604-05, 1607 (Mikkelsen Cross). In addition to grid modernization, Rider DMR funds could be used for "other activities associated with modernizing the Companies' grid, perhaps for debt that is maturing over the term, potentially for funding of pensions, by way of example." *Id.*, p. 1607 (Mikkelsen Cross).

[157] Mikkelsen Rehearing Rebuttal Test., p. 6.

[158] Mikkelsen Rehearing Rebuttal Test., pp. 6-7.

notch above non-investment grade, and recently revised its outlook to negative.[159] If S&P downgraded FirstEnergy Corp. to non-investment grade, it would also downgrade the Companies to non-investment grade.[160] Moody's rates CEI, Toledo Edison and FirstEnergy Corp. at one notch above non-investment grade, and Ohio Edison at three notches above non-investment grade.[161] If Moody's were to downgrade FirstEnergy Corp. to non-investment grade, it would have a "credit negative" impact on the Companies.[162] If the Companies' and FirstEnergy Corp.'s credit metrics do not support continued investment grade ratings, the Companies and their customers would suffer negative consequences.[163]

The negative consequences of a non-investment grade credit rating for the Companies are many. As Company witness Mikkelsen testified:

> A non-investment grade rating signals significant credit risk to the capital markets. A non-investment grade rating can immediately disqualify a company from competing for some investors' dollars. Typically there are investors who are willing to make investments only in investment grade companies. The investor pool for non-investment grade companies is typically comprised of high-yield investors who are speculators. In periods of market volatility the high-yield market is the first to close. Maintaining an investment grade rating enables a company to continue seeking capital from investment grade investors, like insurance companies, who tend to buy and hold. A downgrade to noninvestment grade limits a company's access to capital to more restrictive terms and conditions, such as requiring a pledge of security and more rigid financial covenants, which limits a company's financial flexibility during periods of uncertainty. If a downgraded company must

[159] Mikkelsen Rehearing Rebuttal Test., p. 7; Buckley Rehearing Test., Att. 3; Rehearing Tr. Vol. III, pp. 657, 744 (Buckley Cross); Rehearing Tr. Vol. X, p. 1611 (Mikkelsen Cross).

[160] Mikkelsen Rehearing Rebuttal Test., p. 7; Rehearing Tr. Vol. I, pp. 101-02 (Mikkelsen Cross); Rehearing Tr. Vol. X, p. 1612 (Mikkelsen Cross).

[161] Mikkelsen Rehearing Rebuttal Test., pp. 6-7.

[162] Mikkelsen Rehearing Rebuttal Test., p. 7; Rehearing Tr. Vol. I, pp. 101-02 (Mikkelsen Cross); Rehearing Tr. Vol. X, p. 1612 (Mikkelsen Cross).

[163] Mikkelsen Rehearing Rebuttal Test., p. 7.

> access capital from a less liquid market, at higher borrowing costs, on more onerous terms and conditions, its long-term cost of debt will increase. Eventually, increases in the long-term cost of debt are recovered from customers in a distribution base rate case. During a period of a distribution base rate freeze, the higher debt carrying costs reduce the funds available to the Companies for investment in the safe, reliable operation of the distribution system.
>
> In addition, a downgrade may have negative impacts on existing borrowings and other contracts. It may give rise to a collateral requirement. Additional cash calls would erode liquidity and leave less cash available for the Companies to use in their business operations. A downgrade may also trigger more stringent terms in existing agreements, such as a shortened period to pay invoices.[164]

These negative impacts drive up the Companies' cost of doing business, which ultimately impacts the Companies' customers.[165]

Intervenor witnesses agreed. Dynegy witness Ellis agreed that the ability of the Companies to fund grid modernization is partially dependent on their credit ratings.[166] OCC witness Kahal confirmed that a company's credit rating is important in terms of having access to capital and having access to liquidity.[167] He also confirmed multiple harms to the Companies and their customers if the Companies were to fall below investment grade, including:

- reduced access to capital;
- potentially sharp increases in the cost of capital and long-term debt;
- limiting the pool of possible investors;
- potentially lead to a less liquid capital market;
- an increase in collateral calls;

---

[164] Mikkelsen Rehearing Rebuttal Test., pp. 7-8.

[165] Mikkelsen Rehearing Rebuttal Test., p. 8.

[166] Rehearing Tr. Vol. IV, p. 819.

[167] Rehearing Tr. Vol. VIII, p. 1384.

- more onerous contract terms and conditions.[168]

Staff witness Buckley explained that it is better to forestall a credit downgrade than have to reverse a credit downgrade: "There's a substantial dropoff between being investment grade and not being investment grade. So if you wait for that dropoff to occur, to get them back up could take a substantial amount of time, and we're worried that constituents would be negatively affected, including the ratepayers."[169] Staff also believes that it may be more expensive for customers if Rider DMR is not approved and the Companies have to pay a higher rate and have more unfavorable terms and conditions.[170]

The credit support provided by Rider DMR would improve the Companies' CFO to debt credit metric used by Moody's as part of its rating methodology.[171] Rider DMR revenues also would improve the Companies' Debt to Capitalization credit metric to the extent those revenues were used to reduce debt or to fund pension obligations.[172] Rider DMR credit support also likely would be viewed favorably by Moody's when it assesses "the regulatory framework the Companies operate in as part of its rating methodology."[173] Staff witness Buckley expressed a similar sentiment, noting that more investment in FirstEnergy Corp.'s regulated operations would cause Moody's to reduce some of Moody's credit metric thresholds.[174]

---

[168] Rehearing Tr. Vol. VIII, pp. 1390-91.

[169] Rehearing Tr. Vol. III, p. 599.

[170] Rehearing Tr. Vol. V, pp. 1229-30 (Choueiki Cross).

[171] Mikkelsen Rehearing Rebuttal Test., p. 8; Buckley Rehearing Test., pp. 3-4.

[172] Mikkelsen Rehearing Rebuttal Test., p. 8.

[173] Mikkelsen Rehearing Rebuttal Test., p. 8.

[174] Rehearing Tr. Vol. III, pp. 570-71, 643.

By improving the Companies' credit metrics, the Companies would have better access to capital markets on more favorable terms, which would benefit customers.[175] Customers would also benefit from having Companies that are financially stable and strong.[176] In addition to reducing borrowing costs, appropriate credit support also could result in the Companies obtaining more favorable terms from vendors and suppliers associated with grid modernization, which could reduce Rider AMI dollars collected.[177]

2. Staff's calculation of the Rider DMR annual amount must be modified.

Staff witness Buckley's assumptions used to calculate the Rider DMR amount must be revised to enable the Companies to jumpstart grid modernization and benefit customers. The necessary revisions to the Rider DMR calculation are:

1. The target goal for CFO to Debt should be 15 percent, rather than 14.5 percent;
2. The calculation of Rider DMR revenue should have used a three-year average from 2012-2014 instead of a five-year average;
3. To achieve the goal of a 15 percent CFO to Debt, it is necessary to use pre-tax revenues; and
4. An allocation factor of 40 percent should be used.[178]

In addition, the Rider DMR amount should fully reflect the value of the conditions Staff is seeking as an element of the Staff Proposal.[179]

---

[175] Mikkelsen Rehearing Rebuttal Test., p. 8.

[176] Rehearing Tr. Vol. X, p. 1723 (Mikkelsen Cross).

[177] Rehearing Tr. Vol. X, pp. 1610-11 (Mikkelsen Cross).

[178] Mikkelsen Rehearing Rebuttal Test., p. 9.

[179] Mikkelsen Rehearing Rebuttal Test., pp. 13-14.

a. CFO to Debt target should be 15 percent.

Mr. Buckley testified that a financial metric of 14.5 percent CFO to Debt – the "CFO" in this metric represents net cash flows (i.e., cash inflows net of outflows)[180] – is the appropriate metric to use to judge FirstEnergy Corp.'s credit worthiness.[181] Mr. Buckley based this on a Moody's credit opinion dated January 20, 2016. In that opinion, Moody's stated that a negative rating action could occur if ESP IV, as modified by the Commission, did not allow FirstEnergy Corp. to maintain a CFO to Debt ratio of 14-15 percent.[182] Mr. Buckley averaged this range to arrive at a 14.5 percent CFO to Debt target.

A CFO to Debt target of 15 percent is more appropriate, based on updated data. An opinion issued by Moody's on April 28, 2016 includes a CFO to Debt target range of 14-16 percent.[183] Thus, using Staff's methodology, the midpoint of 15 percent is a more appropriate CFO to Debt target.[184]

b. Rider DMR revenues should be calculated using a three-year average of CFO shortfall in years 2012-14.

Mr. Buckley calculated his "average annual revenue need" using an average of the "CFO shortfall" over a period of four years and nine months, 2011 through the first nine months of 2015, which he presented as a five-year average.[185] However, using a five-year historical average

[180] Rehearing Tr. Vol. III, pp. 735-36.

[181] Buckley Rehearing Test., p. 4.

[182] Buckley Rehearing Test., p. 4.

[183] Direct Energy Ex. 1; Mikkelsen Rehearing Rebuttal Test., p. 10. Notably, although certain parties have suggested that FES's cash flow is responsible for the CFO shortfall, FES's CFO/debt metric is currently 24%, with Moody's projecting it will fall to 16% by 2018. P3/EPSA Ex. 21, p. 3.

[184] Mikkelsen Rehearing Rebuttal Test., p. 10.

[185] Buckley Rehearing Test., pp. 3-4; Rehearing Tr. Vol. III, p. 537 (Mr. Buckley agreeing that row in Table on page 4 of his testimony showing "CFO Pre W/C / Debt at 14.5%" represented "CFO shortfall"); *id.*, p. 735 (Mr. Buckley stating that last column in page 4 table reflected nine months of data).

"ignores a trend of worsening CFO to Debt at FirstEnergy Corp. beginning in 2012 and continuing through 2014."[186] By including 2011 in his calculation, Mr. Buckley used a year in which CFO to Debt was 14 percent, at the low end of Moody's CFO to Debt range for an investment grade rating.[187] In contrast, the credit support calculation should be based on actual data representing the deteriorating credit worthiness situation, which necessarily excludes 2011.[188]

Additionally, the data for the first nine months of 2015 should be excluded from the calculation of Rider DMR revenue. The 2015 data in Mr. Buckley's table "are anomalous as a result of a one-year spike in capacity prices in the ATSI zone."[189] Starting June 1, 2015 and ending May 31, 2016, the weighted average capacity market price in the ATSI zone was $338.87MW-day, far in excess of any capacity market price before or since.[190] Mr. Buckley was unaware of the impact that these anomalous capacity prices had on his 2015 data.[191] In addition, the 2015 data in Mr. Buckley's table does not cover an entire 12-month period ending December 31, 2015 and, thus, is not comparable.[192]

As Ms. Mikkelsen explained, "A three-year range beginning in 2012 (the year when FirstEnergy Corp.'s CFO to Debt first fell below Moody's 14-16 percent target range) more accurately reflects FirstEnergy Corp.'s circumstances, and more accurately addresses the objective

---

[186] Mikkelsen Rehearing Rebuttal Test., p. 10.

[187] Mikkelsen Rehearing Rebuttal Test., p. 10; Buckley Rehearing Test., p. 4.

[188] Mikkelsen Rehearing Rebuttal Test., p. 10. Use of historical data is necessary because projections would be material, non-public information. Hearing Tr. Vol. X, pp. 1617-18 (Mikkelsen Cross).

[189] Mikkelsen Rehearing Rebuttal Test., p. 10; Rehearing Tr. Vol. III, p. 735 (Mr. Buckley stating that last column in page 4 table reflected nine months of data).

[190] Co. Ex. 75, pp. 186-89, Table 5-9 and Figure 5-5; Co. Exs. 25, 182 and 183.

[191] Rehearing Tr. Vol. III, p. 735 (Buckley Cross).

[192] Mikkelsen Rehearing Rebuttal Test., p. 10; Rehearing Tr. Vol. III, p. 735 (Mr. Buckley stating that last column in page 4 table reflected nine months of data).

of facilitating the Companies' access to capital markets to jump-start distribution grid modernization initiatives."[193] Mr. Buckley agreed that the Commission could use a three-year average.[194] Thus, the Commission should use a three-year average of the CFO shortfall in years 2012-14 to calculate the annual amount of Rider DMR.

c. Rider DMR revenues must be grossed up for income taxes.

Mr. Buckley did not gross up his annual Rider DMR amount to reflect that those revenues are subject to income tax.[195] He agreed, however, that it would be appropriate to use the actual composite tax rates of the Companies to gross up the Rider DMR amount.[196] Grossing up Rider DMR revenue for income taxes is necessary because the additional revenue will generate additional income subject to income tax.[197] If Rider DMR is not grossed up, it would fall short of achieving the target CFO.[198] In order for the Companies to receive the full cash flow benefits intended, the Rider DMR revenue should be grossed up by the Companies' average tax rate of 36 percent.[199]

---

[193] Mikkelsen Rehearing Rebuttal Test., p. 10.

[194] Rehearing Tr. Vol. III, p. 741.

[195] Rehearing Tr. Vol. III, p. 739 (Buckley Cross).

[196] Rehearing Tr. Vol. III, p. 740.

[197] Mikkelsen Rehearing Rebuttal Test., p. 11.

[198] Mikkelsen Rehearing Rebuttal Test., p. 11.

[199] Mikkelsen Rehearing Rebuttal Test., p. 11; Rider DCR update filing, Case No. 14-1628-EL-RDR *et al.* (July 1, 2015) (showing composite income tax rates for CEI – 36.09%; Ohio Edison – 35.82%; and Toledo Edison – 35.68%). *See* Hearing Tr. Vol. XXXIV at 7116-17, 7178 (bench took administrative notice of Rider DCR update filing).

d. The allocation percentage for the Rider DMR calculation should be 40 percent.

Mr. Buckley used an allocation factor of 22 percent that inappropriately understates the significance of the Companies to FirstEnergy Corp.[200] Mr. Buckley calculated his allocation factor by using the Companies' share of FirstEnergy Corp.'s gross operating revenues in 2015.[201] But using gross revenues is misleading given that gross revenues are heavily influenced by the level of shopping in each utilities' service territory.[202] Therefore, because the Companies have a high level of shopping compared to other FirstEnergy Corp. service territories, the Companies' relative contribution to FirstEnergy Corp.'s shortfall is understated.[203]

Using gross operating revenues as an allocation factor also is inappropriate because the relevant metric – CFO – is a net cash flow number. The "energy operating revenues" used by Mr. Buckley recognize only gross cash inflows and not any offset for cash outflows or expenses.[204] Thus, the allocation factor used by Mr. Buckley does not match the metric he used. The correct allocator should also reflect cash inflows and outflows, such as net income, so as to reflect more accurately the Companies' contributions to FirstEnergy Corp.'s cash flow.[205] Mr. Buckley agreed that "you could definitely use net income" and that using net income would show the Companies' contributions to FirstEnergy Corp.'s cash flow from operations.[206]

---

[200] Buckley Rehearing Test., p. 3; Mikkelsen Rehearing Rebuttal Test., p. 11.

[201] Buckley Rehearing Test., p. 3; Mikkelsen Rehearing Rebuttal Test., p. 11; Rehearing Tr. Vol. III, p. 736 (Mr. Buckley agreeing that "energy operating revenue" he used is a gross revenue number).

[202] Mikkelsen Rehearing Rebuttal Test., pp. 11-12.

[203] Mikkelsen Rehearing Rebuttal Test., pp. 11-12.

[204] Mikkelsen Rehearing Rebuttal Test., p. 12.

[205] Mikkelsen Rehearing Rebuttal Test., p. 12.

[206] Rehearing Tr. Vol. III, p. 738.

The Companies' contribution to FirstEnergy Corp.'s cash flow in 2015 using net income as a more appropriate metric was 40 percent. This is easily calculated from Mr. Buckley's Attachment 1:

	2015 Net Income
CEI	66,000,000
Ohio Edison	142,000,000
Toledo Edison	25,455,000
Total:	233,455,000

Dividing the Companies' combined net income of $233,455,000 by FirstEnergy Corp.'s net income of $578,000,000 results in an allocation factor of 40 percent.[207] Notably, other methods of estimating the Companies' contributions to FirstEnergy Corp.'s cash flow, such as comparing distribution sales (36 percent), distribution employee headcounts (34 percent) or customer counts (35 percent), produce results much closer to 40 percent than Mr. Buckley's 22 percent.[208] Therefore, a 40 percent allocation factor should be used in the calculation of the annual Rider DMR revenue amount instead of Mr. Buckley's understated allocation factor of 22 percent.[209]

e. The revised Rider DMR revenue amount should also reflect the full value of Staff's proposed conditions and have an eight-year term.

Once the appropriate revisions are made to the Rider DMR revenue amount, the allocated average annual Rider DMR revenue amount, after tax gross up, is $558 million.[210] This is not the end of the story, however, because the Staff Proposal includes two conditions: (1) FirstEnergy Corp. must keep its corporate headquarters and nexus of operations in Akron, Ohio, for the entire

[207] Buckley Rehearing Test., Att. 1.

[208] Mikkelsen Rehearing Rebuttal Test., p. 12.

[209] Mikkelsen Rehearing Rebuttal Test., p. 12.

[210] Mikkelsen Rehearing Rebuttal Test., p. 13.

term of ESP IV or else refund all Rider DMR revenues to customers; and (2) Rider DMR will immediately terminate if FirstEnergy Corp. or the Companies announce a change in ownership.[211] Staff believes that the first condition provides job retention benefits because "it provides jobs. With a multiplier effect of, you know, money being spent, it really helps invigorate the Akron area and the State of Ohio in general."[212] Mr. Buckley noted that this condition also would support the state of Ohio through income and property taxes.[213] However, Staff did not attempt to quantify this benefit of the Staff Proposal.[214]

Company witness Murley testified that the condition to maintain FirstEnergy Corp.'s headquarters and nexus of operations in Akron, Ohio, has significant economic benefits for the region.[215] In fact, the headquarters has an estimated annual economic impact of $568 million on Ohio's economy.[216] The Staff Proposal does not recognize the substantial value of this condition in terms of economic development and job retention.[217] As such, the Rider DMR revenue amount should be increased to include the value to the state of Ohio of the headquarters condition.[218] The

---

[211] Buckley Rehearing Test., p. 7; Rehearing Tr. Vol. III, p. 582 (Buckley Cross).

[212] Rehearing Tr. Vol. III, p. 694 (Buckley Cross); Rehearing Tr. Vol. V, p. 1256 (Staff witness Choueiki stating that the headquarters condition "is an economic positive").

[213] Rehearing Tr. Vol. III, p. 679.

[214] Rehearing Tr. Vol. III, p. 694 (Buckley Cross).

[215] Rebuttal Rehearing Testimony of Sarah Murley ("Murley Rebuttal Test."), pp. 3-6; Mikkelsen Rehearing Rebuttal Test., p. 13.

[216] Murley Rebuttal Test., pp. 3-4.

[217] Mikkelsen Rehearing Rebuttal Test., p. 13.

[218] Mikkelsen Rehearing Rebuttal Test., p. 14; Rehearing Tr. Vol. IX, p. 1464 (Company witness Murley testifying that "the benefit of keeping the headquarters in Akron should be accounted for in Rider DMR.").

Commission should determine an additional amount to include in Rider DMR associated with keeping the headquarters and nexus of operations in Akron, Ohio.[219]

In addition, the Staff Proposal illogically limits Rider DMR to a three-year term, with the opportunity for an additional two years, while applying the headquarters commitment to the entire eight-year term of ESP IV.[220] Because one element of the Staff Proposal is to incent FirstEnergy Corp. to maintain its headquarters and nexus of operations in Akron through May 31, 2024, and together with the other reasons stated above for an eight-year term for Rider DMR, Rider DMR should run concurrently with this incentive through May 31, 2024.[221] For each year of ESP IV, provided the headquarters condition is met, Rider DMR should collect $558 million as credit support for grid modernization and other operations, plus an additional amount determined by the Commission not to exceed the value of the headquarters condition.

The need for Rider DMR to have a term coincident with ESP IV is apparent from the Companies' significant cash requirements over the term of ESP IV. Recent experience does not support Staff's belief that three years is sufficient credit support for the Companies.[222] Nor does historical experience at Centerior when CEI's and Toledo Edison's credit metrics were below investment grade in excess of three years.[223] Moreover, the Companies' grid modernization needs will not end in 2019, but will extend through at least 2026 and perhaps as far out as 2033.[224] The

---

[219] Rehearing Tr. Vol. X, pp. 1599-1600 (Mikkelsen Cross). *See id.*, p. 1600 ("The Companies' Proposal is that the Commission will determine an appropriate value associated with the condition established by the Staff to retain the corporate headquarters and the nexus of operations in Akron, Ohio. . . . The Companies are not making a proposal with respect to the amount.").

[220] *See* Buckley Rehearing Test., p. 7; Mikkelsen Rehearing Rebuttal Test., p. 14.

[221] Mikkelsen Rehearing Rebuttal Test., p. 14.

[222] Mikkelsen Rehearing Rebuttal Test., p. 15.

[223] Rehearing Tr. Vol. X, p. 1729 (Mikkelsen Cross).

[224] Mikkelsen Rehearing Rebuttal Test., p. 15.

Companies' grid modernization business plan includes significant dollars that will be spent throughout the term of ESP IV and beyond.[225] Staff's broader vision for grid modernization also would entail dollars incremental to the business plan for investments in battery technologies, SCADA or a self-healing distribution system.[226] The Companies also have significant pension funding obligations of $750 million to one billion dollars, with ongoing commitments in future years.[227] The Companies also have $1.1 billion in debt maturing over the period of ESP IV.[228] Thus, it is reasonable to maintain Rider DMR for the entire ESP IV term, subject to the headquarters condition, to provide the Companies with adequate capital support for their multiple significant ongoing cash requirements.

If the Commission does not approve the Companies' modifications to the Rider RRS calculation (which is the preferred option) and decides instead to approve Rider DMR, the Commission should authorize Rider DMR as revised above for the eight-year term of ESP IV, effective for service rendered September 1, 2016 or as soon as practically possible thereafter.[229] Rider DMR collection cannot wait until the Commission authorizes specific grid modernization programs; the Companies need Rider DMR revenues to "prime the pump" to obtain lower financing costs prior to commencing grid modernization and other cash requirements.[230] The Rider DMR amount should include the needed $558 million in credit support for grid

---

[225] Rehearing Tr. Vol. X, p. 1623 (Mikkelsen Cross).

[226] Rehearing Tr. Vol. X, p. 1733 (Mikkelsen Cross).

[227] Rehearing Tr. Vol. X, pp. 1623, 1761 (Mikkelsen Cross).

[228] Rehearing Tr. Vol. X, p. 1623 (Mikkelsen Cross).

[229] Mikkelsen Rehearing Rebuttal Test., p. 16. A September 1 start mitigates the rate impact on customers as it coincides with the shift from summer to winter rates. *Id.*

[230] Mikkelsen Rehearing Rebuttal Test., p. 16. *See* Rehearing Tr. Vol. V, pp. 1254-55 (Staff witness Choueiki agreeing that Rider DMR is an effort to prime the capital pump).

modernization plus an additional amount to reflect the economic development and job retention benefits of the headquarters condition.

Further, the Commission should direct that, if FirstEnergy Corp. ceases to maintain its headquarters and nexus of operations in Akron, Rider DMR collection will end without refund of already collected amounts.[231] Staff's proposal that the Companies refund all Rider DMR revenues received if the headquarters condition is triggered is practically unworkable and, as demonstrated below regarding possibly refunding Rider DMR revenue as part of SEET proceedings, would defeat the purpose of Rider DMR by threatening the value of the credit support to be provided.[232]

3. Rider DMR revenues should be excluded from the SEET calculation.

Including Rider DMR revenues in the SEET calculation would defeat the purpose of the rider to provide credit support to the Companies.[233] If Rider DMR revenues were not excluded from the SEET calculation, the cash received by the Companies for credit support in one year might have to be refunded to customers in the following year at the same time that the Companies need to make significant cash investments in their operations.[234] The risk of this happening would place a figurative asterisk on the Companies' cash flow numbers as reviewed by Moody's and S&P, thereby making it less likely that these rating agencies would treat Rider DMR revenues as a credit positive. And SEET refunds would harm the Companies' access to capital markets.[235] SEET refunds also would work contrary to the headquarters condition included in the Staff

---

[231] Mikkelsen Rehearing Rebuttal Test., pp. 14-15; Rehearing Tr. Vol. X, p. 1603 (Mikkelsen Cross) (Companies' Proposal is that any amounts collected under Rider DMR would not be subject to refund).

[232] *See* Mikkelsen Rehearing Rebuttal Test., p. 22.

[233] Mikkelsen Rehearing Rebuttal Test., p. 22.

[234] *See* R.C. 4928.143(F).

[235] Mikkelsen Rehearing Rebuttal Test., p. 22.

Proposal because the incentive to retain the headquarters and nexus of operations in Akron would be lacking.[236]

Excluding Rider DMR revenues from the SEET calculation is consistent with the Commission's 09-786 Order because they are "extraordinary."[237] Rider DMR revenues qualify as an extraordinary item because the twin purposes of Rider DMR – credit support to jumpstart grid modernization and economic development and job retention – are extraordinary in nature.[238] OCC witness Duann testified that an extraordinary item for purposes of the 09-786 Order is any item that is "out of the ordinary, not ordinary, or unusual,"[239] which certainly applies to Rider DMR revenues.

Rider DMR revenues also should be excluded from the SEET calculation because otherwise the Commission would be unable to conduct the comparison required by statute of the Companies' return on equity to that of comparable companies.[240] None of the comparable companies used in the SEET calculation has a Rider DMR designed to incent grid modernization through improved access to capital markets on more favorable terms and conditions, or a commitment to maintain a Fortune 200 company headquarters in the state.[241]

Rider DMR revenues also qualify for exclusion from the SEET calculation under the Companies' existing exclusion "associated with any additional liability or write-off of regulatory

---

[236] Mikkelsen Rehearing Rebuttal Test., p. 22.

[237] *See* 09-786 Order, p. 18; Mikkelsen Rehearing Rebuttal Test., pp. 22-23. *See also* Rehearing Tr. Vol. V, p. 1165 (EDF/OEC witness Finnigan agreeing that extraordinary items may be excluded from the SEET calculation).

[238] Mikkelsen Rehearing Rebuttal Test., pp. 22-23.

[239] Rehearing Tr. Vol. IV, p. 926.

[240] Mikkelsen Rehearing Rebuttal Test., p. 23.

[241] Mikkelsen Rehearing Rebuttal Test., p. 23.

assets due to implementing the Companies' ESP IV."[242] The credit support provided by Rider DMR would be associated with liabilities, *i.e.*, the additional debt need to fund grid modernization as envisioned by the Staff Proposal.

Lastly, because Rider DMR is designed to support the Companies' capital requirements for future capital investments related to grid modernization, the Commission may exclude Rider DMR revenues from the SEET calculation on the same basis as it has previously excluded the Companies' deferred carrying charges from the SEET calculation.[243]

For all of these reasons, Rider DMR revenues can and should be excluded from the SEET calculation.[244]

4. ESP v. MRO test

The Staff Proposal affects the ESP v. MRO test performed by the Commission in the March 31 Order by removing Rider RRS and adding Rider DMR. None of the qualitative benefits of ESP IV recognized in the March 31 Order are affected.[245] In fact, Rider DMR would enhance the qualitative benefits of ESP IV by advancing Ohio policy (1) by encouraging smart grid programs and advanced metering infrastructure, and (2) encouraging implementation of

---

[242] Mikkelsen Rehearing Rebuttal Test., p. 23.

[243] *See In the Matter of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Authority to Provide for a Standard Service Offer Pursuant to Section 4928.143, Revised Code, in the Form of an Electric Security Plan*, Case No. 12-1230-EL-SSO, Opinion and Order, p. 48 (July 18, 2012) (finding that it is lawful to exclude deferred carrying charges from the SEET where "such deferred carrying charges are related to capital investments in this state and where the Commission has determined that such deferrals benefit ratepayers and the public interest.").

[244] If the Commission includes Rider DMR revenues in the SEET calculation, "the Commission would need to make appropriate adjustments to the Companies' capital structure by increasing the average equity balances to recognize, among other things, 1) the weak credit metrics of the Companies; 2) the additional debt that may be necessitated by the grid modernization efforts; and 3) increased risk to the Companies." Mikkelsen Rehearing Rebuttal Test., pp. 23-24.

[245] Rehearing Tr. Vol. II, pp. 448-49 (Turkenton Cross); Mikkelsen Rehearing Rebuttal Test., p. 20.

distributed generation, which is facilitated by grid modernization.[246] Staff witness Turkenton also testified that Rider DMR would promote diversity of supplies and suppliers by "enabling competitive providers to offer innovative products and services to serve customers in Ohio."[247] RESA witness Crockett-McNew agreed with Ms. Turkenton that encouraging the deployment of SmartGrid would cause more competitive suppliers to enter and to offer more products to retail customers.[248] Thus, ESP IV, as modified by the Staff Proposal, is more favorable qualitatively than the expected results of an MRO.[249]

Quantitatively, the $51.1 million of quantitative benefits from shareholder funding commitments remains unchanged.[250] Because Staff's Proposal removes Rider RRS from ESP IV, its $256 million quantitative benefit also is removed from the calculus.

Rider DMR does not add quantitative costs to that calculus because the portion of Rider DMR revenues used to support grid modernization would be a wash for purposes of the ESP v. MRO test. The Commission has found that when the Companies would recover the equivalent of the same costs over the long term under either an ESP or MRO, those costs should be removed from the ESP v. MRO analysis.[251] The same is true here, since revenues equivalent to Rider DMR revenues could be recovered under an MRO in a base rate case proceeding, in the Companies'

---

[246] Mikkelsen Rehearing Rebuttal Test., p. 20; Rehearing Testimony of Tamara S. Turkenton ("Turkenton Rehearing Test."), p. 4. *See* R.C. 4928.02(D) and (K).

[247] Turkenton Rehearing Test., p. 4; Rehearing Tr. Vol. II, p. 464 (Turkenton Cross) ("through the deployment of this advanced technology, we will have a more intelligent grid which will allow suppliers, either wholesale or retail suppliers, to provide more innovative and, you know, customer-type-friendly products to the marketplace").

[248] Rehearing Tr. Vol. IV, pp. 844-45.

[249] Mikkelsen Rehearing Rebuttal Test., p. 20.

[250] Mikkelsen Rehearing Rebuttal Test., p. 20; Turkenton Rehearing Test., p. 3. As noted by the Commission in the March 31 Order at p. 119, "the low-income funding furthers state policy by protecting at-risk populations as provided by R.C. 4928.02(L)."

[251] *See*, *e.g.*, March 31 Order, p. 119.

existing Rider AMI, or in another mechanism similar to Rider DMR.[252] Ms. Turkenton agreed that the costs to acquire capital and expenses incurred as part of the modernization distribution program would normally be recovered as part of a distribution rate case.[253] Ms. Turkenton also believes that the qualitative benefits of ESP IV are so valuable to the Companies' customers and the state of Ohio that ESP IV, if revised to include the Staff Proposal, would pass the ESP v. MRO test even if Rider DMR revenues were counted only on the ESP side of the equation.[254] Given the Companies' work to date and Staff's support for grid modernization, "it is likely that the Companies would still move forward with a grid modernization initiative under an MRO."[255] Thus, under an MRO and over the long term, the Commission likely would authorize equivalent revenues in base rate, Rider AMI or a mechanism similar to DMR in order to fund grid modernization or necessary make-ready work.[256]

Moreover, the headquarters condition in the Staff Proposal offers an additional quantitative benefit, given its $568 million annual economic impact on the state of Ohio.[257] As discussed above, the Companies are recommending that the annual Rider DMR amount equal to $558 million needed for credit support plus an additional amount not to exceed the economic development and job retention value of the headquarters condition.[258] Given that this portion of

---

[252] Mikkelsen Rehearing Rebuttal Test., p. 19. For example, in a base distribution rate case, the Commission could make an adjustment, as it deems appropriate, to test year expense, or normalize test year expenses, or provide an incentive return on equity.

[253] Rehearing Tr. Vol. II, pp. 482-83, 85.

[254] Rehearing Tr. Vol. II, p. 485.

[255] Mikkelsen Rehearing Rebuttal Test., p. 19.

[256] Mikkelsen Rehearing Rebuttal Test., p. 19.

[257] *See* Murley Rebuttal Test., p. 4.

[258] *See* Mikkelsen Rehearing Rebuttal Test., p. 14.

Rider DMR will not exceed the value added, it will either be quantitatively neutral or more likely positive for purposes of the ESP v. MRO test.[259]

As a result, the Commission-approved ESP with Rider RRS removed and Rider DMR added would produce at least $51.1 million and as much as $619.1 million in quantitative benefits plus multiple qualitative benefits.[260] Thus, the Commission-approved ESP IV, with the Companies' proposed revisions to Rider DMR, is more favorable in the aggregate than the expected results of an MRO.[261]

III. CONCLUSION

The Commission should determine on rehearing that the Companies' Proposal provides the greatest benefit for customers and should approve the proposed modifications to Rider RRS. In addition, there is sufficient evidence in the record for the Commission to approve a properly designed Rider DMR.

Respectfully submitted,

/s Carrie M. Dunn

Carrie M. Dunn (0076952)
Counsel of Record
FIRSTENERGY SERVICE COMPANY
76 South Main Street
Akron, OH 44308
Telephone: (330) 384-5861
Fax: (330) 384-8375
Email: dunn@firstenergycorp.com

David A. Kutik (0006418)
JONES DAY
901 Lakeside Avenue
Cleveland, OH 44114

[259] Mikkelsen Rehearing Rebuttal Test., pp. 19-20.

[260] Mikkelsen Rehearing Rebuttal Test., pp. 20-21.

[261] Mikkelsen Rehearing Rebuttal Test., p. 21.

Telephone: (216) 586-3939
Fax: (216)579-0212
Email: dakutik@jonesday.com

James F. Lang (0059668)
N. Trevor Alexander (0080713)
CALFEE, HALTER & GRISWOLD LLP
The Calfee Building
1405 East Sixth Street
Cleveland, OH 44114
Telephone: (216) 622-8200
Fax: (216) 241-0816
Email: jlang@calfee.com
Email: talexander@calfee.com

ATTORNEYS FOR OHIO EDISON
COMPANY, THE CLEVELAND ELECTRIC
ILLUMINATING COMPANY, AND THE
TOLEDO EDISON COMPANY

CERTIFICATE OF SERVICE

I certify that this Post-Hearing Brief was filed electronically through the Docketing Information System of the Public Utilities Commission of Ohio on this 15th day of August, 2016. The PUCO's e-filing system will electronically serve notice of the filing of this document on counsel for all parties. Further, a courtesy copy has been served upon parties via electronic mail.

s/ James F. Lang
One of Attorneys for the Companies