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-HEARING BRIEF OF
DIRECT ENERGY SERVICES, LLC AND DIRECT ENERGY BUSINESS, LLC

TABLE OF CONTENTS

I. INTRODUCTION

How many legs does a dog have if you call his tail a leg?

Four. Saying that a tail is a leg doesn't make it so.

— Abraham Lincoln

Lincoln's riddle is an appropriate metaphor for the FirstEnergy[1] and Staff rehearing proposals. The proposals seek the same objective by different means: to bailout the FirstEnergy utilities' sole shareholder and parent company from the consequences of decisions that have landed the parent on ratings watch with Wall Street. Ohio law forbids shareholder bailouts of utility holding companies, so FirstEnergy and Staff are forced to describe their proposals as something other than what they are. But saying that money collected under either proposed rider would offer a "hedge" or promote "distribution modernization" doesn't make it so. A bailout is a bailout, regardless of what you call it.

The bailout mechanisms are deceptively simple. FirstEnergy proposes to change the formula for calculating charges and credits under Rider RRS by declaring costs that it *projected* it would incur under an affiliate power purchase agreement (PPA) to be "actual costs." Because its *actual* "actual costs" will be $0, any revenue generated under the modified Rider RRS would become excess profits to the utilities and payable to their shareholder. Staff proposes a smaller bailout but through more direct means. Staff wishes to begin funneling $131 million in annual "credit support" to the parent/shareholder by means of a "distribution modernization rider" (Rider DMR) levied and administered by the utilities. Both proposals seek the same objective by different means.

[1] The applicants in this proceeding are The Cleveland Electric Illuminating Company, Ohio Edison Company and Toledo Edison Company. This brief generally adopts the convention used at hearing to refer to these companies collectively as "FirstEnergy."

Direct Energy's brief will focus primarily on this point: ***neither Rider RRS nor Rider DMR are intended or necessary to recover any cost the utilities will incur to provide SSO service***. The March 31, 2016 Opinion and Order approving FirstEnergy's electric security plan (ESP) already satisfies the Ohio utilities' standard service offer (SSO) revenue requirements for the next eight years. The rehearing proposals advocate mechanisms to create an *additional* revenue stream, *above and beyond* the SSO revenue requirement. Because the approved ESP rates already satisfy the utilities' revenue requirements, any additional funds collected under Rider RRS or Rider DMR would *necessarily* increase the utilities' net income. This increased net income would *necessarily* be available to FirstEnergy Corp. because FirstEnergy Corp. is the sole shareholder of the utilities' common stock. Once the utilities' net income is paid to FirstEnergy Corp. as a dividend, the parent corporation may *necessarily* do with this money whatever it wishes. FirstEnergy Corp. is *not* regulated by the Commission and cannot be told what to do with its earnings, regardless of which subsidiary generated them. The idea that the Commission can *require* FirstEnergy Corp. to stay in Akron (let alone that FirstEnergy should be paid a ransom to do so) is not even a topic for intelligent conversation. The Commission has no power but what it is given by law, and no law authorizes it to simply hand over ratepayer dollars to bolster the bottom line of a shareholder or parent company.

Both rehearing proposals are unlawful, but Staff's offers something that FirstEnergy's does not: a conceptual framework for funding grid modernization. Despite its name, Rider DMR as proposed is simply a means of allowing the utilities to become collection agents for FirstEnergy Corp. But if the rider were modified to function as its name implies, the Commission would be within its authority to approve it. Rather than issue a blank check to collect dollars now and justify later whatever spending occurs (if any; none is promised), the Commission should first require FirstEnergy to identify grid modernization projects. Funds authorized to pursue these projects should be accounted for. The FirstEnergy utilities should be compensated for their *legitimate* costs, not the made-up "costs" of affiliates, or projections based on transactions that are not going to occur. No one should be heard to complain about modifications to Rider DMR that actually cause it to operate in line with its given name.

Direct Energy[2] is in this case because it cares about competition. Competition is a pillar of state energy policy. *See generally* R.C. 4928.02. Good competition means fair competition, and to be fair, everyone must play by the same rules. Direct Energy, like most CRES providers, is not affiliated with an Ohio electric distribution utility. If business decisions or market conditions cause Direct Energy to fail, it cannot look to an affiliate's captive ratepayers as a backstop. But that is exactly what FirstEnergy Corp. is doing; it is seeking special treatment to allow its regulated subsidiaries to function as a backstop for their unregulated affiliates. FirstEnergy is not entitled to special treatment. The Commission should reject the proposal to modify Rider RRS, as well as Staff's alternative Rider DMR.

II. BACKGROUND

It is important to play close attention to the term "FirstEnergy." The same name is often used to describe different entities or subsidiaries. It is critical for the Commission to understand and distinguish the "FirstEnergy" it regulates (the Ohio distribution utilities) from the "FirstEnergy" it does not (FirstEnergy Corp. and the rest of its subsidiaries).

No party will dispute the following: FirstEnergy Corp. (NYSE: FE) is not a party in this proceeding. FirstEnergy Corp. not a public utility. It does not have customers. It does not have tariffs. It does not even have employees. FirstEnergy Corp. is a holding company. Its business is

[2] "Direct Energy" collectively refers to Direct Energy LLC and Direct Energy Business Services LLC.

to own the common stock of subsidiary corporations, which are managed in four segments: Regulated Distribution, Regulated Transmission, Competitive Energy Services, and Corporate. The FirstEnergy utilities fall under the Regulated Distribution segment.

Although the Commission regulates the three Ohio subsidiaries that are the applicants in this proceeding, it does not regulate FirstEnergy Corp. The Commission cannot tell the parent company whether to issue dividends, when, or in what amount. It has no approval authority for issuances of holding company equity or debt. It cannot direct the holding company to deploy resources to certain businesses or withdraw resources from others. It has no say in corporate governance. It cannot levy fines or penalties against the parent. The Commission has no more direct legal authority over FirstEnergy Corp. than it does Goodyear.

While lacking direct supervisory authority over the parent company, the Commission does owe a responsibility to FirstEnergy Corp. in one respect. It setting rates, the Commission must authorize a "fair and reasonable" return on equity to shareholders. R.C. 4909.15(A)(2). FirstEnergy Corp. is the sole shareholder and thus the beneficiary of the authorized return. But the Commission is not required to authorize returns that will ensure the "financial integrity" of the utilities, let alone their shareholder (FirstEnergy Corp.), let alone the shareholder's shareholders (individual and institutional investors of FirstEnergy Corp.'s publicly traded stock). "[T]he rates' effect on the company's financial integrity (i.e., debt rating and dividend level) is but another of the risks which a utility, as any other unregulated enterprise, must bear. . . . ." *Ohio Edison Co. v. Pub. Util. Comm*., 63 Ohio St.3d 555, 564-65, 589 N.E.2d 1292 (1992). *See also Columbus Southern Power Co*., Slip Op. No. 2016-Ohio-1608 at ¶¶ 36-37 (rejecting "financial integrity" as grounds to authorize collection of capacity revenues exceeding capacity costs).

The FirstEnergy Ohio utilities are each a separate "electric distribution utility." R.C. 4928.01(A)(5). The rates they charge for distribution service are a function of regulation, not markets, and regulation has been very good to them. During the pendency of this case, the utilities' respective FERC Form 1s show double-digit increases in net income for 2015 compared to 2014. Toledo Edison's net income rose from just under $20 million to over $25 million, a 25% increase. (Direct Ex. 3 at 120.) Ohio Edison did even better, with net income rising 37%, from $103 million in the prior year to $141 million. (Direct Ex. 2 at 120.) CEI's net income soared 80%, from $36 million in 2014 to over $65 million in 2015. (Direct Ex. 4 at 117.) As the sole shareholder, FirstEnergy Corp. is entitled to *all* of this net income, which it may use to reinvest in any regulated or unregulated business, or pay to its own shareholders in dividends. (Tr. 75; 158.)

The Ohio utilities do not own electric generation facilities and therefore incur no generation costs. (Tr. 1252.) Under the most recently approved ESP and the one before it, generation for SSO customers is priced through an auction. (Tr. 308; 389-90.) The costs the utilities incur to secure generation is recovered through Rider GEN. (Tr. 377, 380.)

The FirstEnergy utilities rely on equity and debt capital to finance investment in their systems. As with any borrower, utilities with higher credit ratings are able to secure debt capital on the best terms. Thus, "the parent has a long history of providing equity to the utility companies, when it's necessary, in order to help those companies maintain their investment grade status . . . ." (Tr. 85.) Wall Street ratings agencies take different approaches in assigning credit ratings to holding companies and affiliates. Standard & Poor's assigns a credit rating to the consolidated operations of FirstEnergy Corp., which has the effect of the utilities receiving the same rating as the parent. (Tr. 101.) Moody's rates the parent company and its subsidiaries separately. (*Id*. at 101-102.) Although Moody's has placed FirstEnergy Corp. and its generation-owing affiliates on notice that it may downgrade their ratings to below investment grade, it has *not* issued a downgrade, and has *not* put the utilities' on ratings watch. (Direct Ex. 1; Tr. 171.) Even if Moody's eventually decides to downgrade FirstEnergy Corp., "the [utility] companies may still remain investment grade . . . ." (Tr. 102.)

The March 31, 2016 Order in this proceeding approved an ESP. FirstEnergy and other stipulating parties agreed, and the Commission found, that the ESP will allow the utilities to recover their cost of SSO service—that cost including a just and reasonable return on the investment of their shareholder, FirstEnergy Corp.[3] To the extent FERC's April 2016 action revoking FirstEnergy's affiliate waivers has dashed hopes for a ratepayer bailout of generation facilities the Ohio utilities do not own (*see* Tr. 1919), the consequences of that decision should be addressed with FERC, not the Commission. The Commission has already fulfilled its responsibility to ratepayers, the utilities, and their shareholder.

III. ARGUMENT

The argument portion of this brief has two sections. Section A explains why both the FirstEnergy and Staff proposals are unlawful. Section B proposes modifications to Staff's Rider DMR proposal that would make it more acceptable than the concept proposed, in the event the

[3] The stipulated return of 10.88 percent is *far* higher than the utilities could reasonably expect to receive in a distribution rate case. (See March 31, 2016 Order at 22-23.) The stipulated return is based on the return authorized in the utilities' 2007 distribution rate case. That return was based on financial models that relied on U.S. Treasury yields, which are the time ranged from 4.76% for 10-year bonds and 4.94% for 30-year bonds. *See* Case No. 07-551-EL-AIR, Staff Report at 17. The Commission may take administrative notice that 10-year treasuries currently yield 1.46% and 30-year treasuries 2.18%. *See* https://www.treasury.gov/resource-center/data-chart-center/interest-rates/Pages/TextView.aspx?data=yield (visited Aug. 15, 2016.) It is beyond dispute that the cost of capital generally, and FirstEnergy's specifically, is far lower now than it was in 2007. The continuing distribution rate "freeze" approved in the ESP benefits FirstEnergy greatly.

Commission decides there is merit in spending even more money on distribution modernization than the approved ESP already allows.

A. The proposals are unlawful.

Saying that FirstEnergy has "modified" Rider RRS is quite an understatement. A rider originally designed to recover the costs of generation purchases would now spare the utilities the inconvenience of actually purchasing generation. Rather than purchase from their affiliate at above-market prices, selling it at a loss, and billing distribution customers for the difference (*see* Tr. 318), the utilities would cut to the chase and begin collecting the money they projected would flow under these transactions without actually undertaking the transactions. (*See generally* Tr. 175-76.) There would be no strings attached to the money; the utilities might use it for distribution projects or they might use it to pay a dividend to their shareholder—they refuse to either commit to how they will spend the money or even take anything off the table. (Tr. 176-77.)

Staff's "distribution modernization rider" alternative, or Rider DMR, would accomplish the same result. The name is mere window-dressing. The mechanism would allow the utilities to start collecting \$131 million annually *not* as compensation for actual distribution investment, but for the express purpose of lending "credit support" to FirstEnergy Corp. This "credit support" (which FirstEnergy did not ask for in seeking rehearing) is intended to prevent a downgrade of the parent's investment-grade credit rating. If FirstEnergy Corp. has not received enough "credit support" after three years, it has an open invitation from Staff to come back and ask for more—for an amount even greater than \$131 million if they want. (Tr. 507-08.)

1. The rider charges would not be based on any "costs" incurred by the FirstEnergy utilities.

A threshold requirement of any ESP is that it function to recover "costs" of an electric distribution utility in providing SSO service. R.C. 4928.143(A); R.C. 4928.143(B)(2)(a-i). Modified Rider RRS does not seek recovery of "costs." Neither does Rider DMR.

a. Modified Rider RRS would impose a charge that is not based on any underlying cost.

Rider RRS was approved under the assumption that the FirstEnergy utilities would purchase generation from their unregulated affiliate, sell the power into the wholesale market, and charge or credit customers for the difference. (Tr. 160-62; 318.) Setting aside considerations of fairness and sound regulatory policy, the purpose of the rider was to recover costs the utilities would incur in purchasing generation from their affiliate. The proposal had some tangible economic substance, at least in the sense that the utilities would have paid for something and gotten something in return.

This is no longer the case. As a consequence of FERC's April 2016 decision revoking a waiver to engage in affiliate transactions, the utilities apparently have no intent of seeking approval to move forward with the PPA. The utilities are not going to purchase affiliate generation. (Tr. 114-15.) Because they are not going to purchase generation, there will be no transactions in which the utilities incur "costs" from their affiliate. (Tr. 175-76; 196; 315-19; 377; 380-82.) This is a problem for FirstEnergy because $0 actual costs means $0 recovery under Rider RRS.

The FirstEnergy proposal asks the Commission to call a tail a leg by treating projections and estimates relied on in the March 31 Order as "actual costs." (Tr. 315; 385.) FirstEnergy is not representing that this change is warranted because current projections will match future experience. It *cannot* make that claim because its "actual costs," under any sensible understanding of those words, will be $0: the transactions for which the projections were developed in the first place are not going to occur. The projections would become, as FirstEnergy describes them, "proxy costs" for calculating the "hedge." (Tr. 162.) In plain English, this means the "actual cost" variable in the Rider RRS formula would be populated with cost projections already in the record, not "actual costs" the FirstEnergy utilities will incur.

The "proxy costs" described by FirstEnergy are not "costs" authorized for recovery under R.C. 4928.143. The term "cost" is not defined in R.C. Chapter 4928, so there is no reason to give the term a different meaning than it has under "traditional" ratemaking specified in Chapter 4909. Under traditional ratemaking, a "cost" is generally understood to mean an "actual expenditure" or the equivalent. *See* R.C. 4909.151 (defining "costs" to include "operation and maintenance expense, depreciation expense, tax expense, and return on investment *actually incurred* by the utility.")(Emphasis added.) The same definition applies to rates established in an ESP. In *Columbus Southern Power Co.,* 128 Ohio St.3d 512, 2011-Ohio-1788 (*AEP ESP I*), the Commission characterized AEP Ohio's POLR charge as "cost based" because it reflected the output of financial models AEP used to guesstimate the "value" to shopping customers of having a standard service offer to switch back to. *See id.* ¶ 25. The Court deemed this finding an abuse of discretion. "Value to customers (what the model shows) and cost to AEP (the purported basis of the order) are simply not the same thing." *Id*. ¶ 26. AEP's failure to produce evidence of "any specific costs that they are incurring related to the POLR obligation" or other "actual out of pocket expense" precluded the Commission from finding that the charge was "cost-based." *Id*. ¶ 27 (internal quotations omitted).

Just like the AEP Ohio POLR Charge, FirstEnergy's proposal would authorize a charge based on the "value" to customers of the alleged "hedge" provided by Rider RRS. The utilities produce no evidence that they will incur any "cost" to provide this hedge. To the contrary, FirstEnergy continues to sell Rider RRS based on the alleged value it will provide for "economic development," "grid modernization" and, expressly, its "economic value." (FirstEnergy Ex. 197 at 12-13.) None of the factors allegedly giving Rider RRS the "value" ascribed to it has any relevance to whether the utilities incur a cost to provide a "hedge," and if so, how much.

Indeed, modified Rider RRS lacks both a "cost" *and* "service" component. The approved ESP establishes a standard service offer whereby the "services" necessary to receive electricity (generation, transmission, distribution, ancillary services) are provided for, and recovery of the "cost" of providing these services recovered. The modified Rider RRS offers no additional *utility* "service" to customers, nor imposes any additional "costs" on the utilities. Whether a pseudo-financial instrument such as the "hedge" provides value to customers as a "service" (Tr. 209) only begs the question of whether the charge associated with this "service" has any relation to its "costs"—whatever those are, if there are any. *See AEP ESP I*, ¶ 27 ("Even assuming AEP accurately priced the option, we fail to see how the amount a customer would be willing to pay for the right to shop necessarily establishes AEP's cost to bear the attendant risk.").

The Court's recent decision in *Columbus Southern Power Co*., Slip Opin. No. 2016-Ohio-1608 (Apr. 21, 2016) (*AEP ESP II*) should put to rest any lingering debate about whether an ESP's revenue mechanisms must be tied to "costs." The Commission approved a rider allowing AEP Ohio to collect capacity revenues in excess of AEP's cost of capacity. The excess revenue was necessary, the Commission said, for AEP to "maintain its financial integrity as well as its ability to attract capital." *Id*. ¶ 36. The Court found this argument not only unpersuasive, but completely irrelevant. "In short, none of the evidence cited in the ESP Order is relevant to whether it was necessary for AEP to recover additional revenue through the RSR *beyond the* *costs that the company incurred to provide capacity service*." *Id*. ¶ 37 (emphasis added). The Court found no error in the calculation of *actual* capacity costs, but directed the Commission to cease any further recovery of amounts *above and beyond* these costs. *Id*.

The Court's subsequent (and highly unusual) decision reversing the Commission's bailout of DP&L shareholders by merely citing the *AEP ESP II* decision must surely put the Commission on notice that the ends do not justify the means. *See Dayton Power & Light Co*., Slip Opin. No. 2016-Ohio-3490 (June 20, 2016). R.C. 4928.143 leaves no discretion; the principle of cost-based ratemaking cannot be sacrificed at the alter of "financial integrity." The only distinguishing factor among FirstEnergy's Rider RRS, AEP Ohio's Rider RSR, and DP&L's SSR, is the jumbling of the letters in in the acronyms. That Rider RRS will allegedly provide "economic value" or help maintain "financial integrity" simply does not establish that the charge to be levied is necessary to recover "costs" incurred by the utilities.

b. Rider DMR is a pretext for the collection of excess profit distributable to FirstEnergy Corp.

Staff also points to the lack of any economic substance underlying FirstEnergy proposal. The lack of an economic basis for the calculation, combined with the fact that it would be levied as a non-bypassable generation charge, leads Staff to conclude that the modified Rider RRS would collect the equivalent of transition charges. (Staff Ex. 15 at 13-14.) Staff is correct, and Direct Energy agrees. But the same lack of economic substance that confirms Rider RRS is a transition-cost recovery mechanism in disguise also dooms the Staff alternative. What is sauce for the goose is sauce for the gander.

On the surface, a "distribution modernization rider" would seem consistent with R.C. 4928.143. Only an "electric distribution utility" may provide distribution service, and it is commonly understood that modernization projects entail "costs"—actual expenditures to provide a service useful to Ohio customers. If Rider DMR functioned as advertised, R.C. 4928.143 would present no obstacle to its approval.

But Rider DMR will not function as advertised, and is not intended to. We know this because Staff admits this, coming right out and saying: “Rider DMR is not a revenue requirements rider.” (Tr. 1254.) Then what is it? The Commission may wonder how the idea of a yet another distribution rider found any traction to begin with. The Commission would be in good company. The approved ESP already assures the utilities ample opportunity to recover distribution costs generally, and grid modernization costs in particular. (Tr. 1222-23; 1228-29.)

So Rider DMR either (a) is unnecessary or (b) would allow double-recovery of grid modernization costs. When asked whether customers would be paying twice for grid modernization—once through Rider AMI and again through Rider DMR—the architect of Staff’s proposal, Dr. Choueiki, denied that they would. These riders “would be for different purposes. One of them is for credit support and one of them for modernization . . . .” (Tr. 1229.) Echoing the fact that these riders serve different purposes, Ms. Turkenton explained that “one is credit support and one is plant infrastructure.” (Tr. 473-74.)

The testimony explaining away concerns about double recovery of grid modernization costs confirms that Staff witness Mr. Buckley meant what he said in explaining the purpose of Rider DMR. “Staff is recommending the new rider [Rider DMR] be created to allow for recovery of $131 million from the Ohio Regulated Distribution Utilities’ customers. *The rider would be established to allow the Ohio Regulated Distribution Utilities to provide the appropriately* *allocated support for FirstEnergy Corporation (FE) to maintain investment grade by the major credit rating agencies.*" (Buckley at 2.)(emphasis added)[4]

That is no less than *three* Staff witnesses testifying under oath that Staff's proposed Rider DMR is *not* about modernizing the grid, but about "credit support" for FirstEnergy Corp. While a theoretical "distribution modernization rider" could pass muster under R.C. 4928.143, the one Staff actually proposes does not. Staff *admits* that the purpose of the rider is *not* to fund distribution modernization for the utilities; it is to provide "credit support" for FirstEnergy Corp. Tr. 509-10.[5] Nothing in Staff's proposal requires the utilities to modernize the grid. (Tr. 433-34.) Indeed, for its part, FirstEnergy is unwilling to commit to spend the money it would receive under Rider RRS for grid modernization, or for anything else. (Tr. 69-70; 1609-10.) Not even FirstEnergy believes that the money Staff wants to dole out is needed for "grid modernization."

Staff believes it is necessary to support the parent company's credit rating because if the parent gets downgraded, so will the utilities. Borrowing costs will increase and ratepayers will pick up the tab, so everyone should think of the proposal as helping ratepayers, not the shareholder. Staff is wrong. The utilities are not guaranteed to recover their cost of long-term debt, whatever that cost happens to be. They are entitled to recover prudent, reasonable expenses. To the extent the utilities maintain their investment grade rating but the parent does not, the utilities should remain able to secure debt based on their separate credit rating. A decision to

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[4] By "appropriately allocated," Mr. Buckley means the Ohio utilities' portion of the full level of additional cash FirstEnergy Corp. purportedly needs in order to stay within the metrics necessary to maintain its investment-grade status. (Staff Ex. at 3.) If the Ohio utilities pony-up their 22% portion but their affiliates do not contribute their remaining 78% share (and no evidence is offered that they will), then Staff's proposal will not fulfill its stated goal. The Commission would simply authorize the utilities to throw good money after bad.

[5] At this point in the proceeding, notwithstanding Staff's sworn testimony, the hearing examiner forbade the parties from calling Staff's proposal a "credit support rider" and admonished the parties "to refer to the staff's proposed rider the way they have characterized it." (Tr. 444.)

secure debt through the parent at a higher cost (because of the parent's lower credit rating) would necessarily flag a ratemaking disallowance for the difference between the interest rate actually secured and the rate the utilities could have obtained on their own. Even if market conditions were such that the utilities had no practical alternative but to secure debt through the parent, the Commission would be well within its authority to partially disallow the excess portion of interest expense caused by the parent's non-Ohio, non-utility activities. *See Cincinnati Gas & Elec. v. Public Util. Comm'n,* 86 Ohio St.3d 53, 59, 999-Ohio 81 (affirming disallowance of imprudent project development costs; citing "institutional hubris" of the utility.)

Thus, the entire premise for offering "credit support" to the parent is simply wrong. Any rational actor who could obtain more favorable loan terms under its own credit that it could by applying for a loan with a co-signer would do so. Staff is basically offering an incentive to the utilities to act irrationally by foregoing lower cost financing under their own credit rating so they can obtain higher cost debt with their parent. This makes no sense. In public utility regulation, the term for engaging in financial transactions that make no sense is called "imprudence." *See City of Cincinnati v. Public Util. Comm'n*, 67 Ohio St. 3d 523, 1993-Ohio-79, at 528 (defining a "prudent decision" as "one which reflects what a reasonable person would have done in light of conditions and circumstances which were known or reasonably should have been known at the time the decision was made.")(Internal quotation omitted.)

Staff is also mistaken to believe that a bailout disguised as a distribution rider is somehow superior to a bailout disguised as a generation rider. The Court's fundamental problem with AEP Ohio's Rider RSR was not that it was structured as a generation charge. The problem was that the charge exceeded the costs for which the rider was being levied. *AEP ESP II* ¶ 37 ("[N]one of the evidence cited in the ESP Order is relevant to whether it was necessary for AEP to recover additional revenue through the RSR beyond the costs that the company incurred to provide capacity service."). Indeed, while at least *some* of the revenue under AEP's rider was tied to costs, *none* of the revenue generated under Rider DMR would be. The lack of any nexus between revenues recovered under Rider DMR and costs incurred by the utilities is what makes the rider unlawful, not whether the rider is characterized as generation or distribution.

Rider DMR is not about distribution. It is not about modernization. It is not even about the FirstEnergy EDUs. Rider DMR is a mechanism designed to collect money to be made available to FirstEnergy Corp. Saying the rider is for a different purpose doesn't make it so.

2. The proposals have the express purpose and effect of subsidizing non-utility businesses.

Neither proposal finds any authorization under Ohio law, and they must be rejected. But even if the proposals did pertain to costs recoverable under R.C. 4928.143, there is another problem.

The Commission has a mandatory duty to effectuate state energy policy. R.C. 4928.06(A) ("[T]he [Commission] shall ensure that the policy specified in section 4928.02 of the Revised Code is effectuated."). These policies include the avoidance of anticompetitive subsidies. Thus, the Commission's decision on rehearing must "[e]nsure effective competition in the provision of retail electric service by avoiding anticompetitive subsidies flowing from a noncompetitive retail electric service to a competitive retail electric service or to a product or service other than retail electric service, and vice versa, including by prohibiting the recovery of any generation-related costs through distribution or transmission rates[.]" R.C. 4928.02(H).

Rider RRS seeks authority to do that which the Revised Code expressly prohibits: levy a charge on customers of a "noncompetitive retail electric service" (i.e., distribution) to produce a revenue stream that *exceeds* the cost of providing this service. The excess revenue will be available to FirstEnergy Corp., who may use it to invest in subsidiaries that furnish "competitive retail electric service," as well as "product[s] or service[s] other than retail electric service." This would result in a blatant "anticompetitive subsid[y]" of FirstEnergy Corp.'s unregulated subsidiaries, which compete against CRES providers like Direct Energy.

Rider DMR is problematic for the same reason. The FirstEnergy utilities would collect money that they *do not* need for "grid modernization" (and did not ask for in seeking rehearing). When—surprise of surprises—the utilities are unable to come up with ways to spend an additional $131 million annually (on top of the additional distribution revenue already authorized under the ESP), the money will be available for FirstEnergy Corp. Once the money has been paid to FirstEnergy Corp. (by dividend or otherwise), the parent may do with it as it pleases.

Staff may say, and the Commission may even believe, that FirstEnergy Corp. could be forced to use revenue collected through Rider RRS or Rider DMR for projects and activities that benefit the Ohio utilities and their customers. This is wishful thinking. The Commission has authority to restrict the *payment* of dividends from the utilities to the shareholder. R.C. 4905.45, 4905.46. The Commission also has approval authority for debt issuances *by the utilities*. R.C. 4905.401. But once FirstEnergy Corp. *receives* a dividend, that money belongs to FirstEnergy Corp. (Tr. 158.) However the parent wishes to spend this money is "ultimately up to the parent to decide." (*Id*.) Any side agreements, understandings, or wink-nod arrangements to the contrary do not have the force of law.

FirstEnergy Corp. may manage its empire however it sees fit. Nothing in Rider RRS or Rider DMR changes that. Whatever funds these riders generate would ultimately be available to FirstEnergy Corp. and will be used in *its* discretion—and no one else's.

B. If the Commission approves Rider DMR, it should modify the rider and impose conditions.

To be abundantly clear, Direct Energy supports the principle of grid modernization. Initiatives like AMI, Volt/VAR control and other enhancements will provide a platform for CRES providers to offer new and better programs. FirstEnergy *should* recover these costs. If Rider DMR is approved, it should be modified to ensure that sensible grid modernization projects are pursued and the money authorized for such projects be spent for the purpose authorized.

The approved stipulation required FirstEnergy to commence a grid modernization docket within 90 days, and the company complied with that directive. FirstEnergy's Grid Modernization Business Plan is now before the Commission in Docket 16-0481. Surely that docket provides the appropriate forum to address grid modernization proposals by FirstEnergy and other stakeholders. If the Commission is serious about modernizing the grid, it should give FirstEnergy and other stakeholders the opportunity to vet proposals with each other and Staff, and try to reach consensus where possible. Simply giving FirstEnergy $131 million up front and effectively telling the parties, "Go figure out how (or whether) to spend it," would reflect indifference to any notion of value, accountability, or cost-effectiveness.

Rider DMR should also function like a rider, not a cash-infusion device. The rider should be set initially at $0 and trued-up at regular intervals. Like any other rider, the burden should be on FirstEnergy to establish that how it spent the money was prudent, and how much it spent is just and reasonable. FirstEnergy should also be put on notice that the Commission will not tolerate the expenditure of money on projects that give affiliated interests an advantage over competitors.

These limitations and conditions are not asking for much, and only what would be required of any other utility seeking a rider. A mechanism called a "rider" should function as a rider. If the Commission is intent on funneling cash from distribution customers to FirstEnergy Corp., it should do so transparently. Calling a ratepayer-from- money separation device a "rider" would conceal the true nature of what the Commission is being asked to do.

IV. CONCLUSION

This is a high-profile case involving many stakeholder interests. But that doesn't make it a complicated case. It is actually a simple case. The FirstEnergy utilities got what they needed from the approved ESP. Now they are back to get something for their parent and sole shareholder. Staff wants to give FirstEnergy *something*, just not everything it wants. In the past few years, three different ESPs have been shot down by the highest Court in Ohio for precisely the same flaws on display in this case. The reputation of this Commission as an institution is now at stake. It is important for the Commission to get this case right.

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Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that a copy of this Post-Hearing Brief was served by electronic mail this 15th day of August, 2016, to the following Parties of Record.

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