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BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of The East Ohio Gas Company d/b/a Dominion East Ohio for Authority to Increase Rates for its Gas Distribution Service.	**Case No. 07-829-GA-AIR**
In the Matter of the Application of The East Ohio Gas Company d/b/a Dominion East Ohio for Approval of an Alternative Rate Plan for its Gas Distribution Service	**Case No. 07-830-GA-ALT**
In the Matter of the Application of The East Ohio Gas Company d/b/a Dominion East Ohio for Approval to Change Accounting Methods	**Case No. 07-831-GA-AAM**
In the Matter of the Application of The East Ohio Gas Company d/b/a Dominion East Ohio for Approval of Tariffs to Recover Certain Costs Associated with a Pipeline Infrastructure Replacement Program Through an Automatic Adjustment Clause, And for Certain Accounting Treatment	**Case No. 08-169-GA-ALT**
In the Matter of the Application of The East Ohio Gas Company d/b/a Dominion East Ohio for Approval of Tariffs to Recover Certain Costs Associated with Automated Meter Reading Deployment Through an Automatic Adjustment Clause, and for Certain Accounting Treatment	**Case No. 06-1453-GA-UNC**

APPLICATION FOR REHEARING OF THE EAST OHIO GAS COMPANY D/B/A DOMINION EAST OHIO

Pursuant to R.C. 4903.10 and Rule 4901-1-35, Ohio Administrative Code, The East Ohio Gas Company d/b/a Dominion East Ohio, hereby files its Application for Rehearing of the Opinion and Order issued in the above-captioned case on October 15, 2008 ("Order"). As

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explained in more detail in the attached Memorandum in Support, the Order in this case is unreasonable and unlawful on the following grounds:

1. The Commission denied DEO due process by not permitting DEO to brief or argue the rate-of-return issue and then by reducing the rate of return.

2. The portion of the Order reducing DEO's rate of return was unlawful because it lacked record support.

3. The portion of the Order reducing DEO's rate of return was unreasonable on its face, because it relied on a factor increasing risk to reduce the rate of return.

4. The Order violated R.C. 4909.15(D)(2)(a) by authorizing a cost of debt lower than DEO's actual embedded cost of debt.

For these reasons, as demonstrated in the Memorandum in Support of this Application, attached hereto, the Commission should grant this Application for Rehearing and modify the October 15, 2008 order to reflect the rate of return and revenues recommended as stipulated to by the parties.

Respectfully submitted,

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MEMORANDUM IN SUPPORT OF APPLICATION FOR REHEARING OF THE EAST OHIO GAS COMPANY D/B/A DOMINION EAST OHIO

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I. INTRODUCTION

In its October 15, 2008 Opinion and Order (the "Order") in these matters, the Commission, while purporting to approve the Stipulation reached by the parties, nevertheless modified the Stipulation by reducing the Company's recommended rate of return by 20 basis points to 8.29 percent. The Commission's stated rationale was purportedly based on the proposed modified straight-fixed variable ("SFV") rate design, testimony at the public hearings and "deteriorating economic conditions." But none of these bases can support the Commission's decision: the modification to the stipulated rate of return was unsupported, unreasonable and, ultimately, unlawful.

When the parties presented their oral arguments in this case to the Commission on September 24, 2008, no party had reason to expect that the Order would reach any substantive issue but rate design. The stipulation was opposed by no one. It was the result of lengthy and serious negotiations; it resulted in a unanimous recommendation that the Company was entitled to a $40.5 million rate increase and an 8.49% rate of return. A single issue was reserved for dispute: rate design. The Commission recognized this reservation and instructed the parties to brief and argue that issue—and only that issue.

If there was any issue the parties could have reasonably expected to be *off* the table, rate of return would have been it. Not only was it a stipulated issue, but DEO was the only party who even introduced testimony regarding a specific rate of return into the record. Indeed, no witness ever recommended on the record that DEO's rate of return be reduced below the Stipulated return. Further, in the Attorney Examiner's instructions for briefing (Tr. VI, pp. 85-86) and in its September 19, 2008 Order, the Commission expressly precluded the parties from briefing or arguing any issue other than rate design. Thus, no arguments were heard regarding rate of

return. Indeed, DEO was given no opportunity to defend its position on the rate of return in the Stipulation in response to any challenge to that return.

The Commission's actions to cut DEO's rate of return — without a record support, without a valid reason to do so, and without allowing the parties to be heard — represented not just surprise, but an ambush. As demonstrated more fully below, the Order violated Ohio law and stands subject to reversal. DEO respectfully requests the Commission to grant rehearing and adopt the unopposed Stipulation as filed regarding the rate of return and revenues recommended therein.

II. ARGUMENT

A. The Commission's Opinion and Order Reducing the Stipulated Rate of Return and Revenue Requirement Was Unlawful and Unreasonable.

The Supreme Court "shall" reverse, vacate, or modify "[a] final order made by the public utilities commission . . . if, upon consideration of the record, such court is of the opinion that such order was unlawful or unreasonable." R.C. 4903.13. The Commission's *sua sponte* adjustment to DEO's rate of return and revenue requirement was unlawful and unreasonable. The appropriate remedy is for the Commission to grant rehearing and adopt the stipulation as filed on those issues.

The Commission reduced DEO's rate of return by 20 basis points and DEO's revenue requirement by $3 million. The sole stated justification for doing so was two sentences:

> [T]he Commission is cognizant of the reduction in risk assumed by the company as a result of the rate design approved by the Commission. This, in conjunction with the testimony heard in local hearings and, *most importantly*, taking notice of deteriorating economic conditions, leads us to alter downward the approved rate of return by 20 basis points, to 8.29 percent.

(Order, p. 27 (emphasis added).)

This portion of the Order is unlawful. There are four reasons why. First, it represents a denial of due process. Second, it lacks any record support. Third, it is facially unreasonable and self-contradictory. Lastly, it unlawfully authorizes a less-than-complete recovery of DEO's embedded cost of debt. In addition, the Commission's action, unless corrected, will chill efforts to settle cases before it. The Commission should therefore grant rehearing, abandon this adjustment, and adopt the unopposed stipulation.

B. The Commission Denied DEO Due Process.

The Commission prohibited DEO from presenting argument on the issue of rate of return—and then reduced the rate of return. This straightforward denial of DEO's opportunity to be heard violated due process.

1. Due process requires a fair hearing and an opportunity to be heard.

The Commission may not deprive "any person of . . . property without due process of law." U.S. CONST. amend. XIV; *see Direct Plumbing Supply Co. v. City of Dayton* (1941), 138 Ohio St. 540, 544 (holding that the Ohio due-process clause is "considered the equivalent of the 'due process of law' clause in the Fourteenth Amendment"). Where the law requires a hearing, due process demands the hearing be fair. *State ex rel. Ormet Corp. v. Indus. Comm. of Ohio* (1990), 54 Ohio St. 3d 102, 104 ("[S]tatutory procedural provisions aside, a requirement to conduct a 'hearing' implies a 'fair hearing.'"); *see* R.C. 4909.18, 4909.19 (providing for hearing in this case).

Fundamentally, the Commission must give parties an opportunity to be heard. *Cent. Ohio Gas Co. v. Pub. Util. Comm.* (1924), 110 Ohio St. 663, 663 (reversing the Commission where order was issued "without . . . an opportunity afforded to the plaintiff in error to be heard"). Among other things, it is improper for an administrative agency "to deny [a party] an opportunity to rebut" the evidence on which a decision is based. *State ex rel. Chrysler Plastic*

Prods. Corp. v. Indus. Comm. of Ohio, 39 Ohio App. 3d 15, 16 (10th Dist. Ct. App. 1987); *Forest Hills Utility Co. v. Pub. Util. Comm.* (1974), 39 Ohio St. 2d 1, 3 (reversing the Commission where it denied party "an opportunity to explain and rebut" the evidence on which it relied) (internal quotation marks omitted). By denying DEO an opportunity to be heard, the Order runs afoul of these authorities.

2. The Commission prohibited DEO from presenting argument regarding the rate-of-return adjustment.

In numerous statements on the record and in a procedural entry, the Commission limited argument as to a single issue: rate design. (*See, e.g.*, Tr. VI (Attorney Examiner), p. 85 ("[I]nitial briefs . . . . would address *the sole issue* of rate design.") (emphasis added); *id.*, p. 86 ("[A]ny party . . . would be allowed to orally argue *that issue* [*i.e.*, rate design] because that's *the issue* that the Commission has right now before it.") (emphasis added); *see also* Entry, ¶ 3 (Sept. 19, 2008) (providing "opportunity to present oral arguments on *the rate design issue* before the Commission") (emphasis added).) Thus, when the Commission reduced DEO's rate of return, the Commission did so after explicitly denying the Company any opportunity for brief or argument on that issue. Given the Commission's explicit instructions, its apparent intentions, and the lack of opposition on any other issue, DEO had no reason to seek to argue the rate-of-return issue, or otherwise protest the Commission's limitations.

The Order and underlying process present many problems—problems that go to the heart of fairness. The decision is not rooted in evidence, it does not demonstrate careful reasoning, and it is the fruit of an unfair process. The cure for these problems is not to find a witness who will explain how investors expect lesser returns for greater risk. The cure is to grant rehearing and adopt the Stipulation as filed. The unrebutted record established that the Stipulation was the

product of serious bargaining, that it benefited rate payers and that it violated no important regulatory principle or practice. The Commission should approve the Stipulation accordingly.

C. The Rate-of-Return Reduction Is Unsupported by the Record.

When the Commission ordered a reduction in DEO's rate of return and revenue requirement, it did so without the support of the record. This violates Ohio law and represents reversible error.

In contested cases, the Commission must "file . . . findings of fact and written opinions setting forth the reasons prompting the decisions arrived at, *based upon said findings of fact.*" R.C. 4903.09 (emphasis added). The Revised Code instructs the Supreme Court to reverse a Commission order "if, *upon consideration of the record,* such court is of the opinion that such order was unlawful or unreasonable." R.C. 4903.13 (emphasis added). Accordingly, "factual support for commission determinations must exist in the record." *Tongren v. Pub. Util. Comm.* (1999), 85 Ohio St. 3d 87, 90. Indeed, the Commission "abuses its discretion when it renders an opinion on an issue without record support." *Id.*; *see also Canton Storage and Transfer Co. v. Pub. Util. Comm.* (1995), 72 Ohio St. 3d 1, 26-33 (reversing Commission order in part because no record evidence supported its conclusions); *Conrail v. Pub. Util. Comm.* (1989), 47 Ohio St. 3d 81, 84-85 (reversing Commission order where conclusions were based on speculation and "unsupported by the record"). As with any Commission ruling, cost-of-equity and rate-of-return determinations must be supported by the record to be lawful. *Gen. Tel. Co. v. Pub. Util. Comm.* (1972), 30 Ohio St. 2d 271, 276 (reversing the Commission where "[t]he only evidence found in the record pertaining to the rate of return is that provided by appellant" and stating that "[t]he record being incomplete, no decision as to the reasonableness of the determined rate of return can be made"); *cf. Babbit v. Pub. Util. Comm.* (1979), 59 Ohio St. 2d 81, 92 ("Considering that

the hearings before the commission involved extensive testimony on rate of return by four expert witnesses, we cannot say that the [order] was against the weight of the evidence.").

Here, the Commission ostensibly relied on three factors to reduce DEO's rate of return and revenue requirement: (1) the impact of straight-fixed variable rate design ("SFV") on the cost of capital; (2) "testimony heard in public hearings"; and (3) "deteriorating economic conditions." (Order, p. 27.) As shown below, not one of these bases is supported by the record.

1. The record does not show that SFV should reduce the cost of equity in this case.

One basis for the cost-of-capital reduction was a purported "reduction in risk assumed by the company as a result of [SFV] rate design." (Order, p. 27.) No evidence in the record supports this statement.

The only witness to offer testimony regarding the impact of rate design on the cost of capital (in fact, the only witness to offer direct testimony on rate of return) was DEO witness Dr. Michael Vilbert. Dr. Vilbert's testimony does not support an SFV-related reduction. (*See* DEO Ex. 9.0 & 9.1; Tr. I, pp. 10–82.) He testified that it was "not likely that a decoupling mechanism [such as SFV] will substantially affect the cost of equity." (DEO Ex. 9.1, p. 10.) He explained that "investors get compensated for bearing risk that cannot be diversified away" (*id.*, p. 9), and the risks addressed by SFV *can* be diversified away (Tr. I, pp. 72–73). Further, his research showed that "several of the comparable companies in the Staff Report already operate under a decoupling mechanism," meaning that an SFV-related cost-of-capital adjustment would constitute an unnecessary and unwarranted adjustment. (*Id.*, p. 10.) Thus, the only witness that testified on this point specifically contradicted the Commission's adjustment.

Dr. Vilbert's testimony stands unrebutted. No other party introduced testimony concerning the calculation of the cost of equity, and the record contains little else addressing the impact of SFV on capital cost. Staff witness Steve Puican came closest to testifying on the issue. Although he offered no direct testimony regarding rate of return, Mr. Puican fielded a single question from the bench on whether the stipulated rate of return incorporated a reduction for SFV. Mr. Puican explained that Staff had made an adjustment to its original rate-of-return analysis and that this revised analysis reflected that "there is reduced risk associated with the SFV rate design." (Tr. VI, p. 84.) Notably, Mr. Puican did not testify about how Staff determined its recalculated range of returns or the basis for any redaction in that range. Nevertheless, he further testified that the rate of return in the Stipulation fell within the recalculated range of returns recommended by Staff. (*Id.*)

Consequently, there is nothing in the record to support a reduction of the Stipulation's recommended rate of return. To the extent that SFV rate design purportedly reduces risk, such risk assessment was already reflected in the Stipulation's recommended rate of return. Because nothing in the record supports any further reduction—not to mention any specific amount of a reduction—the Commission's rejection of the rate of return set forth in the Stipulation is without record support.

2. "Testimony at public hearings" does not support a reduction in DEO's rate of return.

The Commission also referenced "testimony heard at public hearings" as a basis to reduce DEO's rate of return. (Order, p. 27.) As a purported basis for the reduction, however, this is fatally imprecise. *Tongren*, 85 Ohio St. 3d at 90 (reversing the PUCO's order where the Court could not "determine what record evidence was considered by the Commission"). The Commission failed to specify which witness (or witnesses) at which of the ten public hearings

recommended or justified a rate-of-return reduction. Of greater concern, the Commission failed to describe in any way the content of the pertinent testimony and why it persuaded the Commission to make the reduction.

As the Commission observed, "The principal concern expressed by customers, both at the public hearings and in letters, was in response to the recommendation made by the staff pertaining to the appropriate rate design . . . ." (Order, p. 5.)[1] For customers addressing that topic, as Mr. Murphy testified, "a number of those customers were operating under incorrect assumptions." (Tr. IV p. 64-66.)[2]

At most, the public testimony (to the extent that it did not deal with rate design) discussed the public's dislike for any rate increase or a particular customer's circumstances in potentially having to deal with a rate increase. None of that testimony justifies modifying the Stipulation's rate of return. In fact, as the Commission has recognized, the Stipulation includes a number of features that will help customers having trouble coping with their bills, including: over $9,500,000 in DSM spending, most of which is targeted for low-income customer programs (Order, p. 7), and $1,200,000 to organizations assisting low-income customers (*id.*). Further, the Commission established a pilot program to provide discounts to low-income customers. (*Id.*, pp. 26-27.) Given the assistance provided in the Stipulation (and elsewhere in the Opinion) and given the Commission's finding that the SFV rate design proposed by Staff, DEO and OOGA actually *benefits* low-income customers by lowering their bills (on average) (Order, p. 23), any

[1] Notably, in the Commission's discussion of the public hearings, the issue of rate of return is not mentioned at all.

[2] As an example, one customer testified that no matter how much he conserved, he would still pay the same amount to the gas company. (*Id.*) This view ignores the role played by the commodity cost in a customer's total bill. (*Id.*)

additional relief for such customers through an unsupported reduction in the Company's rate of return is unjustified.

Moreover, all of the parties to the Stipulation were either present at, or had access to transcripts from, the local hearings. The timing of the Stipulation was no accident. Several parties made it clear that they wanted to consider all of the comments made at the local hearings before entering into even a partial Stipulation. As a result, the Stipulation was not finalized and filed until all ten local public hearings were conducted. Thus, all parties were keenly aware of the public comments received and nonetheless agreed to an 8.49% rate of return.

Simply put, there is no nexus between anything contributed through public testimony and the Commission's decision to reduce the Stipulation's rate of return. Even if there was such a nexus, the Commission failed to articulate the specific basis for it. For that reason too, the Commission's decision was in error.

3. There is no testimony in the record recommending or justifying a reduction in rate of return based on deteriorating economic conditions.

In the Commission's own words, the "most important[]" factor justifying its rate-of-return reduction was "deteriorating economic conditions." (Order, p. 27.) Yet, no witness even mentioned reducing the rate of return based on "deteriorating economic conditions," much less recommended it. No one testified, with any opportunity for cross-examination, what level of reduction would be appropriate, what methodology should be used to determine the level of reduction, and why such a methodology should be followed.[3]

What methodology, if any, undergirded the Commission's 20-basis-point reduction is unclear. But no factor relied upon by the Commission is supported by the record, which

[3] As shown in Section II.D.1 below, whether a witness *could* make such a recommendation without automatically discrediting himself is doubtful.

undermines the reduction altogether. As noted above, the Stipulation and the Commission's Order otherwise provide a substantial measure of assistance to those who may have trouble paying their bills. As demonstrated further below, reducing DEO's rate of return based on "deteriorating economic conditions" is exactly opposite of what the Commission should do in this economic climate. In sum, to reduce DEO's revenue requirement without evidence is reversible error, and the Commission should reinstitute the unanimously stipulated rate-of-return.

D. The Portion of the Order Reducing the Rate of Return Is Facially Unreasonable and Self-Contradictory.

In addition to being unsupported by the record, the Order is demonstrably unreasonable. The Commission must approve a "fair and reasonable" rate of return, R.C. 4909.15(A)(2), and Commission orders must be reasonable, *see* R.C. 4903.13. Because the most important factor relied upon by the Commission in *reducing* the return—deteriorating economic conditions—in fact, justifies an *increase*, the Order contradicts itself and otherwise exhibits inconsistent reasoning.

1. Increased risk does not justify a reduced rate of return.

The Commission's order, insofar as it reduced rate of return based on a factor that increases risk, is not "reasonable." Risk and return are of a feather—they rise together, and they fall together. The Supreme Court has recognized that factors increasing risk tend to justify an increased rate of return. *See Consumers' Counsel v. Pub. Util. Comm.* (1983), 4 Ohio St. 3d 111, 114–15 (upholding "higher rate of return" authorized based on finding of "increased risk to investors"); *Ohio Edison Co. v. Pub. Util. Comm.* (1992), 63 Ohio St. 3d 555, 563 ("[T]he return to the equity owner should be commensurate with returns on investments in other enterprises having corresponding risks."); *Consumers' Counsel v. Pub. Util. Comm.* (1980) 64 Ohio St. 2d 71, 78 (noting that "investors . . . require an increased yield to compensate for . . . industrial and

financial risks"). Accordingly, if a factor increases risk, it does not support reducing the rate of return.

The Commission's adjustment, however, is premised on just such reasoning. While deteriorating economic conditions at least arguably support the approval of items like more DSM spending, assistance to low-income customer support organizations, or the low-income pilot program, such conditions do not support reducing the return to investors. A deteriorating economy may mean a loss of major commercial or industrial customers. It may mean greater cut-backs in usage by all customers and thus a potential loss of revenue. In this instance, it means tightening credit markets and an increased—not decreased—cost of capital. In short, "deteriorating economic conditions" mean more risk, not less.

This point hardly requires proof. Numerous economic articles and treatises demonstrate that investors become risk-averse in times of economic downturn and thus require an added risk premium. As one commentator observed:

> The risk premium is highest in a recession because the stock is a poor hedge against the uninsurable income shocks, such as job loss, that are more likely to arrive during a recession. . . even though per capita consumption growth is poorly correlated with stocks returns, investors require a hefty premium to hold stocks over short-term bonds because stocks perform poorly in recessions, when the investor is most likely to be laid off.

G.M. Constantides, "Understanding the Equity Risk Premium Puzzle," *Handbook of the Equity Risk Premium* (2008). Another author similarly noted:

> In economic recessions, investors are exposed to the double hazard of stock market losses and job loss. Investment in equities not only fails to hedge the risk of job loss but also accentuates its implications. Investors require a hefty equity premium in order to be induced to hold equities.

C-J. Kim, et al., "Is There A Positive Relationship Between Stock Market Volatility and the Equity Premium," *36 Journal of Money and Credit Baking* (2004).

Recent headlines bear witness to this truth. Our economy—locally, statewide and nationally—has undergone unprecedented contractions in liquidity and credit. *See, e.g., "Crisis Reverberates in Credit, Stock Markets – Dow Plunges 7.9%, Furthest Since '87, On Recession Fears,"* Wall Street Journal, Oct. 16, 2008, at C1; *"Is the era of easy credit over for the long haul?,"* The Associated Press, Oct. 13, 2008; *"Area firms get swept up in credit-crunch crisis,"* Toledo Blade, Oct. 11, 2008, at B6; *"Crisis on Wall Street: Risk Fears Threaten Economy, Says Fed,"* Wall Street Journal, Oct. 10, 2008, at C4; *"Credit markets still tight as stocks plunge,"* The Associated Press, Oct. 6, 2008; *"...[F]inancial analysts agree that we're heading into a world of tighter credit....,"* Cleveland Plain Dealer, Oct. 5, 2008, at A1; *"Corporate News: Utilities' Plans Hit by Credit Markets,"* Wall Street Journal, Oct. 1, 2008, at B4; *"Local credit can be had, but pinch is tightening,"* Columbus Dispatch, Sept. 27, 2008, at 01A. The stark reality of our deteriorating economy is that the cost of capital has gone up, not down. In fact, if the Commission were to accurately account for deteriorating economic conditions, the Commission would *increase* DEO's rate of return.

Moreover, the Commission's action only exacerbates the true cost of capital for DEO. With an unsupported, apparently arbitrary, and flatly contradictory reduction in the Company's rate of return, the Commission has unwittingly sent a signal to potential investors in Ohio utilities that requests for rate relief will be reduced regardless of the true cost of service or a fair rate of return. When the Commission acts in this way, investors can only wonder whether utility requests will be dealt with fairly and based on the record. To the extent that the Commission, by acting arbitrarily and without justification, is viewed by the investment community as "anti-utility," that could only increase the risk that investors would place on utilities in this state, and thus increase the cost of capital of all of Ohio's public utilities.

After all, "[a] public utility is entitled . . . to earn a return . . . equal to that generally being made at the same time and in the same general part of the country on investments in other business undertakings which are attended by corresponding, risks and uncertainties." *Bluefield Waterworks & Improvement Co. v. Pub. Serv. Comm. of W. Va.*, 262 U.S. 679, 692–93 (1923). If the Commission means what it says, how can it avoid shaving points off of every Ohio utility's rate of return?

2. The Commission's rate-of-return adjustment contradicts other portions of the Order.

As further evidence of its unreasonableness, the Order contradicts itself. Most notably, the Commission stated that there was "no dispute in this case as to the amount of the increase in revenues needed to allow DEO to earn a fair rate of return on its investment." (Order, p. 21.) Despite this recognition, and without basis in the record, the Commission reduced that undisputedly necessary revenue increase by $3 million.

Further, the Commission found that under SFV, "low-income customers, on average, would actually enjoy lower bills." (*Id.*, p. 23.) Nevertheless, the Commission cited the adoption of SFV as a reason to reduce the rate of return, apparently out of concern for low-income customers.

What's more, as noted, the Order already contained numerous approvals and adjustments that rationally addressed low-income customers' needs: SFV rate design, a pilot program to credit bills directly (*see id.*, pp. 26–27), a nearly three-fold increase in DSM spending (*id.*, pp. 22–23), and $1.2 million of shareholder funding to assist low-income customers in the areas of payment assistance and conservation education. But despite these programs assisting low-income customers, the Commission significantly reduced the revenue requirement, and it did so on behalf of the very constituency *already benefiting* from the stipulation.

The rate of return must be "fair and reasonable." R.C. 4909.15(A)(2). *Reducing* DEO's rate of return in response to a factor that *increases* risk is not "reasonable"—in fact, it defies reason. *Reducing* revenues in the face of *increased* capital costs is not "fair." It flaunts fairness. The Order is unreasonable, and the Commission should grant rehearing and adopt the stipulation as filed.

E. The Order Did Not Authorize a Cost of Debt Equal to DEO's Actual Embedded Cost of Debt.

No part of the Commission's reduction to DEO's rate of return should be allowed to stand. But even if the Order was otherwise sound and supported, and even had DEO received all process that was due, the Order effectively substantially reduced the revenue attributable to DEO's embedded cost of debt. This is unlawful.

The Commission must authorize a "cost of debt equal to the actual embedded cost of debt of such public utility." R.C. 4909.15(D)(2)(a). The Commission reduced the "rate of return" (Order, p. 27), not simply the return on equity. Perhaps this was a mere slip of the pen, but by reducing the overall rate of return by 20 basis points, the Commission denied DEO recovery of its actual embedded cost of debt in violation of R.C. 4909.15(D)(2)(a). Considered differently, it reduced DEO's return on equity by roughly twice as much.[4] There is simply *nothing* in the record to support such a reduction. There is no explanation in the Order to justify such a reduction. This reduction is unsupported, unjustified, unreasonable and, hence, unlawful.

F. The Commission's Decision Will Chill Settlement Efforts In the Future.

Although the Commission is not required to accept any stipulation, the Commission's unsupported modification of the Stipulation here will have effects beyond this case. This case

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[4] As shown in Schedule D-1 of the Staff Report, DEO's embedded cost of debt, which comprises nearly 49% of the capital structure used to establish the rate of return, is 6.5%. At an 8.49% overall return on capital, the return on the equity portion is 10.38%. At an 8.29% return on capital, the return on equity is 9.99%, resulting in a decrease of nearly 40 basis points on the equity portion of the return.

was heavily litigated, and the Stipulation was heavily negotiated. Terms were not reached until the evidentiary hearing was two weeks old and all local hearings had been completed. The last rounds of negotiation concerned dollar amounts in the hundreds of thousands, not millions. The Stipulation represented a carefully balanced deal. A three-million-dollar reduction would have been more than enough to spoil the bargain.

It is one thing to upset a settlement when a party opposes it or otherwise suggests the deal is not fair. But when a settlement is opposed by no one, and is supported by the Company, the Staff, and all consumer groups, it should not be lightly disturbed. No good purpose is served by modifying substantially an intensely negotiated, good-faith settlement that satisfied all the parties at the table. This is especially true when the modification does not even help the low-income customers that the Commission is ostensibly concerned about—the amount returned per customer is negligible, less than a quarter a month.

When a case such as this one presents the Commission with a stipulation that is extensively negotiated and widely regarded as fair, and the Commission dramatically modifies that stipulation without support or justification, it sends the wrong signal to parties appearing before the Commission. Why should parties expend time and resources to attempt to bridge differences and craft fair solutions, if their deals will be arbitrary modified?

Courts and other agencies have traditionally welcomed and encouraged parties' attempts to resolve disputes in a way that satisfies those parties. *See Ziegler v. Wendel Poultry Serv., Inc.* (1993), 67 Ohio St. 3d 10, 17; *White v. Brocaw* (1863), 14 Ohio St. 339, 346 ("[i]f there is any one thing which the law favors above another, it is the prevention of litigation, by the compromise and settlement of controversies"); *In re Application of Cincinnati Gas & Elec. Co. for Approval of Electric Transition Plan*, Case No. 99-1658-EL-ETP et al., Entry of Aug. 31,

2000, at 58-59 (noting that the "Commission's longstanding policy has been to encourage settlements in cases that come before it"); *Ganter v. Franklin County Board of Revision*, Case No. 95-A-298, Entry of May 10, 1996 (Ohio Board of Tax Appeals) (explaining that "settlement of disputes is to be encouraged"). Settlement allows the parties to minimize the expense of litigation and to devote their resources to "more productive endeavors." *Convenient Food Mart, Inc. v. Countrywide Petroleum Co.*, 2005 Ohio 1994 at ¶ 2 (8th Dist. Ct. App. 2005). These efforts also normally result in the efficient use of resources of the tribunal as well. *Id.* (noting public interest served by settlement includes "judicial economy and efficiency by eliminating the merits of the settled case").

The result in this case sends the opposite message, discouraging settlements and leading to more contentions and litigated proceedings before the Commission. That is hardly in the best interest of the public and utilities subject to the Commission's jurisdiction.

III. CONCLUSION

The Commission has committed reversible error by reducing DEO's rate of return. DEO was given no opportunity to make the case in support of the stipulated rate of return in the face of any challenge. The Commission's reduction is without any record support and, in fact, contradicts other parts of the Order. The resultant 40-plus basis point reduction in the return on equity is plainly wrong and cannot be squared with deteriorating economic conditions which would merit an increase in the returns on equity and capital. Further, the reduction sends the wrong message to potential investors in Ohio utilities and to those appearing before the Commission.

For the foregoing reasons, the Commission should grant DEO's Application for Rehearing and modify its Opinion and Order appropriately.

Respectfully submitted,

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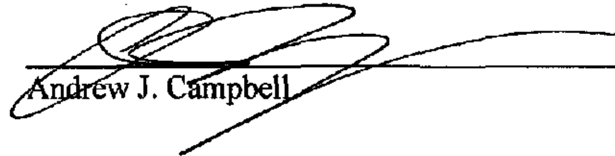
CERTIFICATE OF SERVICE

I certify that a copy of the foregoing Application for Rehearing of The East Ohio Gas Company d/b/a Dominion East Ohio was delivered to the following persons by electronic mail this 14th day of November, 2008.



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