BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

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

REPLY BRIEF OF THE EAST OHIO GAS COMPANY D/B/A DOMINION EAST OHIO

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ATTORNEYS FOR THE EAST OHIO GAS COMPANY D/B/A DOMINION EAST OHIO

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I. INTRODUCTION

The Staff and the Office of the Ohio Consumers' Counsel ("OCC") approach the Pipeline Infrastructure Replacement ("PIR") Cost Recovery Charge as though they were writing on a blank slate. They are not. The Stipulation and Recommendation ("Stipulation") filed in Case No. 08-169-GA-ALT, along with the accompanying PIR Staff Report, base rate case Staff Report, and PIR Application control here. Despite the efforts of Staff and OCC to ignore these controlling documents, the applicable language expressly refutes Staff's and OCC's arguments. DEO calculated its PIR Cost Recovery Charge in accordance with the Stipulation, which Staff and OCC ***agreed to***, and the Commission ***approved***. Settled principles of collateral estoppel prevent Staff and OCC from attempting to relitigate the issues now.

The only time that Staff and OCC even bother to mention the Stipulation is in an unsuccessful attempt to show that the Stipulation does not provide for cost recovery of incremental O&M expenses. As to that issue, Staff and OCC twist the plain meaning of DEO's PIR Application and the PIR Staff Report and ignore the record showing that DEO included incremental O&M expense cost recovery in its: (1) PIR Application; (2) November 14, 2008

presentation to Staff and OCC; (3) Notice of Intent to Adjust the PIR Cost Recovery Charge; and (4) the August 28, 2009 Application to Adjust the PIR Cost Recovery Charge. More importantly, they overlook that Staff expressly ***approved*** recovery of these expenses in the PIR Staff Report. Staff Ex. 2 at 3-5.

Even if the Stipulation (and the documents incorporated therein) did not resolve these issues, and it does, Staff's and OCC's proposals are unjust and unreasonable. No one disputes the vital importance of the PIR program in providing a safe and reliable system. No one disputes that the program will ultimately provide benefits not only to DEO's customers, but also to other stakeholders. And no one disputes that replacing DEO's infrastructure and main-to-curb connections will cost ***over $2.6 billion***. Staff Ex. 2 at 3. DEO's witnesses explained the accounting and ratemaking principles behind each element of the PIR Cost Recovery Charge. *See* DEO Exs. 1, 2, 3. And, contrary to Staff's view, the record evidence shows that DEO's PIR Cost Recovery Charge is consistent with the Commission's treatment of similar charges by Duke Energy Ohio ("Duke") and Columbia Gas of Ohio ("Columbia").

But, in the face of the undisputed benefits that accelerated pipeline replacement offers and the massive capital DEO requires to carry out the program, Staff and OCC seek to deny or to delay DEO's recovery of legitimately-incurred costs. Staff and OCC seek to deny DEO recovery of ***all*** incremental O&M expenses, which amount to over $1.1 million in the first year of the PIR program, as well as the incremental costs, carrying charges and return on its investment in ***all*** new curb-to-meter installations. Staff Br. at 18-25; OCC Br. at 11-19. Staff further recommends that DEO recover its incremental depreciation and property tax expense – expenses incurred entirely within a single year – ***over approximately fifty years***. Staff Br. at 6-10. In the same vein, Staff and OCC seek to delay DEO's recovery of legitimately-incurred costs associated with

plant additions accounted for under blanket work orders, notwithstanding that it is undisputed that DEO used exactly the same blanket work order process to account for those costs that Staff ***has already approved*** in the rate case. Staff Br. at 12-18; OCC Br. at 8-11.

Staff also proposes (and OCC supports) a "heads we win, tails you lose" method for accounting for O&M expense savings. On its face, this proposal is unjust and unreasonable. By ignoring increases in certain components of the baseline level of relevant and prudently incurred O&M expenses and only looking at and counting savings in other components, Staff would artificially reduce the costs needed to be recovered through the PIR Cost Recovery Charge.

Staff's and OCC's efforts to undermine the accelerated cost recovery that lies at the heart of the PIR program will interfere with DEO's ability to obtain capital and to properly manage this vital program. DEO never agreed – and never would have agreed – to a PIR Cost Recovery Charge that would deprive DEO of the opportunity to fully recover its PIR program costs. Yet, this is exactly what Staff and OCC seek to foist upon DEO now.

DEO seeks to recover its costs in accordance with the Stipulation that the Commission has already approved. In reliance upon that Stipulation, DEO has already doubled its investment in PIR (DEO Ex. 3 at 3), an investment that will benefit customers through increased safety and reliability, and reduced pipeline leaks and associated expenses for years to come. The Commission should reject Staff's and OCC's proposals that would impair DEO's efforts to proactively ensure continued safe and reliable service to its customers at the lowest overall lifetime cost.

II. ARGUMENT

A. Staff and OCC Virtually Ignore the Stipulation That They Signed and That the Commission Approved.

1. As to four of the five issues raised, Staff and OCC fail to cite the Stipulation at all.

Staff and OCC concede that the Stipulation – and the documents it incorporates – control. Staff Br. at 20; OCC Br. at 14. Nor is there any dispute that the Commission has the authority to enforce its orders, including the Stipulation. *In the Matter of the Application of Ohio American Water Company to Increase its Rates for Water and Sewer Service Provided to its Entire Service Area,* Case No. 07-1112-WS-AIR (Entry on Rehearing at 4) (February 13, 2008). Further, under settled law, "[t]he doctrine of collateral estoppel operates to 'preclude the relitigation of a point of law or fact that was at issue in a former action between the same parties and was passed upon by a court of competent jurisdiction.'" *Ohio Consumers Counsel v. Pub. Util. Comm'n,* (2007) 114 Ohio St. 3d 340, 342, 872 N.E.2d 269, 273 (*citing Consumers' Counsel v. Pub. Util. Comm.* (1985), 16 Ohio St. 3d 9, 10, 475 N.E.2d 782). Staff and OCC, however, would have the Commission reject these principles, ignore the Stipulation and allow these parties to relitigate issues already settled and decided.

Staff and OCC admit that in interpreting the Stipulation, the Commission must first turn to the language of the Stipulation, then, if necessary, to the applicable Staff Reports, and then, if necessary, to DEO's PIR Application. Staff Br. at 20; Tr. II at 56-57; OCC Br. at 14. Yet, having made that admission, these parties promptly ignore it. The ***only*** evidence Staff adduced about the Stipulation went to a single issue: whether the Stipulation allows recovery of incremental O&M expenses. OCC placed ***no*** evidence in the record regarding the Stipulation (or anything else for that matter), and in its post-hearing brief refers to the Stipulation only in adopting Staff's position as to the Stipulation's impact on recovery of incremental O&M. OCC

Br. at 14-19. Thus, DEO's case regarding the Stipulation, the PIR Staff Report, rate case Staff Report and the PIR Application is ***uncontested*** for all issues except incremental O&M cost recovery. As to the remaining four issues, Staff and OCC fail to even ***cite*** the Stipulation, let alone discuss the relevant language. DEO addressed that language at length in its opening brief, but for the Commission's convenience, DEO summarizes it again here:

- **One-year recovery for incremental depreciation and property tax**: The PIR application specifically provides that the PIR Cost Recovery Charge is "***based on the costs accumulated and bills rendered for the fiscal year ending June 30 of the same year.***" DEO Ex. 13 at 11; DEO Br. at 6 (emphasis added). And the PIR Staff Report adopted "the proposed accounting treatment...." DEO Ex. 7 at 13; DEO Br. at 19-20. Both incremental depreciation and property tax expense are "costs accumulated...for the fiscal year ending June 30 of the same year," and nothing in the Stipulation or PIR Staff Report suggests deferred recovery. *See* DEO Br. at 6-7; DEO Ex. 13 at 11.
- **Plant additions and retirements:** The PIR Application requires DEO to calculate the PIR rate base ***in the same manner*** as rate base was calculated in the underlying rate case. DEO Ex. 13 at 10. The Staff Report in that rate case, in turn, specifically adopted the Blue Ridge Report. Staff Ex. 3 at 3-4. The Blue Ridge Report expressly approved DEO's use of the blanket work order process. DEO Ex. 8 at 83-84. In particular, after noting DEO's use of the blanket work order process, the Blue Ridge Report stated that "***plant additions since the last rate case are reasonable and appropriately used and useful*** in the operation." DEO Ex. 8 at 92: DEO Br. at 13 (emphasis added). Likewise, the Blue Ridge Report also found that "the Company currently has ***adequate policies, procedures, and practices for recording of transfers and retirements***...," and that "the

retirements and transfers reflected in the filing can be relied upon for setting rates." DEO Ex. 8. at 96; DEO Br. at 13 (emphasis added). Having specifically approved DEO's accounting for additions and retirements in the base rate case, which the Stipulation makes controlling for purposes of calculating the rate base here, Staff cannot now reject that accounting and ratemaking treatment. *See* DEO Br. at 12-14.

- **New curb-to-meter installations:** The PIR Staff Report expressly provides that "Staff therefore supports DEO's proposal to assume the responsibility for the installation of ***all*** customer service lines." Staff Ex. 2 at 3; DEO Br. at 17 (emphasis added). Moreover, "Staff believes the PIR Cost Recovery Charge should recover the following costs:...costs associated with assuming ownership of curb-to-meter service lines ***including new installations***...." Staff Ex. 2 at 4-5 (emphasis added). *See also* DEO Br. at 18.
- **Baseline O&M savings:** The PIR Application provided, "***Any savings relative to the test year expense level ... shall be used to reduce the year-end regulatory asset***...." DEO Ex. 13 at 11; DEO Br. at 26 (emphasis added). The Staff Report states that "Staff agrees with DEO that ***this reduction in O&M expenses be used to reduce the fiscal year-end regulatory asset***...." Staff Ex. 2 at 5; DEO Br. at 26 (emphasis added). And the Stipulation provides, "***Any savings relative to a baseline level of O&M expenses" shall be used to reduce the fiscal year-end regulatory asset***. DEO Ex. 7 at 10; DEO Br. at 25 (emphasis added). Thus, the Stipulation, the PIR Staff Report and the PIR Application all envisioned that the aggregate level of all expenses in the PIR program year would be compared to an aggregate test-year level to determine savings to be used to calculate the PIR Cost Recovery Charge. *See* DEO Br. at 25-28.

Staff and OCC fail to discuss any of this clearly applicable language, let alone offer an explanation as to why such language does not control. The Commission should enforce the terms of the Stipulation.

2. On the one issue where Staff and OCC discuss the Stipulation and its supporting documents, they misread the Stipulation's plain language.

As to the remaining issue, incremental O&M expenses, Staff and OCC acknowledge that the PIR Staff Report addresses the issue. Staff Ex. 4 at 3-4; OCC Br. at 14-19. But these parties twist the relevant language to suggest the PIR Staff Report says one thing, when it in fact says just the opposite. In particular, Staff and OCC claim that Staff expressly rejected DEO's proposal to recover incremental O&M expense in the PIR Staff Report. *Id.* The facts are otherwise.

As DEO demonstrated in its Post-Hearing Brief, Staff applies one erroneous and illogical layer upon another to construct its argument. First, Staff contends that DEO only asked for recovery of two specific types of incremental O&M expenses: corporate service company and shared service expenses. Staff Br. at 22-23. But the PIR Application does not support this assertion:

> Incremental O&M expenses associated with the PIR program shall be calculated based on incremental and non-duplicative costs that, but for the existence of the PIR program and assumption of ownership of service lines would not be incurred by DEO. Such incremental O&M ***includes increased corporate service company and shared service expenses*** allocated to DEO that are not charged to the capital project. [DEO Ex. 13 at 9 (emphasis added).]

Staff argues that the second sentence in the paragraph quoted above limits the first. Tr. II at 58-59, 65-66; Staff Br. at 22-23. That approach mangles the language of DEO's PIR Application beyond comprehension. As noted in DEO's Post-Hearing Brief, the word "includes"

was used to show two ***examples*** of the "incremental and non-duplicative costs that, but for the existence of the PIR Program. . . would not be incurred by DEO." DEO Br. at 21-22.

Moreover, even a cursory knowledge of what would be entailed in the PIR Program – with its massive project planning, scheduling and implementation costs – would reveal the absurdity of the Staff's purported interpretation of the PIR Application. In short, it is literally incredible for Staff to assert that the only incremental O&M expenses that DEO would seek to recover would be limited to two relatively minor expense categories. DEO Ex. 3 at Ex. MR-1. This is especially true given that the central purpose of the PIR program was to accelerate the recovery of costs to be incurred in an epic undertaking of capital and other resources to replace a substantial segment of the Company's facilities. Staff Ex. 2 at 3, 5.

Staff fares no better with its second argument. It suggests that incremental O&M expenses should not be recovered because they are not included in a list of expense categories appearing on page 5 of the PIR Staff Report, where Staff recommended: "recovery should include (1) incremental depreciation expense, (2) incremental property taxes, and (3) return on rate base." Staff Ex. 2 at 5; Staff Ex. 4 at 4; Tr. II at 60-64 Staff Br. at 21-22. Yet, as also previously demonstrated, Staff ***admits*** that this list is not an exclusive list of all items for which recovery should be permitted. *See* Tr. II at 103-104. A plain reading of the PIR Staff Report shows that the list of recoverable items was offered specifically with regard to the infrastructure investments for which DEO was seeking recovery. After setting forth this list of recoverable items, the PIR Staff Report goes on, ***on the very same page,*** to expressly address incremental O&M expenses. The PIR Staff Report provides for recovery of such expenses ***except for increased corporate service company and shared service expenses***:

> Regarding the request for incremental O&M expenses, ***Staff recommends they do not include increased corporate service***

> ***company and shared service expenses*** allocated to DEO that are not charged to the capital project. Staff will withhold any recommendation regarding the inclusion of any O&M expenses allocated with relocating inside meters until such time as a meter relocation plan is submitted. [Staff Ex. 2 at 5 (emphasis added).]

If Staff had intended to exclude all O&M expenses, it would have said so, plainly and unequivocally. Reading the PIR Staff Report, in the context of what DEO actually had asked for (not what Staff now construes that request to be), the only fair reading is that Staff sought to exclude only the two specified types of incremental O&M expenses. Staff cannot be permitted to twist the plain language of the PIR Application and the PIR Staff Report after the fact solely to achieve a further reduction of the proposed PIR Cost Recovery Charge that is already 17 percent below the cap approved by the Commission. *See* DEO Br. at 2.

Indeed, the passage from the PIR Staff Report belies the Staff's logic in this case. After recommending the exclusion of two specific categories of incremental O&M expenses, Staff goes on to say that it was "withholding" any recommendation on another category of O&M expenses. If, as Staff now contends, Staff had rejected ***all*** incremental O&M expenses in the first sentence, why would Staff need to "withhold" its determination as to a subset of such expenses in the second sentence?

3. DEO's only burden of proof is to show that it calculated the PIR Cost Recovery Charge in accordance with the Stipulation, and it met that burden here.

Staff and OCC dedicate substantial effort to misplaced arguments regarding DEO's burden of proof. *See* Staff Br. at 6; OCC Br. at 6-7. Those arguments miss the point. As much as Staff and OCC wish to the contrary, this is not a rate case. Thus, DEO's burden of proof is not, as OCC contends, derived from R.C. 4929.04 and 4929.05. OCC Br. at 6-7.

Rather, DEO's sole burden of proof is the burden agreed to in the Stipulation and set forth in the PIR Staff Report: to "demonstrate the justness and reasonableness of the ***level of***

recovery of expenditures associated with the PIR program." Staff Ex. 2 at 6 (emphasis added). Here, DEO has done that. *See* DEO Exs. 1, 2, 5, 7, 8, 13; Staff Ex. 3. DEO has provided schedules showing all of the expenditures associated with the PIR program. DEO Ex. 5 at Ex. A. The evidence also shows that DEO has calculated its expenses consistent with accounting principles, Commission Rules, the FERC Uniform System of Accounts and Commission precedent (to the extent it is applicable). *See* DEO Exs. 2, 9, 10, 17, 18, 19; OCC Ex. 4; O.A.C. 4901:1-13-13.

Further, DEO's witnesses have testified to the necessity of each expenditure, schedule-by-schedule. *See* DEO Exs. 1-4. Tellingly, neither Staff nor OCC has alleged that even a single one of those expenditures was unnecessary to effectuate the PIR program. Similarly, DEO offered testimony that its annual PIR Cost Recovery Charge will recover the expenditures associated with the PIR program. *See* DEO Exs. 1-2. Again, neither Staff nor OCC has alleged otherwise. DEO has met its burden under the Stipulation, and the Stipulation resolves the issues here.

B. Staff and OCC's Proposals are Unjust and Unreasonable.

Even apart from the Stipulation, the proposals from Staff and OCC should be rejected because the proposals would improperly limit DEO's recovery of necessarily incurred costs. Thus, these proposals would seriously hamper the viability of the program. For this reason, these proposals are unjust and unreasonable.

1. The PIR program is a massive undertaking that is vital to the continued safety and reliability of DEO's system in the future.

The undisputed facts in this case demonstrate the problems with the proposals from Staff and OCC. No one disputes either the incredible magnitude of the task DEO is undertaking, nor the benefits that will flow from it. As OCC noted, "Over the next 25 years, the Company is

proposing to replace ***substantially all*** of the bare-steel pipe, cast-iron pipe, wrought-iron pipe and copper pipe in its system," (OCC Ex. 1 at 12), *i.e.*, ***over 4000 miles of pipe***, and "approximately 515,000 main-to-curb connections," (*id.* at 9). In completing this program, DEO will invest over ***$2.6 billion*** in 2007 dollars. Staff Ex. 2 at 3. It is further undisputed that the PIR program is "one of the most significant projects in the Company's history." DEO Ex. 3 at 3.

Nor is there any dispute about the benefits that will flow from pipe replacement. In the underlying case to establish the PIR Cost Recovery Charge mechanism, Case No. 08-169-GA-ALT, DEO witness Timothy McNutt testified at length about the safety and reliability issues that bare steel and cast iron pipe cause. *See* OCC Ex. 1 at 10-12. Not only does the pipe replacement improve safety and reliability, but it also leads to lower lifetime costs. OCC Ex. 1 at 14-15; DEO. Ex. 4 at 3. And, because the replacements are being done proactively, rather than in response to leaks, DEO can work with communities to schedule the replacements in a manner that minimizes disruptions (*e.g.*, interference with traffic or community events), and maximizes potential coordination with a community's other planned infrastructure upgrades. OCC Ex. 1 at 15. Staff conceded that this program is "necessary to enhance the safety and reliability of [DEO's] pipeline system," and noted that, without accelerated replacement, it would take "approximately 89 years" to complete the planned upgrades. Staff Ex. 2 at 3.

Nor is there any dispute about the consequences of not being able to complete the PIR program. DEO has more bare pipe than any gas company in the country. Tr. II at 15; OCC Ex. 1 at 9; (Case No. 08-169-GA-ALT) ("PIR Case Tr.") PIR Case Tr. II at 60-61, 175. DEO also leads the nation's gas companies in the number of corrosion leaks that it repairs annually. PIR

Case Tr. II at 60. As DEO's corrosion-prone facilities age, the leak rate experienced by DEO on those lines will increase exponentially. *Id.* at 61. As Mr. McNutt said:

> [I]t's a fact that bare pipes that are in the ground exposed to the environment that they're exposed to, they are going to leak at some point. It's not a matter of if, it's a matter of when, and sooner or later we're going to have to deal with that through repair or replace. [*Id.* at 82.]
>
> [T]he key driver here is ... the amount of bare pipe, the amount of corrosion leaks that we have, and our concern that that's going to accelerate and our O&M expenses in managing those leaks are going to accelerate and it will become unmanageable for us and it will require significant resource increases just to manage the leak level going forward. [*Id.* at 106.]

DEO, with the agreement of the Staff and OCC, and with the Commission's approval, decided not to wait until the Company was faced with a tsunami of leaks and the possibility that it would be unable to do what needs to be done to keep DEO's system safe and reliable. Rather, acting proactively, the Company asked for and – with the agreement of Staff and OCC – received the ability to recover its incremental costs to systematically replace its bare and ineffectively coated pipe on an accelerated basis and assume ownership of and responsibility for customer service lines. The need for full and timely recovery is necessary for the Company to attract the substantial capital necessary to fund such a massive program. Staff Ex. 2 at 3. No one disputes that this is so.

2. Despite conceding the importance of the program, Staff and OCC seek to prevent DEO from recovering program costs that are indisputably legitimately incurred.

In light of the enormous expenditures undertaken – and yet to be undertaken – by DEO, and the undisputed need for this program, it is unjust and unreasonable for Staff and OCC to expect DEO to implement the PIR program without providing DEO full and timely cost recovery. Yet, Staff's and OCC's proposals would outright ***prohibit*** DEO from recovering over

$1.1 million of incremental O&M expenses. Staff Ex. 1 at 9-10; Staff Ex. 4 at 3-4. Similarly, Staff's and OCC's proposals would ***prohibit*** DEO from recovering costs associated with new curb-to-meter installations. Staff Ex. 1 at 8-9; Staff Ex. 5 at 6-7; OCC Ex. 2 at 5. These proposals represent ***a permanent prohibition to cost recovery***: DEO would recover incremental O&M expenditures and new curb-to-meter installations costs only through a new distribution rate case, and then only prospectively. All such expenses from the beginning of the PIR program until the test year in DEO's next base rate case will never be recovered.

Other Staff proposals seek to delay recovery. For example, Staff's proposals would delay cost recovery for incremental depreciation and property tax expenses for ***up to 50 years,*** as well as delaying recovery for plant additions accounted for under blanket work orders. Staff Ex. 5 at 4-8. That, however, directly contradicts the Stipulation, the PIR Staff Report, and the PIR Application, each of which recognized the importance of ***accelerated*** cost recovery. *See* DEO Ex. 7 at 8, 13; Staff Ex. 2 at 3; DEO Ex. 13 at 3-4. Indeed, a key purpose of this program was the reduction of the regulatory lag typically involved in capital expenditures, thereby reducing the need for frequent rate cases. *See* Staff Ex. 2 at 5; DEO Ex. 13 at 3-4. Staff's proposal directly undermines that purpose.

3. Because recovery of incremental O&M costs that were incurred expressly because of the PIR program is vital to the viability of the program, Staff's proposal to exclude such expense from cost recovery is unjust and unreasonable.

Staff's proposal to deny DEO an opportunity for cost recovery of incremental O&M expenses is unjust and unreasonable. In particular, it is unjust and unreasonable to deny DEO an opportunity to recover "expenditures associated with the PIR program" (Staff Ex. 2 at 6), where Staff acknowledges that DEO must incur such costs in order to manage the PIR program properly (Tr. II at 73-74, 106).

It is undisputed that the incremental O&M expenses that DEO seeks to recover relate to critical activities within the PIR program. As DEO witness Mike Reed explained:

> The sheer magnitude of the PIR program has required – and will continue to require – that DEO invest labor and other resources for O&M activities. Since DEO began implementing PIR, it effectively has doubled its capital budget, making the PIR program one of the most significant projects in the Company's history. For this investment to be successful and properly administered, however, it must be accompanied by appropriate incremental O&M expenditures [DEO Ex. 3 at 3.]

These expenses include:

- **Project management** to "oversee the entire construction process." *Id.* at 4. As Mr. Reed explained, "These activities are critical to maintain the appropriate implementation of what will ultimately be a multi-billion dollar project." *Id.*
- **Prioritizing and scoping** "to ensure that the right projects are constructed at the right time," and "to develop proactive project plans to ensure that DEO is appropriately prioritizing the worst pipeline problems." *Id.* at 5. As Mr. Reed explained, "this task requires a great deal of planning to anticipate contingencies and conflicts." *Id.*
- **Contractor management** to "manage every aspect of our PIR program contractor relationships, from beginning to end." *Id.* As Mr. Reed observed:

  > [the contractor managers] are responsible for coordination of our bidding process; scoping bid documentation, assembling and forwarding bid information to prospective contractors; answering questions regarding bid information; and detailed evaluation of bids." *Id.*

  Contract managers also qualify bidders and contractors. *Id.* at 6. Once contractors are retained, contract managers reconcile invoices, authorize payment of costs properly invoiced and deal with post-contract issues. *Id.*

- **Monitoring and reporting** to provide, among other things, pre- and post-construction mapping and drawings of DEO's facilities. *Id.*

There can be little argument that all of these expenses are critical to the success of the PIR program. DEO Ex. 3 at 3. There also can be little argument that, as documented by DEO, these expenses were: (a) incurred by DEO; and (b) would not have been incurred but for the PIR program. *Id.* at Ex. MR-1. Gutting the accelerated recovery of DEO's most critical expenses, as Staff and OCC suggest, will undermine DEO's ability to attract the capital necessary to go forward with such an aggressive and enormous program, thereby imperiling the program to the detriment of DEO's customers.

In contrast to the overwhelming showing that DEO made to support the propriety – and indeed, the necessity – of including incremental O&M expenses in the PIR Cost Recovery Charge, Staff's and OCC's positions have no support in the record. Aside from a tortured reading of the PIR Application and PIR Staff Report (discussed previously DEO Br. at 19-23; *supra* at 7-9), Staff's argument to exclude these expenses is based literally on nothing.

Staff admits that it did not review the expenses at issue. Staff Ex. 4 at 5; Tr. II at 71. Staff witness Kerry Adkins tried to claim that Staff didn't have sufficient time to do this. *Id.* But the facts show that DEO unequivocally gave Staff timely notice of the Company's intent to recover incremental O&M expenses and, even though faced with such information, Staff did nothing. Staff knew no later than November 14, 2008 – more than six months before DEO filed its Notice of Intent here – that DEO intended to seek such recovery. DEO Ex. 14 at 31. In a PowerPoint presentation made to Staff and OCC, DEO outlined "Potential Incremental O&M Expenditures," which featured a list identical to the list that ultimately became part of DEO's Application here. Further, in May 2009, when DEO filed its Notice of Intent, DEO stated that it

intended to recover incremental O&M expenses. DEO Ex. 6 at PFN Ex. 5, Sch. 1. Later, on August 28, 2009, DEO's Application spelled out the specific incremental O&M expenses (and the amount of such expenses). DEO Ex. 5 at Ex. A, Sch. 15.

Notwithstanding the numerous opportunities and the lengthy period available to Staff to inquire about incremental O&M expenses, Staff did nothing on this issue until the latter part of September. Tr. II at 141. And when it did inquire, DEO promptly provided the requested information. This is not disputed. Tr. II at 142. Staff cannot use its own inaction to argue that DEO should be denied recovery of expenses. This is especially so where DEO has made an unrebutted showing that the expenses at issue were necessary, were actually incurred and would not have been incurred but for the PIR program.

Other than joining Staff in misreading the PIR Application and the PIR Staff Report, OCC's argument to exclude these expenses rests on nothing more than its assertion that DEO's accounting for these expenses is "arbitrary." OCC Br. at 20. OCC never really explains what it means, *i.e.*, why DEO's accounting is anything but proper. Apparently, based on testimony of DEO's witnesses, OCC challenges the fact that certain project-specific expenses were capitalized and certain general expenses (*i.e.*, expenses relating to activities not germane to a specific project but rather to the program as a whole) were included as incremental O&M expenses. OCC presents no evidence that DEO's accounting is wrong or improper either as a general proposition or with regard to specific expenses.

More fundamentally, OCC's argument grossly misunderstands (if not willfully ignores) the nature of the PIR program. As DEO's witnesses (specifically, Messrs. McNutt and Reed) have testified, the PIR program is not just one replacement project, but a collection of many, many construction projects. DEO Ex. 3 at 4; OCC Ex. 1 at 12. These projects, taken together,

are huge in scope. DEO Ex. 3 at 3. It should take little insight to realize that a key aspect of implementing the PIR program, with its large number of projects, is the management of the program as a whole. *Id.* The cost of such management cannot be attributed to any specific project. Accordingly, DEO has properly accounted for its incurred incremental O&M expenses. They should be included in the PIR Cost Recovery Charge.

4. Because it improperly and artificially reduces the PIR Cost Recovery Charge, Staff's proposed calculation of O&M savings is unjust and unreasonable.

The Stipulation provides unambiguous direction on how O&M savings should be factored into the PIR Cost Recovery Charge:

> ***Any savings relative to a baseline level of O&M expenses*** associated with leak detection and repair processes, Department of Transportation inspections on inside meters that may no longer be necessary if meters are relocated outside, and corrosion monitoring expenses ***shall be used to reduce the fiscal year-end regulatory asset*** eligible for recovery through the PIR Cost Recovery Charge. [DEO Ex. 7 at 10 (emphasis added).]

The Stipulation thus required the Company to compare its baseline level of total O&M expense from these specified categories to the recovery year's total of the same categories. As the Stipulation requires, DEO added the expenses from leak detection processes, leak repair processes, and corrosion monitoring together for each period.[1] Then, DEO added another expense item, for corrosion remediation, to come up with a total "level of O&M expenses" for each of the two periods. It then compared the total O&M expense in one period to that in the other.

Staff and OCC now have a problem with this method. The problem arises from the undisputed fact that the O&M expenses for the three items called out in the Stipulation were

[1] Because DEO had not yet obtained approval for a meter relocation plan, there were no savings associated with Department of Transportation inspections on inside meters that were relocated outside.

greater in the first program year than in the baseline period. DEO Ex. 5 at Ex. A, Sch. 16. Faced with this circumstance, Staff proposed a new method of counting savings: if expenses in a category went up, they would be ignored; if expenses went down, the savings would be counted. Staff Ex. 4 at 7-8. This methodology necessarily overstates any savings, of course, because increases in expenses are not considered. The Staff's proposal thus attributes savings to the Company that do not exist and, in the process, artificially and improperly reduces the PIR Cost Recovery Charge.

To justify its approach, Staff doesn't bother to cite to the Stipulation, the PIR Staff Report or the PIR Application, nor could it. Instead, Staff makes two arguments. Both are flat out wrong.

First, Staff contends that its new cost savings counting methodology is consistent with the revenue requirement calculation in the Duke and Columbia accelerated main replacement program ("AMRP") cases. Staff Ex. 5 at 9-10. That is simply not true. Duke and Columbia calculate baseline O&M savings ***exactly the same way that DEO proposes doing here.*** Tr. II at 83-85; DEO Ex. 10 at Stipulation Ex. 1, Page 4 of 5, Sch. 22 Revised; DEO Ex. 9 at Stipulation Attachment 2 Sch. AMRP-1. In fact, Duke and Columbia showed ***negative*** savings during their most recent main replacement program period. DEO Ex. 9 at Stipulation Attachment 2 Schedule AMRP-1 shows that Columbia's savings are $0 at line 28. Line 28 shows that Columbia's savings calculation is set forth at Schedule 9B. Schedule 9B may be found at In the Matter of the Annual Application of Columbia Gas of Ohio, Inc. for an Adjustment to Rider IRP and to Rider DSM Rates, Case No. 09-0006-GA-UNC (Application at Schedule 9B) (June 2, 2009). *Id.* Thus, the Duke and Columbia AMRP cases provide no support for Staff's proposal here.

Second, Staff asserts that its approach is "superior because it maximizes cost savings." Staff Br. at 30. But maximizing cost savings is not the standard for determining proper cost recovery. Rather, as Staff admits, the recovery mechanism and charge should be just and reasonable. Staff Br. at 1-2.

As noted, Staff's real problem is that it wants to ignore the fact that DEO's O&M expenses went up. Staff attempts to blame DEO for this, claiming that DEO failed to deliver on "promised" savings. Staff Br. at 26-27. But this is not only untrue, it ignores the nature of both DEO's system and the PIR program.

As Ms. Friscic testified, DEO has more bare steel pipelines than any other company. Tr. II at 15 (*citing* McNutt Testimony, PIR Case Tr. II at 60-61, 175). As Mr. McNutt testified, these lines will corrode with age. PIR Case Tr. II at 61. The rate of corrosion-related leaks will increase exponentially. *Id.* Thus, absent any program, as DEO's bare steel lines continue to age, DEO will face higher levels of corrosion and leak-related costs each year.

The PIR program approved by the Commission includes a five-year initial period for the recovery of costs. DEO Ex. 7 at 8. But the replacement of pipelines is proposed to take ***25 years***. Staff Ex. 2 at 3. Thus, the first year of the program represents only 4 percent of the work to be done. To suggest that DEO should have had significant decreases in O&M expenses after a single year of the PIR is to suggest that DEO's bare steel lines should magically stop corroding. Staff overlooks that the costs associated with the 96 percent of the lines still to be replaced will continue to increase, perhaps exponentially.

The assertion that DEO promised more savings is also directly rebutted by Mr. McNutt's testimony in the underlying PIR case. He explained that, at the time of the initial application,

DEO had no specific plans for which projects would be done, or when they would be done.[2] Accordingly, Mr. McNutt repeatedly stated that no one from DEO could possibly provide any estimate for the savings that would actually be achieved:

> I think "comparable" is a broad term . . . . [W]e aren't sure exactly what we're going to save until we get into the project level and actually start replacing specific areas . . . where we have leaks. [PIR Case Tr. II at 105.]

Later, Mr. McNutt testified:

> Q. Is it possible that you could experience considerably greater O&M savings than Duke?
>
> A. Again, we aren't sure exactly what's going to unfold in front of us until we get into the specifics of the projects. Again, we used the term . . . "comparable" with a couple of these other utilities that have embarked on a similar program to the program that we're proposing.
>
> Q. Let me try it this way: You don't know for a fact that you'll achieve $8½ million in savings, correct?
>
> A. Like I've stated before, you know, until we get into the detail of the projects that we're going to do, I mean we're working at a program level right now, as we drive down to a project level you replace a piece of pipe, it's going to eliminate . . . the leaks that exist there, it's going to eliminate potential leaks that you're going to have in the future on that piece of pipe, and then that's going to result in savings going forward.
>
> We aren't sure exactly . . . what that number's going to be or the magnitude it's going to be, but we do know that . . . based on these other programs . . . when you spend the money to replace those assets, you're going to see a benefit on the O&M side. [*Id.* at 106-107.]

Still later, Mr. McNutt similarly testified:

> We know we're going to save some money. Again, for somebody to ask me what exactly are we going to save, . . . when we're dealing with almost 4,000 miles of pipe. I don't know the exact – it's impossible for me to identify an exact number. [*Id.* at 108.]

[2] Projects would be determined and prioritized once the program was approved. PIR Case Tr. II at 83-84.

DEO remains confident that customers will realize savings. The fact that those savings did not occur in year one is no reason to change the rules for counting O&M expense savings established by the Stipulation.

For its part, OCC attempts to support Staff's new "let's forget any increase in O&M expense" methodology by faulting DEO for focusing on transmission lines rather than distribution lines. OCC Br. at 23-29. This line of attack falls flat. The most important benefit for customers that results from the PIR program is the enhanced safety and reliability of the PIR program. OCC Ex. 1 at 14; Staff Ex. 2 at 3. It is undisputed that DEO chose to deal first primarily with its bare steel transmission lines because the failure of those lines would have more serious consequences. Tr. I at 93-94. There is no evidence that DEO's PIR program mainline replacement prioritization is improper.

Indeed, the undisputed evidence is directly to the contrary. Although Staff neglects to mention it, DEO reviewed its approach ***with Staff***, and Staff raised no objections. DEO Ex. 14 at 4-8. In fact, Staff expressly found that DEO's approach was reasonable:

> Based upon a review of DEO's job determination, bidding, and contracting procedures, job monitoring, and contracting controls in this proceeding; the ***Staff finds that the current management operation and bidder selection and contractor oversight of the PIR program are reasonable.***" [Staff Ex. 1 at 7 (emphasis added).]

Rather than focus on cost savings, DEO instead chose to focus first on system reliability for the benefit of its customers, a choice that Staff approved. To increase the likelihood that its customers would realize savings, DEO also chose voluntarily to include cost reductions associated with corrosion remediation in its savings calculation, even though corrosion remediation is not a baseline O&M cost savings category included in the Stipulation. *See* DEO Br. at 26. In sum, DEO has gone out of its way to pass through cost savings to its customers.

The Commission should reject Staff's unjust and unreasonable proposal. The Commission should approve DEO's calculation of cost savings, a calculation done in a manner consistent with the Stipulation and with the calculation that the Commission approved for both Duke and Columbia.

5. Because the parties agreed to include such expenses, Staff's and OCC's proposal to exclude from cost recovery new curb-to-meter installations is unjust and unreasonable.

As noted in DEO's Post-Hearing Brief, the PIR Staff Report specifically addressed the recovery of new curb-to-meter installations. Staff Ex. 2 at 3-5; DEO Br. at 17-18. The PIR Staff Report recognized that such work would be part of the PIR program. Staff Ex. 2 at 3-5. Thus, costs incurred to do that work are appropriately included through the PIR Cost Recovery Charge.

In rebuttal, Staff and OCC rely solely on partial testimony of DEO witness Jeffrey Murphy. Staff Ex. 5 at 7; Staff Br. at 18; OCC Br. at 12. Staff witness Ibrahim Soliman quoted Mr. Murphy's Supplemental Direct Testimony, filed on May 30, 2008. Staff Ex. 5 at 7. That testimony was offered ***prior to*** DEO's agreement to the Stipulation. *Id.* In his Fourth Supplemental Direct Testimony (filed August 25, 2008), Mr. Murphy testified as to the deal the parties actually reached. In that testimony – the only testimony that is relevant here – Mr. Murphy expressly recommended approval of the Stipulation on the ground that the PIR program will "promote the continued safe and reliable operation of its pipeline system, with DEO taking over ownership and responsibility for ***newly installed***, replaced and repaired curb-to-meter service lines." Case No. 08-169-GA-ALT, Fourth Supplemental Direct testimony of Jeffery A. Murphy at 4-5 (August 25, 2008) (emphasis added). In short, the only ***relevant*** testimony expressly recognized the need for DEO to receive cost recovery associated with new curb-to-meter installations.

Moreover, the testimony relied upon by Staff and OCC does not support their argument. In that testimony, Mr. Murphy was answering a question about whether DEO proposed to include costs for mainline extensions. He answered in the negative and also stated DEO's desire to exclude "other revenue-generating infrastructure investments." Neither Staff nor OCC have demonstrated or can demonstrate that new customer service lines are revenue-generating or any different in their revenue-generating capacity than existing customer service lines.

6. Because Staff's proposal is based on a fundamental misunderstanding of the nature of these expenses, Staff's proposal to require DEO to amortize incremental depreciation and property tax expense over the life of the PIR assets is unjust and unreasonable.

Staff's attempt to amortize incremental depreciation and property taxes over an asset's lifetime rests on a misunderstanding of the facts. Staff Ex. 5 at 4-6. As DEO demonstrated in its Post-Hearing Brief, the Staff essentially would have DEO depreciate depreciation. DEO Br. at 4-5; DEO Ex. 2 at 3; Staff Ex. 5 at 4. Moreover, Staff's proposal flies in the face of the approval granted to DEO for accelerated cost recovery. Case No. 08-169-GA-ALT (Opinion and Order at 32) (October 15, 2008). This is especially important here. DEO must have cost recovery commensurate with incurred expenses to raise the capital necessary for the PIR program. Staff Ex. 2 at 3. Not only that, but DEO's approach benefits customers, because contemporaneous recovery ensures that customers in one period are not paying expenses incurred serving customers in a different period. DEO Br. at 5. In an attempt to avoid this illogical result, Staff resorts to four arguments. None carries the day. Instead, they merely serve to further demonstrate Staff's misunderstanding of the issue.

First, Staff asserts that DEO will collect more than a year of depreciation expense if it collects both incremental and annualized depreciation. Staff Br. at 8-9. That is incorrect. During the course of the PIR program, a given year's depreciation expense includes two parts:

annualized depreciation expense and incremental depreciation expense. Depreciation expense incurred in a year on all assets placed in service ***prior to the beginning of the year*** is called annualized depreciation. DEO Ex. 2 at 4. There is no dispute that DEO should recover this annualized depreciation expense in the current year's PIR Cost Recovery Charge. Staff Ex. 5 at 3; DEO Ex. 13 at 11.

As used in this context, incremental depreciation is separate and apart from annualized depreciation. As DEO witness Vicki Friscic testified, incremental depreciation expense is the depreciation expense incurred in a program year associated with assets added ***during that year***. DEO Ex. 2 at 3-4. For example, if DEO placed an asset in service in the middle of the year – say, *e.g.*, six months into the program year – then DEO would incur depreciation expense for the six months of the year that the asset was in service. But, because that asset was not in place at the beginning of the year, the annualized depreciation would not include this six months of depreciation expense. Staff is just wrong to suggest otherwise.[3] In order to avoid showing this expense on its income statement, DEO defers the expense in a regulatory asset until the Company has revenue to offset that expense. DEO merely seeks to recover the revenue necessary to offset that expense through the PIR Cost Recovery Charge. As noted above, contrary to Staff's claims, this expense is not recovered through the recovery of annualized depreciation expense.

Staff's proposal to instead take the partial year depreciation expense and amortize that over the lives of the PIR asset, approximately 50 years, deprives DEO of timely recovery of an important part of the depreciation expense that it incurs each year. DEO and Staff agree that

[3] To be sure, depreciation expense incurred in all years ***after*** the year in which the asset is in service will be part of annualized depreciation. The initial year's (or initial partial year's) depreciation expense of an asset, however, is incremental depreciation expense.

depreciation is already an amortization over the life of the asset. DEO Ex. 2 at 3; Tr. II at 20; Staff Ex. 5 at 4. It simply makes no sense to re-amortize an amortization.

Second, not satisfied with misconstruing what incremental depreciation expense is, Staff attempts to misdirect the Commission by claiming that, because DEO seeks to defer incremental depreciation and property tax expense through a "regulatory asset," expenses comprising the asset should be amortized over the life of the asset. Staff Ex. 5 at 5. That is a stunning *non sequitur*. The creation of a regulatory asset occurs when an expense is deferred for subsequent recovery through rates. Indeed, this is required by Financial Accounting Standard ("FAS") 71. *Id.* Yet, FAS 71 does not prescribe that such assets be amortized or that they be amortized over any particular period. *Id.* The depreciation and property tax expenses, even after becoming part of a regulatory asset (so that the expense may be deferred), remain expenses that are associated exclusively with the service provided when the depreciation expenses (or property taxes) are incurred. The mere fact that these expenses are collected through a regulatory asset does not – indeed cannot – require that DEO wait nearly 50 years to achieve recovery of expenses incurred now.

Staff next relies on what it claims to be Commission precedent to support its proposed treatment. Staff Ex. 5 at 6; Tr. II at 162-164. But the only Commission "precedent" Staff cites is the Stipulation in Columbia's AMRP. *Id.* The Columbia AMRP Stipulation, however, expressly provides that it is ***not to be used as precedent***. *See* DEO Ex. 9 at 4. Further, it was signed and approved *after* the Commission order approving the Stipulation in Case No. 08-169-GA-ALT. *See* DEO Ex. 9 at 1. Thus, it cannot constitute "precedent" for the Stipulation here.[4]

[4] Apparently even Staff believes that the Columbia Stipulation is of limited value. In its arguments relating to O&M expense recovery, for example, Staff wholly omits any reference to that Stipulation's provisions. The reason for this omission is obvious: the Columbia Stipulation directly contradicts Staff's position on that issue here.

Third, while claiming the Commission should look to precedent, Staff completely fails to address the precedent that is most directly applicable here – DEO's Automated Meter Reading ("AMR") case, Case No. 09-38-GA-UNC. DEO Ex. 19 at Stipulation Attachment 1. The AMR case was based upon the very Stipulation at issue here, and the Commission approved a one-year amortization for incremental depreciation and property tax expense. *Id.* That same result follows in full force here.

Fourth, in an effort to revive its flagging position, Staff seeks to make much of the fact that DEO agreed to amortize post in service carrying charges ("PISCC") over the life of the associated capital investment. PISCC is similar in nature to the allowance for funds using during construction ("AFUDC") in that it recognizes the cost of funds attributable to construction activity that occurs over a long period of time. Because AFUDC is amortized over the life of the plant, DEO agreed to treat PISCC in a similar manner. Such is not the case with depreciation and property tax expenses, which are not similar in nature to AFUDC and should not therefore be treated in a similar fashion.[5] Accumulated depreciation reduces rate base and, therefore, reduces the amount of the return. Accordingly, delaying recovery of the incremental depreciation is unjust and unreasonable.

As noted previously, the Staff's proposal to amortize incremental depreciation and property tax is fundamentally unfair not just to DEO, but to DEO's customers. The proposal requires some customers to pay for costs that were not incurred in providing service to them, and allows other customers, for whom the cost was incurred, to avoid paying. This type of intergenerational subsidy defies both basic cost recovery principles and common sense.

[5] Indeed, DEO would prefer to obtain more timely recovery. However, because the full amount of PISCC, net of related deferred taxes, is included in the PIR rate base on which a return is permitted, DEO is willing to concede to Staff's recommended amortization.

7. Because DEO has accounted for rate base here the same way that it did in the Company's rate case, and because Staff and OCC seek to impose a different methodology, Staff's and OCC's proposal regarding plant additions and retirements is unjust and unreasonable.

Staff and OCC seek to deny DEO timely recovery by asserting that plant additions closed monthly through the "blanket work order" process should be excluded from the PIR rate base if a particular project was not completed by June 30, 2009. Staff Br. at 12-17; OCC Br. at 8-11. This proposal is unjust and unreasonable for at least two reasons. As noted above, the proposal is in direct conflict with: (1) the Stipulation, which requires DEO to determine its rate base as it did in Case No. 07-829-GA-AIR; and (2) the way rate base is determined for the infrastructure replacement riders of Duke and Columbia. DEO Ex. 18 at 82; DEO Ex. 17 at 3, 50; Tr. II at 181; *In the Matter of the Application of Duke Energy Ohio, Inc. for an Increase in Gas Rates,* Case No. 07-589-GA-AIR (Blue Ridge Report at 86, Staff Report at 4, 57) (December 20, 2007).

Staff and OCC attempt to avoid the impact of their prior agreement to the inclusion of such plant additions for purposes of determining the PIR Cost Recovery Charge by talismanic and meaninglessly repetitive incantations of the phrase "used and useful." Simply put, they contend that to be included in the PIR rate base, plant additions must be in service by the end of the PIR cost recovery year (here, by June 30, 2009). These parties assert that since DEO accounts for its numerous distribution construction projects using blanket work orders, and such blanket work order costs are closed to plant monthly, the amounts reflecting such plant additions for assets not complete by June 30, 2009, must be excluded. There are at least four things wrong with this argument.

First, Staff and OCC fail to recognize that the Blue Ridge Report essentially defined "used and useful" for purpose of DEO's rate base. Blue Ridge determined that phrase to ***include*** projects accounted for under the blanket work order process. DEO Ex. 8 at 83. Blue Ridge's

review of DEO's rate base in the rate case included a review of plant additions "completed through the blanket order process." *Id.* Blue Ridge specifically found that DEO's "plant additions since the last rate case are reasonable and appropriately used and useful in the operation." DEO Ex. 8 at 92.

Second, Blue Ridge's view of the "used and useful" nature of plant additions reflected in blanket work orders is not confined to DEO's facilities. Blue Ridge similarly audited Duke's and Columbia's blanket work order processes (which work identically to DEO's) and found no issues. DEO Ex. 18 at 82; *In the Matter of the Application of Duke Energy Ohio, Inc. for an Increase in Gas Rates*, Case No. 07-589-GA-AIR (Blue Ridge Report at 86) (December 20, 2007). In fact, in the recent rate cases of all three companies (*i.e.*, DEO, Duke and Columbia), Staff accepted Blue Ridge's recommendations and made no adjustment to distribution rate base resulting from the blanket work order process. Staff Ex. 3 at 55; Tr. II at 171; DEO Ex. 17 at 3, 50; Tr. II at 181; *In the Matter of the Application of Duke Energy Ohio, Inc. for an Increase in Gas Rates*, Case No. 07-589-GA-AIR (Staff Report at 4, 57) (December 20, 2007).

Nor can there be any doubt that Blue Ridge knew that, in approving the "blanket work order" process, it was approving inclusion in the rate base of projects not yet completed. "The use of blanket work orders is a commonly used process in the industry." *In the Matter of the Application of Duke Energy Ohio, Inc. for an Increase in Gas Rates*, Case No. 07-589-GA-AIR (Blue Ridge Report at 86) (December 20, 2007). Blanket work orders "are typically closed on a 30-day cycle." DEO Ex. 18 at 82. Blanket work orders include projects "of short duration." DEO Ex. 8 at 83. FERC's system of accounts expressly provides that "[w]ork orders covering jobs of short duration may be cleared monthly," independent of whether the project is complete. OCC Ex. 4 at 620; 18 CFR 201 at Gas Plant Instructions(11)(B). Given Blue Ridge's familiarity

with the industry, and with FERC accounting practices, it certainly knew that among the thousands of projects covered by blanket work orders, there had to be projects not yet completed. Yet, Blue Ridge approved the addition of ***all*** blanket work order expenditures into the "used and useful" category for ratemaking purposes.

Third, Staff's insistence here that all plant in rate base must be "in service" ignores that there is no definition of the term "used and useful" in the applicable statutes or Commission rules. "Used and useful" is determined by a report filed by each utility pursuant to R.C. 4909.05. Here, Blue Ridge expressly approved DEO's accounting methods. Neither Staff nor OCC has challenged DEO's valuation report.

Fourth, the Blue Ridge Report's treatment of blanket work order projects as used and useful makes sense. Because these projects are all of short duration (*i.e.*, will be in service soon, if not already), blanket work order projects are closed monthly and moved into rate base regardless of the completion status of a particular project. DEO Ex. 2 at 6-7; Tr. II at 7, 16. The only other alternative, of course, would be to account for each small project of short duration manually, which would also result in AFUDC that would be charged to customers. This is impractical for the thousands of projects DEO accounts for through the blanket work order automated process. It would require additional accounting resources and thus generate additional overhead expense which provides no clear benefit to anyone. That is undoubtedly why the FERC system of accounts has adopted the blanket work order process for these short duration projects. OCC Ex. 4 at 620; 18 CFR 201 at Gas Plant Instructions(11)(B).

III. CONCLUSION

For the foregoing reasons and for reasons stated in DEO's Post-Hearing Brief, DEO respectfully requests that the objections of Staff and OCC be overruled, and that the Commission approve in full DEO's Application for the PIR Cost Recovery Charge, adjusted only to account for Staff's recommendation relating to the calculation of the accumulated depreciation expense in Application Schedule 5.

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Respectfully submitted,

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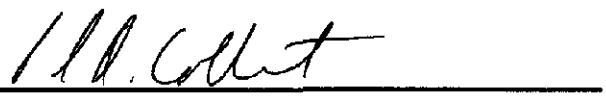
CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing was sent by electronic mail to the following party on this 12th day of November, 2009.



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