BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Duke Energy Ohio Inc., for an Increase in Gas Rates.	:	Case No. 12-1685-EL-AIR
In the Matter of the Application of Duke Energy Ohio Inc., for Tariff Approval.	:	Case No. 12-1686-EL-ATA
In the Matter of the Application of Duke Energy Ohio Inc., for Approval of an Alternative Rate Plan for Gas Distribution Service.	:	Case No. 12-1687-EL-ATA
In the Matter of the Application of Duke Energy Ohio Inc., for Approval to Change Accounting Methods.	:	Case No. 12-1688-EL-AAM

INITIAL POST-HEARING BRIEF

SUBMITTED ON BEHALF OF THE STAFF OF
THE PUBLIC UTILITIES COMMISSION OF OHIO

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I. Introduction

The Commission has been deciding what utility expenses can be recovered from customers for a very long time. For decades, the Commission has applied the statutory formula established by the General Assembly to make this decision. The point of this statutory formula is, in essence, to match the cost incurred by the utility while providing service to customers with the amount customers pay in rates. The Commission looks to Ohio Supreme Court cases and prior Commission decisions for guidance when interpreting this statutory formula. This is the exact process envisioned by the General Assembly.

Duke Energy Ohio, Inc. ("Duke") wants to upset this process. Duke wants the Commission to treat the expenses Duke incurred in this case differently because these expenses relate to Duke's remediation of long-retired manufactured gas plants ("MGP Sites"). Although Ohio law requires a matching of expenses with used and useful facilities, Duke asks the Commission to ignore this fundamental legal principle. Duke believes its remediation costs are "special" and, therefore, wants gas customers to pay all of these costs, even if these costs have nothing to do with the provision of gas service for current gas customers. There is no legal basis for such a broad request. Under Ohio law, the used and useful standard must be applied.

Putting aside the "used and useful" issue, Duke's request presents other legal problems. Allowing Duke to recover all of its remediation costs would cause various inequitable cross-subsidies. Here are just a few examples:

- Current gas customers would be subsidizing electric customers by paying for the remediation of electric facilities.
- Current gas customers would be subsidizing prior generations of Duke's customers by paying for the remediation of manufactured gas facilities that have not provided gas in at least fifty years.
- Current gas customers will be subsidizing future generations of Duke's customers by paying for the remediation of vacant properties that may (or may not) be used in the future to provide gas service.

Duke asks the Commission to enter dangerous legal terrain. The Commission does not need to do so. The statutory ratemaking formula, as written, avoids these very problems of cross-subsidies by requiring an alignment of the cost of providing service with the amount customers pay in rates.

Staff recommends that the majority of the remediation costs be disallowed. Staff came to this conclusion after thoroughly inspecting the MGP Sites to determine if the remediation costs were associated with properties that were used and useful. Staff found that the overwhelming majority of the MGP Sites were not used and useful. Therefore, based upon the facts, Staff believes that its recommendation is consistent with Ohio law and should be adopted.

II. Statement of Facts and Procedural History

The MGP Sites at issue in this case are referred to as the East End Site and the West End Site. It is undisputed that Duke's customers have not benefited from any manufactured gas operations at the either of the MPG Sites for at least fifty years. No gas has been manufactured at the East End Site since 1963.[1] No gas has been manufactured at the West End Site since 1928.[2]

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1 Company Ex. 21 (Direct Testimony of Jessica L. Bednarcik ("Direct of Bednarcik")) at 5.

2 *Id.*

In Case No. 09-712-GA-AAM, Duke sought approval from the Commission to defer costs associated with the remediation of the MGP Sites.[3] On November 12, 2009, the Commission granted Duke's request to defer the remediation costs.[4] In the Finding and Order that granted deferral authority, the Commission stated:

> Since the requested authority to change Duke's accounting procedures does not result in any increase in rate or charge the Commission approves this application without a hearing. The recovery of the deferred amounts will be addressed in a base rate case proceeding should Duke ever seek to recover the deferrals.[5]

The Commission stated that nothing in the Finding and Order was "binding upon [the] Commission in any subsequent investigation or proceeding involving the justness or reasonableness of any rate [or] charge."[6] The Commission did not consider whether the properties were used and useful at the time of granting deferral authority, a fact that Duke acknowledged during the *Deferral Case*.[7] Further, as Duke has admitted, the

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3 *In the Matter of the Application of Duke Energy Ohio, Inc., for Authority to Defer Environmental Investigation and Remediation Costs*, Case No. 09-712-GA-AAM ("*Deferral Case*") (Application) (August 10, 2009).

4 *Deferral Case* (Finding & Order) (November 12, 2009).

5 *Id.* at 3.

6 *Id.*

7 OCC Ex. 11 (*Deferral Case*) (Memorandum Contra Applications for Rehearing) (December 18, 2009) at 9-10 ("There is no reason to believe that the Commission was underhandedly determining the used and useful nature of the properties.... The Commission did not consider whether the property was used and useful.").

Commission did not make any decision regarding what remediation costs might be recoverable in the *Deferral Case*.[8]

On June 7, 2012, Duke filed a notice of intent to file an application to increase gas rates.[9] In this notice, Duke proposed a date certain of March 31, 2012. In its July 2, 2012 Entry, the Commission accepted Duke's proposed date certain of March 31, 2012.[10] On July 9, 2012, Duke filed an application to increase the rates of its natural gas customers ("Application").[11] In the Application, Duke sought recovery of the deferred remediation costs.[12] When it filed the Application, Duke proposed to amortize approximately $65 million in remediation costs over a three year period.[13] Duke subsequently modified the amount of remediation costs it is seeking to recover to $62.8 million, which reflects the actual remediation costs plus carrying costs as of December 31, 2012.[14]

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8 OCC Ex. 11 (*Deferral Case*) (Memorandum Contra Applications for Rehearing) ("Memorandum Contra") (December 18, 2009) at 2-3 ("This is not an application for recovery of these costs. This is merely a request for authority to defer the amounts so that their recovery can be assessed at a later point in time."); *Id.* at 10 ("[S]uch proof [that the properties are used and useful] is not required at this juncture. This proceeding merely allows deferral, not recovery.").

9 Company Ex. 1 (*In the Matter of the Application of Duke Energy Ohio, Inc., for an Increase in Gas Rates,* Case Nos. 12-1685-GA-AIR, *et al.* ("*In re Duke Gas Rates*") (Notice of Intent) (June 7, 2012)).

10 *In re Duke Gas Rates* (Entry) (July 2, 2012).

11 Company Ex. 2 (*In re Duke Gas Rates* (Application) (July 9, 2012)).

12 *Id.* at 5-6.

13 *Id.* ($47 million actual costs + $15 million projected cost + $3 million in carrying charges and deferrals = $65 million).

14 Company Ex. 19C (Third Supplemental Testimony of William Don Wathen, Jr. (Wathen Third Supp.)) at 3; Tr. III at 775-776.

On January 4, 2013, Staff filed its Staff Report of Investigation ("Staff Report").[15] In the Staff Report, Staff recommended that the Commission allow Duke to recover a total of $6,367,724 in remediation costs. During its investigation, Staff determined that the majority of the remediation costs were associated with properties that were not used and useful in rendering gas service on March 31, 2012, the date certain.[16] The Staff Report discusses in detail the basis for Staff's conclusion.[17] Staff witness Adkins testified regarding how Staff developed its recommendation and Staff's process of inspecting the MGP Sites.[18] Mr. Adkins explained the step-by-step process Staff used to determine where the remediation work was actually performed and where facilities that are currently used to provide gas service for customers are located.[19]

In the Staff Report, Staff included detailed maps of the MGP Sites to show the results of its investigation.[20] These maps are consistent with the descriptions of the MGP Sites contained in the Staff Report and consistent with Mr. Adkins's testimony regarding the results of Staff's investigation.[21] Duke provided Staff with these maps and the

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15 Staff Ex. 1 (*In re Duke Gas Rates*) (Staff Report of Investigation) (January 4, 2013) ("Staff Report").

16 *Id.* at 40-47.

17 *Id.*

18 Staff Ex. 6 (Prefiled Direct Testimony of Kerry J. Adkins) (April 22, 2013) ("Adkins Direct")) at 3-16.

19 *Id.*

20 Staff Ex. 1 at 57-64 (Staff Report – Attachment MGP-5 through MGP 12).

21 *Id.* at 40-47, 57-64; Staff Ex. 6 (Adkins Direct) at 3-16.

information contained on these maps in response to Staff's data requests.[22] Duke admits that these maps accurately reflect where the remediation work was performed at the MGP Sites and accurately reflect where the facilities that currently provide gas service for customers were located during Staff's investigation.[23]

After the Staff Report was filed, many of the parties agreed to stipulate all of the issues related to Duke's Application except for issues regarding recovery for remediation cost. As part of the stipulation, the parties agreed to $0.00 increase in gas base rates and agreed that Duke may establish a rider to recover the remediation costs if the Commission approved recovery of such costs. The parties also agreed to litigate their positions regarding Duke's entitlement to recovery of the MGP remediation costs. From April 29, 2013 to May 2, 2013, the parties litigated their positions.

III. Staff's recommendation to exclude the majority of the remediation costs comports with Ohio law

When fixing rates, the Commission must determine "[t]he valuation as of the date certain of the property of the public utility used and useful ... in rendering the public utility service for which rates are to be fixed and determined."[24] This valuation of property is the "rate base" portion of the ratemaking formula. Property cannot be

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22 Staff Ex. 1 at 57-64 (Staff Report-Attachment MGP-5 through MGP 12); Staff Exhibit 7 (Duke's Response to Staff DR 68); Staff Ex. 3 (Map of West End Site – North of Mehring Way); Staff Ex. 4 (Map of West End Site – South of Mehring Way); Tr. 450-462.

23 *Id.*

24 R.C. 4909.15(A)(1).

included in rate base unless it is used and useful in providing service for customers on the date certain.[25] Whether property is used and useful is a question of fact and must be resolved on a case-by-case basis.[26]

In addition to determining what property should be included in rate base, the Commission must determine the "cost to the utility of rendering the public utility service for the test period..."[27] The Ohio Supreme Court stated that "R.C. 4909.15(A)(4) is designed to take into account normal, recurring expenses incurred by utilities in the course of rendering service to the public for the test period."[28]

The true issue in this case is whether the remediation costs Duke seeks to recover are recoverable expenses under R.C. 4909.15(A)(4). It is well-established precedent that expenses associated with property that is not used and useful must be excluded from recovery. Long ago the Commission accepted this principle of "matching" expenses with property that is used and useful.[29] The Commission has applied this "matching" principle to various kinds of expenses, including operation and maintenance ("O&M") expenses.

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25 Although Staff determined the majority of properties at the MGP Sites were not used and useful, Staff did not make any adjustment to Duke's plant in service. This was an omission on the part of Staff. Tr. IV at 888-890. However, any adjustment to the rate base would have been *de minimis* due to the age of the properties and the fact the properties are largely vacant land.

26 *Consumers' Counsel v. Pub. Util. Comm.*, 58 Ohio St. 2d 449, 453 (1979) ("*Toledo Edison*").

27 R.C. 4909.15(A)(4).

28 *Consumers' Counsel v. Pub. Util. Comm.*, 67 Ohio St. 2d 153, 164 (1981).

29 *In the Matter of the Application of Ohio Edison Company*, Case No. 89-1001-EL-AIR, 1990 Ohio PUC LEXIS 912 (Opinion and Order) (August 16, 1990).

In *In the Matter of the Application of Ohio Edison Company*, 89-1001-EL-AIR, 1990 Ohio PUC LEXIS 912, 143-144 (Ohio PUC 1990) ("*In re Ohio Edison*"), the Commission applied the matching principle to exclude O&M expenses associated with a facility that was not in operation during the test year:

> There is no dispute that the West Lorain plant was not in operation during the test year and the company has indicated that it will not be placed into service for at least two to three years....Given these facts, we are not inclined to deviate from the concept of matching test-year expenses to used and useful plant and equipment.[30]

The Commission has applied this matching principle in recent rate cases also.[31] In *In re Ohio Edison II*, Ohio Edison sought recovery of expenses associated with securing and maintaining several retired generation facilities.[32] Staff objected to recovery of these expenses because they were associated with facilities that were no longer used and useful.[33] Ohio Edison argued that the used and useful concept was inapplicable because

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30 *Id.* at *143-144; See also *In re The Toledo Edison Company*, 79-143-EL-AIR at 61-62, 1980 Ohio PUC LEXIS 3 (Order) (February 29, 1980) ("[W]e concluded that a portion of the Edison Plaza should be excluded from the Applicant's rate base. Since the excluded portion is not used and useful in providing electric service to the public, *the expenses associated with that portion should also be excluded from the Applicant's test year expenses.*") (emphasis added).

31 *In re Application of Ohio Edison Company*, Case No. 07-551-EL-AIR (Opinion and Order) (January 21, 2009) ("*In re Ohio Edison II*").

32 *Id.* at 14.

33 *Post-Hearing Brief Submitted on Behalf of the Staff of the Public Utilities Commission of Ohio*, (March 18, 2008) (*In re Ohio Edison II*) at 23 (See excerpt from brief - **Attachment A**); *Reply Submitted on Behalf of the Staff of the Public Utilities Commission of Ohio*, (April 14, 2008) (*In re Ohio Edison II*) at 5-6 (See excerpt from brief - **Attachment B**).

Ohio Edison was not attempting to include the facilities in rate base.[34] Rather, Ohio Edison claimed that it was entitled to recovery because it was only seeking to recover expenses related to the facilities.[35]

Duke's theory of recovery in this case is strikingly similar to the argument Ohio Edison made in *In re Ohio Edison II*. Ohio Edison argued that the retired generating units' "existence [could] cause safety issues if not properly maintained and secured."[36] Much like Duke argues here, Ohio Edison claimed that current customers benefited from these expenses because the expenses prevented potential future liability for the utility and customers.[37] Ohio Edison even claimed that current customers should be responsible for the expenses because past customers benefited from the operation of the plants when the plants were in service:

> The costs incurred for maintenance and security at these facilities provide for the safety of the surrounding communities, help to prevent potential terrorist activity and

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34 *Initial Brief of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company*, (March 28, 2008) at 38-39 (*In re Ohio Edison II*). (See excerpt from brief - **Attachment C**).

35 *Id.*

36 *Supplemental Direct Testimony of Trevor J. Fernandez on Behalf* of *Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company,* (filed January 1, 2008, admitted into record as Company Ex. 9B) at 7 (*In re Ohio Edison II*). (See testimony- **Attachment D**).

37 *Id.* This argument is similar to Duke witness Bednarcik's claim that Duke is entitled to recover remediation costs because its decision to remediate the MGP Sites may limit potential future liability. Company Ex. 21A (Bednarcik Supplemental Testimony (Bednarcik Supp. Test.)) at 3 ("The actions taken were… designed to resolve environmental liability and **mitigate future risk** to the Company, ratepayers, shareholders, and others.)(emphasis added).

> benefit all of Ohio Edison's customers by minimizing opportunities for death or injury that may result in legal liability – and increased costs – to the Operating Companies. Additionally, customers received benefits throughout the many years that these generating units were producing electricity. **The cost obligations that exist today are a direct result of those benefits received by customers while these plants were in service.**[38]

The Commission rejected Ohio Edison's argument outright. The Commission found that the "generation [facilities] were not used to provide generation service during the test year" and concluded that the expenses associated with the generation facilities did not "reflect costs to the utility of rendering public utility service for the test period in accordance with Section 4909.15(A)(4), Revised Code."[39] Therefore, none of these costs were recoverable.

Duke contends that whether or not the MGP Sites were used and useful on the date certain is "irrelevant."[40] Duke claims that it is automatically entitled to the recovery of the remediation costs if it proves the costs were prudently incurred.[41] This argument is inconsistent with Ohio law. In *Dayton Power & Light Co. v. Pub. Util. Comm.*, 4 Ohio

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38 **Attachment D** (emphasis added). Duke makes this same "historical use" argument, claiming that is entitled to recovery of the remediation costs because the clean-up of the MGP Sites arose from historical MGP operations and "[c]ustomers benefitted from the services provided by the plants at this location." Company Ex. 21A at 5, (Bednarcik Supp. Test.).

39 *In re Ohio Edison II* (Opinion and Order) at 14.

40 Tr. III at 756 (Cross Examination of Duke witness William Don Wathen – ("Used and useful is irrelevant"))' Tr. III at 795 ("[W]hen we filed the application [in Case No. 12-1685-GA-AIR] and found out we were doing this case, my understanding was this was prudence, not whether costs were used or useful.").

41 *Id.*

St. 3d 91, 102-103 (1983), the Ohio Supreme Court determined that the Commission properly excluded costs that were associated with plants that were not used and useful on the date certain.[42] Although the costs were prudently incurred, the Court held that the costs were not recoverable from ratepayers under R.C. 4909.15(A)(4).[43] The Court relied specifically upon the used and useful standard:

> In [*Toledo Edison*] this court held that the Davis-Besse Unit 1 generating station, which was not "used and useful in rendering the public utility service" pursuant to R.C. 4909.15(A)(1), could not be included in the utility's rate base. ...While we again note that *Toledo Edison* involved rate base consideration under 4909.15(A)(1), as opposed to matters relating to cost of service under R.C. 4909.15(A)(4), the analogy is a fair one insofar as it indicates that the General Assembly has adopted a consistent position in balancing investor and consumer interests in utility ratemaking. Pursuant to the statutory ratemaking formula investors are assured a fair and reasonable return on property that is determined to be used and useful, R.C. 4909.15(A)(2), plus the return of costs incurred in rendering the public service, R.C. 4909.15(A)(4), while consumers may not be charged "for utility investments and expenditures that are neither included in the rate base ***nor properly categorized as costs***." We see no constitutional infirmity in the balance thus struck by the General Assembly.[44] (emphasis added)

The Ohio Supreme Court's position on the "matching principle" is clear. The application of the used and useful standard is not limited to determining what property belongs in

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42 *Id.* at 102-103.

43 *Id.*

44 See also *Consumers' Counsel v. Pub. Util. Comm.*, 67 Ohio St. 2d 153, 163-164 (1981) (the Court held that costs incurred by a utility to construct a nuclear facility, although prudently incurred, could not be recovered from ratepayers under R.C. 4909.15(A)(4)) (emphasis added).

rate base. The standard must be applied to costs utilities seek to recover under R.C. 4909.15(A)(4) as well.

Applying this law to the facts of Duke's case, the Commission should exclude the vast majority of Duke's remediation costs.

IV. The Staff Report and evidence presented at the hearing prove that the majority of the remediation costs are not associated with facilities that are used and useful.

a. West End Site

The Commission should not allow Duke to recover any remediation costs related to the West End Site.

i. North of Mehring Way

At the North of Mehring Way Parcel, there are no gas facilities currently used and useful in the provision of gas service where the remediation work was performed.[45] The parcel is primarily a compacted gravel lot.[46] The only facilities currently being used in the North of Mehring Way Parcel are a few electric transmission towers.[47] It goes without saying that electric transmission towers do not provide gas service for customers.

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45 Staff Ex. 1 (Staff Report) at 44 and 61; Staff Ex. 6 (Adkins Direct) at 8-11, Ex. KA-2.

46 Staff Ex. 1 (Staff Report) at 44 and 61; Staff Ex. 6 (Adkins Direct) at 8-11, Ex. KA-2.

47 Staff Ex. 1 (Staff Report) at 44 and 61; Staff Ex. 6 (Adkins Direct) at 8-11, Ex. KA-2.

There is no legal basis for charging gas customers for the cost of remediating properties used to serve electric customers.

Although a portion of the North of Mehring Way Parcel was previously used as a parking lot, the parking lot was not replaced as of the date certain or at any time during Staff's investigation.[48] The Ohio Supreme Court has stated that utilities have total control over when they file their applications for rate increases, which allows the utilities to control the used and useful status of their property.[49] Duke chose the date certain in this case and chose to seek a rate increase when the parking lot was not used or useful.[50] Therefore, Duke must live with the date certain.

There are other problems with allowing recovery associated with the parking lot. For one, it is unclear when Duke will reinstall this parking lot if at all.[51] It is unfair to force customers to pay today for expenses associated with a nonexistent parking lot, especially if Duke does not know when this parking lot will be reinstalled. In addition, the parking lot was used by numerous Duke Energy Ohio units that were not solely devoted to providing services for gas customers.[52] Assuming, *arguendo*, that Duke is entitled to recover remediation costs related to the parking lot, these costs should be

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48 Staff Ex. 1 at 44 (Staff Report); Staff Ex. 6 (Adkins Direct) at 8-11.

49 *Ohio Edison Co. v. Pub. Util. Comm.*, 63 Ohio St. 3d 555, 559 (1992); and *Consumers' Counsel v. Pub. Util. Comm.*, 58 Ohio St.2d 449, 457, 12 O.O.3d 378, 383, 391 N.E.2d 311, 315 (1979).

50 Company Ex. 1 (Notice of Intent) (requesting March 31, 2012 as the date certain).

51 Tr. II at 468-469.

52 Company Ex. 21A at 10 (Bednarcik Supp. Test.); Tr. II at 467-468.

allocated among the various units so that gas customers only pay a portion of the costs. If Duke's gas customers are required to pay all of the remediation costs related to the parking lot, they will be subsidizing units within Duke that have little or nothing to do with the provision of gas services.

ii. South of Mehring Way

The South of Mehring Way Parcel presents essentially the same problem as North of Mehring Way Parcel. Most of the South of Mehring Way Parcel is used for electric transmission and distribution services.[53] The only gas facilities at the South of Mehring Way Parcel are two 12-inch natural gas pipelines and a "city gate building" on the far eastern edge of the parcel. These gas facilities are at least 300 feet away from the remediated work zone.[54] Despite the fact these gas facilities are far away from the remediation zones, Duke insists that it is entitled to recover remediation costs associated with the entire West End Site because it plans to replace the two 12-inch natural gas pipelines in the future. Duke claims that replacing these pipelines will involve boring operations, which will require a substantial amount of space for boring equipment. Duke, however, does not know what sections of the West End Site will be needed for potential boring operations. Duke witness Hebbeler admitted that the logistics of the boring operations are still being coordinated.[55] Even if the logistics were solidified, there is no

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53 Staff Ex. 1 (Staff Report) at 44-45; Staff Ex. 6 (Adkins Direct) at 9-11.

54 Staff Ex. 6 (Adkins Direct) at 9-11.

55 Tr. III at 733.

evidence that Duke will need the entire West End Site to perform these boring operations. Further, these future boring operations are not associated with the current provision of gas service for customers.

Duke's arguments about potential boring operations in the future distract from the relevant issues of this case. Nothing Staff is recommending will affect Duke's ability to perform boring operations at the West End Site. Duke owns the entire West End Site and can use it in any manner it chooses. But simply because Duke owns all of the West End Site does not necessarily mean that all of the West End Site was used and useful in providing gas service for customers on the date certain. Cost recovery, under R.C. 4909.15(A)(4), must be connected to facilities that are currently used and useful. For the majority of the remediation costs, Duke failed to prove that this connection exists.

b. The Purchased Property

Recovery of costs related to the Purchased Property is even more problematic than the West End Site. Duke bought this property as part of a confidential settlement agreement in order to prevent potential liability.[56] As part of this confidential settlement, Duke agreed to pay an extra $2,159,000, an above-market "premium".[57] Duke now wants to recovery this "premium" from ratepayers.

There is no legal basis for the recovery of any costs associated with the Purchased Property. The "premium" Duke paid to purchase the property was not a cost of rendering

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56 Tr. II at 311-313, 363-364.

57 Staff Ex. 1 (Staff Report) at 34; Tr. II at 363-364.

service to customers. No remediation work was performed on the Purchased Property. No facilities are currently located on the Purchased Property.[58] It is simply a vacant field.[59] Duke witness Wathen admits that the Purchased Property is not included in rate base and is not used and useful.[60] There is no evidence the Purchased Property will eventually be used to provide gas service to customers. Duke witness Bednarcik admitted that Duke has not determined what it will do with this property yet.[61] Although Duke may claim it needs the Purchased Property for some future purpose, the Commission has refused to accept similar arguments as a basis for recovery in the past.[62] In *In re Toledo Edison*, the Commission summarized its position on similar "future use" arguments quite aptly:

> While prudent planning may demand acquisition of land sites some time before such land is put to actual use, such land is not "used and useful" as envisioned by the controlling statutory provision until it is contributing to providing the utility service to the consuming public. Likewise, land lying adjacent to or contiguous with a generating unit or substation which is clearly not attendant to the operation of the facility but is excess land not necessary for the practical functioning of the station must be deemed land not includable in the utility's rate base. At hearing applicant's witness stated such

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58 Staff Ex. 6 (Adkins Direct) at 15-16, Exhibit KA-6.

59 *Id.*

60 Tr. III at 755, 792.

61 Tr. II at 465, 467-468. Company Ex. 21 at 19 (Bednarcik Direct) ("Future use of the [Purchased Property] will be determined base upon the needs of the Company after completion of all investigation and remediation, if required").

62 *In the Matter of the Toledo Edison Company,* Case No. 75-758-EL-AIR, 1976 Ohio PUC LEXIS 1, *9-10 (Order) (November 30, 1976).

> areas were ultimately going to be used and that the areas were being held for "long-term" use with no "firm" plans currently established. Clearly land of this character must be considered as land held for future use and must be excluded from applicant's rate base.[63]

The evidence in this case proves that the Purchased Property is not "contributing to providing the utility service to the consuming public." No remediation costs should be allowed related to the Purchased Property.

c. East End Site

i. Eastern Parcel

1. Brief description of the parcel

The Eastern Parcel is approximately 9.7 acres.[64] The parcel had no visible, above-ground facilities located on it during Staff's investigation.[65] The only facilities identified in the Eastern Parcel are three 20-24 inch underground gas mains (Lines "E", "D", and "N") and two 16 inch transmission lines ("AMO2").[66] Lines E, D, and N traverse the Eastern Parcel and feed into Duke's distribution system and the propane injection facility.[67] The AM02 lines connect with Line E on the south side of the Eastern Parcel

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63 *Id.* (citations removed)

64 Staff Ex. 6 (Adkins Direct) at 13.

65 *Id.* at 13, Ex. KA-4.

66 Staff Ex. 1 (Staff Report) 41, 57, and 64; Staff Ex. 6 (Adkins Direct) at 12-13; Company Ex. 22C (Second Supplemental Testimony of Gary J. Hebbeler (Hebbeler Sec. Supp.)) at 3-4.

67 Company Ex. 22C (Hebbeler Sec. Supp.) at 3-4.

and cross the Ohio River into Kentucky. Only a small portion of the AM02 lines are within the area that was remediated in the Eastern Parcel.[68]

2. Staff's recommendation

Staff recommends that the Commission allow Duke to recover remediation costs associated with remediating the land within a 50-foot buffer zone around the pipelines located in the Eastern Parcel.[69] Although the pipelines are no larger that 24 inches wide, Staff believes a portion of the property surrounding the pipelines should also be considered part of the pipelines. Staff witness Adkins explained that his 50 foot "buffer" recommendation was developed based upon advice of the Commission's Pipeline Safety Division ("Pipeline Safety"). Mr. Adkins, in discussions with Pipeline Safety, also relied upon a U.S. Sixth Circuit Court of Appeals decision, which states that a 50-foot buffer is a reasonable industry standard.[70]

Considering that the Eastern Parcel is approximately 9.7 acres and almost completely vacant, Staff believes it would be unreasonable to allow Duke to recover all of the remediation costs associated with the entire parcel.[71] Although Duke needs a reasonable amount of space to operate, maintain, and repair the pipelines, it should not be

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68 Staff Ex. 5 (Copy of Attachment MGP 11 – circle indicating where the AM0 line is located); Tr. III at 701-703.

69 Staff Ex. 6 (Adkins Direct) at 12-13.

70 *Andrews v. Columbia Gas Transmission Corp.*, 544 F.3d 618 (6th Cir. 2008).

71 Staff Ex. 6 (Adkins Direct) at 13; Tr. IV at 894-897.

allowed to recover the costs of remediating thousands of feet of vacant property that are not directly associated with used and useful facilities.

3. Replacement of the AM02 line

Duke claims that it is entitled to recover all of the remediation costs associated with the Eastern Parcel because it may need to use the entire Eastern Parcel to replace the AM02 line in the future. [72] This argument is completely speculative and hinges upon an underlying premise that may never occur. It is evident from Duke witness Hebbeler's testimony that Duke does not know if or when it will need to replace the AM02 line. Duke witness Hebbeler admitted that he does not know when the AM02 will need to be replaced.[73] As far as Mr. Hebbeler knows, the AM02 lines are not corroding or leaking.[74] Mr. Hebbeler admits that if there was a major corrosion issue on the AM02 lines, he would have learned of this problem.[75] He admits that the AM02 lines are cathodically protected, which helps to substantially reduce the likelihood of corrosion.[76] In fact, Mr. Hebbeler admits that cathodic protection theoretically provides the AM02 an unlimited

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72 Company Ex. 22C (Hebbeler Sec. Supp.) at 4-7.

73 Tr. III at 689-690, 706.

74 *Id.* at 718.

75 *Id.*

76. *Id.* at 684.

life expectancy.[77] Further, even if the AM02 lines begin to leak or corrode, Mr. Hebbeler admits that replacing the AM02 lines would not necessarily be the only remedy.[78]

Assuming, *arguendo*, that Duke does need to replace the AM02 in the near future, it is unclear why Duke Energy Ohio ratepayers should bear all the costs of remediating a potential construction area for replacing the AM02. Mr. Hebbeler admitted that Duke Energy Kentucky owns the vast majority of the AM02 and that this pipeline is recorded on Duke Energy Kentucky's books.[79] He also admitted that Duke Energy Kentucky would share the cost of replacing the AM02.[80] Despite these facts, Duke wants Ohio ratepayers to pay millions of dollars today for a potential construction area for the potential replacement of a pipeline owned primarily by Kentucky ratepayers. But, as far Duke knows, it might be decades before the AM02 lines need to be replaced.

The speculative nature of Duke's argument is not the only problem. Duke ignores where the existing pipelines are located and ignores where the remediation work was actually performed. It is undisputed that many of the remediated portions of the Eastern Parcel are extremely far from the existing pipelines. The Eastern Parcel is 9.7 acres, which is approximately 422,532 square feet.[81] Some of the remediated areas, which are

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77 *Id.*

78 Tr. III at 718-720.

79 *Id.* at 713-716.

80 *Id.* at 715-716.

81 Staff Ex. 6 (Adkins Direct) at 13. Mr. Adkins testified that the Eastern Parcel is approximately 9.7 acres. One acre is approximately 43,560 square feet. 9.7 acres x 43,560 square feet = 422,532 square feet.

still vacant, are well over a hundred feet away from any of the pipelines.[82] Remediating these unused sections of the property was not necessary to operate or maintain Duke's pipelines. Duke may claim it needs to use the entire Eastern Parcel in the future. Even if this is true, it is irrelevant. Nothing Staff is recommending in this case prevents Duke from using its property as it pleases:

> **Q. [by Mr. Parram]** If Duke doesn't recover any remediation costs at all in this case, would you still be able to use the eastern parcel, the central parcel, western parcel if you need to replace the AM02 line?
>
> **A. [by Duke witness Hebbeler]** From an operations standpoint you would physically be able to do that, yes.
>
> **Q.** Okay. So …you would still be able to use the property to do what you need to do?
>
> **A.** Yes…[83]

Duke's ability to operate its facilities in the future is not at issue. The question before the Commission is whether the remediation costs constitute recoverable expenses associated with used and useful facilities. The only way to answer this question is to perform a detailed analysis of (1) where the remediation work was *actually* performed and (2) where gas facilities that are currently used and useful are *actually* located. Staff performed this analysis and determined that only a portion of the remediated area in the

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82 Staff Ex. 1 (Staff Report) at 57, 63, 64 (Attachment MGP-5,11, and 12).

83 Tr. III at 708-709, 717 (**Q.** "[Y]ou've indicated earlier [that] nothing in this hearing would prevent Duke Energy Ohio from using that parcel if they needed to stage equipment to do the horizontal directional drilling?" **A.** "That's correct.").

Eastern Parcel is associated with used and useful facilities. The record supports Staff's conclusion.

4. Clean fill site

Duke argues that the Eastern Parcel is used and useful because Duke previously used the parcel as a clean fill site.[84] Duke, however, stopped using the Eastern Parcel as a clean fill site before the parcel was remediated and was not using the Eastern Parcel as a clean fill site on the date certain.[85] Further, Duke only occasionally used the Eastern Parcel as a clean fill site when it needed to excavate main and service lines.[86] There is no evidence regarding how often the Eastern Parcel was needed to dump fill from these excavation operations. Although Duke previously had a permit that allowed it to use the Eastern Parcel as a clean fill site, it is unclear whether Duke still has authority to continue using the parcel as a clean fill site.[87] In addition, there is no evidence that Duke used all of Eastern Parcel as a clean fill site, nor is there any evidence establishing what specific portions of the 9.7 acre site will be used as a clean fill site in the future.

In summary, the only evidence in the record regarding the clean fill site shows that Duke sporadically dumped fill on an undefined portion of the parcel in the past and may (or may not) sporadically dump fill on an undefined portion of the parcel in the future.

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84 Company Ex. 22C (Hebbeler Sec. Supp.) at 7.

85 *Id.*; Tr. III at 720.

86 Company Ex. 22C (Hebbeler Sec. Supp.) at 7.

87 Tr. II at 471.

This is not a basis for allowing Duke to recover all the remediation costs associated with the Eastern Parcel.

ii. Western Parcel

1. Brief description of the parcel

Until very recently, the Western Parcel was vacant.[88] On the date certain, the Western Parcel contained no facilities that were used and useful in the provision of gas service for customers.[89] Although Duke recently began construction of vaporizers in the Western Parcel, these new vaporizers were not in operation on the date certain or during Staff's on-site investigations.[90]

2. Staff's recommendation

Because there were no facilities located in the Western Parcel that were used and useful on the date certain, Staff recommends that almost all of the remediation costs associated with the Western Parcel be excluded from recovery. Staff recommends that the Commission allow Duke to recover remediation costs associated with the northeastern corner of the Western Parcel. This portion of the Western Parcel falls within a 50-foot minimum setback from an existing vaporizer building located in the northwest

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88 Staff Ex. 1 (Staff Report) at 42, 59, and 63; Staff Ex. 6 (Adkins Direct) at 14-15, Exhibit KA-5.

89 Staff Ex. 1 (Staff Report) at 42, 59, and 63; Staff Ex. 6 (Adkins Direct) at 14-15, Exhibit KA-5.

90 Staff Ex. 1 (Staff Report) at 42; Staff Ex. 6 (Adkins Direct) at 14.

corner of the Central Parcel.[91] This 50-foot minimum setback from the existing vaporizer building is based upon the National Fire Protection Association ("NFPA") Code minimum-set back requirements for liquid gas vaporizers and gas-air mixers.[92]

3. Propane pumps

Duke claims that it is entitled to all the remediation costs associated with the Western Parcel because it uses portions of the parcel to maintain its propane pumps. Duke witness Hebbeler claims that the "maintenance process requires the propane pumps to be removed occasionally," which also involves filling the pumps shafts with water and then dispersing this water onto the Western Parcel.[93] The fact Duke "occasionally" disperses water on the Western Parcel is not a basis for recovery of all the remediation costs associated with this parcel.

The first flaw in Duke's argument regarding the propane pumps is that these facilities are not located in the Western Parcel. Staff did not observe any propane pumps in the Western Parcel during its investigation, nor did Duke indicate that there were any propane pumps located in the Western Parcel during Staff's investigation.[94] Further, Mr. Hebbeler admitted that these propane pumps are located in the Central Parcel:

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91 Staff Ex. 1 at 42 (Staff Report); Staff Ex. 6 at 14 (Adkins Direct).

92 *Id.*

93 Company Ex. 22C (Hebbeler Sec. Supp.) at 9.

94 Staff Ex. 1 (Staff Report) at 42-43, 59 63; Staff Ex. 6 (Adkins Direct) at 14-15; Tr. II at 462 (Ms. Bednarcik admitting that Attachment MGP-12 of the Staff Report accurately reflects where the gas facilities were located at in the Western Parcel during Staff's investigation).

Q. **[By Mr. Hart]** You are pointing to what's labeled as the "valve pit"?

A. **[By Mr. Hebbeler]** Yes, I believe those are the two areas.

Q. One of which is on the middle parcel and the other is slightly onto the western parcel?

A. Both of them are on the middle parcel.

Q. They are both on the middle parcel.

A. That's correct.

Q. You are saying you need the western parcel to discharge the water from those – those valve pits?

A. That's correct.[95]

Because Staff recommended recovery for the entire Central Parcel, recovery for remediation costs associated with the actual propane pumps is not in dispute.

Another reason why the propane pumps are not a basis for recovery associated with the Western Parcel is because Duke did not use the entire Western Parcel to disperse water from the propane pumps.[96] Mr. Hebbeler testified that water was dispersed near the eastern border at the Western Parcel, slightly south of the "tar well."[97] He did not "know the exact operations", but Mr. Hebbeler believed that water was dispersed onto the Western Parcel from this location. Because he does not how much water is discharged, Mr. Hebbeler has no clue how much of the Western Parcel was actually used when

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95 Tr. III at 693.

96 *Id.* at 691-692.

97 *Id.*

dispersing water.[98] In addition, Duke does not routinely disperse water from the pumps.[99] Duke only needs to disperse water from the pumps if it discovers a problem during its annual pump-inspection process.[100] Years could go by before Duke needs to disperse water on the Western Parcel again.

Further, Duke failed to prove why the remediation costs associated with the Western Parcel were incurred to operate or maintain the propane pumps. Duke is trying to recover millions of dollars for remediating an empty piece of property just so Duke can occasionally pour water on it. Duke, however, did not remediate the Western Parcel to disperse water. In fact, if Duke never remediated the Western Parcel, its operation and maintenance of the propane pumps would not have changed at all. It would continue dispersing water from the propane pumps as usual.

4. Flaring station

Duke witness Hebbeler referred to a "new flaring station" and an "old flaring station" in the Western Parcel. Mr. Hebbeler testified that the new flaring station was not operational until after November 1, 2012.[101] This is approximately seven months after the date certain.[102] Because the remediation work was not performed to *operate or*

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98 Tr. III at 694.

99 *Id* at 727-731.

100 *Id.*

101 Tr. III at 722.

102 *In re Duke Gas Rates* (Entry) (July 2, 2012)(establishing March 31, 2012 as the date certain).

maintain a flaring station that was used and useful on the date certain, Duke should not be allowed to recover these expenses. Rather, the costs to install the new flaring station should be capitalized and recovered in Duke's next base rate case because these costs are associated with a new installation. In addition, Duke failed to identify this facility when Staff asked Duke to identify all facilities that are operational at the East End Site.[103]

Mr. Hebbeler also discussed an old flaring station. At the hearing, Mr. Hebbeler admitted that this flaring station was a "portable setup."[104] This portable flaring station was not located at the Western Parcel during Staff's investigation. And despite the fact Staff asked Duke to identify all the facilities located in the Western Parcel during Staff's investigation, Duke did not mention the flare off valve until it filed Mr. Hebbeler's Second Supplemental testimony. This was almost four months after the Staff Report was filed. Duke should not be allowed to belatedly identify additional facilities long after Staff has completed its investigation.[105]

In addition, there is no evidence that remediation was necessary to operate or maintain this portable flaring station. Further, there is no evidence that the entire parcel was needed or even used to operate the old flare off valve. While referring to Bednarcik

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103 Staff Ex. 1 (Staff Report) at 42-43, 59, 63.

104 Tr. III at 722.

105 *Ohio Edison Co. v. Pub. Util. Comm.*, 63 Ohio St. 3d 555, 558 (1992) ("The company's attempt to supplement its application with this additional plant after the issuance of the staff report and its failure to provide timely information with which the commission could verify the plant's status effectively prevented the commission from performing its statutory duty.")

Supp. Attachment JLB SUPP 3, Mr. Hebbeler described where the old flare off valve was located:

> **Q.** Okay. Where is the old one currently?
>
> **A.** The old one is around the words of "abandoned gas field" -- let's see, "abandoned gas" [Bednarcik Supp. Attachment JLB SUPP 3].
>
> **Q.** [Abandoned Gas] Cavern well?
>
> **A.** Right up above that, just north of that and just west of the fence line that runs down St. Andrews [Street][106]

Considering the fact that the old flaring station was located in the far southeast corner of the Western Parcel, Duke failed to explain why the entire Western Parcel should be considered part of its routine flaring operations.

5. Buffer Zones

Duke does not dispute the fact that Staff accurately identified the facilities that were used and useful at the Western Parcel during Staff's investigation.[107] Duke, however, claims that it is entitled to all of the remediation costs associated with the Western Parcel because it uses the entire Western Parcel as a "buffer zone".[108] Duke Witness Hebbeler claimed that "flaring operations require use of the entire [Western

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106 Tr. III at 692; Company Ex. 21A (Bednarcik Supp. Test.) at Attachment JLB SUPP 3.

107 Tr. II at 460-462.

108 Company Ex 22C (Hebbeler Sec. Supp.) at 8-9.

Parcel] as a buffer."[109] He also claimed that Duke needs the entire Western Parcel to help protect the sensitive utility infrastructure.[110] The Commission has rejected similar "buffer zone" arguments in the past.[111]

In *In re Ohio American Water,* Staff recommended that a portion of Ohio American's property be removed from base rates because the property was not used and useful.[112] Staff made this determination after an on-site inspection of the property.[113] Staff testified that the "exclusion of the parcel in no way deprives the Company of water rights", nor did the exclusion "create any interference in the efficient operation of [Ohio American's] present plant."[114] Ohio American contended that the property should not be excluded from base rates because the "property [was] necessary to operate and maintain the facilities and to provide an adequate buffer area…"[115]

The Commission rejected Ohio American's argument and concluded that the property was not used and useful. The Commission explained:

> [T]here are a number of factors which must be considered in evaluating adjustments involving the elimination of minor portions of land parcels on the theory that the total acreage at

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109 Company Ex 22C (Hebbeler Sec. Supp.) at 8-9.

110 *Id.*

111 *In the Matter of the Application of The Ohio-American Water Company*, Case No. 79-1343-WW-AIR, 1981 Ohio PUC LEXIS 3, (Order) (January 14, 1981).

112 *Id.* at *6-8.

113 *Id.*.

114 *Id.*

115 *Id.*

> a site is above that reasonably required to support a given installation.... [T]he Commission [previously] found the critical evidence in this area to be the admissions of Applicant's own witness with respect to the Company's specific plans for the future use of much of the area excluded by the Staff.[116]

The Commission found that Ohio American's witness failed to "propose a future use for the land, but stated the land would be needed as a buffer...."[117] Noting that similar "buffer" arguments had been rejected in the past, the Commission agreed with Staff's exclusion of the portion of the property that was not used and useful.[118]

Duke's broad sweeping "buffer zone" argument is similar to those raised in *Ohio-American* and *Ohio Edison Company*. Duke may intermittently use the Western Parcel for its flaring operations but it failed to explain why remediating several acres of vacant property was necessary to operate or maintain its flaring station. Much of the remediation work (which involved excavating then replacing dirt) was performed hundreds of feet away from the flaring station. As Staff acknowledged, Duke may be entitled to remediation costs that fall within reasonable, specifically-defined setbacks. However, specifically- defined setbacks are not what Duke is proposing. Rather, Duke is seeking blanket "buffer zones" that cover acres of vacant land. Duke wants to recover all

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116 *Id.* at *7-8.

117 *Id.*

118 *Id.* See also, *Ohio Edison Company*, Case No. 77-1249-EL-AIR (Order) (November 17, 1978) at 4 (the Commission excluded the company's "buffer zones" from base rates because the company failed to show that "a determination had been made by the company that *a specific amount of land was necessary for particular types of buffer zones*") (emphasis added).

of the remediation costs related to the Western Parcel despite the fact the only gas facilities in the Western Parcel may be hundreds of feet away from areas where remediation work was performed. With respect to Duke's proposed buffer zone for the sensitive utility infrastructure, Duke admits that nothing that Staff is recommending in this case will threaten Duke's ability to protect this sensitive utility infrastructure.[119]

Duke's only reasons for designating the entire Western Parcel as a "buffer zone" is because it owns the Western Parcel and has historically considered it part of the East End Site. This, however, is not evidence that Duke determined "a specific amount of land was necessary" to properly operate its flaring operations or its sensitive utility infrastructure. *Ohio Edison Company*, Case No. 77-1249-EL-AIR. Rather, this shows that Duke's decision to label the entire Western Parcel as a "buffer zone" is arbitrary.

V. The *Deferral Case* has no bearing on Duke's entitlement to recovery in this case

Recognizing that the used and useful standard precludes recovery of the majority of the remediation costs, Duke tries a different tack. Duke claims that the used and useful standard simply does not apply. Duke insinuates that the Commission, by allowing Duke to defer the remediation costs, implicitly determined that the used and useful standard

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119 Tr. III at 725.

will not apply in this case.[120] Duke even claims that the deferral provided "assurance of recovery in the future."[121] Ohio Supreme Court precedent disproves all of these claims.

The Ohio Supreme Court held that the Commission's grant of deferral authority has no bearing on whether the utility is entitled to rate recovery.[122] In *Elyria*, the Court stated that a deferral did not affect customers' distribution rates because the Commission was going to consider whether these deferred expenses were recoverable in a future rate case. [123]

Duke is fully aware of the import of *Elyria*. Duke cited to it extensively in the *Deferral Case*.[124] In fact, while relying upon *Elyria*, Duke argued that the Commission did not make any determination regarding the used and useful nature of the MGP Sites.[125] Duke now claims that the Commission is somehow precluded from examining the used and useful nature of the MGP Sites because it granted the deferral. Aside from being glaringly inconsistent, Duke is ignoring the plain language of the Commission's Entry on Rehearing in the *Deferral Case*:

> Once again, we emphasize that, at no point in our order, did we determine that the MGP sites are currently used and useful. Our summary of the application in the order merely

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120 Tr. III at 799-780.

121 Company Ex. 19C (Wathen Third Supp. Test.) at 9.

122 *Elyria Foundry Co. v. Pub. Util. Comm.*, 114 Ohio St.3d 305, 308 (2007).

123 *Id.* at 309.

124 OCC Ex. 11 (*Deferral Case*) (Memorandum Contra) (December 18, 2009) at 6-8.

125 *Id.* at 10.

> states that Duke claims that the MGP sites are still involved in the provision of utility service. As we stated in our order, the Commission has not yet made a determination on what costs, if any, may be appropriate for recovery.[126]

As the Commission and Duke stated previously, the *Deferral Case* was not the time to determine whether the MGP Sites were used and useful. That time is now.

VI. MGP Rider Issues

To the extent the Commission allows Duke to recover remediation costs, Staff believes a rider would be the most appropriate recovery mechanism. Duke agrees with Staff's recommendation to establish a rider to recover remediation costs.[127] Duke proposes to amortize the remediation costs over a three year period. Staff agrees to a three year recovery period if the Commission adopts Staff's recommended recovery amount of $6,367,724 million. [128] However, if the Commission allows Duke to recover the entire $62.8 million, Staff believes a ten year amortization period is more appropriate.[129]

Duke witness Wathen proposes an annual review of the actual MGP costs to determine whether these costs were prudently incurred.[130] Staff agrees that an annual review process is necessary but believes this annual review should not be limited to

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126 *Deferral Case* (Entry on Rehearing at 6) (January 7, 2010).

127 Company Ex. 19C (Wathen Third Supp. Test.) at 2.

128 Staff Exhibit 6 (Adkins Direct) at 25-26.

129 *Id.*

130 Tr. III at 750-751.

whether the costs where prudently incurred. Rather, Staff believes Staff should be allowed to investigate other issues regarding the appropriateness of recovery, including, but not limited to, whether the remediation costs are associated with facilities that are used and useful.

VII. Conclusion

Ohio's statutory ratemaking formula requires the application of the used and useful standard in this case. The application of this standard is consistent with decades of Ohio Supreme Court and Commission precedent. This standard must be applied in order to ensure that the rates customers pay are associated with services rendered by the utility. Staff applied the used and useful standard and determined that Duke is entitled to $6,367,724 in remediation costs. Staff's recommendation is consistent with the evidence in the record and Ohio law. It should be adopted by the Commission.

Respectfully submitted,

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PROOF OF SERVICE

I hereby certify that a true copy of the foregoing **Initial Post-Hearing Brief** submitted on behalf of the Staff of the Public Utilities Commission of Ohio, was served by email upon the following Parties of Record, this 6th day of June, 2013.

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FILE

BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company and The Toledo Edison Company for Authority to Increase Rates for Distribution Service, Modify Certain Accounting Practices and for Tariff Approvals.	:	Case No. 07-551-EL-AIR
	:	Case No. 07-552-EL-ATA
	:	Case No. 07-553-EL-AAM
	:	Case No. 07-554-EL-UNC

POST-HEARING BRIEF
SUBMITTED ON BEHALF OF THE STAFF OF
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March 28, 2008

ATTACHMENT A

the expense is spread and the resulting rates accurately reflect the FE companies' cost. This is the treatment for any such short-term tax timing issue in this and any other case and the Staff approach should be adopted.

29. FE Objection I.26 – Retired Plant

The FE companies believe that ratepayers should pay the cost associated with security and other maintenance of retired plant sites.[66] The law is otherwise.

For an expense to be recoverable it must reflect "...the cost to the utility of rendering the public utility service for the test period."[67] These expenses simply do not reflect the cost of rendering any public utility service.[68] No electricity was produced at any of these facilities during the test year or indeed in any previous year for longer than the witness could remember. These plants are retired. While maintaining them in a secure fashion might be of benefit to the neighbors of the old plants, that benefit is not a public utility service. Since these expenditures fail the test, they are not recoverable.[69]

30. FE Objection I.27 – PUCO and OCC Assessments

Although the FE companies' objection is incorrect, it does go to an error in the Staff Reports for Ohio Edison and Toledo Edison. The correct treatment for the PUCO and OCC assessments is two-fold. First the test-year values must be eliminated from

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66 Supplemental Testimony of Trevor J. Fernandez at 7-8.

67 Ohio Rev. Code Ann. § 4909.15(A)(4) (West 2008).

68 Tr. III at 86-91.

69 *Consumers' Counsel v. Pub. Util. Comm'n*, 67 Ohio St. 2d (1981).

FILE

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BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company and The Toledo Edison Company for Authority to Increase Rates for Distribution Service, Modify Certain Accounting Practices and for Tariff Approvals.	:	Case No. 07-551-EL-AIR
	:	Case No. 07-552-EL-ATA
	:	Case No. 07-553-EL-AAM
	:	Case No. 07-554-EL-UNC

REPLY BRIEF

SUBMITTED ON BEHALF OF THE STAFF OF
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the use of end of year values for the deferrals. This is nonsense. Such a reading would be illegal. Parties cannot agree among themselves to give, and the Commission cannot take, powers other than those granted by the General Assembly. The law requires that rate base items be valued at date certain. That is all there is to it.

vi. Annualized Employee Count

The dispute over the employee count is unfortunate. It should not exist. Both the company and the Staff would prefer to use the actual year end number. This is known, having happened already, but it is not available in this record. In the absence of this information, two alternatives present themselves. The Staff uses the known values which exist in the record. The company uses estimates as to what the end of year number was projected to be at the time the case was filed. The company number is a guess, albeit an informed one. The Staff number is real and verifiable, known and measurable in the Staff's parlance. The Staff's view is preferable. Rates should be based on real numbers.

vii. Steam Plant Expenses

The company discussion of this topic is marked by the absence of any reference to the controlling law indeed it only talks about rate base which does not matter. To be recoverable, an expense must reflect "the cost to the utility of rendering the public utility service for the test period. . . ."[3] The ancient, closed plants rendered no public utility service during the test year. Indeed they have not run for decades. Even if they operated,

[3] Ohio Rev. Code Ann. § 4909.15(A)(4) (West 2008).

they would produce electricity which is not regulated currently[4] and is not related to this distribution case. These plants produce only losses. This has nothing whatever to do with rendering the public utility service during the test year. There is no basis under law to allow recovery of these costs.

viii. Depreciation of Meters

The company argues that its depreciation rates for meters should be adjusted because some or all of the meters might be replaced with some unspecified alternatives with unknown life expectancies and costs at some point. This is quite obviously premature. Depreciation rates are set based on the characteristics of the assets being depreciated. Without any details, there is no basis on which to adjust the depreciation rates. A plan is needed with sufficient details so that informed adjustments can be made to these depreciation rates.

The company understands the need to have a plan before moving ahead. Indeed it criticizes the OCC DSM proposal on just this very basis. Why, in the company's view, it is unacceptable to have DSM without a plan but it is acceptable to adjust this depreciation without a plan, is not clear to the Staff. The better course is to make adjustments based on knowledge. Until there is a plan, there is nothing on which an adjustment could be done.

[4] The pun seems unavoidable.

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BEFORE THE

PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Authority to Increase Rates for Distribution Service, Modify Certain Accounting Practices and for Tariff Approvals	))))))	**Case No. 07-551-EL-AIR** **Case No. 07-552-EL-ATA** **Case No. 07-553-EL-AAM** **Case No. 07-554-EL-UNC**

INITIAL BRIEF OF OHIO EDISON COMPANY, THE CLEVELAND ELECTRIC ILLUMINATING COMPANY, AND THE TOLEDO EDISON COMPANY

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ATTACHMENT C

the record often will, as here, reflect only cursory, conclusory, and opposing opinions regarding allowability.[16] We submit Mr. Burgess' position reflects the better view and should be accepted.

7. Uncollectible expense

Staff determines its allowance for uncollectible expense by multiplying distribution revenues by an uncollectibles ratio (*i.e.*, uncollectible expense as the numerator, revenue as the denominator). In its calculation of that ratio, however, Staff uses total company parameters (which reflects not only the retail business subject to the jurisdiction of this Commission but sales for resale which is not) which distort the computation and understate the proper allowance. Conceptually this is wrong because it brings non-jurisdictional data into the calculation of an expense for Ohio ratemaking – an exercise which is intended to be representative of Ohio jurisdictional transactions. (Co. Exh. 1-C, p. 14) Moreover, the practical effect here is that under the Staff's methodology the ratio's denominator – revenues – obviously increases with the inclusion of the sales for resale revenue. The numerator, however, is unchanged since during the test year the Companies did not incur (*i.e.*, did not budget) this expense on this type of revenue (which represents predominantly inter-company (FirstEnergy affiliate) transactions where there is no uncollectible component). (*Id.*) Staff's adjustment inappropriately and unfairly skews the calculation downward and should be rejected.

8. Steam Plant Expenses

The facts giving rise to this issue (Co. Objection II.26) are not in dispute. Ohio Edison owns several facilities which for many years provided service to customers but which are now retired. (Co. Exh. 9-B, p. 7) Although no longer giving rise to any operational related expense,[17]

[16] Companies' witness Burgess views the material as informational, Ms. Smith considers it promotional.

[17] Nor is any return of or return on the facilities sought in this case.

the existence of the facilities does give rise to certain expenses associated with securing them including security guards as well as security fence repair, replacement of security lights and maintenance of aircraft warning lights on the stacks. (Co. Exh. 9-A, pp. 2-3) No suggestion is made that these expenditures are not ordinary and necessary or that they are unreasonable in amount.[18]

Staff removes the expenses based on two theories – both are wrong. The first is that the expenses involved are generation related and therefore not properly a part of a distribution case. The short answer to this is that the underlying assets essentially ceased to provide generation at the point they were retired and are not currently deregulated assets. They are, rather, simply assets of the distribution company which at one time provided utility service and which now, in the course of their ordinary life cycle, continue to have certain expenses associated with them. Were the company not to incur these expenses, there arises the possibility for other, even larger expenses (*e.g.*, potential liability for personal injury to entrants on the property) to arise for the Company, and, derivatively, its customers. (Co. Exh. 9-B, p. 7)

The second Staff objection to recognition of the expense is that the facilities are no longer in use and provide no service to customers. This, however, is essentially an argument that the facilities are not "used and useful", a concept applicable to whether the facilities should be included in rate base as plant in service. No claim for rate base inclusion is made here. This is solely an issue of expense and, on the facts here, the expenses should be allowed.

[18] It is important as well to recognize that these expenses were not included in prior amounts for salvage values included in the calculation of Commission-approved depreciation expense for these assets. Thus customers have not previously paid through rates for the upkeep of these facilities upon retirement. (Co. Exh. 9-B, p. 8)

[Company Exhibit 9-B]

BEFORE THE

PUBLIC UTILITIES COMMISSION OF OHIO

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SUPPLEMENTAL TESTIMONY OF

TREVOR J. FERNANDEZ

ON BEHALF OF

OHIO EDISON COMPANY
THE CLEVELAND ELECTRIC ILLUMINATING COMPANY
THE TOLEDO EDISON COMPANY

___ Management policies, practices, and organization

_X_ Operating income

_X_ Rate base

_X_ Allocations

___ Rate of return

___ Rates and tariffs

___ Other –Case Overview,
Revenue Requirements
Gross Rev. Conversion Factor

ATTACHMENT D

I. Background

Q. PLEASE STATE YOUR NAME FOR THE RECORD.

A. My name is Trevor J. Fernandez.

Q. ARE YOU THE SAME TREVOR J. FERNANDEZ THAT PROVIDED INITIAL AND UPDATE TESTIMONY THAT WAS FILED IN THIS PROCEEDING ON JUNE 7, 2007 AND AUGUST 6, 2007, RESPECTIVELY?

A. Yes, I am.

Q. WHAT IS THE PURPOSE OF YOUR SUPPLEMENTAL TESTIMONY?

A. The purpose of my Supplemental Testimony is to address certain Objections to the Staff Reports of Ohio Edison Company, The Cleveland Electric Illuminating Company ("CEI") and The Toledo Edison Company (collectively, "Operating Companies").

Q. PLEASE IDENTIFY THE OPERATING COMPANIES' OBJECTIONS THAT YOU WILL BE ADDRESSING.

A. I will be addressing Objection Nos. (a)(1), and (c)(1) and (c)(2) in Section I of the Operating Companies' Objections to the Staff Reports of Investigation that were filed on January 3, 2008, as well as Objection Nos. 22, 23 and 26 in Section II of the same filing.

Q. DOES YOUR TESTIMONY REGARDING THESE OBJECTIONS APPLY TO ALL THREE OPERATING COMPANIES?

A. Unless otherwise stated, yes, it does.

II. Transmission Land and Land Rights

Q. WHAT IS THE BASIS FOR OBJECTION (a)(1) IN SECTION I OF THE OPERATING COMPANIES' OBJECTIONS TO THE STAFF REPORTS?

A. This objection deals with the exclusion of certain property from FERC Account No. 350. On Schedule B-2.2, Staff removed the plant in service for FERC Account No. 350, Transmission Land and Land Rights. However, the Staff failed to recognize that a portion of the FERC Account No. 350 balance is property associated with the sub-transmission function. For purposes of this proceeding, sub-transmission property has consistently been considered distribution-related property because it is owned by the Operating Companies and used to distribute electricity to customers that take service below 69,000 volts. Therefore, the Staff should not have removed the sub-transmission property included in FERC Account No. 350.

Q. WHICH AMOUNTS RELATED TO SUB-TRANSMISSION PROPERTY SHOULD STAFF NOT HAVE REMOVED FROM FERC ACCOUNT NO. 350?

A. Attached Exhibit TJF-1 indicates the property balances for each of the Operating Companies that were improperly removed from rate base, along with the jurisdictional allocation factors that should apply to Staff's adjustment of FERC Account No. 350 included on Schedules B-2.2a. According to the Operating Companies' respective property records, virtually all of the investment comprising these balances pertains to either substations or wires supporting voltages below 69 Kv. The remaining costs are also related to similar voltage equipment.

Q. IS THE SUB-TRANSMISSION PROPERTY ACCOUNTED FOR IN THE OPERATING COMPANIES' CHARGES FOR TRANSMISSION AND ANCILLARY SERVICES?

A. No. The charges that customers pay for Network Integrated Transmission Service (NITS) is, in part, based on the level of expenses incurred by the Operating Companies' transmission service provider, American Transmission Systems, Inc. (ATSI). The sub-transmission property in FERC Account No. 350 is not an asset accounted for in the ground lease charge that the Operating Companies bill to ATSI, nor is it an expense associated with NITS. Therefore, it is not a charge included in the Operating Companies' transmission and ancillary service riders.

Q. SHOULD A RETURN ON THE SUB-TRANSMISSION PROPERTY BE INCLUDED IN SUCH TRANSMISSION AND ANCILLARY SERVICE RATES?

A. No. This property is used to support sub-transmission level operations, not operations related to NITS. Therefore, this property should earn a return in distribution rates.

Q. YOUR EXHIBIT TJF-1 EXCLUDES RESERVE BALANCES. WERE THESE RESERVE BALANCES ALSO REMOVED FROM FERC ACCOUNT NO. 350?

A. Yes, they were. On Schedule B-3.1a, Staff removed the reserve for amortization in FERC Account No. 350, Transmission Land and Land Rights.

Q. WHY DIDN'T THE OPERATING COMPANIES OBJECT TO THE REMOVAL OF THE RESERVES RELATED TO FERC ACCOUNT NO. 350?

A. Upon closer review of the reserve included in FERC Account No. 350, it was determined that the balance associated with this reserve actually represents salvage and removal costs pertaining to land that has been sold. The Company erroneously failed to remove this reserve from rate base during its filing. The Staff's adjustment to remove the reserve, while probably made for different reasons, achieves the desired result of eliminating this reserve from rate base and, therefore, the Operating Companies do not object to the Staff's adjustment set forth on Schedule B-3.1a.

III. Customer Deposits and Related Interest

Q. WHAT IS THE BASIS FOR OBJECTION NOS. (c)(1) AND (c)(2) IN SECTION I OF THE OPERATING COMPANIES' OBJECTIONS TO THE STAFF REPORTS?

A. These objections involve customer deposits and the interest expense thereon. When calculating the uncollectible expense adjustment, the Staff properly recognized that a portion of the revenues to which the uncollectible expense applies is generation-related and jurisdictionally allocated the uncollectible expense accordingly. When determining customer deposit balances on Schedule B-6, however, as well as the interest thereon as calculated on Schedule C-3.16, the Staff failed to make a similar jurisdictional allocation, improperly including all customer deposits and related interest as distribution-related. If customer deposits and related interest are to be

treated consistent with Staff's treatment of uncollectible expense, then, provided that certain clarifications discussed later in my testimony are made, the jurisdictional allocation factors included on attached Exhibit TJF-2 should be applied to the respective customer deposits balances included on each of the Operating Companies' Schedules B-6 and the associated interest expense adjustment on Schedules C-3.16, all of which are consistent with those used to jurisdictionally allocate uncollectible expense.

Q. WHY SHOULD CUSTOMER DEPOSITS AND THE INTEREST EXPENSE THEREON BE TREATED THE SAME AS UNCOLLECTIBLE EXPENSE?

A. Just as the provision for uncollectible expense is determined based on components of a customer's entire bill, including generation, transmission and distribution, so too is the customer deposit balance based on these same billing components.

Q. IF THE OPERATING COMPANIES BELIEVE THAT CUSTOMER DEPOSIT BALANCES SHOULD BE JURISDICTIONALLY ALLOCATED, WHY DID THEY APPLY A 100% ALLOCATION FACTOR TO THE CUSTOMER DEPOSITS BALANCE ON SCHEDULE B-6 OF THEIR FILING?

A. The Operating Companies believe that a portion of the customer deposits and related expenses should be recovered in this proceeding with the remaining portion being recovered in the Operating Companies' generation procurement filing. At the time of the Operating Companies' original and update filings, it was unclear as to how generation-related customer deposits and the associated interest expense would be recovered. Therefore, in an abundance of caution, the Operating Companies

included the entire balance of each in this proceeding so as to avoid any "waiver" arguments. This uncertainty continues today and, pursuant to Objection Nos. 22 and 23 in Section II of the Operating Companies' Objections to the Staff Reports, the Operating Companies ask the Commission to confirm that the Operating Companies will have the opportunity to recover generation-related customer deposits and associated interest expense in their generation procurement case, or some other appropriate proceeding.

Q. GIVEN THE STAFF'S TREATMENT OF UNCOLLECTIBLE EXPENSE, WOULD YOU RECOMMEND THAT A PORTION OF THE CUSTOMER DEPOSITS BALANCE AND ASSOCIATED INTEREST EXPENSE BE ALLOCATED BASED ON THE JURISDICTIONAL ALLOCATION FACTORS INCLUDED ON EXHIBIT TJF-2?

A. Provided that the Commission grants to the Operating Companies specific permission to include the customer deposits balance and the related interest expense in either the generation procurement case or some other appropriate proceeding and either (i) authorizes appropriate rate recovery mechanisms for the same that become effective concurrent with the date on which distribution rates take effect or (ii) authorizes recovery of costs arising from any lag between the dates on which distribution and generation rates become effective, then yes, I would recommend making the adjustments set forth on Exhibit TJF-2.

IV. Ohio Edison Retired Steam Plants

Q. PLEASE EXPLAIN THE BASIS FOR OBJECTION NO. 26 IN SECTION II OF THE OPERATING COMPANIES' OBJECTIONS TO THE STAFF REPORTS.

A. This objection involves the Staff's exclusion of certain costs associated with steam generating units at the Gorge, Toronto, Rockaway, Edgewater and Mad River power plants, all of which are owned by Ohio Edison Company and are retired. As explained in my Update Testimony (Co. Exh. 9-A), costs associated with the maintenance and security of these retired units are charged to FERC Account No. 514. A 100% jurisdictional allocation factor was applied to Account No. 514 in both the original and update filings. On Schedule C-3.3, Staff removed these vital expenditures, amounting to $375,080. These expenses, despite their inclusion in a FERC designated "Production" account in accordance with regulatory accounting guidelines, are not incurred to support a production-related function. As retired generating units, they no longer produce electricity. But their existence can cause safety issues if not properly maintained and secured. The costs incurred for maintenance and security at these facilities provide for the safety of the surrounding communities, help to prevent any potential terrorist activity and benefit all of Ohio Edison's customers by minimizing opportunities for death or injury that may result in legal liability -- and increased costs -- to the Operating Companies. Additionally, customers received benefits throughout the many years that these generating units were producing electricity. The cost obligations that exist today are a direct result of those benefits received by the customers while these plants were in service.

Q. WERE ALL OF THESE GENERATING UNITS RETIRED PRIOR TO THE TEST YEAR?

A. Yes, they were.

Q. WERE ANY OF THESE RETIRED GENERATING UNITS PRODUCING ELECTRICITY ON OR AFTER JANUARY 1, 2001?

A. Only Unit 4 at the Edgewater Plant was producing electricity after January 1, 2001. It stopped producing electricity on September 30, 2002.

Q. WERE THE CURRENT EXPENSES EVER ACCOUNTED FOR THROUGH THE COST OF RETIREMENT FACTORS USED TO CALCULATE THE DEPRECIATION ACCRUAL RATES ASSOCIATED WITH THE GENERATING UNITS IN QUESTION?

A. No. These expenses are incurred in the current period and were never recognized in prior Commission approved depreciation accrual rates. Accordingly, these expenses must now be recovered in rates as they are incurred.

Q. DOES THIS CONCLUDE YOUR SUPPLEMENTAL TESTIMONY?

A. Yes, it does.

Summary: Brief Initial Post Hearing Brief electronically filed by Mrs. Tonnetta Y Scott on behalf of PUCO