BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of The Dayton Power and Light Company for Authority to Recover Certain Storm-Related Service Restoration Costs	: : :	Case No. 12-3062-EL-RDR
In the Matter of the Application of The Dayton Power and Light Company for Approval of Certain Accounting Authority	: :	Case No. 12-3266-EL-AAM

**THE DAYTON POWER AND LIGHT COMPANY'S
REPLY COMMENTS**

Of counsel:

Charles J. Faruki (0010417)
FARUKI IRELAND & COX P.L.L.
500 Courthouse Plaza, S.W.
10 North Ludlow Street
Dayton, OH 45402
Telephone: (937) 227-3705
Telecopier: (937) 227-3717
Email: cfaruki@ficlaw.com

Judi L. Sobecki (0067186)
THE DAYTON POWER AND
LIGHT COMPANY
1065 Woodman Drive
Dayton, OH 45432
Telephone: (937) 259-7171
Telecopier: (937) 259-7178
Email: judi.sobecki@dplinc.com

Jeffrey S. Sharkey (0067892)
(Counsel of Record)
FARUKI IRELAND & COX P.L.L.
500 Courthouse Plaza, S.W.
10 North Ludlow Street
Dayton, OH 45402
Telephone: (937) 227-3747
Telecopier: (937) 227-3717
Email: jsharkey@ficlaw.com

Attorneys for The Dayton Power
and Light Company

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THE DAYTON POWER AND LIGHT COMPANY'S
<u>REPLY COMMENTS</u>

I. <u>INTRODUCTION AND SUMMARY</u>

The Commission has approved a series of Stipulations in DP&L rate plan proceedings. Those Stipulations froze DP&L's distribution rates through 2012 but authorized DP&L to recover certain expenses, including "storm damage expenses" outside of a distribution rate process. DP&L fulfilled its end of the bargain in those Stipulations, and in this proceeding seeks to recover certain storm damage expenses pursuant to those Stipulations.

As demonstrated in DP&L's pre-filed testimony, DP&L experienced the three worst storms in its history in 2008, 2011, and 2012, and DP&L incurred extraordinary expenses in response to those storms. DP&L is thus entitled to recover those expenses and the expenses of other 2008 and 2011 storms pursuant to the Stipulations that the Commission approved.

Staff nevertheless argues that DP&L should not be permitted to recover its 2008 expenses; and Staff and OCC both argue that DP&L should not be permitted to recover its 2011 expenses. As demonstrated below, the arguments by Staff and OCC are not only inconsistent with the Stipulations that the Commission approved, but also ignore various fundamental principles of utility rate-making.

Staff, OCC, and Kroger also argue that DP&L's recovery should be reduced by its prior three-year average of storm costs. If the Commission decides to reduce DP&L's recovery by a three-year average, then it should perform two calculations to make sure that the results are representative of reality and are consistent with DP&L's reliance on the Stipulations. <u>First</u>, it should exclude from the three-year average years in which DP&L experienced extraordinary storms. If extraordinary storms were included in the average, then DP&L would not be able to recover fully the expenses that it incurred in response to extraordinary storms. Second, to ensure that there is an apples-to-apples comparison, the Commission should subtract the three-year average from the total expenses that DP&L incurred in the years of the major storms. Subtracting the three-year average from the expenses that DP&L incurred in response to a particular storm would be an apples-to-oranges comparison that would prevent DP&L from fully recovering its extraordinary storm expenses.

Staff and OCC also argue that DP&L should not be permitted to recover capital expenditures because DP&L did not previously seek to defer those capital expenditures. That argument ignores the fact that the effect of a deferral is to convert expenses into capital; DP&L did not seek to defer (i.e., to capitalize) its capital expenditures because those expenditures were already capital. The Commission has authorized every other Ohio utility to recover distribution capital investment through a rider outside of a distribution rate case, and should do the same for DP&L.

The Commission should establish a Storm Recovery Rider to allow DP&L to recover its O&M expenses, return on rate base, depreciation expense, and taxes associated with major storms. The baseline amount for the rider should be calculated in a manner that excludes the years in which DP&L experienced extraordinary storms (2005, 2008, 2011 and 2012); those years should be excluded because including them would inflate the average storm expense to an amount greater than the amount DP&L recovers in distribution rates for major storms.

II. BACKGROUND FACTS

In 2008, 2011 and 2012, DP&L experienced three of the largest storms that it has experienced in its history. 2008 Hurricane Ike, the 2011 ice storm and the 2012 Derecho were the three largest storms that DP&L has experienced in terms of numbers of customers impacted; and three of the four largest in terms of costs. Nickel Test., p. 4. Specifically:

2008 Hurricane Ike: Hurricane Ike hit DP&L's service territory on September 14, 2008. Id. at 2. The storm included sustained winds in excess of 80 mph for over 10 hours; over 300,000 customers were without power. Id. at 2-3. DP&L customers also experienced 13 other storms in 2008. Id. at 3. DP&L incurred $13.6 million in O&M expenses in response to Hurricane Ike, and another $3.6 million in O&M expenses in response to the 13 other storms. Schedule C-1.

2011 Ice Storm: On February 1, 2011, a major ice storm hit DP&L's service territory, and over 156,000 customers lost power. Nickel Test., p. 3. DP&L customers experienced four other major storms in 2011 that caused between 21,332 and 93,979 customers to lose power. Id. DP&L incurred $10.0 million in O&M expenses in response to the 2011 major storms. Schedule C-1.

2012 Derecho: On June 28, 2012, a Derecho struck DP&L's service territory; the Derecho had sustained winds of 58 mph, gusting to 82 mph; over 185,000 customers lost power. Nickel Test., p. 3. An additional storm hit DP&L's service territory on July 1, 2012, affecting 40,000 additional customers. Id. at 4. DP&L incurred $4.8 million in O&M expenses in response to the 2012 Derecho. Schedule C-1.

III. THE COMMISSION SHOULD AUTHORIZE DP&L TO RECOVER ITS O&M EXPENDITURES FROM THE 2008, 2011 AND 2012 STORMS

Staff and OCC make various arguments that DP&L should not be permitted to recover its O&M expenses associated with the unusually large storms in 2008, 2011 and 2012 and the other storms in 2008 and 2011. DP&L responds to those arguments in this section; DP&L addresses arguments regarding the amounts to be recovered in the next section.

Before responding to their specific comments, it is important to highlight important points that are not in dispute. Staff and OCC do not dispute that the storms in 2008, 2011 and 2012 were extraordinary; nor do they dispute that DP&L needed to incur extraordinary expenses to respond to those storms. While Staff has asked for more time to address DP&L's specific requests, at this stage, neither Staff nor OCC claim that the expenses that DP&L seeks to recover were imprudent,[1] or that they were incurred for matters other than storms from those three years.

A. 2008 Hurricane Ike

Staff asserts (pp. 4-6) that the Commission should deny DP&L's request to recover O&M expenditures associated with 2008 Hurricane Ike because DP&L's historic O&M expenditures have been too low and DP&L's historic earnings have been too high. Specifically, Staff asserts (pp. 4-6) that DP&L was authorized to recover approximately $39.6 million per year

[1] OCC states in the Introduction section of its comments (p. 2) that DP&L "failed to prove that the storm costs were prudently incurred and reasonable." However, OCC does not further address prudence in its comments; at no point does it explain its claim that DP&L's costs were not prudently incurred. DP&L presented evidence that its costs were prudently incurred. Nickel Test., pp. 10-11. The Commission should thus disregard OCC's reference to prudence.

in distribution O&M expenses in DP&L's 1999 ETP case,[2] and that DP&L has spent a total of $149.4 million less than the authorized total amount since that case. Staff also asserts (pp. 4-6) that DP&L's allowed rate of return from its 1991 rate case was 12.06%-13.19%, and that DP&L has earned a return of 19.65% since 1999. From those points, Staff argues (pp. 4-6) that DP&L should not be permitted to recover its O&M expenses associated with 2008 Hurricane Ike.

As demonstrated below, the Commission should reject Staff's argument for six separate and independent reasons. The first five reasons demonstrate that the Commission should not consider DP&L's historic expenditures and earnings at all. Those reasons are: (1) the Commission approved a Stipulation that authorized DP&L to recover storm expenses; (2) the Staff's proposal would disrupt the balancing of risks and interests created by a rate order; (3) the Staff's proposal would effectively implement a significantly excessive earnings test, without statutory authorization; (4) the Staff's proposal would create an unfair surprise to investors; and (5) the Staff's proposal would alter utilities' incentives to respond to extraordinary storms.

The sixth reason is that if the Commission elects to consider DP&L's historic O&M expenditures, then the Commission should also consider the fact that DP&L has made substantial new investments in its distribution system since 1991. The net effects of DP&L's increased distribution investment on DP&L's revenue requirement significantly exceed the effect of the decreased O&M expenditures.

OCC similarly argues (pp. 15-17) that DP&L's ROE for 2011 was higher than its Commission-approved ROE, and DP&L thus cannot establish a "financial need" to recover 2011

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[2] Staff states (p. 4) that DP&L's 1999 ETP case (Case No. 99-1687-EL-ETP) was DP&L's "last distribution rate case," but that is not accurate. DP&L's last distribution rate case was in 1991 (Case No. 91-414-EL-AIR). DP&L's rates were unbundled into distribution, transmission and generation components in the 1999 ETP case.

storm expenses. As demonstrated below, the Commission should reject that argument for the same reasons that it should reject the Staff's argument.

1. DP&L Is Authorized to Recover Its 2008 Hurricane Ike Storm Expenses Pursuant to a Stipulation That the Commission Approved

As an initial matter, the Commission should reject Staff's argument because Staff signed and the Commission approved a Stipulation that authorized DP&L to recover storm damage expenses in 2008. Specifically, the Stipulation in DP&L's 1999 ETP case created a distribution rate freeze for DP&L through December 31, 2006; that Stipulation contained an exception to the rate freeze that authorized DP&L to seek an increase in distribution rates after December 31, 2003 for "relief from storm damage expenses." June 1, 2000 Stipulation and Recommendation, § IV (Case No. 99-1687-EL-ETP) ("ETP Stipulation").

That distribution rate freeze and the storm damage expense exception were extended through December 31, 2012 by subsequent Stipulations. May 28, 2003 Stipulation and Recommendation, § IX.C. (Case No. 02-2779-EL-ATA) ("MDP Stipulation") (extending DP&L's Market Development Period and creating Rate Stabilization Period through December 31, 2008); November 3, 2005 Stipulation and Recommendation, § I.E. (Case No. 05-276-EL-AIR) ("RSP Stipulation"); and February 24, 2009 Stipulation and Recommendation, ¶ 1 (Case No. 08-1094) ("ESP Stipulation"). DP&L is entitled to recover its storm-related expenses pursuant to the May 28, 2003 Stipulation that Staff signed and the Commission approved.

Significantly, part of the quid-pro-quo associated with DP&L's agreement to freeze distribution rates was that DP&L would be entitled to recover its storm damage expenses. The distribution rate freeze provided an important protection to customers, but that rate freeze included an important benefit to DP&L -- DP&L could recover its storm expenses. Further, the various Stipulations included a wide range of other important customer benefits, including:

1. DP&L agreed to provide below-market generation to customers. MDP Stipulation, § IX.A.; RSP Stipulation, § I.A; ESP Stipulation, ¶ 1.

2. DP&L agreed to provide a 5% residential generation rate discount on the generation component, including RTC and CTC (i.e., "Big G"). ETP Stipulation, § III. DP&L subsequently agreed to extend that discount through its RSP, and to provide an additional 2.5% reduction on the unbundled generation component (i.e., "little g"). MDP Stipulation, § IX.A.

3. DP&L agreed to an operational support pro forma supplier tariff. ETP Stipulation, § V.

4. DP&L agreed to limit its recovery of transition costs. ETP Stipulation, § VII.

5. DP&L agreed not to alter its line-extension policies. ETP Stipulation, § VI; MDP Stipulation, § VII.

6. DP&L agreed to implement a Voluntary Enrollment Procedure. ETP Stipulation, § XVII; MDP Stipulation, § VI; RSP Stipulation, § I.F.

7. DP&L agreed to extend its MDP to five years. MDP Stipulation, § II.

The various Stipulations thus provided significant customer benefits.

Prior to agreeing to these Stipulations, DP&L carefully considered each package as a whole and weighed the costs and benefits of each package. It is reasonable to expect that the other Signatory Parties, including Staff and OCC, did the same. The Commission should not now deny DP&L a benefit of its bargain, and should allow DP&L to recover its O&M expenses associated with the 2008 storms.

2. The Commission Should Maintain the Balance That a Rate Order Maintains

The Staff's recommendation also ignores the fundamental balancing of risks that a decision in a rate case establishes. Specifically, as the Commission knows, utility rates are set prospectively. Once a rate is set, the utility bears the risk that its actual revenue will fall below its approved revenue requirement; and customers bear a corresponding risk that the utility's actual revenue will be higher than its approved revenue requirement. It is well-settled that retroactive rate-making is prohibited.[3] The utility and its customers thus both face corresponding risks that a utility's actual recovery will not match its approved revenue requirement.

As the Commission also knows, the Commission has long had a practice of normalizing extraordinary expense items in a rate case; as a result of that practice, a utility will be denied recovery of extraordinary expenses that occur during a test year.[4] However, a utility will inevitably incur extraordinary expenses from time to time. The Commission has historically allowed utilities to recover those extraordinary expenses when they do occur.[5] The Commission's practice of normalizing expenses in a test year, but allowing the recovery of extraordinary expenses, creates a reasonable balance between the interests of customers (by excluding extraordinary expenses from the test year) and the utility (by allowing recovery when extraordinary expenses do occur).

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[3] Keco Indus., Inc. v. Cincinnati & Suburban Bell Tel. Co., 166 Ohio St. 254141 N.E.2d 465, paragraph two of the syllabus, cert. denied, 355 U.S. 182, 78 S. Ct. 267, 2 L. Ed. 2d 187 (1957); In re Columbus S. Power Co., 128 Ohio St. 3d 512, 2011-Ohio-1788, 947 N.E.2d 655, ¶ 9-11.

[4] In re the Application of The Ohio Edison Co. to Increase Certain of Its Filed Schedules, No. 82-1025-EL-AIR, 1983 Ohio PUC LEXIS 40, at *89 (PUCO Sept. 14, 1983) ("Test year operating income should be reflective of the results of normal operations for the company. The impact of unusual or nonrecurring events should be excluded from the determination of expenses if they are not reflective of what the company is reasonably expected to experience.").

[5] E.g., July 12, 2006 Finding and Order, p. 5 (Case No. 05-1090-EL-ATA).

The Staff's argument -- that DP&L be denied recovery of extraordinary expenses because DP&L's historic earnings were high -- ignores the balancing of risks and interests that is created by the rule against retroactive rate-making and the practice of normalizing expenses. Staff's proposal would shift additional risks to the utility, without shifting any corresponding benefits to the utility. The Commission should maintain the existing balance of risks and interests, and should thus reject the Staff's proposal.

3. The General Assembly Has Addressed How Excessive Utility Earnings Should Be Treated

As the Commission knows, in 2008, the General Assembly passed S.B. 221, which required electric utilities to operate under SSOs beginning January 1, 2009. Ohio Rev. Code § 4928.141(A). Among other items, S.B. 221 included a significantly excessive earnings test ("SEET") for utilities operating under ESPs. Ohio Rev. Code § 4928.143(F). Prior to S.B. 221, there was no provision in the revised code authorizing any type of earnings test.

The SEET in S.B. 221 was not applicable to DP&L in 2008, but the Staff's proposal here would effectively apply a SEET to DP&L in 2013 related to 2008. There is nothing in Ohio Substitute Senate Bill 3 (implemented in 1999) that would authorize the Commission to consider whether DP&L had excessive earnings in 2008.

4. The Staff's Proposal Would Be Inconsistent with the Commission's Authorization of a Deferral

As the Commission knows, absent a Commission order granting a deferral, a utility must record storm-related O&M expenses as an expense on its financial statements, which has the effect of decreasing net income. The Uniform System of Accounts, promulgated by the Federal Energy Regulatory Commission ("FERC"), authorizes a utility to record an expense as a regulatory asset if it is "probable that such items will be included in a different period(s) for purposes of developing rates that the utility is authorized to charge for its utility services." FERC Uniform System of Accounting, Account 182.3, ¶ B (emphasis added).

Standards promulgated by the Financial Accounting Standards Board[6] similarly provide that:

> "Rate actions of a regulator can provide reasonable assurance of the existence of an asset. An entity shall capitalize all or part of an incurred cost that would otherwise be charged to expense if both of the following criteria are met:
>
> a. It is probable (as defined in Topic 450) that future revenue in an amount at least equal to the capitalized cost will result from inclusion of that cost in allowable costs for rate-making purposes.
>
> b. Based on available evidence, the future revenue will be provided to permit recovery of the previously incurred cost rather than to provide for expected levels of similar future costs. If the revenue will be provided through an automatic rate-adjustment clause, this criterion requires that the regulator's intent clearly be to permit recovery of the previously incurred cost.
>
> A cost that does not meet these asset recognition criteria at the date the cost is incurred shall be recognized as a regulatory asset when it does meet those criteria at a later date."

Financial Accounting Standards Codification, § 980-340-25-1 (emphasis added).

A utility may therefore defer expenses under governing accounting rules only if subsequent recovery of the expense is "probable." When the Commission authorizes a utility to defer certain amounts, that authorization therefore indicates to the investment community that it is "probable" that the utility will be able to recover those amounts. In the absence of the deferral

[6] The text of the Securities and Exchange Commission order requiring utilities to comply with FASB standards is available at http://www.sec.gov/rules/other/2013/33-9398.pdf.

order here, DP&L's 2008 earnings would have been lower (since the deferred amounts would have been recorded as an expense, and lowered 2008 net income). Further, due to the deferral, the investment community would see a substantial regulatory asset on DP&L's books. Investors purchased DPL Inc. shares and/or AES shares in reliance upon those financial statements.[7]

When a utility seeks to recover amounts that the Commission has authorized to be deferred, there is thus some tension between the expectations of investors (who expect recovery) and the expectations of customers (who expect to be permitted to challenge recovery). The Commission should balance those competing expectations by denying recovery of a deferred amount only in the rarest of circumstances, such as if the denial is required by a well-established principle of utility rate-making.

For example, it has long been the Commission's practice to review deferred amounts for prudence. Investors therefore could not claim unfair surprise if the Commission were to review deferred expenses to determine whether they were prudently incurred.

On the other hand, investors would be unfairly surprised if the Commission made a material change to its historic review practices when the utility seeks to recover the deferred amounts. Once the Commission has authorized a deferral and thus indicated that recovery is "probable," the Commission should not adopt a new test or practice to review the request for recovery (unless the new practice is required by law). Implementing a new test or practice in

[7] DP&L is not suggesting that an order authorizing a deferral is binding in later cases. An order of the Commission granting a deferral is not binding on the Commission in subsequent cases. Elyria Foundry Co. v. Pub. Utils. Comm'n, 114 Ohio St. 3d 305, 2007-Ohio-4164, 871 N.E.2d 1176, ¶ 19-23. The Commission's order granting DP&L permission to defer the 2008 Hurricane Ike expenses stated: "nothing in this Entry shall be binding upon the Commission in any subsequent investigation or proceeding involving the justness or reasonableness of any rate, charge, rule, or regulation." January 14, 2009 Finding and Order, p. 3 (Case No. 08-1332-EL-AAM).

such a situation would be an unfair surprise to investors and harmful to the utility's financial viability.

To be clear, DP&L is not suggesting that the Commission should forever be barred from implementing new practices to review a deferral request. Specifically, if the Commission believes that a new practice should be implemented, then the Commission could grant the deferral but state that the new practice will be included in its review prospectively, when the utility seeks recovery. DP&L's point is simply that once a deferral is granted, the Commission should not adopt a new practice to review the utility's request to recover the deferred amounts because doing so would constitute an unpredictable and unfair surprise to investors.

Here, the Staff's suggestion that the Commission should deny DP&L's request for the recovery of the authorized deferral out right based only upon DP&L's historic O&M expenditures and historic ROE is not a well-established principle of rate-making. Indeed, it is a departure from history. Staff does not cite any case in which the Commission has previously used such a practice. Implementation of such a new practice here would be inconsistent with the Commission's order granting a deferral and would be an unfair surprise to investors.

5. Staff's Proposal Would Create the Wrong Incentives for Future Storms

In response to the 2008 Hurricane Ike, DP&L incurred extraordinary expenses. DP&L paid substantial overtime to its employees and incurred significant costs to bring utility crews from many neighboring states to its service territory so that it could restore service as quickly and safely as possible. DP&L's practices were not unusual – every Ohio utility incurs extraordinary expenses in response to extraordinary storms.

Ohio utilities' willingness to incur those extraordinary expenses in response to extraordinary storms is encouraged by the Commission's authorization of their recovery (when they are prudently incurred). Altering this practice would be bad policy. If the Commission were to alter its rule of permitting the recovery of extraordinary expenses that are incurred in response to extraordinary storms, Ohio utilities would be incentivized to change their practices. Every Ohio utility would have to re-evaluate which expenses were necessary for them to incur when restoring service after an extraordinary storm.

The Commission's long-held practice of normalizing extraordinary expenses in a rate case and allowing for the recovery of extraordinary expenses when they do occur is reasonable and creates the appropriate incentive for utilities to restore service as quickly and safely as possible. The Commission should not alter those incentives.

6. The Staff Ignored DP&L's Increased Distribution Investment

The Commission should not consider DP&L's historic O&M expenditures and historic earnings for each of the preceding five reasons. If the Commission rejects those five arguments and elects to consider DP&L's historic expenses and earnings, then the Commission should consider also the fact that DP&L's historic distribution capital investments have increased significantly. This subsection demonstrates that the revenue requirement effect of DP&L's increased distribution investment greatly exceeds the revenue requirement effect of DP&L's lower O&M expenditures.

Specifically, since 1991, DP&L has made substantial new distribution-related investments to improve its system. As Exhibit A shows, DP&L's distribution-only revenue requirement (based on rate of return on distribution capital, O&M expenses and distribution depreciation) from the 1991 rate case was $93.7 million. As Exhibit A also shows, DP&L's distribution-only revenue requirement for 2008 through 2012 exceeded the revenue requirement amounts from the 1991 rate case by $348.8 million. Thus, although DP&L's O&M expenses have decreased since the 1991 rate case, DP&L's required revenue requirement associated with the returns on its increased investments and increased depreciation expenses have increased by a much larger amount. Staff's proposal turns a blind eye to this fact.

Focusing on 2008 -- the year of Hurricane Ike -- DP&L's distribution O&M expense was approximately 25% less than the O&M expense approved in the 1991 case ($39 million in 1991; $29 million in 2008). Ex. A. However, DP&L's required return on net plant more than doubled ($40.5 million in 1991; $82.8 million in 2008), and DP&L's depreciation expense more than tripled ($13 million in 1991; $42 million in 2008). Ex. A. The net result is that the amount of revenue that DP&L would need to compensate it for its distribution investments and O&M expenses increased from $94 million in 1991 to $155 million in 2008.

If the Commission decides to consider DP&L's historic distribution-related O&M expenses in evaluating DP&L's request to recover Hurricane Ike O&M expenses, then the Commission should also consider all of DP&L's distribution-related expenditures. By so doing, the Commission will see that DP&L's 2008 through 2012 revenue requirement was $348 million <u>higher</u> than the 1991 figure. Thus, the fact that DP&L's O&M expenses have decreased is more than offset by the fact that DP&L's distribution investments and depreciation expense associated with those investments have increased.

B. A DEFERRAL IS NOT NECESSARY TO RECOVER STORM EXPENSES

Staff (pp. 4-5) and OCC (pp. 7-9) assert that DP&L should not be permitted to recover costs associated with other 2008 storms because the Commission denied DP&L's request to defer expenses associated with those storms. Staff (p. 6) and OCC (pp. 13-15) also assert that the Commission should deny DP&L's request to recover storm expenses associated with 2011 storms because DP&L did not seek to defer those amounts in a timely manner. The Commission should reject those arguments because there is no requirement that a utility seek or receive a deferral before it seeks to recover extraordinary expenses.

Specifically, as demonstrated above, the Stipulations that the Commission approved permit DP&L to recover "storm damages expenses." June 1, 2000 Stipulation and Recommendation, § IV (Case No. 99-1687-EL-ETP); May 28, 2003 Stipulation and Recommendation, § IX.C. (Case No. 02-2779-EL-ATA); November 3, 2005 Stipulation and Recommendation, § I.E. (Case No. 05-276-EL-AIR); and February 24, 2009 Stipulation and Recommendation, ¶ 1 (Case No. 08-1094). There is no requirement in those Stipulations that DP&L receive or seek a deferral of the storm damage expenses before DP&L seeks to recover them. Such a requirement could have been written into the Stipulations, but was not.

Further, Ohio Rev. Code § 4909.18 supports DP&L's application in this case. (The "increase in any rate" requirements in that section are inapplicable, since DP&L seeks to implement new rates in this proceeding.) There is nothing in that statutory section that requires a utility to receive or seek a deferral before a new rate can be implemented.

Indeed, neither Staff nor OCC cite to a statutory requirement that a utility receive or seek an order authorizing a deferral before the utility seeks to recover extraordinary expenses.

Their argument is, in fact, inconsistent with the fact that an order granting a deferral is not binding upon the Commission in subsequent cases. Staff and OCC do not explain why DP&L's failure to seek a non-binding order should bar DP&L from seeking to recover expenses that it would otherwise be entitled to recover.

Staff's assertion that the Commission denied DP&L's application to defer 2008 storm expenses other than those associated with Hurricane Ike misconstrues the Commission's Finding & Order in Case No. 08-1332-EL-AAM. The first sentence of paragraph (2) of the order provides that DP&L's application seeks "authority to defer, as a regulatory asset, a portion of its Operation and Maintenance (O&M) expenses associated with restoring electric service to its customers in the aftermath of Hurricane Ike's destructive wind storm." The very next sentence goes on to provide that the amount the Company proposed to defer in the application included Hurricane Ike and other 2008 storms, specifically acknowledging: "[t]he portion of the O&M expenses the Company proposes to defer is the amount by which the total O&M expenses associated with the Hurricane Ike-related service restoration expenses and other storms experienced in 2008 exceeds the three-year average service restoration O&M expenses associated with major storms." (Emphasis added.) Paragraph 4 of the Order approves of the application, which would include the deferral of other storms experienced in 2008. DP&L acknowledges that the provision approving of the application refers specifically to Hurricane Ike and not the other storms. While somewhat ambiguous, a fair reading of the Commission's decision supports the conclusion that the Commission approved of DP&L's application –meaning the application as-filed. This interpretation is also supported by the fact that the Commission did not expressly disallow, or reject the portion of DP&L's application seeking to defer the costs associated with other storms. If the Commission were disallowing a portion of DP&L's

application, it would have done so expressly, but it did not. The Commission's general approval of the application, along with silence as to any disallowance support the conclusion that DP&L's deferral of the other 2008 storms was appropriate.

Finally, as demonstrated below in § IV.A.2., a denial of DP&L's request to recover expenses associated with other 2008 major storms would be inconsistent with the use of a three-year average. If the Commission is going to reduce DP&L's allowed 2008 O&M expenses by its three-year average of major storm expense, then the allowed amount (which serves as the starting point before the three-year average is subtracted) should be DP&L's entire 2008 expenses associated with storm restoration. Subtracting the three-year average only from DP&L's 2008 Hurricane Ike expenses is irrational, would not be an apples-to-apples comparison, and would not result in a full recovery or a logical conclusion.

C. WHETHER THE STORMS WERE "MAJOR EVENT" STORMS AS DEFINED BY COMMISSION RULES IS IRRELEVANT

OCC argues (pp. 3-4) that DP&L's application should be denied outright because DP&L failed to submit evidence as to which storms constitute "major event" storms under the Commission's rules. The Commission should reject that argument because whether a storm is a "major event" storm is irrelevant to whether DP&L may recover the costs of that storm. The Stipulations that the Commission approved authorize DP&L to recover "storm damage expense." There is no requirement in the Stipulation that the particular storms satisfy the definition of major event storms to be recoverable. Again, such a requirement could have been written into the Stipulation, but was not.

In order to be consistent with reliability standards, DP&L proposed in its application to use the Commission's definition of a major storm in making the determination for cost recovery. This determination was a purposeful decision by the Company, not the fulfillment of an obligation. DP&L has already provided the appropriate calculations for its major event storms to both the OCC and Staff through discovery (OCC INT-10 and Staff DR #5). DP&L would ask for leave to supplement the record if the Commission were to find the record insufficient in this regard.

IV. THE AMOUNTS OF O&M EXPENSES TO BE RECOVERED

A. THE THREE-YEAR AVERAGE SHOULD EXCLUDE UNUSUALLY LARGE STORMS AND SHOULD BE CALCULATED ON AN APPLES-TO-APPLES BASIS

1. If Recovery Is to Be Reduced by A Three-Year Average, Then Unusually Large Storms Should Be Excluded

Staff (p. 5), OCC (pp. 10-11) and Kroger (pp. 2-3) assert that DP&L's recovery of storm-related expenses should be reduced by the three-year average of DP&L's major storm expenses. As demonstrated below, if the Commission decides to deduct the three-year average from DP&L's recovery, then the Commission should exclude years with unusual storms from the three-year average.

As an initial matter, as the Commission knows, the issue of storm damage recovery and the calculation of a three-year average was raised in DP&L's recent ESP hearing (relating to a forward-looking storm rider) (Case No. 12-426-EL-SSO). Staff witness Lipthratt sponsored testimony on that subject, and DP&L witness Seger-Lawson filed rebuttal testimony. DP&L thus cites to evidence that was submitted in that case.

In establishing the amount of the three-year average, it is important to understand that there is a difference between a "major event" storm and an unusual storm. The term "major event" storm is defined by Commission rule. Ohio Admin. Code § 4901:1-10-01(Q).

Attachment A to Mr. Lipthratt's testimony in the pending ESP case shows that DP&L has incurred O&M expenses for major event storms every year from 2002-2011. However, as Attachment A to Mr. Lipthratt's testimony demonstrated, DP&L's major event storm O&M expenses for three of those years (2005, 2008, 2011) were much higher than its major event storm O&M expenses for other years[8]:

Year	Major Events O&M
2002	$926,958
2003	$1,386,639
2004	$1,717,105
2005	$6,094,093
2006	$872,528
2007	$1,715,226
2008	$15,950,806
2009	$774,841
2010	$302,919
2011	$10,035,297
Total	$39,776,412
10 Year Avg.	$3,977,641
2009 - 2011 Avg.	$3,704,352

Staff Ex. 6, Att. A.[9]

Mr. Lipthratt conceded that DP&L's O&M expenses for 2005, 2008 and 2011 were "outliers." Tr. 1605. DP&L witness Seger-Lawson explained in her rebuttal testimony in

[8] OCC (p. 6) points out that the major storm amounts listed in Attachment A for 2006 and 2007 differ from the same amounts provided in Schedule C-2 of DP&L's application. This is due to the fact that Attachment A employs the current definition of major event, adopted in 2009, and applies it backward. The amounts used in DP&L's application are based on the major storm definition in place for those years.

[9] Mr. Lipthratt's prefiled testimony refers to a "2009-2001" average of $3,704,352. Staff Ex. 6, Attachment A. He agreed at the ETP hearing that the date range was a typographical error, and that it should be 2009-2011. Tr. 1604. DP&L corrected that typographical error in the chart in the text.

the ESP case that there were extraordinary storms in those years -- a 2005 ice storm, the 2008 Hurricane Ike wind storm, and a 2011 ice storm. DP&L Ex. 12, p. 18.

It is also important to understand that DP&L's last rate case was in 1991 (Case No. 91-414-EL-AIR), and that case was resolved via a "black box" Stipulation. Tr. 1602-03 (Lipthratt). While Staff believes that there was some recovery in DP&L's distribution rates set in that case for major event storms, there is no way to determine from that Stipulation how much DP&L is currently recovering in its distribution rates for major storms. Tr. 1600-02 (Lipthratt). Accord: Tr. 2359 (Seger-Lawson). The Commission should find that DP&L's current distribution rates do not include any recovery associated with unusually large storms, because there is no such evidence.

Specifically, as discussed above, it has long been the Commission's practice to exclude unusually high costs associated with major storms from the test year in rate cases. For example, in determining a utility's test-year expenses, the Commission held: "Test year operating income should be reflective of the results of normal operations for the company. The impact of unusual or nonrecurring events should be excluded from the determination of expenses if they are not reflective of what the company is reasonably expected to experience." In re the Application of The Ohio Edison Co. to Increase Certain of Its Filed Schedules, No. 82-1025-EL-AIR, 1983 Ohio PUC LEXIS 40, at *89 (PUCO Sept. 14, 1983).

The Commission applied that rule to exclude unusual major storm costs from DP&L's test-year expenses in DP&L's 1983 rate case. In re the Application of The Dayton Power &Light Co. for Auth. to Modify & Increase Its Rates, No. 82-517-EL-AIR, 1983 Ohio PUC LEXIS 70, at *69 (PUCO Apr. 27, 1983). In that case, "[t]he Staff proposed to reduce test year operating expenses by $1,224,032 to account for the abnormally high level of storm damage expense included by the company . . . ." Id. The Commission approved that recommendation. Id. at *72. Accord: In re the Application of The Ohio-American Water Co. to Increase Rates, No. 79-1343-WW-AIR, 1981 Ohio PUC LEXIS 3, at *19 (PUCO Jan. 14, 1981) ("The record in this case indicates that the severe storm occurred in 1977 that generated the expense at issue and there have not been recurring storms of such a nature every year. Thus, the Commission can only conclude that this was an unusual and non-recurring expense and should be excluded from the cost of service of the Applicant.").

Indeed, in AEP's recent ESP case, the Commission set AEP's storm recovery rider after excluding from its calculation unusually high storm expenses in prior years. AEP Order, pp. 68-69 ("In the event AEP-Ohio incurs costs due to one or more unexpected, large scale storms, AEP-Ohio shall open a new docket and file a separate application by December 31 each year throughout the term of the modified ESP, if necessary."); Tr. 1612-13 (Lipthratt); DP&L Ex. 12, p. 19 (Seger-Lawson Rebuttal). The Commission should follow the same method that it used in the AEP case, and should exclude years with unusual storms from the three-year average.

Given that DP&L's current rates do not include any recovery for unusually large storms, it is unreasonable to include the 2005, 2008 and 2011 storms in any three-year average that is used to determine the amount that DP&L could recover in this case. As to DP&L's request to recover expenses for 2011 storms, the Commission should exclude 2008, and the three-year average should be based upon 2007, 2009 and 2010; the three-year average for those years is $930,995. As to DP&L's request to recover expenses for 2012 storms, the Commission should exclude 2008 and 2011, and the three-year average should be based upon 2007, 2009 and 2010; the three-year average for those years is $930,995.

2. The Commission Should Apply A Three-Year Average on An Apples-to-Apples Basis

As discussed above, in 2008, DP&L experienced Hurricane Ike and thirteen other storms. Nickel Test., pp. 2-3. OCC asserts (p. 7) that the Commission should not permit DP&L to recover costs associated with 2008 storms other than Hurricane Ike, and also argues (p. 10) that DP&L should deduct a three-year average to calculate the amount of recovery. The Commission should reject that approach because it results in a comparison of DP&L's expenses associated with <u>one particular storm</u> to an average of <u>all</u> of the expenses that DP&L incurred in response to major storms in the <u>three prior years</u>.

When a utility seeks to recover storm expenses associated with an unusually large storm(s), the Commission could reasonably calculate the amount to be recovered in two different ways. <u>First</u>, the Commission could simply allow the utility to recover all of the expenses associated with the particular storm(s). <u>Second</u>, in the alternative, the Commission could subtract the prior three-year average associated with all major storms from all of the major storm expenses that the utility incurred in the year of the unusually large storm(s).

Either of those methods would allow the utility to recover only its extraordinary expenses. However, it is not rational to subtract the prior three-year average associated with all major storms from the expenses that a utility incurred in response to a particular storm. That would be an apples-to-oranges comparison that would result in incomplete recovery, and should be rejected by the Commission.

B. STRAIGHT-TIME LABOR EXPENSES

OCC asserts (pp. 17-19) that DP&L should be denied recovery of its straight-time labor expenses. OCC argues that DP&L's straight-time labor expenses are recovered in DP&L's base rates.

As an initial matter, OCC ignores the fact that hourly employees who are working on the storm during their normally-scheduled hours are not performing their normally-scheduled work. That normally-scheduled work still needs to be done, and it is reasonable to compensate DP&L for the straight-time hours that were dedicated to storm restoration.

Indeed, OCC cites (p. 18) to Duke's recent case relating to its request to recover costs associated with 2008 Hurricane Ike; however, OCC neglects to mention that the Commission rejected the argument that Duke should not be permitted to recover straight-time labor expenses. Specifically, in that case, Staff recommended that Duke should not be permitted to recover $986,244.62 associated with Duke's straight-time labor expenses. January 11, 2011 Opinion and Order, p. 10 (Case No. 09-1946-EL-RDR). However, the Commission did not accept that recommendation; the Commission deducted Duke's recovery for other items (supplemental compensation to salaried employees, affiliate labor and contractor labor), but did not adopt the Staff's recommendation related to straight-time labor. Id. at 17-18.

C. SUPPLEMENTAL PAY TO SALARIED EMPLOYEES

OCC also argues (p. 19) that DP&L should not be permitted to recover overtime labor costs that it provided to salaried employees associated with the storms at issue. OCC argues that the Commission ruled that Duke could not recover certain discretionary payments that Duke made to salaried employees related to 2008 Hurricane Ike, and the Supreme Court of Ohio affirmed that decision as reasonable.

The defect in OCC's argument is that Duke's payments that the Commission disallowed were discretionary, but DP&L had a contractual obligation to pay them. Specifically, in the Duke order, the Commission stated that the payments made by Duke to salaried employees were "totally within the discretion of the company." January 11, 2011 Opinion and Order, p. 13. The Commission therefore concluded that customers should not have to bear the costs. Id.

In contrast, DP&L has a contract with its salaried employees that is titled Management Team Incentive Compensation Plan, and which is signed by the salaried employees and DP&L. That contract states that its purposes include "encourag[ing] Employee participation on a Storm Team." The payments to salaried workers capitalize on the expertise of DP&L employees and reduce the need for DP&L to hire expensive contractors which saves customers money and also results in quicker restoration. That contract specifically requires DP&L to make certain payments to salaried employees for "hours worked on the Storm Team outside of the employee's normally-scheduled work day."

Thus, unlike Duke, the DP&L payments at issue were not discretionary. DP&L was required by contract to pay those amounts, and the events that triggered that obligation were the storms. (OCC does not claim that it was imprudent for DP&L to sign those contracts.) DP&L should thus be entitled to recover those amounts.

V. CAPITAL EXPENDITURES

A. DP&L SHOULD BE PERMITTED TO INCLUDE CAPITAL IN ITS STORM RECOVERY RIDER

The Staff states (p. 6) that "DP&L requests recovery for capital expenses; however, the Commission did not expressly permit authority to defer any capital expenditures." OCC makes a similar argument (p. 12): "[n]othing in the Commission's Finding and Orders . . . authorizes DP&L to defer or recover capital costs related to service restorations due to storms." These comments demonstrate a lack of understanding of utility accounting principles. O&M expenses are deferred for future recovery based on fundamental accounting matching principles. If there is a probability that the utility will be granted authority to recover O&M expenses in a future period, then those expenses are not recognized as an expense in the period that they are incurred, but are instead capitalized (deferred) and expensed (amortized) over the same period and on the same basis as they are recovered through rates. DP&L did not seek to defer capital costs, because capital costs are already capital; there is no need to capitalize them. The fact that DP&L did not request to defer capital costs is not a basis to deny recovery of capital associated with restoring service after a major storm.

Further, although both Staff (p. 6) and OCC (pp. 12-13) argue that distribution capital should be recovered through a distribution rate case, that argument ignores the fact that all Ohio EDUs with the exception of DP&L recover distribution capital costs through stand-alone Distribution Investment Riders, which are not set through distribution rate cases. Simply because one utility calls it a Distribution Investment Rider and another utility calls it a Storm Recovery Rider is not a basis to deny recovery of capital costs. Clearly there is Commission precedent to recover capital costs through a separate rider, outside of a full distribution rate case.

Ohio Power Case No. 12-2627-EL-RDR; First Energy Case No. 12-2680-EL-RDR; and Duke Case No. 12-1811-GE-RDR.

B. TRANSMISSION CAPITAL

OCC asserts (p. 25) that DP&L has sought to recover transmission-related capital through a rider in this case. OCC refers to documents that DP&L produced in discovery, but the documents are voluminous spreadsheets, and OCC does not cite to any particular spreadsheet (much less a particular line), and one cannot determine how OCC calculated the amounts that it cites. DP&L thus cannot respond to OCC's specific claims. DP&L will, nevertheless, make two points in response.

First, DP&L's transmission employees are qualified to work on DP&L's distribution system, and do perform certain work on DP&L's distribution system in response to major storms. It is therefore appropriate to include costs associated with that work in this case.

Second, DP&L's employees charge certain expenditures associated with transmission capital that is replaced in major storms to the charge numbers that DP&L establishes for the various storms at issue. However, DP&L managers subsequently review the amounts charged to those billing codes and remove transmission capital from the amounts that DP&L seeks to recover. DP&L's application seeks only recovery of Distribution related capital and O&M.

VI. RATE DESIGN & FUTURE PROCEEDINGS

Staff (p. 7) and Kroger (pp. 3-5) make various recommendations regarding how long a rider to recover past storm expenses should be in place and how that rider should be designed. DP&L believes that the three-year recovery period that it proposed is reasonable to avoid rate shock to customers, and it does not oppose the rate designs proposed by Staff or Kroger.

OCC (p. 24) suggests that the Commission order DP&L to file an application by December 31st each year to commence a proceeding for the Storm Cost Recovery Rider. DP&L notes that the Commission also established that AEP would file an application by December 31st each year to recover large-scale storm costs and that many extraordinary storms are likely to affect both the DP&L and AEP service territories. If the Commission chooses to establish a similar procedure for DP&L, DP&L suggests that its procedural timing be offset from AEP's to allow the Staff and the OCC a more thorough review of each Company's storm costs.

VII. STORM RECOVERY RIDER BASELINE

Staff recommends (p. 7) that the Commission establish a storm recovery rider for DP&L of $2.6 million. Under Staff's proposal, if DP&L's major storm expenses exceed $2.6 million in a given year, then DP&L could apply to the Commission to recover the excess. However, if DP&L's major storm expenses were lower than $2.6 million in a given year, then DP&L would record the difference as a regulatory liability to offset future expenditures or issue a refund to customers.

Staff explained that it calculated the $2.6 million figure as follows:

> "Staff believes that a portion of base rates recovers major storm repair costs, which have averaged around $4,000,000 over the last ten years. However, one of those years, 2008, had an extremely high level of storm expenses, approximately $16 million, mostly due to Hurricane Ike. Eliminating 2008 from the average reduces the average to $2.6 million."

Staff Comments, p. 7.

DP&L agrees that its 2008 major storm expenses should be excluded from the average. As discussed above, there is no way to determine how much DP&L recovers in its distribution rates for major storms, but Staff states (p. 7) that it believes that DP&L's distribution rates include recovery for major storms. Given the Commission's well-established practice of normalizing expenses, it is reasonable to conclude that DP&L's current distribution rates do not include any recovery associated with extraordinary storms. DP&L thus agrees with the Staff's recommendation that the "extremely high level of storm expenses" for 2008 should be eliminated from the average.

However, Staff left 2005 and 2011 in the average. As discussed above, the 2011 ice storm was the fourth largest storm in terms of cost in DP&L's history. Nickel Test., p. 4. Staff does not explain why it included in its average the fourth most expensive storm or the 2005 Ice Storm which the Commission previously recognized as a severe weather event and granted DP&L authority to defer and recover costs related to the 2005 Ice Storm.

In addition, a review of the chart that Mr. Lipthratt submitted in the ESP case demonstrates that DP&L's major storm expenses for 2005 and 2011 were significantly out-of-line with its historic costs. Indeed, Mr. Lipthratt admitted at the ESP hearing that the 2005 and 2011 amounts were "outliers." Tr. 1605.

The best way for the Commission to determine whether a given year should be included in the average is for the Commission to ask itself this question: if that year was the test year in a distribution rate case, would the Commission normalize the storm expenses? If the answer is yes, then the year should be excluded from the average; if the answer is no, then the year should be included in the average. Given how far out-of-line DP&L's expenses were in

2005 and 2011, certainly the Commission would have normalized its expenses in those years. They should thus be excluded from the average, and the baseline should be established at $1.1 million.

VIII. THE RECORD IN THIS CASE

If the Commission elects not to conduct a hearing in this case, then DP&L asks that it:

(1) Admit into the record in this case DP&L's pre-filed testimony (including associated schedules and workpapers), which DP&L hereby offers into evidence;

(2) To the extent that the Commission believes that any of the comments have merit, permit DP&L to submit additional evidence in response to them; and

(3) Provide to DP&L an opportunity to submit additional evidence in response to any purported insufficiency in DP&L's filing that Staff identifies in its subsequent review of DP&L's records.

IX. CONCLUSION

DP&L incurred substantial costs to respond to major storms in 2008, 2011 and 2012. The Commission approved Stipulations that authorize DP&L to recover the amounts that DP&L incurred to respond to those storms, and the Commission should therefore approve DP&L's application in this case.

Of counsel:

Charles J. Faruki (0010417)
FARUKI IRELAND & COX P.L.L.
500 Courthouse Plaza, S.W.
10 North Ludlow Street
Dayton, OH 45402
Telephone: (937) 227-3705
Telecopier: (937) 227-3717
Email: cfaruki@ficlaw.com

Respectfully submitted,

s/ Judi L. Sobecki
Judi L. Sobecki (0067186)
THE DAYTON POWER AND
LIGHT COMPANY
1065 Woodman Drive
Dayton, OH 45432
Telephone: (937) 259-7171
Telecopier: (937) 259-7178
Email: judi.sobecki@dplinc.com

s/ Jeffrey S. Sharkey
Jeffrey S. Sharkey (0067892)
(Counsel of Record)
FARUKI IRELAND & COX P.L.L.
500 Courthouse Plaza, S.W.
10 North Ludlow Street
Dayton, OH 45402
Telephone: (937) 227-3747
Telecopier: (937) 227-3717
Email: jsharkey@ficlaw.com

Attorneys for The Dayton Power
and Light Company

CERTIFICATE OF SERVICE

I certify that a copy of the foregoing The Dayton Power and Light Company's Reply Comments has been served via electronic mail upon the following counsel of record, this 1st day of July, 2013:

Melissa R. Yost, Esq., (Counsel of Record)
Larry S. Sauer, Esq.
Assistant Consumers' Counsel
Office of The Ohio Consumers' Counsel
10 West Broad Street, Suite 1800
Columbus, OH 43215-3485
yost@occ.state.oh.us
sauer@occ.state.oh.us

Attorneys for Office of the Ohio Consumers' Counsel

Mark S. Yurick, Esq.
(Counsel of Record)
Zachary D. Kravitz, Esq.
TAFT STETTINIUS & HOLLISTER LLP
65 East State Street, Suite 1000
Columbus, OH 43215
myurick@taftlaw.com
zkravitz@taftlaw.com

Attorneys for The Kroger Company

Bryce A. McKenney
Gregory A. Price
Attorney General's Office
Public Utilities Commission of Ohio
180 East Broad Street, 6th Floor
Columbus, OH 43215
Bryce.McKenney@puc.state.oh.us
Greg.Price@puc.state.oh.us

s/ Jeffrey S. Sharkey
Jeffrey S. Sharkey

733434.1

EXHIBIT A

The Dayton Power and Light Company

Comparison of O&M, Capital and Depreciation Expense to Amount Authorized in Rates in 1991

	91-414-EL-AIR [1]	2008	2009	2010	2011	2012
O&M [2]						
Distribution:						
Operation	$ 10,724,000	$ 3,758,805	$ 5,296,561	$ 4,488,740	$ 5,963,518	$ 5,258,572
Maintenance	$ 28,872,000	$ 26,198,281	$ 25,245,876	$ 27,903,152	$ 35,451,920	$ 25,228,434
Total Distribution O&M	$ 39,596,000	$ 29,957,086	$ 30,542,437	$ 32,391,892	$ 41,415,438	$ 30,487,006
Difference from 1991		$ (9,638,914)	$ (9,053,563)	$ (7,204,108)	$ 1,819,438	$ (9,108,994)
Total 5 yr Difference						$ (33,186,141)
Net Plant in Service						
Gross Plant [3]	$ 467,018,000	$ 1,166,164,597	$ 1,228,340,149	$ 1,278,652,158	$ 1,393,667,520	$ 1,503,519,404
Accumulated Depreciation [4]	$ 125,670,000	$ 468,914,201	$ 578,253,259	$ 605,786,197	$ 650,535,255	$ 682,224,552
Net Distribution Plant	$ 341,348,000	$ 697,250,396	$ 650,086,890	$ 672,865,961	$ 743,132,265	$ 821,294,852
Quick Distribution Revenue Requirement						
Distribution Capital	$ 341,348,000	$ 697,250,396	$ 650,086,890	$ 672,865,961	$ 743,132,265	$ 821,294,852
Rate of Return [5]	11.87%	11.87%	11.87%	11.87%	11.87%	11.87%
Return on Net Plant	$ 40,518,008	$ 82,763,622	$ 77,165,314	$ 79,869,190	$ 88,209,800	$ 97,487,699
Distribution O&M	$ 39,596,000	$ 29,957,086	$ 30,542,437	$ 32,391,892	$ 41,415,438	$ 30,487,006
Distribution Depreciation Exp [6]	$ 13,606,000	$ 41,989,571	$ 44,485,047	$ 43,151,268	$ 46,888,092	$ 50,590,534
Return, O&M and Dep Exp	$ 93,720,008	$ 154,710,279	$ 152,192,798	$ 155,412,350	$ 176,513,330	$ 178,565,239
Annual Rev Requirement Exceeding Rates		$ 60,990,271	$ 58,472,790	$ 61,692,342	$ 82,793,322	$ 84,845,231
Total Quick Revenue Requirements Exceeding Rates (2008 - 2012)						$ 348,793,956

[1] DP&L's Distribution Rates were last set in Case No. 91-414-EL-AIR and were unbundled in Case No. 99-1687-EL-ETP, Part A, Schedule UNB 4

[2] O&M 2008 - 2012 DP&L FERC Form No 1, page 322, line 156

[3] Gross Plant 2008 - 2012 DP&L FERC Form No 1, page 207, line 75 col (g)

[4] Accumulated Depreciation 2008 - 2012 DP&L FERC Form No 1, page 219, line 26, col (c)

[5] Return on Rate base authorized in Case No. 91-414-EL-AIR

[6] Depreciation Expense 2008 - 2012 DP&L FERC Form No 1, page 336, line 8, col (b)

Exhibit A