

**BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO**

In the Matter of the Review of the Delivery)
Capital Recovery Rider Contained in the)
Tariffs of Ohio Edison Company, The) Case No. 12-2855-EL-RDR
Cleveland Electric Illuminating Company,)
and The Toledo Edison Company.)

**REPLY COMMENTS OF OHIO EDISON COMPANY,
THE CLEVELAND ELECTRIC ILLUMINATING COMPANY
AND THE TOLEDO EDISON COMPANY**

On March 25, 2013, Blue Ridge Consulting Services, Inc. (“Blue Ridge” or “Auditor”), the independent auditor selected to perform the audit of the Delivery Capital Recovery (“DCR”) Rider of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company (collectively, “Companies”), filed its Compliance Audit Report (“Report”) with the Public Utilities Commission of Ohio (“Commission”).

On May 23, 2013, the Companies and Commission Staff filed Joint Comments to memorialize their agreement that the Commission should adopt the listed recommendations Blue Ridge made in its Report. On July 17, 2013, the Office of the Ohio Consumers’ Counsel (“OCC”) filed late its comments (“OCC Comments”). In those comments, the OCC recommended that the Commission order a supplemental audit of FirstEnergy’s 2012 Delivery Capital Recovery Rider (“Rider DCR”) or, in the alternative, that the Commission require an investigation in the next scheduled audit. The Companies respectfully request that the Commission reject this recommendation and hereby respond to those comments.

I. OCC's COMMENTS ARE UNTIMELY AND SHOULD BE STRICKEN.

The Companies object to the untimely filing of the OCC's Comments and request that the Commission strike its comments from this proceeding. As noted in the Report, on February 1, 2013, the Companies filed Applications¹ providing "all additions, retirements, transfers, and adjustments to plant in service that have occurred for that actual year ended December 31, 2012."² Initial recommendations and/or objections by all parties are to be filed within 120 days of those Applications pursuant to the Combined Stipulation approved by the Commission;³ therefore, all interested parties' comments or objections were due to be filed no later than June 3, 2013.⁴ The Combined Stipulation states,

If no objections are filed within 120 days after the filing of the Application, the proposed DCR rate will remain in effect without adjustment, except through the normal quarterly update process or as may be ordered by the Commission as a result of objections filed in a subsequent audit process. If the Companies are unable to resolve any objections within 150 days of the filing of the application, an expedited hearing process will be established in order to allow the parties to present evidence to the Commission regarding the conformance of the application with this Stipulation, and whether the amounts for which recovery is sought are not unreasonable.⁵

The OCC filed its Comments 44 days beyond the due date for comments and objections, and 14 days beyond the 150-day deadline for the Companies to attempt to resolve any objections raised, which, if unresolved, would trigger further proceedings.

¹ Case Nos. 12-2679-EL-RDR, 12-2680-EL-RDR, and 12-2681-EL-RDR for The Cleveland Electric Illuminating Company, Ohio Edison Company and The Toledo Edison Company, respectively.

² Blue Ridge Audit Report, Case No. 12-2855-EL-RDR, filed March 25, 2013, at page 22.

³ *Second Supplemental Stipulation*, filed July 22, 2010, Case No. 10-388-EL-SSO, approved August 10, 2010. ("Second Supplemental Stipulation"). *See also*, the April 20, 2012 Attorney Examiner's Entry, Case No. 11-5428-EL-RDR.

⁴ Since June 1, 2013, falls on a Saturday, initial comments were due on the next business day, Monday, June 3, 2013.

⁵ *Second Supplemental Stipulation* at 4.

The OCC has provided no justification for, or even acknowledgement of, failing by more than six weeks to meet the Commission-approved due date for objections. Notably, the OCC actively participated as a party in Case No. 10-388-EL-SSO, and filed comments in the 2011 DCR audit, Case No. 11-5428-EL-RDR, and therefore had knowledge of the 120-day window of opportunity to timely file comments or objections in this proceeding.⁶ The Companies therefore object to the OCC's late-filed Comments and hereby move to strike the Comments.

In the event the Commission decides to consider OCC's untimely Comments, the Companies provide specific reply comments below.

II. OCC MISUNDERSTANDS THE NATURE AND SCOPE OF THE DCR AUDIT.

OCC misunderstands the nature and scope of the audit established by the Commission's approval of the Companies' ESP 2 set forth in Case No. 10-388-EL-SSO. Rider DCR was established to provide the Companies' with the opportunity to recover property taxes, Commercial Activity Tax, associated income taxes and earn a return of and on plant in service associated with distribution, subtransmission and general and intangible plant not included in the Companies' last base rate case. The Combined Stipulation provides "[t]he audit of Rider DCR shall include a review to confirm that the amounts for which recovery is sought are not unreasonable" and that "the determination of whether the amounts for which recovery is sought are not unreasonable shall be determined in light of the facts and circumstances known to the Companies at the time such expenditures were committed."⁷ Thus, only capital expenditures, depreciation

⁶ The OCC timely filed comments in Case No. 11-5428-EL-RDR.

⁷ *Second Supplemental Stipulation* at 4.

expense, property tax expenditures, CAT expenditures and associated income taxes are reviewed during the annual audit. No other operations and maintenance expenses are included in Rider DCR revenue requirements; O&M expenses for which recovery is not being sought are therefore not reviewable in the annual audit.

Rider DCR is **not** an application for establishment or change in rate under Section 4909.18, Revised Code.⁸ The annual audit of Rider DCR is not a rate case. The Commission expressly rejected the argument that adjustments to riders authorized under an ESP must be filed pursuant to Section 4909.18, Revised Code.⁹ Therefore, none of the provisions of Section 4909.18(B), Revised Code, regarding “receipts, revenues, and incomes...operating costs and expenditures” are applicable to the Rider DCR annual audit beyond the items expressly included in the Combined Stipulation as modified and approved by the Commission.

III. OCC MISCONSTRUES THE RECOMMENDATIONS SET FORTH IN THE REPORT.

OCC misconstrues the recommendations contained in the Report by asserting that the “Auditor also recommended that FirstEnergy submit more detailed information regarding savings and efficiencies gained due to the merger.”¹⁰ This is simply not true. In fact what Blue Ridge recommended, and the Companies have agreed to do, is to include quantifications of any increase in efficiency and savings within its IT project justifications. Further misconstruing the Report, OCC states that the Auditor “noted the possibility that some merger costs either exceeded expectations or should result in

⁸ Case No. 10-388-EL-SSO, Opinion and Order at 40.

⁹ Id.

¹⁰ OCC Comments at 2.

savings.”¹¹ However, in the Report, the Auditor merely noted that out of the eleven (11) IT work orders selected for testing, six were over budget by more than 15% and four were under budget by more than 15%. The Auditor further noted that the Companies’ explanation that four of the six projects that were identified as being “over budget” were related to merger projects and simply involved a timing issue arising from the 2011 budget close and the merger announcement, leading to actual costs which included both 2011 and 2012 IT project costs being compared with the 2012 budget, which did not include both years.¹² As evidenced by the exact language in the Report, the Auditor did not: i) conclude that some merger costs exceed expectations; ii) conclude that the merger should result in savings; and iii) recommend more detailed information regarding merger savings and efficiencies. Indeed, such conclusions and recommendations would have been unsupported by the findings in the Report, would exceed the scope of the Audit, and were not included in the Companies’ and Staff’s Joint Comments.

Moreover, the OCC mistakenly elevates the Report’s discussion of IT project processes and controls and the justification included in the IT project approval process as a general commentary on merger costs and benefits. The OCC incorrectly states with respect to two IT projects that the “Auditor determined [they] ‘would increase efficiency and promote savings.’”¹³ In reality, during its review of the Companies’ “Processes and Controls,” the Auditor noted that the Companies justified approval of these two IT projects on the basis that they were expected to “increase efficiency and promote

¹¹ OCC Comments at 4.

¹² Audit Report at 48.

¹³ OCC Comments at 4.

savings.”¹⁴ Determining whether IT merger-related projects would increase efficiency and promote savings as a result of the merger is beyond the scope of the audit authorized by the Commission and beyond the scope of the Stipulation approved by the Commission in Case No. 10-388-EL-SSO.¹⁵ In other words, Blue Ridge properly was not tasked with determining anything at all regarding the merger except for the Commission’s sole test as to whether there have been net job losses as a result of involuntary attrition due to the merger as the condition for the inclusion of general plant allocated from FirstEnergy Service Company – as specifically set forth in the Stipulation.

Blue Ridge’s observation that the Companies provided “no indication of how the benefits will be given back to the ratepayers” was made without reference to any legal obligation for the Companies to do so, and without connection to its audit objectives outlined in Scope Area 1 and Scope Area 2.¹⁶ The OCC does not allege in its Comments that the Commission Opinion and Order in Case No. 10-388-EL-SSO includes an obligation for the Companies to “give back” to customers any savings that may or may not arise from any given IT project in particular, or for merger-related costs and savings generally, or if any such net savings exist at all. The OCC also does not allege that any other Commission Order regarding the Companies creates such an obligation.

¹⁴ Blue Ridge Audit Report at 48. The OCC mistakenly attributes all of the cost to work order #ITS-SC-M00009-1, when the Audit Report clearly identifies “Total Combined Cost \$20,178,564.”

¹⁵ “The Project Scope as defined in the RFP addresses two areas: Scope Area 1: Determine if FirstEnergy has implemented its Commission-approved DCR Rider and is in compliance with the Combined Stipulation agreement set forth in...Opinion and Order (Case No. 10-388). Scope Area 2: Examine the effects of the merger between FirstEnergy and Allegheny Energy to determine that there are no net job losses at the Companies or with respect to FirstEnergy Service Company employees who provide support for distribution services provided by the Companies and are located in Ohio, per Commission order in 10-388-EL-SSO, as a result of involuntary attrition as a result of the merger between FirstEnergy Corp. and Allegheny Energy, Inc.” Blue Ridge Audit Report at 10. (internal caption omitted).

¹⁶ Blue Ridge Audit Report at 48.

With respect to Processes and Controls that properly were part of the Audit Scope, Blue Ridge concluded that “FirstEnergy’s and the Companies’ controls were adequate and not unreasonable.”¹⁷ This conclusion covers “processes and controls that affect each of the categories within Rider DCR”¹⁸ (emphasis added), which includes the IT project justification and approval process. Moreover, Blue Ridge specifically noted that a change control tool had been added by IT in 2013 for “creating, approving, and tracking project changes.”¹⁹ This change tool is expected to improve the Companies’ ability to provide supporting justification of 2013 IT projects and subsequent audit analysis of budgeted versus actual costs. Similarly, supplying quantification going forward for those IT project approvals justified on the basis of increased efficiency and promotion of savings will also assist future audits to evaluate Processes and Controls.

IV. THE OCC RECOMMENDATION THAT O&M SAVINGS BE PASSED BACK TO CUSTOMERS BASED ON PRECEDENT OF NATURAL GAS INDUSTRY CASES IS MISPLACED.

Next, the OCC complains that the “[a]uditor did not conduct, and was not instructed to conduct, a review of any possible O&M savings that may have resulted (and will result) from Rider DCR.”²⁰ The OCC speculates that “it stands to reason” that the Companies “should have reduced, and will continue to further reduce, many of the O&M costs imbedded in existing base rates associated with an older distribution system.”²¹ The statements are both pure speculation and beyond the scope of the audit. The OCC cites several natural gas industry cases implementing aging pipeline infrastructure

¹⁷ Blue Ridge Audit Report at 11, 37.

¹⁸ Blue Ridge Audit Report at 37. (Blue Ridge was able to obtain an understanding of the Companies’ processes and controls that affect each of the categories within Rider DCR from the documents reviewed and interviews conducted.”)

¹⁹ Blue Ridge Audit Report at 48.

²⁰ OCC Comments at 5.

²¹ OCC Comments at 5.

replacement trackers and opines that the Commission “should similarly recognize the importance of identifying the O&M cost savings that are likely to be realized by FirstEnergy from the DCR investments” and that “[i]f such benefits are being realized by FirstEnergy as part of the DCR program,²² then such benefits should be identified and passed back to customers.”²³ However, the OCC ignores important distinctions between the relief sought and granted in those cases and the scope and purpose of the Combined Stipulation that established the Companies’ Rider DCR.

As noted by the OCC, the natural gas companies predicated their requests for the new Riders upon anticipated reductions in costs.²⁴ In contrast, the Commission approved Rider DCR is part of an entire Electric Security Plan with numerous provisions in the Combined Stipulation as modified by the Commission, specifically under the statutory authority of Section 4928.143 of the Ohio Revised Code without any contemplation of O&M off-sets in Rider DCR.²⁵ The purpose and justification for the Riders are fundamentally different as between the natural gas cases cited and the Companies’ Rider DCR.

The offset for targeted O&M savings in the natural gas industry PIR Rider cases cited by the OCC were proposed by those companies and included in the Commission’s approval of those mechanisms. In contrast, the Commission’s approval of Rider DCR in Case Nos. 10-388-EL-SSO and 12-1230-EL-SSO, respectively, included no such O&M savings pass-back. Moreover, the Commission’s Opinion and Order in the Companies’

²² OCC does not define what is meant by the term “DCR Program” and that term does not appear in the Blue Ridge Audit Report or the Commission’s order approving the Companies’ ESP2.

²³ OCC Comments at 6.

²⁴ OCC Comments at 6, especially footnote 18 quoting the Commission’s Order issued In re Dominion 2009 PIR Case, Case No. 09-458-GA-RDR (December 16, 2009) (“Because immediate customer savings were articulated as a goal of the PIR Program...”).

²⁵ The predecessor for Rider DCR which was approved in Case No. 08-935-EL-SSO, also specifically did not contain any off-sets to reflect reductions in costs.

ESP 2 case discussed numerous provisions of the Combined Stipulation benefiting customers other than Rider DCR.²⁶ The OCC seeks to impose a new provision that is beyond the scope of both the approved Combined Stipulation as well as the Commission's Order approving it. The pass-back of savings in the natural gas Riders effectuated the prior Commission's Orders whereas here the OCC proposes a *contravention* of the prior Commission Order.

The OCC also argues that the Commission should establish a new pass-back of "savings" to protect customers from shareholders being "unjustly enriched...through the retention of savings."²⁷ To be clear, a theoretical reduction in operation or maintenance costs for a specific purpose does not necessarily result in a net reduction in O&M costs for an electric distribution utility, and OCC's speculation in that regard should be rejected as being both incorrect and beyond the scope of the audit.

Further, the OCC ignores the statutory built-in safeguard contained in 4901.143(F), the significantly excessive earnings test ("SEET"), and that any charges billed through Rider DCR after January 1, 2012, will be included as revenue in the return on equity calculation for purposes of applying the SEET and will be considered as an adjustment eligible for refund.²⁸ As an accounting-based measure, the SEET already prevents "unjust enrichment." No additional pass-back of targeted cost "savings" in the Rider DCR mechanism is necessary or appropriate to protect customers.

²⁶ *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Authority to Establish a Standard Service Offer Pursuant to Section 4928.143, Revised Code in the Form of an Electric Security Plan*, Case No. 10-388-EL-SSO, Opinion and Order, August 25, 2010, page 36-37.

²⁷ OCC Comments at 6.

²⁸ Case No. 10-388-EL-SSO, Opinion and Order at 12.

V. THE OCC RECOMMENDATION THAT ANY HYPOTHETICAL O&M SAVINGS AND ADDITIONAL REVENUES BE INCLUDED AS AN OFFSET TO THE RIDER DCR REVENUE REQUIREMENT CALCULATION IS CONTRARY TO AND A COLLATERAL ATTACK UPON THE COMMISSION ORDER.

Last, the OCC complains “the Blue Ridge Auditor did not take into account the extent to which the new infrastructure has resulted in new customer growth and additional revenues for FirstEnergy as the assets are (and continue to be) put into service pursuant to the DCR program.”²⁹ The OCC recommends that the Commission “order a supplemental audit in order to determine and quantify whether [the Companies have] recognized any additional revenues, and if so, ensure those additional revenues are accounted for in the Rider DCR revenue requirement calculation and the benefits of the additional revenues have been passed back to customers (and are not being enjoyed by the Utility’s shareholders).”³⁰ However, like the OCC’s recommendation to include O&M savings in Rider DCR, this recommendation is beyond the scope of the audit and in contravention of the Commission’s Order approving the Companies’ ESP 2 in Case No. 10-388-EL-SSO.

As discussed above regarding O&M expenses, the OCC simply ignores the basic design of the Companies’ Rider DCR that was approved by the Commission by failing to address the provision for annual revenue caps included in the Commission’s approval of Rider DCR.³¹ Rider DCR is expressly designed to collect revenues up to the amount specified in those caps pursuant to the Commission’s determination that such revenue

²⁹ OCC Comments at 7.

³⁰ OCC Comments at 7-8.

³¹ Case No. 10-388-EL-SSO, Opinion and Order at 11.

collection under the total package comprising the Combined Stipulation benefits customers and the public interest.³²

The Rider DCR mechanism approved by the Commission does not, and was not approved to, include incremental base distribution revenues and O&M expenses, if any. The Commission found that the Combined Stipulation, which includes the approved Rider DCR mechanism, “does not violate any important regulatory principles or practices.”³³ The OCC’s proposed supplemental audits represent a sea change in design and function that is contrary to the approved design of Rider DCR, which has been subject to two Commission directed external audits during the year and a half it has been in effect. The audits were conducted in a manner consistent with the Commission-approved terms of the Combined Stipulation in the Companies’ ESP 2.

VI. CONCLUSION

The Commission should strike OCC’s untimely comments. Nevertheless, should the Commission consider those comments, they are without merit and should be rejected. The OCC’s recommendations are based upon a mischaracterization of the Blue Ridge Auditor’s findings and recommendations regarding IT project work orders, which are then bootstrapped into a collateral attack on the Commission’s Order approving the Companies’ ESP 2 in Case No. 10-388-EL-SSO.

³² Case No. 10-388-EL-SSO, Opinion and Order at 36.

³³ Case No. 10-388-EL-SSO, Opinion and Order at 42.

Respectfully submitted,

/s/ James W. Burk

James W. Burk (0043808)

Counsel of Record

Carrie M. Dunn (0076952)

FIRSTENERGY SERVICE COMPANY

76 South Main Street

Akron, OH 44308

(330) 761-7735

(330) 384-3875 (fax)

burkj@firstenergycorp.com

cdunn@firstenergycorp.com

*Attorneys for Ohio Edison Company, The
Cleveland Electric Illuminating Company and
The Toledo Edison Company*

CERTIFICATE OF SERVICE

I hereby certify that the foregoing Reply Comments were served this 16th day of August, 2013 by electronic mail on the persons listed below.

/s/ James W. Burk

James W. Burk

Thomas McNamee
Asst. Attorney General
180 East Broad Street, 6th Floor
Columbus, Ohio 43215
Email: Thomas.mcnamee@puc.state.oh.us

Larry S. Sauer
Assistant Consumers' Counsel
Office of the Ohio Consumers' Counsel
10 West Broad Street, Suite 1800
Columbus, OH 43215-3485
(614) 466-1312 – Telephone (Sauer)
Email: sauer@occ.state.oh.us

This foregoing document was electronically filed with the Public Utilities

Commission of Ohio Docketing Information System on

8/16/2013 5:21:09 PM

in

Case No(s). 12-2855-EL-RDR

Summary: Reply Reply Comments of Ohio Edison, The Cleveland Electric Illuminating Company and The Toledo Edison Company, Case No. 12-2855-EL-RDR electronically filed by Mr. Robert M. Endris on behalf of Burk, James W. Mr.