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Via E-FILE

August 15, 2016

Public Utilities Commission of Ohio
PUCO Docketing
180 E. Broad Street, 10th Floor
Columbus, Ohio 43215

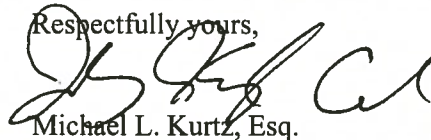
In re: Case No. 14-1297-EL-SSO

Dear Sir/Madam:

Please find attached the REHEARING BRIEF OF THE OHIO ENERGY GROUP e-filed today in the above-referenced matter.

Copies have been served on all parties on the attached certificate of service. Please place this document of file.

Respectfully yours,



Michael L. Kurtz, Esq.

Kurt J. Boehm, Esq.

Jody Kyler Cohn, Esq.

BOEHM, KURTZ & LOWRY

MLKkew

Encl.

Cc: Certificate of Service

**BEFORE THE
PUBLIC UTILITIES COMMISSION OF OHIO**

In The Matter Of The Application Of The Ohio Edison :
Company, The Cleveland Electric Illuminating Company, :
And The Toledo Edison Company For Authority To : **Case No. 14-1297-EL-SSO**
Establish A Standard Service Offer Pursuant To R.C. :
§4928.143 In The Form Of An Electric Security Plan. :

**REHEARING BRIEF OF THE
THE OHIO ENERGY GROUP**

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August 15, 2016

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**REHEARING BRIEF OF THE
THE OHIO ENERGY GROUP**

The Ohio Energy Group (“OEG”) submits this Rehearing Brief in support of its recommendations to the Public Utilities Commission of Ohio (“Commission”).

ARGUMENT

I. Revised Rider RRS Is A Reasonable Substitute For The Rate Stability Mechanism Already Approved By The Commission.

On March 31, 2016, the Commission approved with modifications the proposal by The Ohio Edison Company, The Toledo Edison Company, and The Cleveland Electric Illuminating Company’s (collectively, “FirstEnergy” or “the Companies”) to establish a Retail Rate Stability Rider (“Rider RRS”). The Commission’s decision was sound. In accordance with R.C. 4928.143(B)(2)(d), the Commission-approved Rider RRS would have stabilized retail customer rates by creating a cost-based hedge to counterbalance market-based pricing. And by ensuring that several generating plants located in Ohio would continue to operate, that Rider would have also provided reliability, economic development, and fuel diversity benefits to customers.

However, on April 27, 2016, the Federal Energy Regulatory Commission (“FERC”) effectively blocked the transaction.¹ By rescinding part of the waiver on affiliate transactions previously granted to FirstEnergy Solutions (“FES”), the FERC forced FirstEnergy to reevaluate and revise the Commission-approved Rider RRS so that the

¹ Order Granting Complaint, 155 FERC ¶61,101 (April 27, 2016).

costs flowed through that Rider would no longer be associated with a wholesale transaction between FirstEnergy and FES. On rehearing, FirstEnergy now proposes the following changes to the Commission-approved Rider RRS: 1) replacing actual costs with costs that are known and already evidence of record; 2) replacing actual generation output with a known measure of generation output that is already evidence of record; and 3) replacing actual capacity (MWs) cleared in the PJM capacity market with the capacity (MWs) projected to clear, which is already evidence of record.²

Like its predecessor, revised Rider RRS will provide rate stability to customers in furtherance of the objectives of R.C. 4928.143(B)(2)(d). The cost-based rates that FirstEnergy proposes to guarantee through revised Rider RRS are more stable than the volatile market pricing experienced in the PJM energy and capacity markets.³ The revised Rider RRS results in a cumulative 19.7% increase in cost-based pricing over the seven full years 2017-2023, with an average annual increase of 3.0%.⁴ In contrast, retail generation rates for shopping customers increased by 35% over the first four months after the polar vortex.⁵ Allowing part of FirstEnergy's generating pricing to be set using these fixed cost-based rates would therefore help smooth out rates that could otherwise fluctuate significantly depending upon market conditions and modifications to PJM's administratively-determined and ever-changing market construct. The financial end result of approving revised Rider RRS is that customers would have generation rates comprised of approximately 40% at the guaranteed cost-based pricing and 60% at the federally-regulated market rate.⁶

In response to FirstEnergy's new proposal, Staff now recommends that the Commission reject revised Rider RRS. Staff notes that the revised Rider RRS proposal "*is no longer comprised of a PPA that is tied to specific power stations in the state.*"⁷ Consequently, Staff states that two of the categories of benefits cited by the

² OEG Exs. 4 and 5C (Rehearing Testimony of Stephen J. Baron) at 1:11-21.

³ Id. at 5:7-8:15.

⁴ Id. at 8:3-5.

⁵ Company Ex. 146 (Rebuttal Testimony of Eileen M. Mikkelsen) at 4:15-17.

⁶ OEG Exs. 4 and 5C at 8:1-3.

⁷ Staff Ex. 15 (Rehearing Testimony of Hisham M. Choueiki, Ph.D., P.E.) at 13:15:16.

Commission in approving the original Rider RRS – fuel diversity benefits and economic benefits derived by maintaining the operation of the generating plants – would be eliminated under the revised proposal.⁸

While Staff raises legitimate and important concerns with respect to FirstEnergy’s revised RRS proposal, approval of revised Rider RRS could still benefit customers since it would still provide rate stability. Therefore, and in accordance with its obligations under the Stipulations filed in this proceeding, OEG supports FirstEnergy’s revised Rider RRS proposal.

II. Staff's Proposed Distribution Modernization Rider Addresses Valid Concerns And Is Lawful, But OEG Takes No Position At This Time With Respect To Whether The DMR Should Be Approved, Its Level, Or Its Term.

Staff proposes that the Commission establish a Distribution Modernization Rider (“DMR”) to assist FirstEnergy in receiving more favorable terms when accessing the capital market, which Staff believes will enable the Companies to procure funds to jumpstart their distribution and grid modernization initiatives.⁹ Staff also recommends that FirstEnergy Corp. (“FE”) keep its corporate headquarters and nexus of operations in Akron, Ohio for the term of the Companies’ current Electric Security Plan (“ESP”) or that the proposed DMR be subject to refund, which gives the DMR an economic development component.¹⁰ Staff calculates that the Companies’ proportionate share of FE’s operating revenue necessitates a fixed annual DMR charge to customers of \$131 million.¹¹

At this time OEG takes no position with respect to whether the Commission should approve or disapprove the proposed DMR, at what level, or for what period of time. But Staff raises valid concerns with respect to the continued location of FE’s corporate headquarters as well as FirstEnergy’s access to capital. Staff’s proposed DMR is innovative and constructive. And the proposed mechanism is lawful under R.C. 4928.143(B)(2)(h) since it is both a single-issue ratemaking and incentive ratemaking provision regarding FirstEnergy’s distribution service. The DMR will provide FirstEnergy sufficient capital to incentivize the Companies to make additional

⁸ Id. at 13:7-18.

⁹ Staff Ex. 15 at 14:9-16:2.

¹⁰ Staff Ex. 13 at 7:7-14.

¹¹ Rehearing Tr. Vol. III (July 13, 2016) at 507:11-15.

investments in distribution infrastructure. The proposed DMR is also lawful under R.C. 4928.143(B)(2)(i) since maintaining FE's corporate headquarters in Ohio will implement economic development and job retention in the State. FE's corporate headquarters is a critical driver of the otherwise depressed economy of the City of Akron, providing \$568 million of annual economic benefits.¹²

Some parties may argue that the proposed DMR would provide FirstEnergy with unlawful "transition revenues" contrary to the Supreme Court of Ohio's recent decisions with respect to AEP Ohio and Dayton Power & Light.¹³ Such arguments misapply the Court's decisions. As an initial matter, the proposed DMR is authorized under entirely different provisions of the ESP statute than the charges struck down by the Court, which were authorized under R.C. 4928.143(B)(2)(d). And the proposed DMR is distinct from the charges recently struck down by the Court because it is a distribution-related charge rather than a generation-related charge. Moreover, even if the costs included in the proposed DMR could appropriately be considered "transition revenue," the "notwithstanding" language of R.C. 4928.143(B) creates an exception from the prohibition against transition revenues for charges that may lawfully be authorized under the ESP statute, including charges such as the proposed DMR.¹⁴

¹² Company Ex. 205 at 4:8-10.

¹³ *In re Application of Columbus S. Power Co.*, Slip Opinion No. 2016-Ohio-1608 (citing R.C. 4928.38); *In re Application of Dayton Power & Light Co.*, Slip Opinion No. 2016-Ohio-3490 (June 20, 2016).

¹⁴ R.C. 4928.143(B) provides "Notwithstanding any other provision of Title XLIX of the Revised Code to the contrary except division (D) of this section, divisions (I), (J), and (K) of section 4928.20, division (E) of section 4928.64, and section 4928.69 of the Revised Code:

(2) The [electric security] plan may provide for or include, without limitation, any of the following:

(h) Provisions regarding the utility's distribution service, including, without limitation and notwithstanding any provision of Title XLIX of the Revised Code to the contrary, provisions regarding single issue ratemaking, a revenue decoupling mechanism or any other incentive ratemaking, and provisions regarding distribution infrastructure and modernization incentives for the electric distribution utility....

(i) Provisions under which the electric distribution utility may implement economic development, job retention, and energy efficiency programs, which provisions may allocate program costs across all classes of customers of the utility and those of electric distribution utilities in the same holding company system."

III. If The Distribution Modernization Rider Is Approved, Then It Should Be Allocated To Customers On The Basis Of 50% Demand And 50% Distribution Revenues.

OEG's only recommendation with respect to the proposed DMR at this juncture concerns cost allocation and rate design, which Staff did not expressly address in its written testimony. The most appropriate cost allocation for the proposed DMR would be based entirely upon distribution revenues. As its nomenclature suggests, the DMR is primarily a distribution-related Rider since the revenues received by the Companies under that Rider are intended to incentivize increased investment in distribution modernization.¹⁵ Additionally, the provision that Staff cites as legal authority for the proposed DMR (R.C. 4928.143(B)(2)(h)) specifically relates to distribution service.¹⁶ A distribution allocation of a distribution charge also supports the argument that the DMR is lawful.

However, due to the unique nature of the proposed DMR, the Commission should take a different approach with respect to cost allocation. Because the DMR is also intended to incentivize FE to remain headquartered in Ohio, there is an economic development component to the Rider. Given that the Rider has both distribution and economic development components, the Commission should take a hybrid approach to cost allocation. The Companies should allocate DMR costs to rate schedules 50% on the basis of distribution revenues and 50% on the basis of demand (4 Coincident Peak).¹⁷

After the 50/50 cost allocation to the various rate schedules takes place, the Companies should collect the allocated DMR costs using a kWh charge calculated separately for each rate schedule.¹⁸ This rate design, as opposed to a kW or kVa charge for the demand-metered rate schedules, would benefit low load factor customers at the expense of high load factor customers (including OEG members). Such an outcome is contrary to cost causation principles, but produces a balanced outcome in this instance. As OEG witness Baron explained:

¹⁵ OEG Ex. 7 (Rebuttal Testimony of Stephen J. Baron) at 2:17-21.

¹⁶ Staff Ex. 14 (Rehearing Testimony of Tamara S. Turkenton) at 2:8-13 (citing R.C. 4928.143(B)(2)(h)).

¹⁷ OEG Ex. 7 at 3:1-9.

¹⁸ OEG Ex. 7 at 4:1-5.

Q. Now, there is a kilowatt-hour or an energy component to your rate design, correct?

A. Yes.

Q. Okay. And you described how that is a balance between the high- and the low-load factor customers within the same rate schedule?

A. Correct. That's -- once the costs are allocated to the class, it would tend to balance the impact among various load factors within the class.

Q. And as opposed to a demand charge for demand-metered customers, what type of customer does a kilowatt-hour rate design help? The high-load factor or the low-load factor customers?

A. Because -- the answer is it would help the low-load factor customers. The very large manufacturing customers tend to have high-load factors and so those customers are going to -- all else being equal, they would be paying less under a pure demand allo -- recovery, rate recovery. And so an energy recovery within the class helps lower-load factor, typically smaller customers.

Q. And would you agree that this aspect of your rate design proposal actually hurts the OEG members who tend to be the higher-load factor customers within the rate schedules?

A. Yes. There's no question about it.

Q. And then why did you propose it?

A. Again, because it was -- we are -- I tried to come up with a method that was balanced, that recognized -- that considered tradeoffs of rate impacts and cost causation and all of the factors that I really discuss.¹⁹

None of the non-variable DMR costs of \$131 million per year should be allocated to rate schedules on the basis of variable energy usage. There is no nexus between the fixed DMR expense and the volume of energy used by any given customer. Regardless of the amount of energy usage on the system, the \$131 million per year remains a fixed distribution expense.

At the hearing, OEG witness Baron reinforced how allocating any distribution-related costs on the basis of energy would be directly counter to regulatory practice throughout the country:

Q. Okay. How many times have you testified?

A. I've testified in about 335 cases. I had to do the calculation the other day. It's been 40 years; it's not like last week.

Q. And how many of those cases involved cost of service revenue allocation type issues?

A. Well over 100.

Q. And those 100 cases, I assume this is across the country?

A. Yes.

¹⁹ Rehearing Tr. Vol. VI (July 21, 2016) at 1319:8-1320:14.

Q. Over 20, 30 states or so?

A. Yes. At least.

Q. Okay. In those over 100 cases, in at least 20 to 30 states, have you ever seen a Commission allocate distribution costs on the basis -- basis of energy usage?

A. No. I've never in my experience -- I have seen some proposals for that, but I've never seen -- I've never seen a utility propose it and I've never -- I am not aware of any regulatory Commission approving an allocation of distribution-related costs on the basis of energy. It's simply distribution costs -- first of all, they would only be assigned to the rate classes that use the distribution system. So a customer class like GT that takes service at transmission that does not use the distribution system wouldn't pay for secondary lines and primary lines and transformers and poles which are distribution-related costs. That's the grid -- that's the grid system that would tend to be modernized.²⁰

Mr. Baron's experience across 20-30 states over 40 years is not surprising given the position of the National Association of Regulatory Utility Commissioners ("NARUC"). NARUC's *Electric Utility Cost Allocation Manual* advises against allocating any distribution-related costs on the basis of energy, explaining "[t]o ensure that [distribution] costs are properly allocated, the analyst must first classify each account as demand-related, customer-related, or a combination of both...Because there is no energy component of distribution-related costs, we need only consider the demand and customer components."²¹

Allocating the non-variable DMR costs of \$131 million per year on the basis of variable energy usage would also harm economic development in Ohio, contrary to one of the primary goals of establishing the proposed DMR. Adopting an energy-based allocation for the fixed DMR distribution expense would force large transmission voltage customers, who must compete both nationally and internationally and who would derive little benefit from additional distribution infrastructure modernization, to pay a disproportionate amount of DMR costs.²² This outcome would be inconsistent with R.C. 4928.02(H)'s directive to "[f]acilitate the state's effectiveness in the global economy."

²⁰ Rehearing Tr. Vol. VI (July 21, 2016) at 1318:1-1319:7.

²¹ National Association of Regulatory Utility Commissioners, *Electric Utility Cost Allocation Manual* (January 1992), available at <https://efile.mpsc.state.mi.us/efile/docs/17689/0078.pdf> at 89.

²² OEG Ex. 7 at 3:11-23.

IV. The Commission Could Also Adopt An Alternative Approach To DMR Cost Allocation To Lessen The Rate Impact On Residential Customers.

Although OEG supports its recommended DMR cost allocation methodology, a reasonable alternative exists. Under that alternative, DMR costs would first be allocated to *only* the residential class based 50% on demand and 50% on energy. Then, the residual DMR costs left over after that first step would be allocated to the remaining rate schedules as OEG recommends (50% on distribution revenues and 50% on demand). This would give the residential customers the cost allocation suggested by Staff witness Turkenton during cross examination.²³

This alternative approach lessens the rate impact of the DMR on the residential class by \$15.4 million per year, or 26% from OEG's primary cost allocation recommendation. The details of this alternative approach are shown on Attachment A, which was derived from OEG Ex. 8.

Allocating the residual revenue requirement (including the \$15.4 million reduction to the residential class) among all other rate schedules based on 50% distribution/50% demand²⁴ increases the DMR rate on all non-residential rate schedules, but by an amount which is reasonable. OEG members have load on Rates GS, GP, GSU and GT, all of which would be negatively impacted by this compromise alternative. The results of adopting either OEG's primary recommendation or the compromise alternative are derived from OEG Ex. 8 and are set forth in Table 1 below. The results on Table 1 are on a consolidated FirstEnergy basis, instead of individually for each of the three operating companies.

²³ Rehearing Tr. Vol. II (July 12, 2016) at 431:4-13.

²⁴ OEG Ex. 8; *See also* Attachment A to this Brief.

TABLE 1

	OEG		Compromise Alternative	
	50% on Dist. Rev. 50% on 4 CP Demand	Rate \$/mWh	Residential per Staff Residual per OEG	Rate \$/mWh
RS	\$57,835,488	3.34	\$42,454,667	2.45
GS	\$43,914,248	2.91	\$55,165,061	3.65
GP	\$7,263,473	1.79	\$8,843,194	2.18
GSU	\$7,297,598	1.50	\$7,889,161	1.62
GT	\$12,299,790	1.07	\$13,085,962	1.14
STL	\$1,593,417	5.37	\$2,417,811	8.15
POL	\$744,371	7.37	\$1,073,495	10.63
TRF	\$51,615	1.46	\$70,648	2.00
Total	\$131,000,000	2.46	\$131,000,000	2.46

Residential Typical Bill at 750 kWh per month	\$2.50	\$1.84
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One final issue. The Commission needs to decide if each of the three operating companies will have a separate DMR by rate schedule; or whether there will be a uniform FirstEnergy DMR by rate schedule. A uniform FirstEnergy DMR by rate schedule, as shown on Table 1 above, would be easier to administer and would be more reasonable.

CONCLUSION

WHEREFORE, for the foregoing reasons, the Commission should: 1) approve revised Rider RRS; or 2) if the DMR is approved, adopt OEG's primary or alternative cost allocation.

Respectfully submitted,



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August 15, 2016

COUNSEL FOR THE OHIO ENERGY GROUP

ATTACHMENT A

Compromise Allocation of \$131 Million DMR
Residential Allocation per Staff
Residual Allocation Based on 50% Distribution Revenue/50% 4 CP Demands

<u>Allocation to Companies</u>	4 CP Demand ¹	MWh ¹	MWh Allocation	50% 4CP	50% Energy	Allocated Rev. Req.	Rate \$/MWh
OE	45.58%	24,203,560	45.42%	29,854,900	29,749,701	59,604,601	2.46
CEI	36.02%	18,615,656	34.93%	23,593,100	22,881,353	46,474,453	2.50
TE	18.40%	10,469,830	19.65%	12,052,000	12,868,946	24,920,946	2.38
total	100.0%	53,289,046	100.00%	65,500,000	65,500,000	131,000,000	2.46

<u>Rate Class Allocation</u>	4CP ¹	MWh ¹	Distribution Revenue Allocation ³	50% 4CP	50% kwh / Dist. Rev	Allocated Rev. Req.	
OE							
RS	37.34%	9,274,426	62.450%	11,147,820	11,399,621	22,547,440	2.43
Residual for Allocation				18,707,080	18,350,080	37,057,161	
GS	33.31%	6,592,253	26.210%	9,944,667	12,808,405	22,753,072	3.45
GP	10.95%	2,630,586	5.030%	3,269,112	2,458,080	5,727,192	2.18
GSU	3.49%	978,431	1.400%	1,041,936	684,157	1,726,093	1.76
GT	14.86%	4,554,538	2.700%	4,436,438	1,319,447	5,755,885	1.26
STL	0.00%	122,532	1.390%	-	679,271	679,271	5.54
POL	0.00%	36,054	0.760%	-	371,400	371,400	10.30
TRF	0.05%	14,740	0.060%	14,927	29,321	44,248	3.00
total	100.0%	24,203,560	100.000%	29,854,900	29,749,701	59,604,601	2.46

CEI							
RS	29.09%	5,535,410	47.550%	6,863,233	6,803,825	13,667,058	2.47
Residual for Allocation				16,729,867	16,077,528	32,807,395	
GS	41.90%	6,536,798	39.140%	9,885,509	11,997,606	21,883,115	3.35
GP	2.21%	445,966	0.580%	521,408	177,788	699,195	1.57
GSU	18.38%	3,778,472	5.485%	4,336,412	1,681,320	6,017,732	1.59
GT	8.40%	2,120,383	1.895%	1,981,820	580,875	2,562,696	1.21
STL	0.00%	125,007	3.530%	-	1,082,053	1,082,053	8.66
POL	0.00%	55,212	1.790%	-	548,690	548,690	9.94
TRF	0.02%	18,408	0.030%	4,719	9,196	13,915	0.76
total	100.0%	18,615,656	100.000%	23,593,100	22,881,353	46,474,453	2.50

TE							
RS	26.20%	2,507,876	57.18%	3,157,624	3,082,545	6,240,169	2.49
Residual for Allocation				8,894,376	9,786,401	18,680,777	
GS	25.16%	1,965,008	32.80%	3,032,283	7,496,591	10,528,874	5.36
GP	10.75%	987,134	4.91%	1,295,590	1,121,217	2,416,807	2.45
GSU	1.00%	116,054	0.11%	120,520	24,816	145,336	1.25
GT	36.88%	4,832,776	1.41%	4,444,778	322,604	4,767,381	0.99
STL	0.00%	49,050	2.87%	-	656,487	656,487	13.38
POL	0.00%	9,702	0.67%	-	153,406	153,406	15.81
TRF	0.01%	2,230	0.05%	1,205	11,280	12,485	5.60
total	100.0%	10,469,830	100.00%	12,052,000	12,868,946	24,920,946	2.38

Ohio Total		53,289,046		65,500,000	65,500,000	131,000,000	2.46
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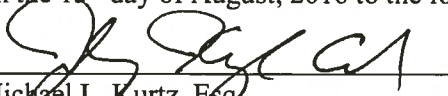
¹ JMS-2

² Case No. 07-0551, Schedule E-4

³ Stipulation, Case No. 07-0551, Schedule A (TE adjusted to remove negative allocation to Contract class)

CERTIFICATE OF SERVICE

In accordance with Rule 4901-1-05, Ohio Administrative Code, the PUCO's e-filing system will electronically serve notice of the filing of this document on the parties referenced on the service list of the docket card who have electronically subscribed to this case. In addition, the undersigned certifies that a courtesy copy of the foregoing document is also being served (via electronic mail) on the 15th day of August, 2016 to the following:


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