BEFORE THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company for Authority to Provide for a Standard Service Offer Pursuant to R.C. 4928.143 in the Form of An Electric Security Plan	**)))))))**	**Case No. 14-1297-EL-SSO**

SIERRA CLUB'S POST-HEARING REPLY BRIEF ON REHEARING

Public Version

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For more than two years now, the Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company (collectively, "FirstEnergy" or "Companies") have litigated at the Commission with a single-minded focus – to collect hundreds of millions to billions of dollars of new revenue from their customers. Over that timeframe, FirstEnergy, and more recently the Staff, have offered a series of proposals – the Retail Rate Stability Rider ("Rider RRS"), Modified Rider RRS, Staff's Distribution Modernization Rider ("DMR") proposal, and FirstEnergy's modifications to the DMR proposal – each with different purported goals and justifications. While the resulting record is voluminous and filled with often conflicting information, three critical points have been clearly established:

1. Customers would lose hundreds of millions to billions of dollars under any of the rider proposals pending before the Commission.

2. FirstEnergy would be able to funnel any revenues collected under these riders to FirstEnergy Corp., and is unwilling to commit to not doing so. Once such revenues are funneled to FirstEnergy Corp., they can easily be distributed to FirstEnergy Solutions ("FES") or to shareholders.

3. FirstEnergy steadfastly refuses to commit to spending any of the revenues that it would receive under these proposed riders on distribution modernization or any other initiatives that would benefit its customers.

FirstEnergy tries to sell such losing propositions for customers by highlighting a couple of nice-sounding purported benefits, such as rate stability or distribution modernization, and by raising the specter of credit downgrades and FirstEnergy Corp. moving its headquarters out of Akron if the proposed riders are rejected. But upon close inspection, the claimed benefits are illusory and the threats of negative consequences are empty.

After 51 days of hearing, hundreds of exhibits, and multiple rounds of testimony, this proceeding boils down to this: FirstEnergy is asking for hundreds of millions to billions of dollars of free cash from its customers to do with what it pleases. Meanwhile, customers would get little to no benefit in return. Such an arrangement is not lawfully authorized, or just and reasonable. As such, the Commission must reject Modified Rider RRS and the DMR, both as proposed by Staff and as modified by FirstEnergy.

I. The Modified Rider RRS Proposal Must Be Rejected as Unlawful, Unjust, and Unreasonable to the Companies' Customers.

As Sierra Club explained in its initial post-hearing brief on rehearing, Modified Rider RRS must be rejected because it is an unlawful and losing proposition for the Companies' customers. First, the Modified Rider RRS proposal is nothing more than a brazen attempt at an end run around the jurisdiction of the Federal Energy Regulatory Commission ("FERC") that is unlawful and that the Commission should not enable.[1] Second, Modified Rider RRS cannot be lawfully included as part of ESP IV because it is not authorized under any provision of R.C. 4928.143.[2] Third, the record demonstrates that customers would almost certainly lose hundreds of millions to billions of dollars under Modified Rider RRS, which renders the rider unreasonable and unable to satisfy the ESP vs. MRO test.[3] For each of these reasons, FirstEnergy's Modified Rider RRS proposal should be rejected as unlawful, unjust, and unreasonable.

In its initial post-hearing brief on rehearing, FirstEnergy offers little in the way of an affirmative case in support of its Modified Rider RRS proposal. In particular, the Companies do not identify in their brief a single statutory provision under which Modified Rider RRS could purportedly be approved, nor do they even attempt to justify their continued reliance on a projection of customer charges and credits that is based on market price forecasts that are more

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[1] Sierra Club's Initial Post-Hearing Brief on Rehearing ("SC Br.") at 3-7.

[2] *Id.* at 7-18.

[3] *Id.* at 19-38.

than two years old and already shown to be wrong. Instead, FirstEnergy tries to shield its unreasonable proposal from as much review as possible by contending that none of the grounds that the Commission relied on in approving the initial Rider RRS have changed as a result of the proposed modifications, and that customers would receive more certainty and benefits under Modified Rider RRS than they would have under Rider RRS. Unfortunately for FirstEnergy, even if the Commission's March 31, 2016 approval of Rider RRS were lawful and reasonable,[4] significant legal and factual developments that have occurred since the March 31 Order clearly demonstrate that Modified Rider RRS is unlawful, unjust, and unreasonable for customers. Consequently, the Modified Rider RRS proposal should be rejected.

A. The Commission Should Reject Modified Rider RRS as an Improper Attempt to Evade FERC Review.

One significant development that occurred since the March 31 Order was FERC's April 27, 2016 Order, which put a hold on the Affiliate PPA that was associated with Rider RRS.[5] As Sierra Club explained in its initial rehearing brief,[6] FirstEnergy's Modified Rider RRS proposal is a transparent attempt to do an end-run around that FERC Order, which held that the Affiliate PPA must be submitted for review under FERC's affiliate transaction standards[7] before any sales could be made under the PPA.[8] In so holding, FERC explained that Rider RRS and the Affiliate PPA "could be used to effectuate precisely the type of affiliate abuse" that FERC's affiliate

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[4] As Sierra Club has explained in its Application for Rehearing filed in this proceeding on April 29, 2016, the Commission's March 31, 2016 Order approving Rider RRS is unlawful, unreasonable, and against the manifest weight of the evidence. The Order should, therefore, be modified by rescinding the approval of Rider RRS and removing that rider from ESP IV.

[5] *Elec. Power Supply Ass'n, et al. v. FirstEnergy Solutions Corp., et al.*, 155 FERC ¶ 61,101 (Apr. 27, 2016) ("FERC Order").

[6] SC Br. at 3-7.

[7] 18 C.F.R. § 35.39.

[8] FERC Order at ¶¶ 53 & n.91, 62.

transaction standards are intended to prevent by "transfer[ring] benefits to the affiliates and its stockholders to the detriment of the captive customers."[9] Modified Rider RRS does nothing to eliminate the potential for affiliate abuse identified in FERC's April 27 Order, as the customer money collected under the rider could easily be transferred to FirstEnergy Corp. and then to shareholders or unregulated affiliates such as FES.[10] Modified Rider RRS would therefore enable the very abuse FERC seeks to prevent. The Commission should decline to aid FirstEnergy in such an effort.

In its initial post-hearing brief, FirstEnergy barely even attempts to conceal the evasive goal of its Modified Rider RRS proposal. Instead, FirstEnergy contends that "[a]n obvious benefit" of the Modified Rider RRS proposal "is that it avoids the delay resulting from FES obtaining approval" from FERC of the Affiliate PPA.[11] FirstEnergy asserts that the avoidance of such delay "ensures that the entire economic value of the Commission-approved ESP IV is made available in a timely manner to the Companies and their customers."[12] But given that even the Companies' own projections show that customers would begin losing money the day that Modified Rider RRS went into effect and would continue doing so through at least 2018,[13] it is the Companies, not customers, who would benefit from quick approval of Modified Rider RRS.

FirstEnergy attempts to insulate itself from the charge of evading FERC by claiming that Modified Rider RRS is "not designed to transfer regulated revenues to FES," and that "there is

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[9] *Id.* ¶ 60 (citing *Market-Based Rates For Wholesale Sales of Elec. Energy, Capacity & Ancillary Servs. by Pub. Utils.*, 123 FERC ¶ 61,055, FERC Stats. & Regs. ¶ 31,268, Order No. 697-A ¶¶ 188-89 (Apr. 21, 2008) ("Order No. 697-A")).

[10] Tr. I at 158. Note: Unless stated otherwise, all transcripts cited in this brief refer to the rehearing volumes (proceedings held between July 11, 2016, and August 1, 2016).

[11] Post-Rehearing Brief of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company ("Co. Br.") at 12.

[12] *Id.* (citing Co. Ex. 197, Rehearing Testimony of Eileen Mikkelsen ("Mikkelsen Test.") at 2, 4, 13).

[13] SC Ex. 89.

no mechanism within the Companies' organization that would allow them to share dollars with FES or transfer revenues or expenses to FES."[14] But these claims are unpersuasive, because although the Companies may not be able to directly transfer the Modified Rider RRS revenues to FES, they can do so indirectly. In particular, the Companies can use the Modified Rider RRS revenues to pay dividends to FirstEnergy Corp. The Commission would then be powerless to stop FirstEnergy Corp. from transferring the cash received from such dividends to unregulated affiliates such as FES.[15]

At last month's hearing, Companies' witness Eileen Mikkelsen declined to commit to not transferring Modified Rider RRS revenues to FirstEnergy Corp. through dividends and testified instead that nothing in the Companies' proposal would limit their ability to provide such dividends.[16] The Companies spent 21 months trying to funnel customer money directly to FES and some of its merchant generating plants through the Affiliate PPA and Rider RRS. It strains credulity to suggest that the Companies would not seek to achieve that same goal indirectly under Modified Rider RRS, especially when the Companies have refused to commit otherwise. The Commission should not abet FirstEnergy's attempt to achieve indirectly what FERC has stopped FirstEnergy from doing directly.

The Companies try to distract attention from the potential that Modified Rider RRS revenues would be funneled up to FirstEnergy Corp., its shareholders, and/or FES by suggesting that it might use such revenues to fund initiatives such as grid modernization, battery technology, and renewable energy.[17] Sierra Club is certainly supportive of initiatives that advance grid

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[14] Co. Br. at 14.

[15] Tr. I at 158.

[16] *Id.* at 75.

[17] Co. Br. at 12.

modernization, renewable energy, energy efficiency, and battery technology, as detailed in its initial rehearing brief.[18] But without binding commitments or requirements that any Modified Rider RRS revenues would be kept within the Companies and spent on such initiatives, there is no assurance that such revenues would actually go towards benefitting customers. And the Companies have studiously avoided making such a commitment.

For example, in its initial rehearing brief and rehearing testimony, FirstEnergy has been very careful to say only that it "could" or "intend[s]" to use Modified Rider RRS revenues for initiatives within the Companies.[19] What FirstEnergy never says is that it "will" or "commit" to do so.[20] In fact, at hearing, the Companies made clear that they (i) were unwilling to commit to such spending or to using any Modified Rider RRS revenues only within the Companies, (ii) would not propose any restrictions on how such revenues are spent, and (iii) had not developed any plans or identified any specific projects to be funded with Modified Rider RRS revenues.[21] The absence of such commitments and plans further demonstrates that Modified Rider RRS creates exactly the same potential for "transfer[ring] benefits to the affiliates and its stockholders to the detriment of the captive customers"[22] that FERC found so problematic in evaluating the Affiliate PPA and Rider RRS. The Commission should decline to be a part of FirstEnergy's attempt to evade FERC review and, instead, reject Modified Rider RRS.

[18] SC Br. at 83-91.

[19] Co. Br. at 12; Mikkelsen Test. at 12.

[20] The Companies' claim in their initial rehearing brief that they "are committed to going forward with whatever grid modernization/SmartGrid programs are authorized by the Commission," Co. Br. at 12-13, says nothing about whether the Companies would use Modified Rider RRS revenues to cover the costs of such programs. Instead, as proposed in the Companies' Smart Grid Modernization Business Plan, which was filed in Case No. 16-481-EL-UNC, the Companies would presumably seek recovery of a return of and return on any such grid modernization investments through Rider AMI, separate from and in addition to any customer money received under Modified Rider RRS.

[21] Tr. I at 63-64, 71, 176-77.

[22] FERC Order ¶ 60 (citing Order No. 697-A ¶¶ 188-89).

B. The Commission Should Reject Modified Rider RRS Because it is Not Authorized Under Ohio Law.

In its initial rehearing brief, Sierra Club explained that Modified Rider RRS cannot be approved as part of ESP IV because the rider is not authorized under any provision of R.C. 4928.143 and would qualify as an unlawful transition charge.[23] As such, the Commission must, as a matter of law, reject FirstEnergy's Modified Rider RRS proposal.[24] The Companies' initial rehearing brief provides no basis upon which to conclude otherwise.[25]

1. Modified Rider RRS is not related to limitations on customer shopping because it in no way limits such shopping.

In approving Rider RRS, the Commission concluded that the Rider qualified under R.C. 4928.143(B)(2)(d) because it purportedly is a "limitation[] on customer shopping for retail electric generation service"[26] that would "have the effect of stabilizing or providing certainty regarding retail electric service."[27] FirstEnergy has similarly attempted to shoehorn Modified Rider RRS into that provision in an attempt to find a statutory basis for the rider.[28] Sierra Club has already thoroughly explained why Modified Rider RRS does not qualify as a "limitation[] on

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[23] SC Br. at 8-18.

[24] *In re App. of Columbus S. Power Co.,* 128 Ohio St. 3d 512, 2011-Ohio-1788, 947 N.E.2d 655, ¶¶ 31-35 (Commission can only approve as an ESP provision items that are specifically listed in R.C. 4928.143(B)).

[25] FirstEnergy's initial rehearing brief does not provide any argument that Modified Rider RRS is related to bypassability or default service under R.C. 4928.143(B)(2)(d), or that it qualifies as an economic development of job retention program under R.C. 4928.143(B)(2)(i). Sierra Club has already explained in its initial rehearing brief why Modified Rider RRS could not be justified under any of those provisions. SC Br. at 12-14, 15-16.

[26] R.C. 4928.143(B)(2)(d).

[27] Order at 109.

[28] Mikkelsen Test. at 10; Companies' Memorandum in Support of Application for Rehearing ("Co. Rehearing App.") at 21 n.53.

customer shopping for retail electric generation service." Among other fatal shortcomings, this rider has nothing to do with retail electric service, as required by R.C. 4928.143.[29]

Although Sierra Club has already demonstrated that Modified Rider RRS cannot be authorized under (B)(2)(d), it is important to highlight one critical shortcoming that is evident from FirstEnergy's initial rehearing brief – namely that no party has identified any way in which Modified Rider RRS would place a "limitation" on customer shopping.

Where, as here, a "term [is] left undefined by statute[, it] is to be accorded its common, everyday meaning."[30] As the Ohio Court of Appeals has held, "the term 'limitation' in common usage is characterized by enforceable restrictions imposed upon the scope or exercise of a privilege or power."[31] Similarly, Ohio courts have relied on Black's Law Dictionary to conclude that a statutory reference to a "limitation" means a "restriction or restraint."[32]

Modified Rider RRS does not qualify as a "limitation" on customer shopping under R.C. 4928.143(B)(2)(d) because, as the record clearly establishes, the rider would not impose any restriction or restraint on the scope or exercise of a customer's ability to shop for retail electric generation service. As Ms. Mikkelsen acknowledged at hearing:

> Q. And the proposal does not place any restriction on the ability of retail customers to shop for their energy, correct?
>
> A. Yes.

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[29] Sierra Club incorporates by reference, as if fully set forth herein, the arguments made on pages 8-14 of its initial brief.

[30] *State v. Dorso*, 4 Ohio St.3d 60, 62, 446 N.E.2d 449 (1983).

[31] *Gross v. Ohio State Med. Bd.*, 10th Dist. Franklin No. 08AP-437, 2008-Ohio-6826, ¶¶ 35-36.

[32] *Clark v. State Med. Bd.*, 10th Dist. Franklin No. 14AP-212, 2015-Ohio-251, ¶ 16, *appeal not allowed*, 143 Ohio St.3d 1442, 2015-Ohio-3427, 36 N.E.3d 189. See also Ohio Admin. Code 4731-13-36(D), which defines "Limitation" in the context of state medical board disciplinary actions against medical certificate holders to mean "to preclude the certificate holder from engaging in a particular conduct or activity, to impose conditions on the manner in which that conduct or activity may be performed, or to require the certificate holder to abide by specific conditions in order to continue practicing medicine."

> Q. And the proposal does not change the price that a retail customer pays to its generation supplier, correct?
>
> A. Yes.
>
> Q. Okay. And that is true whether the customer is a shopping or nonshopping customer; is that correct?
>
> A. Yes.[33]

Similarly, OEG witness Steven Baron acknowledged in his rehearing testimony that:

> the modified Rider RRS would not harm retail shopping since the Rider would not prevent nor impose a *physical* limit on retail shopping in Ohio. Establishing the modified Rider RRS would not affect the amount of power that retail customers must buy from competitive retail electric service providers nor would it affect FirstEnergy's standard service offer auctions.[34]

As Mr. Baron explained at hearing, Modified Rider RRS would not "affect the level of shopping in terms of the -- the economic choices that customers would make."[35] Mr. Baron further conceded that Modified Rider RRS "doesn't impose any restrictions on shopping, and effectively it's neutral to shopping" because it "doesn't have any impact on the economics of shopping versus nonshopping."[36] In short, customers' ability to shop for their retail electric service would be unaffected by Modified Rider RRS. Therefore, even if Modified Rider RRS had some relationship to retail electric generation service – it does not – the rider cannot qualify as a "limitation[] on customer shopping for retail electric generation service" under R.C. 4928.143(B)(2)(d).

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[33] Tr. I at 49-50.

[34] Ohio Energy Group ("OEG") Ex. 4, Rehearing Testimony of Stephen J. Baron ("Baron Test.") at 3.

[35] Tr. II at 359.

[36] *Id.* at 360-62; *see also id.* at 369 (Mr. Baron agreeing that Modified Rider RRS would "not have an impact on the level of shopping and that it's effectively neutral to shopping," and that it "is not going to have an impact on the ability of any of the customers to shop" and "[n]or would it have an impact on the economic choice."); *Id.* at 370 (Mr. Baron acknowledging that Modified Rider RRS is "not going to change the pricing for a customer who is shopping").

FirstEnergy and OEG both attempt to conjure up "limitations" on customer shopping from Modified Rider RRS by claiming that the rider represents a "financial" limitation on shopping.[37] But this argument fails because Modified Rider RRS does not impose any type of limitation on customer shopping. For example, there is no "physical" limitation on shopping, as Modified Rider RRS does not prohibit any customer from shopping, does not restrict the amount or duration of such shopping, and does not restrain a customer's ability to shift back and forth between shopping and non-shopping. Similarly, Modified Rider RRS does not impose any "financial" limitations on shopping, as it does not establish an extra charge for customers who decide to shop or increase the price at which such shopping would occur. The record is clear that regardless of what form of limitation is being discussed, Modified Rider RRS does not impose "limitations on customer shopping" for purposes of R.C. 4928.143(B)(2)(d).

FirstEnergy and OEG theorize that Modified Rider RRS would lead to a financial "limitation[] on customer shopping" because a shopping customer's bill would no longer be 100% based on shopping but, instead, a portion of that bill would reflect the charge or credit under the modified rider.[38] This fanciful theory fails, however, because the fact that a shopping customer's bill would have an added charge or credit would in no way restrict or restrain the amount, cost, or duration of such shopping that is occurring. In past briefing, the Companies have essentially conceded as much, by claiming that Rider RRS would constitute a limit or restraint on the "consequences of shopping" on a customer's electric bill.[39] But the plain language of the statutory provision at issue requires "limitations on customer shopping" itself,

[37] Mikkelsen Test. at 10; Tr. I at 197; *see also* Co. Rehearing App. at 21 n.53 (claiming that Modified Rider RRS is a "financial limitation on shopping"). OEG witness Stephen Baron also made this "financial limitation" argument. *See* Baron Test. at 3.

[38] Tr. I at 197; Post-Hearing Brief of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company (filed Feb. 16, 2016) ("Co. Feb. 16 Br.") at 117-118.

[39] *Id*.

not a limitation on the impact or consequences of shopping on a customer's electric bill. While FirstEnergy may want to rewrite R.C. 4928.143(B)(2)(d) to meet its needs, the Commission cannot do so and, therefore, should reject any claim that Modified Rider RRS qualifies as a limitation on customer shopping.[40]

2. Modified Rider RRS would not "have the effect of stabilizing or providing certainty regarding retail electric service."

Even if the Modified Rider RRS proposal could satisfy the threshold requirements discussed in Section I.B.1 above – it cannot – the rider could not be approved under R.C. 4928.143(B)(2)(d) because it would not "have the effect of stabilizing or providing certainty regarding retail electric service."[41] In its initial rehearing brief, FirstEnergy never specifically argues that Modified Rider RRS satisfies that statutory provision, but the Companies repeatedly assert that Modified Rider RRS will promote retail rate stability by protecting customers against "rate volatility and price fluctuations."[42] In doing so, FirstEnergy necessarily relies on the Commission's finding in its March 31 Order that Rider RRS would "in theory" serve to stabilize or provide certainty regarding retail rates,[43] and then claims that Modified Rider RRS will provide a "more reliable hedge against increasing market prices"[44] because all the factors that go into calculating charges and credits are fixed except market energy and capacity prices.[45]

[40] As Sierra Club explained in its initial rehearing brief, any type of customer charge could qualify under FirstEnergy and OEG's "financial limitation" theory. SC Br. at 11. As such, the Commission should also reject that theory because it would improperly remove any substantive limit on what an ESP may contain. *In re App. of Columbus S. Power Co.*, 128 Ohio St.3d 512, 2011-Ohio-1788, 947 N.E.2d 655, ¶ 34.

[41] *See* SC Br. at 14, 32-37.

[42] Co. Br. at 1, 2, 7.

[43] Order at 109.

[44] Co. Br. at 16.

[45] *Id.* at 7, 16; Mikkelsen Test. at 2-4, 6, 10, 12, 19-20.

FirstEnergy's claims fail to establish that Modified Rider RRS would "have the effect of stabilizing or providing certainty regarding retail electric service" for three reasons that Sierra Club has explained in its initial rehearing brief. First, Modified Rider RRS is wholly unrelated to and does not in any way impact the electricity that the Companies' customers receive or the rates that they pay for such electricity. As such, Modified Rider RRS cannot be found to provide any stability regarding such "retail electric service" and its rates.[46] Second, the record remains bereft of any evidentiary showing that customers have faced retail price volatility, that they will face such volatility over the proposed term of Modified Rider RRS, or that the rider would be an effective tool in mitigating any volatility that might occur.[47] Third, as discussed in Section I.C.1 below, the most credible and up-to-date information shows that under Modified Rider RRS customers would almost certainly lose hundreds of millions to billions of dollars between now and May 31, 2024.[48] As such, the evidence shows that Modified Rider RRS would provide customers with rate increases, not rate stability and certainty.

In its initial rehearing brief, FirstEnergy attempts to bolster its unsupported rate stability claims by citing to OEG witness Stephen Baron's contention that Modified Rider RRS would "provide[] a fixed price for the generation component for 40 percent of a customer's usage."[49] But this contention is misleading because, while Mr. Baron refers multiple times to Modified Rider RRS leading to 40% of customers' bills being based on "guaranteed" or "fixed" rates and pricing,[50] the proposed rider would do nothing of the sort. In particular, while the hypothetical costs and generation levels that would be used in calculating charges and credits under Modified

[46] SC Br. at 14.

[47] *Id.* at 32-37.

[48] *Id.* at 19-32.

[49] Co. Br. at 8 (citing Tr. II at 352).

[50] Baron Test. at 7-8; *see also id.* at 5.

Rider RRS are fixed, the energy and capacity prices that are a key factor in such calculations are not fixed.[51] As a result, the rates or pricing that customers would actually incur under Modified Rider RRS are not "guaranteed" or "fixed" but, instead, are subject to the risk that market energy and/or capacity prices will be significantly different than what the Companies forecasted. Mr. Baron's claim regarding 40% of customers' rates or pricing being "guaranteed" or "fixed" leaves out a critical source of risk that customers would be incurring under Modified Rider RRS and, therefore, is irrelevant to the question of whether Modified Rider RRS would provide any retail electric rate stability or certainty.[52]

3. Modified Rider RRS would be an unlawful transition charge.

Another major development that has occurred since the Commission approved Rider RRS is that the Ohio Supreme Court rejected as unlawful transition charges the so-called rate stability riders that the Commission had approved as part of ESPs for AEP and Dayton Power & Light ("DP&L").[53] As Sierra Club explained in its initial rehearing brief, Modified Rider RRS would similarly be an unlawful transition charge.[54] As such, it would be unlawful and unreasonable for the Commission to approve Modified Rider RRS.

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[51] As Mr. Baron acknowledged, charges and credits under Modified Rider RRS would be based, in part, on wholesale energy and capacity prices. Tr. II at 298-300.

[52] Mr. Baron presents in his rehearing testimony [redacted] Baron Test. at 7, Fig. 3. Mr. Baron is wrong in suggesting that the information presented in Figure 3 reflects "cost-based rates that FirstEnergy proposes to guarantee through the modified Rider RRS." *Id.* at 7. [redacted].

[53] *In re App. of Columbus S. Power Co.*, Slip Opinion No. 2016-Ohio-1608 (Apr. 21, 2016); *In re App. of Dayton Power & Light Co.*, Slip Opinion No. 2016-Ohio-3490 (June 20, 2016).

[54] SC Br. at 17-19.

Earlier in this proceeding, FirstEnergy relied heavily on the Commission's now-invalidated approval of the AEP and DP&L riders in urging the Commission to reject a transition charge challenge to Rider RRS.[55] Given that the Ohio Supreme Court has concluded that these riders are unlawful transition charges, Staff correctly note the "significant risk" that the Court would also find that Modified Rider RRS is an unlawful transition charge.[56]

In its initial rehearing brief, FirstEnergy offers three reasons why Modified Rider RRS would purportedly not be an unlawful transition charge. None holds water. First, the Companies contend that Modified Rider RRS cannot be a transition charge because the transition to market-based rates already occurred.[57] But the Ohio Supreme Court has made clear that the bar against transition revenue applies not only to costs that were stranded during the transition to market.[58] Instead, any charge "that amounts to transition revenue by another name" is also prohibited.[59] As such, the simple fact that FirstEnergy has transferred its generating assets and shifted to market-based SSO pricing for its customers does not mean thatthe Modified Rider RRS revenues are not transition revenues. As Sierra Club has explained, that is precisely what these revenues are.

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[55] Post-Hearing Reply Brief of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company (filed Feb. 26, 2016) ("Co. Feb. 26 Reply Br.") at 283 & n.1384 (citing Case No. 11-346-EL-SSO, Opinion and Order, 32 (Aug. 8, 2012); Case No. 12-426-EL-SSO, Opinion and Order, 22 (Sept. 4, 2013)).

[56] Post-Hearing Brief Submitted on Behalf of the Staff of the Public Utilities Commission of Ohio, filed Aug. 15, 2016 ("Staff Br.") at 3-4.

[57] Co. Br. at 17-19.

[58] *In re App. of Columbus S. Power Co.*, Slip Opinion No. 2016-Ohio-1608 ("*Columbus Southern Power*" or "2016-Ohio-1608"), ¶ 21 (citing R.C. 4928.38).

[59] *Id.*; *See also In re App. of Dayton Power & Light Co.*, Slip Opinion No. 2016-Ohio-3490.

The Companies' contention that Modified Rider RRS "has no relationship to 'transition revenues'" because it is a "hedge for market prices" similarly fails.[60] In the Companies' telling, transition charges would exist only if the Companies were recovering their own "generating plant costs" or "the difference between . . . actual generating plant costs and the forecasted market value of those costs."[61] But nothing in *Columbus Southern Power* – where the Ohio Supreme Court conducted a record-based inquiry into the actual basis and purpose of the rider – suggests that such an "overly narrow definition of transition revenue" should apply.[62] And, regardless, the Companies have already conceded enough on the record to demonstrate the true nature of Modified Rider RRS as a transition charge. Just as in *Columbus Southern Power*, the charges under the rider are calculated "to achieve a certain rate of return on [FES's] generation assets" based on a pre-determined rate of return on Sammis and Davis-Besse.[63] In addition, as discussed in Section I.A, there is strong evidence that the revenues collected under Modified Rider RRS would be used the same way the Rider RRS charges would have – to support the merchant generation owned by FES, the Companies' unregulated affiliate. Simply pretending that Modified Rider RRS is about providing rate stability to the Companies' customers does not change the fact that Modified Rider RRS charges would qualify as transition charges the collection of which are barred by R.C. 4928.38.[64]

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[60] Co. Br. at 18-19.

[61] *Id.*

[62] 2016-Ohio-1608, ¶ 21.

[63] *Id.* ¶ 23.

[64] FirstEnergy contends that Staff's concern that Modified Rider RRS constitutes a transition charge is undermined by the fact that Staff did not find Rider RRS to be a transition charge. Co. Br. at 17-18. But FirstEnergy's contention ignores the critical fact that since the approval of Rider RRS the Ohio Supreme Court specifically found that two similar riders that were portrayed as providing rate-stability were actually unlawful transition charges. Regardless of whether the Staff, Commission, or any other entity should have found Rider RRS to be an unlawful transition charge at the time of the March 31 Order, the

Finally, FirstEnergy suggests that Modified Rider RRS is not an unlawful transition charge because there are numerous other generation riders that are not transition charges.[65] But this ignores a key distinction between Modified Rider RRS and the other generation riders that FirstEnergy identifies. In particular, those other generation riders are all designed to recover costs that the Companies have or will incur in order to provide retail electric service to their customers. By contrast, Modified Rider RRS is not designed to recover any costs incurred by the Companies. Instead, it is simply a way to generate extra revenue from customers (at least for the first couple of years, and likely for the entire term, of the rider) and to shift energy and capacity price risks to customers. In *Columbus Southern Power*, the Court concluded that AEP's supposed "rate stability" rider was improper because it allowed the company to recover more than its actual capacity costs.[66] In the present situation, there are not even any actual costs to the Companies that Modified Rider RRS would be based on. Given that the Court found the collection of revenues that exceed capacity costs problematic, FirstEnergy's proposal to collect revenues that are not based on any actual costs incurred by the Companies to provide service to its customers is equally if not more problematic.

C. Modified Rider RRS is Not Just, Reasonable, or Beneficial to Customers.

Throughout the rehearing process, FirstEnergy has steadfastly maintained that its projection of a $561 million nominal ($260 million NPV)[67] net benefit and/or the Commission's

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Ohio Supreme Court's rulings since that Order explain and, in fact, compel the conclusion now that Modified Rider RRS (and Rider RRS) are unlawful transition charges.

[65] Co. Br. at 19. In particular, the Companies identify the Generation Service Rider ("Rider GEN"), Generation Cost Reconciliation Rider ("Rider GCR"), Alternative Energy Resource Rider ("Rider AER"), and Non-Distribution Uncollectible Rider ("Rider NDU"), as non-transition charge generation riders.

[66] 2016-Ohio-1608, ¶¶ 32-37.

[67] SC Ex. 89; Mikkelsen Test. at 3-4.

projection of a $256 million nominal[68] ($37 million NPV)[69] net benefit provide a valid basis for evaluating Modified Rider RRS. The record, however, establishes that these projections, which are based on Judah Rose's market price forecasts from mid-2014: (1) were unreasonable and against the manifest weight of the evidence at the time of the Commission's March 31 Order, (2) are even more unreasonable and against the manifest weight of the evidence today, and (3) are inherently inconsistent with the Companies' testimony regarding the DMR proposal.[70]

A full assessment, based on up-to-date information, of likely costs to customers under Modified Rider RRS has been hindered by the Attorney Examiners' striking of large portions of the rehearing testimony of witnesses Comings, Kalt, and Wilson.[71] Using up-to-date market forecasts, those witnesses projected customer losses of $1.3 billion to $3.6 billion over the full term of Modified Rider RRS.[72] As Sierra Club explained in its initial rehearing brief, [73] the rulings excluding such testimony should be reversed so that Modified Rider RRS can be evaluated based on a complete and up-to-date assessment of charges and credits that customers would likely incur.[74]

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[68] Co. Br. at 6, 8, 15, 19.

[69] Sierra Club's Application for Rehearing ("SC Rehearing App.") at 22-24.

[70] SC Br. at 19-28.

[71] Tr. IV at 780, 801-03, 861-65, 875; Tr. V at 1127-30, 1149-51.

[72] SC Ex. 100 & 101c, Rehearing Testimony of Tyler Comings ("Comings Test."), at 21; P3-EPSA Ex. 17, Rehearing Testimony of Joseph P. Kalt, at 17-18; OCC/NOAC Ex. 1, Rehearing Direct Testimony of James F. Wilson, at 12-13.

[73] SC Br. at 28-32.

[74] FirstEnergy's earlier dismissal of Mr. Comings, Dr. Kalt, and Mr. Wilson as "dilettantes" whose projections are purportedly not "worthy of equal weight" with Mr. Rose's (Co. Feb. 26 Reply Br. at 86-90), is rich with irony given that real world developments have shown those three experts' testimony regarding likely trends in market prices to be far more accurate than Mr. Rose's. FirstEnergy suggests that Mr. Rose's forecasts are beyond reproach because he is "one of the foremost experts" in his field who uses "sophisticated computer modeling" from ICF International. Co. Feb. 26 Reply Br. at 25, 88. But the record thoroughly demonstrates that Mr. Rose's energy, capacity, and natural gas price forecasts in this proceeding have turned out to be unreliable and demonstrably wrong. *See, e.g.*, SC Br. at 21. In addition,

But even based only on the updated actual market energy prices and forwards through 2018 that were admitted during the rehearing, the unrebutted evidence shows that customers would likely lose at least $1.130 billion nominal ($965 million NPV) through the end of 2018 under Modified Rider RRS.[75] These losses exceed the credits to customers under Modified Rider RRS for 2019 through May 31, 2024, of $976 million nominal ($623 million NPV) that the Companies projected.[76] So, even if all of the net credits that the Companies' projected for 2019 through May 31, 2024, materialized, current market energy price forwards through 2018 show that customers would incur a net loss of $154 million nominal ($342 million NPV) over the life of Modified Rider RRS.[77] And there is little reason to believe that the levels of credits projected by the Companies for 2019 through May 31, 2024, will materialize given that actual PJM capacity prices for 2018/2019 and 2019/2020 are considerably lower than Mr. Rose projected,[78] and there is no basis in the record upon which to reasonably conclude that capacity and energy prices will escalate to the elevated levels that Mr. Rose forecast for the latter years of Modified Rider RRS.[79] As such, actual customer costs over the life of Modified Rider RRS would likely be considerably higher than the $154 million nominal ($342 million NPV) figure shown just by

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the record demonstrates that Mr. Rose has a lengthy and consistent track record of market forecasts that end up being significantly too high. Post-Hearing Reply Brief of the Sierra Club at 23-29. So, either Mr. Comings, Dr. Kalt, and Mr. Wilson are not the "dilettantes" that FirstEnergy dismisses them as, or ICF and Mr. Rose's "sophisticated computer modeling" has a significant problem (or both). Either way, the Commission should reject any argument by FirstEnergy that the opinions and testimony of Mr. Comings, Dr. Kalt, and Mr. Wilson should be dismissed or given less weight than that of Mr. Rose.

[75] P3-EPSA Ex. 19; SC Br. at 23-24.

[76] SC Ex. 89; Tr. I at 78.

[77] While FirstEnergy's counsel tried to cast doubt on the use of market forwards, the Companies' own witness Judah Rose acknowledged throughout this proceeding that the use of market forwards for a two to three year period is appropriate. Staff witness Dr. Choueiki provided similar testimony in response to questioning from FirstEnergy's counsel. Tr. V at 1232.

[78] Compare OEG Ex. 6 to Co. Ex. 25c, Lisowski Workpapers at page 5 line 2.

[79] SC Br. at 26.

using current market energy forwards through 2018. Either way, the unrebutted evidence shows that Modified Rider RRS would be a net cost to customers and, therefore, Modified Rider RRS is not just, reasonable, or beneficial to customers.

1. Continued reliance on the Companies' 2014 market forecasts and projections is unreasonable and against the manifest weight of the evidence.

In their initial brief on rehearing and rehearing testimony, the Companies urge the Commission to turn a blind eye to the clear evidence that, based on up-to-date information regarding actual and forward market prices, customers would lose money under Modified Rider RRS. Instead, the Companies claim that the previous projections of a net credit under Rider RRS can continue to be relied upon because the proposed modifications to the rider would not change those projections.[80] What FirstEnergy has not done, however, is present any basis for relying, in the fall of 2016, on forecasts from mid-2014 that real world conditions show to be outdated, unreliable, and wrong. In fact, the Companies' initial rehearing brief, rehearing testimony, and rehearing rebuttal do not even attempt to argue that continued reliance on the mid-2014 forecasts is reasonable. Given that such continued reliance is plainly unreasonable, FirstEnergy's silence on this issue is perhaps not surprising. But it is fatal to their contention that Modified Rider RRS would somehow be beneficial to customers.

The unreasonableness of continued reliance on the mid-2014 forecasts is further shown by looking back at arguments that FirstEnergy made during the Rider RRS stage of this proceeding. In particular, when faced with evidence then that Mr. Rose's forecasts were outdated, unreliable, and wrong, the Companies attempted to explain away such evidence with arguments that, regardless of whether they were reasonable then, are patently meritless now.

[80] Co. Br. at 7-8; Mikkelsen Test. at 10-11.

For example, in the post-hearing briefing on Rider RRS, the Companies claimed that "[b]y any measure, Mr. Rose's capacity price forecast has held up extremely well"[81] despite the fact that his forecasted capacity price for the 2018/2019 delivery year was [redacted] than actual results.[82] In support, FirstEnergy asserted that the 38% increase in actual capacity prices between 2017/2018 and 2018/2019 was "in line with Mr. Rose's forecast"[83] of a [redacted].[84] According to FirstEnergy, the difference between Mr. Rose's forecasted increase and actual results was "unremarkable,"[85] especially because prices would purportedly catch up to Mr. Rose's forecast in the future.[86] When confronted with a 2015 ICF publication setting forth a "plausible scenario" that capacity prices would be lower in 2019/2020 than in 2018/2019,[87] the

[81] Co. Feb. 26 Reply Br. at 50.

[82] SC Rehearing App. at 27.

[83] Co. Feb. 26 Reply Br. at 56.

[84] Co. Ex. 25c, Lisowski Workpapers at page 5 line 2.

[85] Co. Feb. 26 Reply Br. at 55. The difference between Mr. Rose's forecasted capacity price and the actual capacity price for 2018/2019 would alone lead to [redacted] revenue. While that amount of money might be "unremarkable" to FirstEnergy, it is not to the customers whose pocketbooks would be put on the line by Modified Rider RRS. We calculated the [redacted] figure as follows: [redacted]

[86] FirstEnergy pointed to a PJM Base Scenario Analysis that purports to estimate the capacity price if the 2018/2019 auction had been 100% capacity performance product rather than only 80% to claim that the significant capacity price increase forecast by Mr. Rose is still coming. *Id.* at 55 & n.198 (citing Co. Ex. 169). PJM, however, has provided no explanation for how the capacity price was projected in that hypothetical scenario. Jan. 19, 2016 Tr. (Vol. XXXVIII) at 8140-41. And both PJM and FERC have made clear that the reason for transitioning in the capacity performance product over five years, rather than having a 100% capacity performance auction for 2018/2019, was to "allow resources to make gradual improvements" so as to "reduce the burdens such improvements may impose" and to minimize exactly the kind of price spikes that Mr. Rose erroneously projected. *See In re PJM Interconnection LLC, Order on Proposed Tariff Revisions*, Docket Nos. ER15-623-000, EL15-29-000, ER15-623-001, and EL15-41-000, 151 FERC ¶ 61,208, at ¶¶ 214, 253 (June 9, 2015); *see also* Jan. 19, 2015 Tr. (Vol. XXXVIII) at 8140. Contrary to FirstEnergy's claim, Co. Feb. 26 Reply Br. at 56 n.200, the fact that Sierra Club has entered other PJM documents into evidence does not cure FirstEnergy's misinterpretation and misapplication of the PJM Base Scenario Analysis.

[87] SC Ex. 87.

Companies dismissed that scenario as merely "illustrative," "conservative," and "low end."[88] FirstEnergy reacted similarly to Sierra Club's observation that PJM capacity prices have never increased for more than three years in a row in disputing Mr. Rose's forecast that such prices would [redacted].[89] FirstEnergy dismissed this argument on the grounds that it "does little more than reveal Sierra Club's failure to understand the nature of forecasts."[90]

Regardless of the merits of this capacity price debate at the time of the post-hearing briefing, it is now clear that FirstEnergy's arguments do not hold water. In contrast to FirstEnergy's claim that capacity prices would [redacted], in May 2016 PJM reported the results of the 2019/2020 capacity auction at $100/MW-day, which is nearly 40% lower than the result for the 2018/2019 auction.[91] Mr. Rose's forecasted price of [redacted] for the 2019/2020 delivery year is [redacted] than the actual result.[92] And while Mr. Rose forecast that the capacity price would [redacted] between the 2017/2018 and 2019/2020 delivery years,[93] the capacity price has declined by nearly 17% over that time period.[94] Even if FirstEnergy's claim that "[b]y any measure, Mr. Rose's capacity price forecast has held up extremely well"[95] had been reasonable at the time of the Rider RRS briefing, there is

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[88] Co. Feb. 26 Reply Br. at 57-58.

[89] Initial Post-Hearing Brief of the Sierra Club at 37-38; Co. Ex. 25c, Lisowski Workpapers at 1 line 2.

[90] Co. Feb. 26 Reply Br. at 58.

[91] OEG Ex. 6.

[92] Co. Ex. 25C, Lisowski Workpapers at page 5 line 2.

[93] *Id.* Mr. Rose's 2019/2020 forecasted capacity price of [redacted] the actual 2017/2018 capacity price of $120/MW-day.

[94] The 2019/2020 capacity price of $100/MW-day is approximately 17% lower than the $120/MW-day price for the 2017/2018 delivery year.

[95] Co. Feb. 26 Reply Br. at 50.

simply no basis upon which one could still reasonably make that claim today.[96] As such, continued reliance on Mr. Rose's mid-2014 capacity price forecast, or any projections growing out of that forecast, would be unjust, unreasonable, and against the manifest weight of the evidence.

A similar dynamic can be seen with regards to Mr. Rose's natural gas and energy price forecasts. In particular, FirstEnergy dismissed intervenors' testimony about actual natural gas prices being substantially lower than Mr. Rose assumed as "extremely short-sighted" because the testimony purportedly relied on prices during a warmer-than-average December 2015.[97] According to the Companies, such low natural gas prices reflected nothing more than short-term volatility that has only a "negligible" impact on long-term natural gas prices and a "*de minimus*" impact on energy prices.[98] Therefore, the Companies claimed, there was no basis for rejecting Mr. Rose's natural gas and energy price forecasts.

FirstEnergy's critique was inaccurate at the time it was made, as Sierra Club's testimony relied not on gas prices for a short period in December 2015 but, among other things, on actual 2015 prices through November of that year, along with forwards prices for 2016 and 2017.[99] Regardless, we now have post-December 2015 data that can be used to test the Companies'

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[96] In support of the unreasonableness of continued reliance on Mr. Rose's mid-2014 capacity price forecast, Sierra Club also proffers ICF's Fall 2015 capacity price forecast, which was publicly disclosed in an Integrated Resource Plan that Dominion Energy filed with the Virginia Corporation Commission in April 2016. *See* Comings Test. at Ex. TFC-46. As witness Comings explained, ICF's Fall 2015 forecast shows that ICF's capacity price "outlook has obviously changed." *Id.* at 18-19. While the Attorney Examiners granted FirstEnergy's motion to strike this forecast and testimony from the record, the Commission should reverse that ruling and admit such evidence and testimony into the record for the reasons set forth at pages 28 to 32 of Sierra Club's initial brief on rehearing.

[97] Co. Feb. 26 Reply Br. at 35.

[98] *Id.* at 36, 41.

[99] In fact, in contrast to FirstEnergy's claim that the intervenors "apparently" relied on December 2015 natural gas prices "to make their criticisms," *id.* at 35, Mr. Comings's testimony specifically noted that his comparison of natural gas prices did "not even incorporate more recent drops in natural gas prices in December 2015." SC Ex. 95, Third Supplemental Testimony of Tyler Comings, at 8-9.

claims. And that data shows that while natural gas prices have increased above the 16-year lows experienced in December 2015, they have just returned to essentially the same level they were at in 2015 before the unseasonably warm winter.[100] In contrast to Mr. Rose's assumption that natural gas prices would average $4.34/mmBtu in 2015 and $4.28/mmBtu in 2016,[101] there has not been even a single day in 2016 when natural gas prices cleared $3/mmBtu.[102] In fact, the last time the daily natural gas price exceeded $3/mmBtu was May 20, 2015, and the daily price has not exceeded $4/mmBtu since December 1, 2014.[103] FirstEnergy's claim – that intervenors' testimony regarding lower than forecasted natural gas prices can be dismissed as nothing more than short-term volatility – is meritless.

Currently available evidence also undermines FirstEnergy's claims that Mr. Rose's longer term natural gas and energy price forecasts remain valid. For example, Sierra Club proffers the NYMEX natural gas price forwards of $3.07/mmBtu in 2017 and $3.00/mmBtu in 2018.[104] Mr. Rose's natural gas price projections for 2017 and 2018 [redacted] those NYMEX forwards by [redacted] and [redacted], respectively.[105] Similarly, energy market forwards for the AEP Dayton Hub as of March 2016 were [redacted] for 2016 through 2018, compared to FirstEnergy's forecast of [redacted]

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[100] *See* EIA, Henry Hub Natural Gas Spot Price, *available at* https://www.eia.gov/dnav/ng/hist/rngwhhdD.htm, which the Attorney Examiners took administrative notice of at Tr. V at 1190.

[101] Co. Ex. 17, Direct Testimony of Judah L. Rose, at 47.

[102] *See* EIA, Henry Hub Natural Gas Spot Price, *available at* https://www.eia.gov/dnav/ng/hist/rngwhhdD.htm, which the Attorney Examiners took administrative notice of at Tr. V at 1190.

[103] *Id.*

[104] Comings Test. at 8. While the Attorney Examiners granted FirstEnergy's motion to strike Mr. Comings's presentation of these market forwards from the record, the Commission should reverse that ruling and admit such evidence and testimony into the record for the reasons set forth at pages 28 to 32 of Sierra Club's initial brief on rehearing.

[105] Co. Ex. 20c, Rose Direct Testimony Workpapers, at 4.

[redacted].[106] Similarly, Dr. Choueiki testified that [redacted].[107]

The unreasonableness of continued reliance on Mr. Rose's mid-2014 market forecasts is also shown by the numerous more recent natural gas and energy price forecasts that Mr. Comings relied on in his rehearing testimony and which Sierra Club hereby proffers.[108] As Mr. Comings explained, there are at least three more recent natural gas price forecasts from ICF that "provide further evidence that the mid-2014 ICF forecast is outdated and should not be relied on in evaluating the Modified Rider RRS in June 2016."[109] Each of those forecasts predict [redacted] natural gas prices than in Mr. Rose's forecast, as do more recent forecasts from PJM and the U.S. Energy Information Administration ("EIA").[110] Similarly, a PJM market energy price reported in a May 2016 PJM analysis shows prices that are [redacted] than what Mr. Rose forecast.[111]

Consistent with the market prices, forwards, and forecasts discussed above, Staff witness Dr. Choueiki testified unequivocally at the hearing that the "Staff does not agree with the [C]ompanies' projections" as to the overall credit or charge under Modified Rider RRS.[112] Dr. Choueiki also made clear that he "did not say that at this point in time, in July of 2016, we are

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[106] P3-EPSA Ex. 20c, Att. JPK-RH-1.

[107] Tr. V Confidential at 1201.

[108] While the Attorney Examiners granted FirstEnergy's motion to strike these forecasts and Mr. Comings' accompanying testimony from the record, the Commission should reverse that ruling and admit such forecasts and testimony into the record for the reasons set forth at pages 28 to 32 of Sierra Club's initial brief on rehearing

[109] Comings Test. at 8.

[110] *Id.* at 8-11.

[111] *Id.* at 13-14.

[112] Tr. IV at 986.

now accepting the [C]ompanies' forecasts."[113] The Commission should similarly decline to accept Mr. Rose's mid-2014 forecasts and any projections based in whole or in part on those forecasts, as the evidence is clear that continued reliance on such forecasts and projections would be unjust, unreasonable, and against the manifest weight of the evidence.

2. The credibility of the Companies' claim that customers would receive a net credit under Modified Rider RRS is undermined by the Companies' testimony regarding the DMR proposal.

As Sierra Club explained in its initial rehearing brief, the credibility of the Companies' testimony is called into question by an inherent inconsistency between the claim that Modified Rider RRS would provide customers with a net credit and the assertion that those same customers need to pay substantial sums of money to the Companies under the DMR.[114] In particular, while the Companies concede that customers would lose money under Modified Rider RRS through 2018, they claim that a net credit would be provided to customers over the life of the rider because Modified Rider RRS would result in a credit of $976 million nominal ($623 million NPV) from 2019 through May 31, 2024.[115] Such credits would represent an equivalent reduction in revenues received by the Companies. Yet in response to Staff's DMR proposal, the Companies claim that they need to receive at least $558 million per year in additional revenue from their customers through May 31, 2024, in order to provide credit support to FirstEnergy Corp. and the Companies. Similarly, while the Companies claim that they could satisfy whatever smart grid investments are needed despite receiving significantly less revenue under Modified Rider RRS,[116] they then justify their proposal to extend the DMR through May 31,

[113] *Id.* at 979.

[114] SC Br. at 27-28, 57-60

[115] SC Ex. 89; Tr. I at 78.

[116] Tr. I at 80-81, 90-91.

2024, in part on the ground that they need the revenue to fund smart grid investments throughout the term of ESP IV.[117]

The Companies do not attempt to explain these inherent inconsistencies in their initial rehearing brief but, instead, double down on them. In particular, with regards to Modified Rider RRS, the Companies state that:

- "any future reduction in the revenues from Rider RRS will not affect the Companies' ability to fulfill their grid modernization commitments"[118]

- "to the extent necessary, FirstEnergy Corp. (as history has shown) could provide equity to the Companies in order to maintain their investment grade status."[119]

- "Looking at the Proposal with all other ESP IV components as a whole over eight years, the Companies expect to remain above investment grade."[120]

Yet with regards to the DMR proposal, FirstEnergy maintains that it needs to receive at least $558 million per year through May 31, 2024, because:

> The need for Rider DMR to have a term coincident with ESP IV is apparent from the Companies' significant cash requirements over the term of ESP IV. Recent experience does not support Staff's belief that three years is sufficient credit support for the Companies.[121]

These two sets of statements are obviously contradictory and strongly suggest that either (or both) the Companies do not really believe their projection that customers would receive nearly a billion dollars in credits under Modified Rider RRS from 2019 through May 31, 2024, or the Companies do not really have "significant cash requirements" that can only be satisfied by

[117] This latter claim is especially disingenuous given that, as explained in Section II below, the Companies steadfastly refuse to commit to spending any revenues they may receive under the DMR on distribution modernization.

[118] Co. Br. at 13.

[119] *Id.*

[120] *Id.* at 20.

[121] *Id.* at 39.

customers paying at least $558 million per year through May 31, 2024. In addition, if history shows that FirstEnergy Corp. would provide equity to make up any credit problems that might be created by the projected reduction in revenues received by the Companies under Modified Rider RRS,[122] then why do customers need to pay at least $558 million per year under the DMR in order to provide credit support to both the Companies and FirstEnergy Corp.? Unfortunately, the Companies' brief fails to even acknowledge these inherent inconsistencies, much less attempt to explain them.[123]

These inherent inconsistencies further demonstrate why it would be unjust, unreasonable, and against the manifest weight of the evidence for the Commission to rely, in whole or in part, on the Companies' projection of credits and charges in evaluating Modified Rider RRS.

II. The Commission Should Reject the Proposed Distribution Modernization Rider as Unlawful, Unjust, and Unreasonable.

In their June 29, 2016 rehearing testimony, the Staff proposed an entirely new rider, the so-called Distribution Modernization Rider ("DMR"), under which customers would pay FirstEnergy $131 million per year for three years and which FirstEnergy could seek to extend for two additional years.[124] Seeing a new opportunity to collect additional revenues from its

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[122] *Id.* at 13.

[123] The unreasonableness of these two sets of statements is further heightened by the fact that the Modified Rider RRS proposal was reviewed by Steven Staub, who serves as the Treasurer of both FirstEnergy Corp. and the Companies, before it was filed. Tr. I at 237-38. Plainly, the Treasurer of the Companies and FirstEnergy Corp. should know if those entities are facing credit metric shortfalls that significant additional revenues are needed to address. And if such shortfalls are expected, then it makes absolutely no sense to make a proposal that is projected to reduce the Companies' revenues by $976 million nominal ($623 million NPV) unless the Companies do not really expect such projected revenue reductions (in the form of credits to customers) to materialize.

[124] While Staff testimonies all described the DMR proposal as being for three years with the possibility of an additional two years, the Staff's initial rehearing brief creates a bit of confusion regarding the duration proposed for the DMR. In particular, the Staff brief says:

> Staff recommends three years with the possibility of a two year extension. This is a sufficient time to allow for the other additional steps

customers, FirstEnergy advocates for modifications to the DMR proposal under which customers would pay at least $558 million, and possibly as much as $1.126 billion, per year through the term of ESP IV.

As Sierra Club detailed in its initial rehearing brief, the Commission cannot approve the DMR, either as proposed by Staff or as modified by FirstEnergy, because it is legally unjustified and has not been shown to be just, reasonable, or beneficial to customers. In particular, the DMR proposal is fundamentally flawed in at least five ways:

- The Commission lacks jurisdiction to consider the DMR, which is an entirely new proposal beyond the scope of the rehearing process;

- As proposed, there is no assurance that the DMR revenues would fund distribution modernization initiatives or otherwise be spent within the Companies for the benefit of customers;

- The DMR is not authorized under R.C. 4928.143 or any other provision of Ohio law;

- The DMR is unjust, unreasonable, and not beneficial to customers as they would lose hundreds of millions to billions of dollars with no assurance of any quantifiable benefits in exchange; and

- The DMR would run afoul of the FERC Order because it would enable FirstEnergy to achieve the same siphoning of customer money to benefit FirstEnergy Corp., its shareholders, and unregulated affiliates that would have been achieved under the initial Rider RRS and Affiliate PPA plan that FERC put a hold on.

Nothing in the Staff and Companies' initial rehearing briefs demonstrate otherwise. In fact, not only do those briefs fail to overcome any of the fundamental flaws summarized above, in many

> to be taken. Should circumstances at that time still present a barrier to grid modernization implementation, the companies could file an application for an additional period of two years.

Staff Br. at 7 (citation omitted). Sierra Club assumes that the "additional period of two years" referenced in the last sentence is the same as the possible two year extension identified in the first sentence, as opposed to being a potential for an additional two years beyond that extension. If that assumption is incorrect, the possibility of the DMR lasting for seven years would make the proposal even more unjust, unreasonable, and costly for customers.

ways they actually confirm or strengthen the bases for concluding that the DMR proposal is unlawful, unjust, and unreasonable.

A. The Commission Lacks Jurisdiction to Consider the DMR Proposal on Rehearing.

The Commission lacks jurisdiction to consider the DMR proposal because it is not a proper issue for rehearing under R.C. 4903.10.[125] In particular, a rehearing is statutorily limited to reconsideration of matters that the Commission already "determined in the proceeding," based on evidence that could not, "with reasonable diligence" have been offered in the original hearing, so that the Commission can decide whether to "abrogate or modify" its order.[126] By contrast, a rehearing is not a proper mechanism for evaluating and approving an entirely new rider proposal that has no connection to the issues that had been debated for nearly 21 months in this proceeding. Yet, as Sierra Club detailed in its initial rehearing brief,[127] that is exactly what the DMR proposal is.

In their initial rehearing briefs, neither Staff nor the Companies provide any argument regarding whether the DMR proposal is a proper issue for rehearing. However, the Staff, perhaps inadvertently, effectively conceded that the DMR should not be considered on rehearing by noting that, in proposing the DMR, they "introduced an entirely new concept into this proceeding."[128] That description is correct, because the DMR, in comparison to Rider RRS, involves a different mechanism that leads to different costs for customers, is presented on the

[125] SC Br. at 41-43.

[126] R.C. 4903.10.

[127] SC Br. at 41-43.

[128] Staff Br. at 5.

basis of different rationales, and purports to provide different benefits.[129] Staff's concession also demonstrates why the DMR proposal is not simply a modification to an existing order but is instead an entirely new proposal that would have to be evaluated in a new proceeding.

In addition to being unauthorized under R.C. 4903.10, the consideration of the DMR proposal on rehearing is also problematic because the expedited rehearing process does not provide for a full and fair evaluation of the proposal. In particular, the Companies' Rider RRS proposal and modifications thereto were debated for nearly two years with extensive discovery, multiple rounds of testimony, and 41 days of hearing. By contrast, the DMR proposal was first made by Staff on June 29, 2016, was significantly expanded in both amount and duration on July 25, and the record closed on August 1. During that less than five week period, no written discovery on any of the issues surrounding the DMR occurred, and intervenors were provided four day's notice of the July 15 deadline for rebuttal testimony regarding the DMR.[130] As a result of this highly expedited timeline, the evidentiary record is severely lacking on issues critical to the full and fair evaluation that would have to occur before customers could be required to pay hundreds of millions to billions of dollars to FirstEnergy. For these reasons, the Commission should hold that the DMR proposal cannot be considered on rehearing.

B. The DMR Cannot be Authorized under Ohio Law.

Even if the Commission had jurisdiction to consider the DMR proposal on rehearing, it cannot approve the proposal because the DMR is not legally authorized under R.C. 4928.143 or any other provision of Ohio law. In its initial rehearing brief, the Staff does not identify what

[129] SC Br. at 41-42.

[130] Tr. I at 16 (note: the transcript erroneously identified the deadline as July 13, but the Friday following Monday, July 11, 2016, was July 15 which was the actual deadline for intervenor rebuttal testimony to the Staff's DMR proposal).

provision it believes authorizes the DMR.[131] FirstEnergy and OEG contend that the DMR can be authorized under R.C. 4928.143(B)(2)(h) and (B)(2)(i).[132] Both contentions are incorrect.

1. The DMR cannot be authorized under R.C. 4928.143(B)(2)(h).

The DMR cannot be approved under R.C. 4928.143(B)(2)(h) because the DMR is wholly unrelated to distribution service, and because the record lacks any of the information necessary for the analysis of the distribution system's reliability that is required before a rider can be approved under (B)(2)(h).[133] The Staff and Companies are silent in their initial rehearing briefs regarding the analysis of the distribution system's reliability, so that issue is fully addressed in Sierra Club's initial rehearing brief.[134] The Companies, Staff, and OEG, however, do attempt in their initial rehearing briefs to portray the DMR as related to distribution service. That attempt falls flat, because the record shows that the DMR would do nothing more than provide FirstEnergy with between $131 million and $1.126 billion per year in no-strings attached cash for three to nearly eight years – not a dime of which would have to be spent on distribution modernization.

a. The DMR is not related to distribution service.

A rider can be authorized under R.C. 4928.143(B)(2)(h) only if it relates to "the utility's distribution service." This threshold requirement is fatal to the argument that the DMR qualifies under (B)(2)(h) because the record clearly establishes that the DMR has nothing to do with such service. Instead, the DMR is simply an attempt to bolster the finances of the FirstEnergy

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[131] In his rehearing testimony, Dr. Choueiki contended that the DMR proposal should be approved under R.C. 4928.143(B)(2)(h). *See* Staff Ex. 15, Rehearing Testimony of Hisham M. Choueiki, Ph.D., P.E, at 15.

[132] Co. Br. at 25; Post-Rehearing Brief of the Ohio Energy Group ("OEG Br.") at 3-4.

[133] SC Br. at 43-52.

[134] SC Br. at 50-51.

corporate family by providing "credit support" to the Companies and their parent, FirstEnergy Corp.[135] While the Staff's proposal is called a "Distribution Modernization" rider, there is no assurance that any of the revenue collected under the DMR would be invested in distribution modernization or even spent within the Companies, rather than simply funneled up to FirstEnergy Corp. for distribution to shareholders or unregulated affiliates such as FES.[136] At the hearing, FirstEnergy witness Mikkelsen steadfastly refused to commit to the Companies spending the DMR revenues on distribution modernization or within the Companies, or to not dividending the revenues up to FirstEnergy Corp.[137] In short, there is nothing in the DMR as proposed by the Staff or with FirstEnergy's modifications that would require any of the revenues to be spent on the distribution grid. As such, the DMR is unrelated to distribution service and cannot be approved under R.C. 4928.143(B)(2)(h).

Nothing in the initial rehearing briefs of the Staff or Companies demonstrates otherwise. Instead, both the Staff and the Companies spend multiple pages of their briefs highlighting various benefits that could arise from investments in distribution modernization.[138] Sierra Club certainly agrees, as it explained in its initial brief, that investments in distribution modernization (and other initiatives such as renewable energy, energy efficiency, and battery technology) could

[135] Tr. IV at 959-60 (Choueiki cross) ("Q. So the purpose of the DMR is to enable the companies to provide credit support to both themselves and FE Corp.; is that correct? A. The purpose of the DMR is to provide credit support, correct."); Tr. III at 590 (Mr. Buckley acknowledging that "the purpose of the 131 million . . . is to provide credit support for the FirstEnergy organization"); *id.* at 598 (Mr. Buckley agreeing that the Staff proposal "is intended to address possible future action by rating agencies"); Tr. II at 443 (Turkenton cross) ("Q. Would you agree with me, Ms. Turkenton, the -- the staff's proposal is for credit support? Isn't that what you state in your testimony? A. That is the purpose of the rider. It's not necessarily the name of the rider, but yes.").

[136] SC Br. at 44-49; Tr. II at 433; Tr. III at 584-85, 613-14, 702-03; Tr. IV at 956-57.

[137] SC Br. at 51-52; Tr. X at 1606-09.

[138] Staff Br. at 1, 5-6, 19; Co. Br. at 25-27.

provide significant benefits to customers.[139] But what is missing from the Staff and Companies' briefs is any demonstration that the DMR revenues would be invested in distribution modernization. This omission is not surprising given that, as noted above, the DMR revenues would not be restricted to spending on distribution modernization (or even remain within the Companies), and there would be no prohibition on dividending those revenues up to FirstEnergy Corp. But without such restrictions and an enforceable requirement that the $131 million to $1.126 billion per year of DMR revenues would be invested in distribution modernization, there is no basis to authorize the DMR under R.C. 4928.143(B)(2)(h).

The Companies do state once in their brief that they "are committing that they intend to use Rider DMR funds for purposes within the Companies' operations, such as jumpstarting grid modernization."[140] But the Companies saying that they are "committing that they intend" is meaningless because it is unenforceable. If the Companies do something different with the DMR revenues in the future, they could simply say that their "intent" changed and there would be nothing for the Commission, Staff, or intervenors to hold them to. If FirstEnergy had wanted to commit to spending DMR revenues on distribution modernization, they easily could have done so. Instead, FirstEnergy has chosen to use evasive language like "committing that they intend" that should not fool anyone.

In its brief, the Staff contends that intervenor concerns about whether funds associated with the DMR will go to distribution modernization are nothing more than misguided "questioning [of] whether the Commission will adequately monitor performance under its own orders."[141] The Staff's contention, however, is meritless because neither the Staff nor the

[139] SC Br. at 83-91.

[140] Co. Br. at 28.

[141] Staff Br. at 13.

Companies are proposing a requirement that DMR revenues be spent on distribution modernization. Without such a binding and enforceable requirement, there would be no performance for the Commission to "monitor," as FirstEnergy would be free to do whatever it wants with the customer money that it collects.[142] Sierra Club's concerns, therefore, stem from the undisputed fact that FirstEnergy would not be required to spend any DMR revenues on distribution modernization.

b. The DMR is not incentive ratemaking.

In contending that the DMR is authorized under R.C. 4928.143(B)(2)(h), both the Companies and OEG assert that the rider qualifies as incentive ratemaking because it will "incentivize" grid modernization.[143] This incentive ratemaking argument is apparently based on the claim that the DMR would "jumpstart" distribution modernization by providing "credit support" to the Companies and FirstEnergy Corp. which, in turn, would enable the Companies to access the financial markets on favorable terms which, in turn, would enable the Companies to obtain funds that they might invest in distribution modernization.[144] This argument fails because the DMR does not qualify as either an "incentive" or "ratemaking" as it is not connected to any costs that the Companies have or will incur.

The DMR does not qualify as an "incentive" because, as discussed above, the Companies would not be required to make any investments in distribution modernization under the DMR but, instead, would simply be provided between $131 million and $1.126 billion per year on the "hope" that they might decide to make distribution modernization investments.[145] Such hopeful

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[142] In fact, Ms. Mikkelsen testified that neither the Companies nor the Staff had proposed any provision for the Commission to be able to review how the DMR revenues are spent. Tr. X at 1608-09.

[143] Co. Br. at 28; OEG Br. at 3.

[144] Co. Br. at 27; Staff Br. at 7.

[145] Tr. II at 426.

thinking stretches the definition of "incentive" far beyond any reasonable interpretation of that statutory language.

The DMR does not qualify as "ratemaking" because it is not connected to any costs that FirstEnergy has incurred or will incur to provide distribution service to its customers. Ohio law sets forth at R.C. 4909.15 a "mandatory ratemaking formula" that bases rates on: (1) valuation of the utility property in service, (2) a reasonable rate of return on that property, and (3) expenses incurred in providing service in a test year.[146] In applying this statutory provision, the Ohio Supreme Court has explained that:

> Pursuant to the statutory ratemaking formula investors are assured a fair and reasonable return on property that it determined to be used and useful, R.C. 4909.15(A)(2), plus the return of costs incurred in rendering the public service, R.C. 4909.15(A)(4), while consumers may not be charged 'for utility investments and expenditures that are neither included in the rate base nor properly categorized as costs.'[147]

Yet the DMR would do exactly what the Court said could not be done through ratemaking – charge customers for expenditures that are neither included in the rate base nor properly categorized as costs. As such, the DMR cannot be approved as "incentive ratemaking."

At hearing, OEG's counsel attempted to get Staff witness Turkenton to equate the DMR with the incentives that FERC provides to encourage transmission investments.[148] But a review of FERC's transmission incentive rules demonstrates why the DMR proposal should not be considered "incentive ratemaking." In particular, in establishing its rules for "Promoting Transmission Investment Through Pricing Reform," FERC made clear that:

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[146] *Columbus S. Power Co. v. Pub. Util. Comm.*, 67 Ohio St.3d 535, 537, 620 N.E.2d 835 (1993). R.C. 4928.15(a) provides that distribution service rates and charges shall be established in accordance with the requirements of Chapters 4905 and 4909 of the Revised Code.

[147] *Dayton Power & Light Co. v. Pub. Util. Comm.*, 4 Ohio St.3d 91, 103, 447 N.E.2d 733 (1983).

[148] Tr. II at 426-27.

> We do agree, however, with the position of certain wholesale customers and state commissions that the Commission should not provide incentives that only serve to increase rates without providing any real incentives to construct new transmission infrastructure. . . . . The purpose of our Rule is to benefit customers by providing real incentives to encourage new infrastructure, not simply increasing rates in a manner that has no correlation to encouraging new investment.[149]

Consistent with these concerns, FERC's transmission incentive rules limit incentives in two ways. First, the types of incentives that are available are all tied to costs that a utility actually incurs for transmission investments, such as increasing the return on equity the company can receive, authorizing the collection of construction work-in-progress ("CWIP") funds, or allowing accelerated depreciation.[150] Second, the FERC rule provides that "each applicant must demonstrate that there is a nexus between the incentive sought and the investment being made."[151] By contrast, the DMR proposal is not based on any costs that the Companies have incurred or any spending on distribution modernization investments that the Companies would make. Instead, the DMR would "only serve to increase rates without providing any real

[149] 71 Fed. Reg. 43,294, 43,295 (July 31, 2006).

[150] *Id.* at 43,305-31.

[151] *Id.* at 43,298. Similarly, FERC rejected a transmission incentive request under the nexus test where the company, Transource Kansas:

> has not identified a transmission project and has not described the details of its financial situation that CWIP would alleviate, it has not met the nexus test under Order No. 679. Transource Kansas did not provide details regarding its financial pressures, delayed cash flow, relative size of its investment, or any adverse impacts to short-term liquidity; instead Transource Kansas provides only general statements that the CWIP incentive will improve cash flow during construction and provide greater regulatory certainty. Transource Kansas also states that the cash flow stability will help it attract capital and secure and maintain a BBB credit rating, although it makes no showing of the size of the effect on cash flow that CWIP would elicit.

Transource Kansas, LLC, 151 FERC ¶ 61010, at ¶ 13 (Apr. 3, 2015); *see also Atx Sw., LLC*, 152 FERC ¶ 61193, at ¶ 48 (Sept. 11, 2015).

incentives to" invest in distribution modernization.[152] As such, the DMR is not "incentive ratemaking" and cannot be approved under R.C. 4928.143(B)(2)(h).

2. The DMR cannot be authorized under R.C. 4928.143(B)(2)(i).

One of only two restrictions the Staff proposes for the DMR is that FirstEnergy Corp. be required to keep its headquarters and nexus of operations in Akron for the full term of ESP IV.[153] FirstEnergy has seized on that proposed condition as a means to attempt to both inflate and justify the DMR. First, the Companies claim that they should be compensated for maintaining the headquarters and nexus of operations in Akron with an additional amount not to exceed $568 million per year, which is the annual economic impact that FirstEnergy witness Murley contends the headquarters and nexus of operations provide to the Akron area. Second, FirstEnergy claims that this condition turns the DMR into an economic development and job retention program that makes it authorized for inclusion in ESP IV under R.C. 4928.143(B)(2)(i).[154]

As Sierra Club explained in its initial rehearing brief,[155] the Commission should reject this transparent attempt to inflate and fabricate a justification for the DMR under R.C. 4928.143(B)(2)(i) for at least four reasons. First, the maintenance of a corporate headquarters and nexus of operations – both of which FirstEnergy Corp. needs just to carry out its day-to-day operations – does not qualify as a program specifically targeted at economic development or job retention, which is what R.C. 4928.143(B)(2)(i) requires. Second, the purported economic development benefits of the requirement to keep the headquarters and nexus of operations in

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[152] 71 Fed. Reg. at 43,295.

[153] Staff Ex. 13, Rehearing Testimony of Joseph P. Buckley, at 7.

[154] Co. Ex. 206, Rehearing Rebuttal and Surrebuttal Testimony of Eileen M. Mikkelsen ("Mikkelsen Rebuttal") at 5, 13-14, 19-20.

[155] SC Br. at 52-55.

Akron are illusory because there is no reason to believe that FirstEnergy Corp. might move its headquarters and nexus of operations during the term of ESP IV.[156] In fact, just last year, FirstEnergy Corp. renewed its lease on its headquarters through June 2025.[157] Third, crediting FirstEnergy's theory would "remove any substantive limit to what an electric security plan may contain"[158] as a requirement for FirstEnergy Corp. to maintain its headquarters and nexus of operations could be tacked on to virtually any rider proposal. Finally, FirstEnergy has not satisfied the requirements of O.A.C. 4901:1-35-03(C)(9)(h), which requires a cost-benefit analysis and quantification of the rate impact of any economic development and job retention rider.

In its initial rehearing brief, FirstEnergy does not offer any explanation for how FirstEnergy Corp. keeping its headquarters and nexus of operations in Akron purportedly constitutes an "economic development" or "job retention" program under R.C. 4928.143(B)(2)(i), and does not identify any basis to think that the headquarters would otherwise be moved. Instead, FirstEnergy claims that Ms. Murley identified "significant economic benefits" that the headquarters and nexus of operations provides to the region.[159] In fact, as Staff notes, Ms. Murley identified purported economic impacts, not economic benefits, of the headquarters and nexus of operations, as she did not perform a cost-benefit analysis that would provide a more accurate picture of the net economic impact of the headquarters and nexus of operations.[160] But, regardless, simply noting that certain activity provides economic impacts (or

[156] Tr. X at 1603-04 (Mikkelsen cross).

[157] *See* Dynegy Ex. 1, Direct Testimony of Dean Ellis, at 10-11 (discussing FirstEnergy Corp.'s commitment to keep the headquarters in Akron).

[158] *In re App. of Columbus S. Power Co.*, 128 Ohio St.3d 512, 2011-Ohio-1788, 947 N.E.2d 655, ¶ 34.

[159] Co. Br. at 38.

[160] Staff Br. at 18 n.52.

even benefits) does not make that activity a program targeted at "economic development" or "job retention" for purposes of R.C. 4928.143(B)(2)(i).

In its initial rehearing brief, the Staff is non-committal about whether the Companies should receive additional revenue for FirstEnergy Corp. keeping its headquarters and nexus of operations in Akron.[161] But outside of noting that the headquarters and nexus of operations provide some economic benefit to Akron (which, as explained above, does not alone qualify the activity as an economic development or job retention program), the Staff does not identify any basis upon which the DMR would qualify under R.C. 4928.143(B)(2)(i). The Staff does, however, identify an additional reason why the Companies should not receive additional revenue related to the headquarters and nexus of operations, namely because they are "already recompensed adequately for the presence of the headquarters."[162] This is an important point because even if FirstEnergy Corp. maintaining its headquarters and nexus of operations in Akron somehow did qualify as an economic development or job retention program, a rider under R.C. 4928.143(B)(2)(i) is limited to allocating the "program costs" to customers. In other words, such a rider cannot be set on the basis of customers compensating the Companies for the benefits that the headquarters and nexus of operations purportedly provide. Instead, if any rider were appropriate here, it would have to be based on the Companies' costs of keeping the headquarters and nexus of operations in Akron, minus any amounts that the Companies are already compensated for (so as to avoid double billing). There is no evidence in the record, however, regarding such costs. This represents another reason that the Commission should reject FirstEnergy's request for additional DMR revenue related to maintaining the FirstEnergy Corp.

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[161] *Id.* at 17-18.

[162] *Id.* at 18.

headquarters and nexus of operations in Akron. And the absence of any such cost evidence is an additional reason why the DMR cannot be authorized on this record.

3. The DMR Would be an Unlawful Transition Charge.

The Commission also cannot authorize the DMR because it would constitute an unlawful transition charge. As noted in Section I.B.3 above, the Ohio Supreme Court recently rejected so-called rate stability riders for AEP and DP&L as unlawful transition charges that are barred by R.C. 4928.38.[163] The DMR proposed here is similar to the rider rejected in the AEP proceedings in two ways that indicate that the DMR would also be rejected. First, a primary justification offered for the AEP rider was that it would provide revenue needed to "maintain [AEP's] financial integrity and ability to attract capital during the ESP."[164] Second, the Court found it improper that AEP was being authorized to recover more capacity revenues from customers than is needed to cover its actual capacity costs.[165] Both of these factors apply to the DMR, which would provide FirstEnergy with additional revenue, unrelated to any costs incurred, in order to help FirstEnergy Corp. and the Companies maintain an investment grade credit rating. This scheme would likely be rejected by the Ohio Supreme Court as an unlawful transition charge just as a similar scheme was rejected in the AEP proceeding.

In attempting to preempt such a challenge, OEG relies heavily on the fact that the Staff has couched the credit support that would be provided by the DMR as a distribution charge, rather than a generation charge.[166] But this does not answer the question of whether the Staff

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[163] *In re App. of Columbus S. Power Co.*, Slip Opinion No. 2016-Ohio-1608 (Apr. 21, 2016); *In re App. of Dayton Power & Light Co.*, Slip Opinion No. 2016-Ohio-3490 (June 20, 2016).

[164] 2016-Ohio-1608, ¶ 8.

[165] *Id.* ¶¶ 32-37.

[166] OEG Br. at 4.

proposal constitutes a transition charge because, as discussed previously, there is no assurance that any of the DMR revenues would be used to bolster distribution initiatives. On the contrary, the Companies are already entertaining the possibility of using the credit support to redeem debt and fund pension obligations.[167] And there is nothing stopping FirstEnergy from simply funneling the DMR revenues up through dividends to FirstEnergy Corp., which could then use such funds to increase shareholder dividends or support FES.

The remaining arguments offered by OEG with regards to transition charges are unavailing. First, there is no significance to the fact that Staff's DMR proposal falls under a different provision of R.C. 4928.143(B)(2) than did the rider that was struck down in *Columbus Southern Power*.[168] To suggest otherwise would be to completely overlook the record-based method of inquiry adopted by the Ohio Supreme Court. Second, the "notwithstanding" language in R.C. 4928.143(B) does nothing to save the DMR's legality.[169] Because the Ohio Supreme Court has rejected unlawful transition charges that purported to be authorized ESP charges in both the AEP and DP&L proceedings, OEG is wrong in claiming that the "notwithstanding" language somehow exempts all ESP charges are exempt from the bar against transition charges.[170] The Commission should reject the DMR proposal because it would permit the unlawful collection of unlawful transition revenues.

[167] Mikkelsen Rebuttal at 8-9.

[168] OEG Br. at 4.

[169] *Id.*

[170] It is also important to note that R.C. 4928.141(A) provides that Standard Service Offers under R.C. 4928.142 and .143 "shall exclude any previously authorized allowances for transition costs."

C. The DMR Proposal is Neither Just Nor Reasonable.

As Sierra Club recounted in detail in its initial rehearing brief, even if the DMR proposal were legally permissible, the Commission must reject it because there has been no showing that it would be just, reasonable, or beneficial to customers. Under the DMR, customers would pay an annual charge of between $131 million and $1.126 billion for three to nearly eight years for the stated purpose of helping provide credit support to FirstEnergy Corp. so that the Companies can maintain an investment grade credit rating and favorable access to the financial markets. But the record is bereft of even the basic evidence that would be needed to attempt to show that customers could somehow benefit from providing such largesse to the Companies. As Sierra Club explained in its initial rehearing brief:[171]

- No forward looking financial information has been provided regarding either FirstEnergy Corp. or the Companies.
- There has been no assessment of what, if any, role the Companies have played in causing whatever credit problems FirstEnergy Corp. may face.
- There has been no quantification of costs that customers could face if FirstEnergy Corp. or the Companies had their credit rating downgraded and, therefore, there is no basis to conclude that the DMR costs would be lower than the impact of such a possible downgrade.
- There is no basis in the record upon which to conclude that the DMR revenues would stave off a credit downgrade that would otherwise occur.
- The purported distribution modernization benefits of the DMR are illusory as there is no requirement that any DMR revenues be invested in distribution modernization.

In short, customers are being asked to pay significant sums of money in response to a problem that has not been quantified and that customers did not cause, with no reasonable assurance that the effort would succeed or that customers would benefit, and without any knowledge of what the costs to customers may be if a credit downgrade occurred. As such, it is clear that the hastily

[171] SC Br. at 56-74.

considered DMR proposal cannot be found to be just, reasonable, and beneficial to customers on the record currently before the Commission.

The Staff and Companies' initial rehearing briefs do not come close to demonstrating that the DMR proposal would somehow be just, reasonable, and beneficial to customers. The Staff contends that the DMR is justified because of "the weak financial position of the companies and the weaker financial position of [FirstEnergy Corp.]"[172] But, as noted, the record contains only historic information about FirstEnergy Corp.'s financial situation, and does not provide any information – either historic or forward-looking – regarding the financial condition and credit metrics of the Companies. As such, there is no basis upon which to conclude what the size of the credit problems FirstEnergy Corp. might be facing really are, and whether the Companies themselves have a weak credit position or whether any credit challenges they face are really derivative of FirstEnergy Corp.'s financial performance. Those are all critical facts that would go towards whether the proposed credit support is likely to succeed, whether the Companies' customers would be better protected through mechanisms such as ring fencing, and why the Companies purportedly need hundreds of millions to billions of dollars in credit support revenues when FirstEnergy is simultaneously proposing a Modified Rider RRS proposal under which customers would purportedly provide hundreds of millions of dollars less revenue to the Companies over the term of ESP IV. All of these issues, however, remain unanswered on this record.

In their briefs, Staff and FirstEnergy highlight the significant capital that would be needed to modernize the distribution grid, and contend that providing credit support is necessary

[172] Staff Br. at 6.

to the Companies being able to access such capital.[173] But there has been no showing that the Companies – which each have an investment grade credit rating – are currently unable to access the financial markets. And, as discussed in Section II.B.1 above, there is no requirement that any of the DMR revenues be invested in distribution modernization or even that the Companies pursue any distribution modernization initiatives. In short, all of the distribution modernization benefits highlighted in the Staff and FirstEnergy's briefs are irrelevant because there is no required connection between the DMR and distribution modernization. The record is clear that the DMR is only a credit support rider, and simply calling it a "distribution modernization" rider does not change that fact.

FirstEnergy highlights in its brief the claims that a credit downgrade could make accessing the capital markets more difficult and/or expensive for the Companies (and, therefore, their customers).[174] But there has been no attempt to quantify the cost impact that such a downgrade might have on customers, which is a critical shortcoming because without such a quantification, there is no way to know whether the potential harm that might be avoided with the DMR is concomitant with the cost that customers would be forced to pay under that rider. The Staff attempt to dismiss this argument as "something of a puzzle" because apparently a concession that a credit downgrade could lead to increased borrowing costs is all one needs to determine that it is appropriate for customers to be asked to pay more to avoid such downgrade.[175] But that argument is meritless, as it could be reasonable to pay $5 to avoid a $50 harm, but it would be wholly unreasonable to pay $500 to avoid that same $50 harm. Here, there is simply no way to know whether the harm that customers are being asked to avoid may amount

[173] Staff Br. at 7; Co. Br. at 26-28.

[174] Co. Br. at 28-30.

[175] Staff Br. at 11.

to, for example, $30 million per year or $300 million per year. Without a reasonable estimate of the credit downgrade harm that customers purportedly face, the Commission cannot determine that it is just and reasonable to require customers to pay hundreds of millions to billions of dollars to avoid such harm.

D. The DMR Cannot Be Added to the ESP IV Because Doing So Would Breach the ESP vs. MRO Test.

The DMR proposal also cannot be approved because ESP IV with the DMR proposal would be less favorable to customers than the expected results under an MRO.[176] As Sierra Club explained in its initial rehearing brief, the DMR would cause ESP IV to have a net cost to customers because the $51.1 million in shareholder-funded initiatives are far outweighed by the Staff's $393 million DMR proposal.[177] If the DMR were extended to five years, or expanded to the between $558 million and $1.126 billion per year through May 31, 2024, urged by FirstEnergy, the net loss to customers under ESP IV would be even larger. And any of those levels of losses would more than swamp the largely illusory qualitative benefits that ESP IV purportedly provides. As such, the DMR simply cannot pass the ESP vs. MRO test and, therefore, cannot be approved.

In their initial rehearing briefs, the Staff and Companies contend that the costs of the DMR need not be considered in evaluating the ESP vs. MRO test because the DMR revenues could be collected through an MRO.[178] In particular, Staff contends that the DMR revenues could be collected under R.C. 4928.142(D)(4), which authorizes adjustments to Standard Service

[176] R.C. 4928.143(C)(1).

[177] SC Br. at 74-75.

[178] Staff Br. at 8; Co. Br. at 44-45.

Offer rates if "necessary to address any emergency that threatens the utility's financial integrity."[179] This argument fails because there is no evidence that the Companies face such an emergency. None of the Staff's written testimony addresses whether there is such a financial emergency, and no witness presented evidence of such an emergency at the hearing.[180] In addition, R.C. 4928.142(D)(4) only allows for adjustments to the SSO price that applies to non-shopping customers. Therefore, an adjustment under that provision could not replace the non-bypassable charge sought under the DMR. The Staff has offered no argument to the contrary on either of these points and, therefore, their claim that the DMR is quantitatively neutral for purposes of the ESP vs. MRO test fails.

The Companies attempt to exclude the DMR from the ESP vs. MRO test by claiming that the DMR revenues could be collected through a base rate case or Rider AMI.[181] But this argument fails because, as discussed in Section II.B.1.b above, the DMR is not based on the recovery of any costs that the Companies have incurred or investments the Companies would make to provide service to their customers. Rider AMI, by contrast, is designed to ensure that the Companies can receive a return of and on any investments that they make in advanced metering for their customers. And, as discussed in Section II.B.1.b above, the Companies can only seek through a base rate adjustment a reasonable rate of return on utility property in service

[179] R.C. 4928.142(D)(4); Staff Br. at 8 (citing Staff Ex. 14, Rehearing Testimony of Tamara S. Turkenton, at 3-4).

[180] *See, e.g.*, Tr. II at 439-40; *id.* at 450 (Ms. Turkenton testifying that she does not know if there is any emergency that threatens the utilities' financial integrity); Tr. III at 515-16 (Mr. Buckley not testifying as to whether the Companies face "any emergency that threatens their financial integrity"); Tr. V at 1214-15 (Dr. Choueiki declining to offer testimony regarding whether the Companies face an emergency on the grounds that Staff witness Buckley addressed that issue).

[181] Co. Br. at 44-45.

and recovery of expenses incurred in providing service to customers.[182] What FirstEnergy cannot do through a base rate case or Rider AMI is to require customers to pay money for nothing, but that is exactly what the DMR would do.

The fact that FirstEnergy could not seek the DMR revenues through a base rate case proceeding is well illustrated by the Ohio Supreme Court's ruling in *Office of Consumers' Counsel v. Public Utilities Commission*.[183] In that case, the Court held that the Commission could not approve for inclusion in rates the amortization of a utility's investment in four proposed nuclear plants that had been terminated because those plants "never provided any service whatsoever to the utility's customers."[184] In so holding, the Court specifically rejected the argument that such costs should be allowed to be recovered because the utility could suffer harm in the capital markets if the costs were not recoverable. As the Court explained:

> The commission, CEI, and the amici argue strenuously that to rule as we have today will seriously disadvantage Ohio utilities in capital markets thereby "driv(ing) up the return on investment required by investors in Ohio utilities." This gloomy scenario, however, does not imbue the commission with the authority to rewrite the statutes. The statutes in question contain no provisions insulating investors from the type of losses sustained in the cancelled-plants venture.
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> If, as has been argued, these are parlous times for the utilities industry, and if, therefore, in order to attract and retain investment capital, utility companies must not only be granted a fair and reasonable rate of return pursuant to statute but must also be assured the return of capital invested in failed projects that would otherwise not be recoverable under the ratemaking formula, then the commission and the utilities should petition the General Assembly to enact changes in the ratemaking structure so as to

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[182] R.C. 4909.15; *Columbus S. Power Co. v. Pub. Util. Comm.*, 67 Ohio St.3d 535, 535, 620 N.E.2d 835 (1993); *Dayton Power & Light Co. v. Pub. Util. Comm. of Ohio*, 4 Ohio St.3d 91, 103, 447 N.E.2d 733 (1983) ("consumers may not be charged 'for utility investments and expenditures that are neither included in the rate base nor properly categorized as costs.'").

[183] *Office of Consumers' Counsel v. Pub. Util. Comm.*, 67 Ohio St.2d 153, 164, 423 N.E.2d 820 (1981).

[184] *Id.* at 164.

> provide this extra modicum of protection for the investors. Absent such explicit statutory authorization, however, the commission may not benefit the investors by guaranteeing the full return of their capital at the expense of the ratepayers. Under the ratemaking formula now in effect consumers are not chargeable for utility investments and expenditures that are neither included in the rate base nor properly categorized as costs.[185]

In other words, the Court found that concerns about capital markets did not justify ignoring the clear requirement that costs recovered from customers should be for service actually provided to customers.[186] Here, the DMR is not based on the recovery of any costs incurred by the Companies or any investments in distribution modernization initiatives to be made. Instead, customers would not receive any services for the money they would pay under the DMR and, therefore, the DMR revenues could not be collected through a base rate case or Rider AMI.

The Commission should also reject FirstEnergy's contention that the retention of the FirstEnergy Corp. headquarters and nexus of operations in Akron should count as a quantitative benefit for the DMR in the ESP vs. MRO test.[187] For one thing, there is no evidence that the headquarters and nexus of operations might move from Akron without the DMR, so the retention provision provides very little if any benefit to customers. In addition, the $568 million per year annual economic impact figure cited by FirstEnergy fails to analyze the costs associated with the headquarters operations,[188] as Ms. Murley did not perform a cost-benefit analysis.[189] Finally, if

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185 *Id. at 167.*

186 It is important to note that credit support can still be provided to the Companies through the traditional approach of providing a utility a return of and on actual investments made to serve its customers. SC Br. at 82. As Ms. Mikkelsen testified "any time a utility makes a filing that includes a return on investment, that return on investment serves to provide credit support to that company." Tr. X at 1642. Therefore, requiring that the Companies spend any DMR revenues on specific distribution modernization, renewable energy, and energy efficiency investments could help ensure that customers receive some benefits while providing credit support to FirstEnergy. SC Br. at 81-91.

187 Co. Br. at 45-46.

188 Tr. IX at 1502.

189 *Id.* at 1489.

any benefits of retaining the headquarters and nexus of operations in Akron were included in the ESP vs. MRO calculation, then the costs to customers both through the DMR and through the other ways in which customers pay for the headquarters and nexus of operations would have to be included in the calculation also. Yet the record does not include any evidence regarding those costs. So, for all of those reasons, there is no evidentiary basis for claiming that this headquarters provision would produce quantitative benefits for purposes of the ESP vs. MRO test.

Finally, FirstEnergy and the Staff contend that there are numerous qualitative benefits of the DMR that should be incorporated into the ESP vs. MRO calculation.[190] But neither party has even attempted to explain how whatever qualitative benefits might arise from ESP IV could outweigh the hundreds of millions to billions of dollars of costs that the DMR would impose on customers. While Staff highlights the benefits of distribution modernization, those benefits cannot be attributed to the DMR because, as discussed numerous times above in this brief, the DMR has nothing to do with distribution modernization and, instead, is only about providing credit support to the FirstEnergy corporate family. Finally, any benefits of the DMR are outweighed by the fact that, as FES has argued in a previous proceeding, "charging above market charges to customers would slow business development and job growth."[191]

Consequently, R.C. 4928.143(C)(1) precludes the DMR from being added to this ESP.

[190] Co. Br. at 46; Staff Br. at 8.

[191] *In Re Dayton Power & Light Co.*, Case Nos. 12-426-EL-SSO, et al., 2013 WL 5221187, Opinion and Order at 48 (Sept. 4, 2013).

E. The DMR Would Run Afoul of FERC's Limits on Using Customer Money to Subsidize the Parent Corporation's Shareholders and Merchant Affiliates.

The DMR should also be rejected because it conflicts with FERC's limits on the siphoning of money from regulated utility customers to cross-subsidize the shareholders and merchant affiliates of the utility's parent company.[192] In particular, the DMR proposal in no way restricts the Companies' ability to transfer the DMR revenues through dividends to FirstEnergy Corp, which could then use those revenues to benefit shareholders or unregulated affiliates such as FES, and the Companies refused to agree to a restriction that would prevent such dividending up to FirstEnergy Corp. As such, the DMR proposal suffers from the same infirmity that FERC identified in placing a hold on the initial Rider RRS/PPA plan.

In its initial rehearing brief, the Staff identifies the FERC affiliate transaction rules as one of the "[s]erious legal concerns" about Modified Rider RRS that justify rejecting that rider proposal.[193] But then the Staff turns around and argues for a proposal that would face the same "[s]erious legal concerns" at FERC because it would allow for the same transferring of customer money to FirstEnergy Corp., its shareholders, and FES. The Staff provides no explanation for how the DMR proposal could avoid FERC concerns while Modified Rider RRS cannot, perhaps because no reasonable explanation can be provided.

[192] SC Br. at 78-79.

[193] Staff Br. at 3-4.

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CERTIFICATE OF SERVICE

I hereby certify that a true and accurate copy of the foregoing public version of Sierra Club's Post-Hearing Reply Brief on Rehearing has been served upon the following parties via electronic mail on August 29, 2016:

s/ Shannon Fisk
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