

**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

**APPLICATION OF OHIO EDISON COMPANY, THE CLEVELAND ELECTRIC ILLUMINATING COMPANY, AND THE TOLEDO EDISON COMPANY FOR
REHEARING OF THE EIGHTH ENTRY ON REHEARING**

Pursuant to Section 4903.10 of the Ohio Revised Code and Rule 4901-1-35 of the Ohio Administrative Code, Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company (the “Companies”), request rehearing of the Eighth Entry on Rehearing issued in this proceeding on August 16, 2017. As demonstrated in the attached Memorandum in Support, the Eighth Entry on Rehearing is unreasonable and unlawful on the following grounds:

1. It would require Staff to retain a “monitor” to ensure funds collected under Rider DMR are expended appropriately. This is wrong because: (1) as the Commission has already noted, the Commission is fully capable of making such an assessment; (2) Rider DMR revenues cannot be tracked in “real time;” (3) the Commission has ample processes available to ensure no affiliate cross-subsidization will occur; (4) quarterly reviews are impractical and unnecessary; and (5) “real-time” monitoring could restrict the use of Rider DMR funds.

2. It failed to restore the 50 basis point adder to the return on equity calculation for the Advanced Metering Infrastructure/Modern Grid Rider (“Rider AMI”), as stipulated and previously approved. The Commission’s rationale for removing the adder: (1) misstates the link

between Rider RRS and the 50 basis point adder; (2) fails to take into account the Commission's PowerForward initiative; and (3) improperly rejects a reasonable grid modernization incentive in advance of the Commission's development of appropriate ratemaking policies in Phase III of the PowerForward initiative.

Accordingly, the Commission should grant the Companies' Application for Rehearing.

Respectfully submitted,

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**MEMORANDUM IN SUPPORT OF APPLICATION OF OHIO EDISON COMPANY,
THE CLEVELAND ELECTRIC ILLUMINATING COMPANY, AND THE TOLEDO
EDISON COMPANY FOR REHEARING OF EIGHTH ENTRY ON REHEARING**

The Commission in its Fifth Entry on Rehearing directed Staff to review periodically how Ohio Edison Company, The Cleveland Electric Illuminating Company and The Toledo Edison Company (the “Companies”) and FirstEnergy Corp. use Rider DMR funds, directly or indirectly, in support of grid modernization.¹ The Commission noted that appropriate uses for Rider DMR funds included: (1) “large cash up front investments to fund grid modernization;” and (2) uses that include “reducing outstanding pension obligations, reducing debt, or taking other steps to reduce the long-term costs of accessing capital.”² Thus, the Companies expect that there will be a Staff review of the use of Rider DMR funds and the Companies are not opposed to such Staff review. Staff’s periodic review should entail an uncomplicated process of confirming that amounts applied by the Companies – and potentially FirstEnergy Corp. – to uses appropriate to further the purposes

¹ Fifth Entry on Rehearing, pp. 127-28.

² Fifth Entry on Rehearing, p. 128.

of Rider DMR exceeded Rider DMR funds received. As the Commission found in its Eighth Entry on Rehearing, the “Commission is fully capable of making such assessment.”³

Notwithstanding this finding – with which the Companies wholeheartedly agree – the Commission also directed in the Eighth Entry that Staff retain a third-party “monitor” to “work with FirstEnergy and FirstEnergy Corp. to ensure that Rider DMR funds are expended appropriately.”⁴ The Commission “intend[s] for this review to be ongoing and conducted in real time,” and for the monitor to provide Staff with “quarterly updates on the use of Rider DMR,” and to prepare mid-term and final reports.⁵ The Commission lacks reasonable grounds for retaining an outside consultant to ensure that Rider DMR funds are expended appropriately. As demonstrated below, the Commission’s rationale for establishing a monitor is flawed and unsupported. Moreover, a monitor not only is unnecessary (because the Staff can ably determine whether the purposes of Rider DMR are being furthered), but also improperly interferes with the prerogative of the Companies’ management.

Additionally, the Commission erred by failing to restore the 50 basis point adder to the return on equity calculation for the Advanced Metering Infrastructure/Modern Grid Rider (“Rider AMI”). This incentive was stipulated to by the diverse parties to the Third Supplemental Stipulation, and it was approved by the Commission in its initial Opinion and Order in this proceeding.⁶ The Commission’s elimination of already-authorized incentives for grid modernization is inconsistent with engaging in a major initiative – PowerForward – to promote

³ Eighth Entry on Rehearing, p. 49.

⁴ *Id.*, p. 49-50.

⁵ *Id.*, p. 50.

⁶ Opinion and Order (Mar. 31, 2016), pp. 69, 95-96 (“March 31, 2016 Order”).

grid modernization. Thus, the Commission should take another look at the merits of the 50 basis point adder.

I. ARGUMENT

A. The Commission Should Amend ESP IV to Eliminate the Requirement for a Monitor Relating to the Use of Revenues Received under Rider DMR.

1. Staff Is Fully Capable of Confirming Whether the Companies Have Acted to Further the Purposes of Rider DMR.

By requiring a monitor, the Commission has improperly assumed that one can track specific dollars collected under Rider DMR to specific expenditures. In reality, revenues collected under Rider DMR lose their identity as “Rider DMR dollars” upon receipt by the Companies. As Company witness Mikkelsen explained, dollars collected under Rider DMR cannot be “painted” such that they can be matched directly to specific expenditures:

Once dollars come into the company, . . . they aren’t specifically marked as they move throughout the companies’ . . . income statement or balance sheet or how they are used. Once the dollars come in collectively, the dollars exist and the expectation is the dollars collected from DMR would be used for credit support and to assist in jump-starting grid modernization.⁷

Thus, no third-party monitor would be capable of “painting” Rider DMR dollars so that those dollars can be directly tracked to their eventual use, directly or indirectly, in support of grid modernization.

Given the inability to track dollars collected under Rider DMR, Staff’s review of the use of funds collected under Rider DMR necessarily will involve a straightforward comparison of the amount of funds received to the amount of funds used by the Companies (and potentially FirstEnergy Corp.) to further the purposes of Rider DMR. These uses include spending or

⁷ Rehearing Tr. Vol. X, pp. 1605-06.

otherwise devoting funds to improve or maintain the Companies' and FirstEnergy Corp.'s respective credit metrics. The Companies will receive a certain amount of funds from Rider DMR and, over time, Staff should be able to confirm that the Companies and FirstEnergy Corp. have used dollars totaling at least that amount, directly or indirectly, in support of grid modernization. The Companies can report to Staff on payments in support of, among other things: (1) grid modernization; (2) pension obligations; (3) debt service obligations; and (4) taxes. They also can provide or demonstrate to Staff any other uses of Rider DMR revenues that improve or maintain credit metrics, or that act to reduce the long-term costs of accessing capital, including comparisons to what the Companies' and FirstEnergy Corp.'s financial statements and metrics would have been absent Rider DMR. If amounts devoted to such things equal or exceed the dollars collected under Rider DMR, then the purposes of Rider DMR have been appropriately furthered. No third-party monitor is necessary for this straightforward demonstration.

Nor is a third-party monitor necessary to "ensure that there is no unlawful subsidy of the Companies' affiliates."⁸ There are controls already in place that are more than adequate to enable Staff to ensure Rider DMR is not used to subsidize affiliates. The Commission has authorized the Companies to participate in a utility money pool arrangement ("Money Pool").⁹ The Money Pool was created via an agreement among the Companies and other FirstEnergy Corp. regulated affiliates.¹⁰ Dollars the Companies collect, including dollars collected through Rider DMR, are

⁸ Fifth Entry on Rehearing, p. 128.

⁹ *In the Matter of the Application of Ohio Edison Company, et al., for Authority to Issue Short-Term Notes and Other Evidences of Indebtedness*, Case Nos. 16-2050-EL-AIS, 16-2051-EL-AIS, 16-2052-EL-AIS, 16-2053-EL-AIS, Finding and Order at 1 (December 21, 2016) ("Money Pool Order").

¹⁰ Money Pool Order at 2-3.

contributed to the Money Pool. FirstEnergy Solutions Corp. (“FES”) is not a participant in the Money Pool; there is a separate non-utility money pool comprised of FirstEnergy Corp. and its unregulated subsidiary companies.¹¹ Further, FirstEnergy Corp. can lend money to the utility Money Pool but cannot borrow from it.¹² The Companies are required to report details of their participation in the Money Pool to the Commission on a quarterly basis.¹³

Additionally, the only way for funds from utility revenues to be transferred to FirstEnergy Corp. is through a dividend, which would be publicly reported. A utility dividend to FirstEnergy Corp. will be easily accessible on FERC Form 1.¹⁴ Also, any equity infusion by FirstEnergy Corp. into FES (or, even though it would be unlikely, loans) would be publicly reported in FES’s publicly filed financial statements.¹⁵ Thus, there is an easy audit trail.¹⁶ There are no special skills possessed by third-party consultants that are needed to perform these functions.

2. Quarterly Reviews are Impractical and Unnecessary.

Because dollars collected under Rider DMR cannot be tracked as they pass through the Companies’ regulated money pool, “quarterly interim updates” to Staff will serve no purpose.¹⁷ Over a given period, the Companies will either use funds from the money pool to further the

¹¹ Money Pool Order at 3.

¹² *In the Matter of the Application of Ohio Edison Company, et al., for Authority to Issue Short-Term Notes and Other Evidences of Indebtedness*, Case Nos. 16-2050-EL-AIS, 16-2051-EL-AIS, 16-2052-EL-AIS, 16-2053-EL-AIS, Staff Review and Recommendation at 2 (December 8, 2016).

¹³ Money Pool Order, at 4.

¹⁴ *See generally* Direct Exhibit 2, Ohio Edison FERC Form 1 for 2015Q4, reflecting “Dividends on Common Stock” on page 121.

¹⁵ *See, e.g.*, OCA Ex. 32, FirstEnergy Corp. and FirstEnergy Solutions Corp. Form 10-K for the Fiscal Year ended December 31, 2014, at p. 118 (line item in FES’s Consolidated Statements of Cash Flows for “Equity contribution from parent”).

¹⁶ Of note, all existing corporate separation controls remain in place and subject to on-going review by Staff, including separation of the regulated and unregulated money pools.

¹⁷ *See* Eighth Entry on Rehearing, p. 50.

purposes of Rider DMR – or the Companies will not do so. And the anticipated expenditures or usage of funds to further the purposes of Rider DMR likely will not occur regularly, i.e., on an hourly, daily or even monthly basis. For example, pension contributions and debt maturity payments typically are not made very frequently and are lump sums, usually large, that are easily tracked and reported. In addition, Rider DMR will aid in the implementation of future grid modernization initiatives upon Commission approval. The Companies can provide Staff annually a list of what funds have been expended to further the purposes of Rider DMR. Further, the Companies’ list could be subject to audit at Staff’s convenience. Of course, the Companies will be accessible to Staff at all times to answer Staff’s queries. There is no need to create “quarterly interim updates” simply to justify retaining and paying a third-party consultant to prepare what effectively would be busy-work.

3. Real-time Monitoring Could Improperly Restrict the Use of Funds Collected Under Rider DMR.

To fulfill the objectives of Rider DMR, the Companies need the flexibility to use funds collected under the rider. The Companies may directly support grid modernization by making investments in grid modernization projects. The Companies can also indirectly support grid modernization by taking steps to improve or maintain their credit ratings and thus reduce the long-term costs of accessing capital.¹⁸ In contrast, the requirement of a monitor appears to curtail the Companies’ need for flexibility. The Eighth Entry’s description of the third-party monitor’s duties suggest more than a monitor and, instead, suggest an active participant in utility management. On this score, the difference between the Fifth Entry and Eighth Entry is striking. While the Fifth Entry only calls for Staff to review periodically how the Companies and FirstEnergy Corp. have

¹⁸ Fifth Entry on Rehearing, p. 128.

spent or devoted funds in furtherance of the purposes of Rider DMR, the Eighth Entry describes an “ongoing” and “real time” process that involves the monitor “working with” the Companies and FirstEnergy Corp. to ensure that funds collected under Rider DMR are expended appropriately. This new, expanded and detailed process cannot be squared with the Commission’s commitment that it will not place restrictions on the use of funds collected under Rider DMR.¹⁹ A process that involves “real-time” second-guessing of the Companies’ management decisions would defeat the purpose of Rider DMR by limiting the Companies’ efforts to improve their CFO to Debt ratio and other credit metrics.²⁰ Given that, as demonstrated above, whether the Companies have worked to further the purposes of Rider DMR will not involve substantial work for any third-party consultant, a consultant will have strong incentives to justify its fees by inserting itself in the decision-making process or seeking opportunities to second-guess utility management. In fact, there can be little purpose for a monitor and for “real time” review other than to seek to stop the Companies (or potentially FirstEnergy Corp.) from using available funds in a certain way as determined by management.

The expansive monitoring process outlined in the Eighth Entry on Rehearing disregards the long-recognized separation of roles between utility management and regulators. Regulators establish guidelines and conduct reviews after-the-fact to ensure compliance. Given that utilities are privately owned and operated, regulators cannot and should not usurp the management role. *See Elyria Tel. Co. v. Pub. Util. Comm.*, 158 Ohio St. 441, 447-448, 110 N.E.2d 59 (1953) (utility “is subject to extensive control and regulation” but “is still an independent corporation and

¹⁹ Fifth Entry on Rehearing, p. 127.

²⁰ Fifth Entry on Rehearing, p. 127 (“Therefore, placing restrictions on the use of Rider DMR funds would defeat the purpose of Rider DMR.”).

possesses the right to regulate its own affairs and manage its own business”); *id.* at 448 (Commission’s “powers do not include the right to manage utilities or dictate their policies”). Thus, while after-the-fact audits of expenses are not uncommon, the Companies are not aware of any rider for any company in Ohio that requires Commission approval via “real time” monitoring prior to incurring expenses. The Commission’s proposed RFP for a third-party monitor unreasonably and unlawfully blurs the line between regulation and management. Therefore, the Commission should reconsider the retention of a third-party “monitor” that could interfere with Rider DMR’s effectiveness.

B. The Commission Should Restore the 50 Basis Point Adder to the Return on Equity (“ROE”) Calculation for Rider AML.

The Commission erred in relying on the elimination of Rider RRS to justify also eliminating the 50 basis point adder to the ROE for plant included in Rider AML.²¹ While Rider RRS was linked indirectly to smart grid modernization, the connection was not, as misstated by the Commission, the \$561 million forecasted to be returned to customers over an eight-year period.²² To the contrary, the link made by Company witness Mikkelsen was that “cash projected to be collected in the first few years of Rider RRS could be used to fund the capital expenditures necessary to modernize the Companies’ distribution grid through advanced metering infrastructure, distribution automation, and Volt/Var controls.”²³ Thus, in the first few years of ESP IV as approved by the Commission in its March 31, 2016 Order, the Companies would be

²¹ Eighth Entry on Rehearing, p. 67-68.

²² See Eighth Entry on Rehearing, p. 67.

²³ Company Ex. 155 (Rehearing Testimony of Eileen M. Mikkelsen), p. 12.

receiving two beneficial incentives – Rider RRS dollars and the 50 basis point adder – to promote grid modernization in different ways.

When the Commission decided to eliminate Rider RRS and thereby eliminate one of these incentives, it lacked reasonable grounds to also eliminate the 50 basis point adder. Rider DMR is little different from Rider RRS in the short term, as the Commission has authorized Rider DMR for only three years. If short-term revenues from Rider RRS plus a 50 basis point adder made sense as alternate methods to encourage grid modernization, then short-term revenues from Rider DMR plus a 50 basis point adder must also make sense. The Commission’s failure to recognize this fact in its Eighth Entry on rehearing is erroneous.

Indeed, given that the Commission has now completed two phases of its PowerForward initiative and is planning the third phase in which the Commission will examine what specific regulations and policies can be instituted to facilitate grid modernization opportunities, the Commission’s decision to reduce its support for incentives related to grid modernization in this proceeding is unreasonable. Through the PowerForward initiative, the Commission intends “to chart a clear path forward for future grid modernization projects, innovative regulations and forward-thinking policies.”²⁴ The 50 basis point adder proposed in the Third Supplemental Stipulation and approved by the Commission in its March 31, 2016 Order is the type of innovative regulation and forward-thinking policy the Commission should support through PowerForward. The 50 basis point adder incentivizes the use of available cash for grid modernization by ensuring that grid modernization projects earn a more favorable return than other competing investments,

²⁴ PowerForward Ohio, accessed on September 9, 2017 at: <https://www.puco.ohio.gov/industry-information/industry-topics/powerforward/>

including investments in the transmission system, over the lives of the grid modernization investments.²⁵ Grid modernization projects compete with other projects for investment dollars.²⁶ The 50 basis point adder provides an incentive to direct those investment dollars to grid modernization in Ohio. Eliminating this 50 basis point adder from the Companies' grid modernization toolkit could reduce the Companies' ability to further the Commission's PowerForward objectives.

The Eighth Entry on Rehearing errs by focusing only on the next few years and not on the long-term future of grid modernization. The Eighth Entry justifies elimination of the 50 basis point adder by reference to Rider RRS and Rider DMR, which were and are, respectively, shorter-term incentives.²⁷ But forward-thinking policies require a longer-term view. The Companies' grid modernization projects will be competing for dollars long after Rider DMR terminates. Thus, the 50 basis point adder should be a part of the Commission's forward-thinking policies to support grid modernization.

Because the 50 basis point adder has received broad support from the many interested parties that were signatories to the Third Supplemental Stipulation, it is possible the Commission's third phase of PowerForward will conclude that incentives such as this 50 basis point adder should be essential elements of any set of innovative grid modernization regulations. But that is no reason for the Commission's refusal in the Eighth Entry on Rehearing to restore this grid modernization incentive to the Companies' ESP IV. At the very least, the Commission should grant rehearing in

²⁵ Hearing Tr. Vol. XXXVII, p. 7775 (Mikkelsen Cross) (explaining that the grid modernization ROE, including the 50 basis point adder, was specifically "designed to incent the investment in grid modernization vis-a-vis other potential investments.").

²⁶ See Rehearing Tr. Vol. VIII, p. 1405-06 (Kahal Rebuttal Cross) (admitting that there is a potential for competition for the same funds among subsidiaries within a corporate structure).

²⁷ Eighth Entry on Rehearing, pp. 67-68.

this proceeding so as to not appear to be prejudging what innovative ratemaking policies the Commission may decide to support during its PowerForward review.

Given the lack of the testimony supporting the view that Rider DMR would supplant the purpose of the 50 basis point adder and the obvious conflict the Commission's actions here pose for its PowerForward initiative, the Commission should reinstate the 50 basis point adder.

II. CONCLUSION

For the foregoing reasons, the Companies respectfully request that the Commission grant rehearing and correct the errors discussed in this Application for Rehearing.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I certify that the above was filed electronically through the Docketing Information System of the Public Utilities Commission of Ohio on this 15th day of September, 2017. The PUCO's e-filing system will electronically serve notice of the filing of this document on counsel for all parties. Further, a courtesy copy has been served upon parties via electronic mail.

/s/ James F. Lang

One of the Attorneys for the Companies

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