

**BEFORE THE
PUBLIC UTILITIES COMMISSION OF OHIO**

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| In the Matter of the Commission's |) | |
| Investigation of the Financial |) | Case No. 18-47-AU-COI |
| Impact of the Tax Cuts and Jobs Act of 2017 |) | |
| on Regulated Ohio Utility Companies. |) | |

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

February 15, 2018

TABLE OF CONTENTS

- I. INTRODUCTION 1
- II. IMPACTS OF THE TCJA NEED TO BE CONSIDERED FOR EACH UTILITY INDIVIDUALLY 2
 - A. The TCJA affects all utilities across the state..... 2
 - B. Each electric distribution utility has its own retail rate plan..... 2
 - C. Actual tax expense reductions resulting from the TCJA can be incorporated into retail rates consistent with the terms and conditions of approved retail rate plans..... 3
- III. THE COMPANIES WILL UPDATE ALL APPLICABLE RIDERS TO REFLECT CUSTOMER SAVINGS, AND HAVE ALREADY TAKEN PROACTIVE ACTIONS TO DO SO..... 3
 - A. The Companies have filed updated Riders DMR and DCR to incorporate the impacts of the TCJA. 3
 - B. Other riders will be updated to comply with the TCJA..... 4
- IV. THE COMPANIES’ BASE DISTRIBUTION RATES ARE NOT IMPACTED BY THE TCJA BECAUSE THE COMMISSION HAS FROZEN THESE RATES THROUGH MAY 31, 2024..... 4
 - A. Customers benefit from the base distribution rate freeze approved in ESP IV. 4
 - B. Exceptions to the base distribution rate freeze are not applicable to the TCJA..... 6
 - C. The Companies’ base distribution rate freeze was fully litigated and approved by the Commission in ESP IV. 9
 - D. Modifying the Companies’ approved base distribution rate freeze would be bad policy..... 10
 - E. Any remaining impacts of the TCJA on the Companies’ base distribution rates can be addressed in the Companies’ next base distribution rate case. 12
- V. CONCLUSION..... 12

I. INTRODUCTION

Ohio Edison Company, The Cleveland Electric Illuminating Company and The Toledo Edison Company (the “Companies”) welcome the opportunity to provide comments on the two issues identified by the Commission for investigation:

- Those components of utility rates that the Commission will need to reconcile with the Tax Cuts and Jobs Act of 2017 (“TCJA”), which reduced the federal corporate income tax rate from 35 percent to 21 percent effective January 1, 2018; and
- The process and mechanics for how the Commission should do so.¹

Given that the TCJA will impact all utilities in the state in different ways and degrees, the Companies encourage the Commission to adopt a flexible approach in this proceeding. The Commission should recognize that each industry, and each utility within each industry, is likely to face different circumstances with respect to the impacts of the TCJA. Indeed, the Companies believe that a one-size-fits-all approach is not practical or appropriate to employ.

With respect to the Companies, the Commission will not need to reconcile any components of the Companies’ rates with the TCJA because the Companies will make all appropriate and lawful reconciliations under existing tariff provisions. Any retail rate adjustments – from the TCJA or otherwise – are limited by the terms and conditions of the Companies’ fourth Electric Security Plan (“ESP IV”), which was approved by the Commission and went into effect June 1, 2016.² The Companies already have filed updates to their Distribution Modernization Rider (“Rider DMR”) and Delivery Capital Recovery Rider (“Rider DCR”),³ and will update in a timely

¹ Case No. 18-47-AU-COI, Entry at ¶ 4.

² *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, Opinion and Order (Mar. 31, 2016) (the “ESP IV Order”); ESP IV Finding and Order (May 25, 2016) (approving tariffs effective June 1, 2016).

³ PUCO Case No. 17-2280-EL-RDR (Rider DMR); PUCO Case No. 17-1919-EL-RDR (Rider DCR).

fashion all other riders approved in ESP IV that have reconciliation provisions and are calculated in part based on the federal corporate income tax rate. The Companies' base distribution rates are not impacted by the TCJA income tax rate reduction because they are frozen through May 31, 2024 under ESP IV. Therefore, the Commission will not need to reconcile any of the Companies' utility rates with the TCJA.

II. IMPACTS OF THE TCJA NEED TO BE CONSIDERED FOR EACH UTILITY INDIVIDUALLY

A. The TCJA affects all utilities across the state.

The Commission should recognize that the TCJA applies to utilities across a range of different industries within the state. As a result, there likely are inherent differences among the different industries when considering potential impacts on retail rates from the TCJA. Therefore, it is not practical to pursue a one-size-fits-all approach to address the impacts of the TCJA on all utilities in the state.

B. Each electric distribution utility has its own retail rate plan.

In addition to inter-industry differences, there are also intra-industry differences among the state's electric distribution utilities ("EDUs") that further the need for each utility to be considered on an individual basis. Electric Security Plans ("ESPs") are filed and approved individually by each EDU, or jointly for EDUs under common ownership. As a result, the EDUs are subject to specific terms and conditions approved by the Commission in their respective ESPs, including, but not limited to, riders, base rate provisions, and other commitments impacting the timing of future rate filings. Further, certain EDUs currently have ESPs or base distribution rate cases pending with the Commission.⁴ The TCJA could factor into the results of these cases. The Companies,

⁴ See, generally, PUCO Case No. 15-1830-EL-AIR (DP&L); PUCO Case No. 17-32-EL-AIR (Duke Energy), PUCO Case No. 17-1263-EL-SSO (Duke Energy), PUCO Case No. 16-1852-EL-SSO (AEP).

however, do not have a pending ESP or distribution rate case – this case is not appropriate for an adjustment. Due to these differences, it is not practical or appropriate to implement a common statewide solution in this proceeding for the state’s EDUs.

C. Actual tax expense reductions resulting from the TCJA can be incorporated into retail rates consistent with the terms and conditions of approved retail rate plans.

EDUs that realize tax expense reductions from the TCJA can incorporate those savings into retail rates within the terms and conditions of the EDUs’ respective Commission-approved retail rate plans. For example, the Companies’ Rider DMR includes recovery of income taxes at the prevailing federal corporate income tax rate.⁵ The impacts of the TCJA can be reconciled in Rider DMR, consistent with the Companies’ Commission-approved tariffs, by calculating the applicable income tax adjustment using a federal corporate tax rate of 21% instead of 35%. In this way, customers receive benefits of the TCJA income tax reduction in a manner that is fair to all parties and consistent with prior Commission decisions.

III. THE COMPANIES WILL UPDATE ALL APPLICABLE RIDERS TO REFLECT CUSTOMER SAVINGS, AND HAVE ALREADY TAKEN PROACTIVE ACTIONS TO DO SO

A. The Companies have filed updated Riders DMR and DCR to incorporate the impacts of the TCJA.

On January 12, 2018, the Companies filed updated Riders DMR and DCR with the Commission.⁶ Both riders are calculated using a federal corporate income tax component. The updated Riders DMR and DCR incorporate the TCJA’s lower federal corporate income tax rate. The annual customer savings resulting from these updated riders equates to nearly \$40 million. For a typical residential customer using 1000 kWh per month, the estimated savings from these

⁵ ESP IV, 5th Entry on Rehearing, p. 95.

⁶ PUCO Case No. 17-2280-EL-RDR; PUCO Case No. 17-1919-EL-RDR.

rider updates is approximately 0.6% on the total monthly electric bill, or almost \$10 per year. On February 1, 2018, the Commission Staff recommended approval of the updated Rider DMR rates effective on a service rendered basis starting March 1, 2018 because they accurately reflect the new tax rates resulting from the TCJA.⁷

B. Other riders will be updated to comply with the TCJA.

Riders other than Riders DMR and DCR will be impacted by the TCJA income tax reduction and will be reconciled accordingly. Riders AMI and DSE2 will be updated with the Commission consistent with their respective authorized reconciliations. These reconciliations due to the TCJA will result in savings to retail customers. The Companies also recently filed a proposed Distribution Platform Modernization Plan, which includes an estimated revenue requirement calculation to be recovered under the existing Commission-approved Rider AMI.⁸ This calculation will be updated to incorporate the impact of the TCJA.

IV. THE COMPANIES' BASE DISTRIBUTION RATES ARE NOT IMPACTED BY THE TCJA BECAUSE THE COMMISSION HAS FROZEN THESE RATES THROUGH MAY 31, 2024

A. Customers benefit from the base distribution rate freeze approved in ESP IV.

One component of the complex balancing of interests that resulted in a partial Stipulation and Recommendation in the Companies' ESP IV proceeding was the Companies' commitment to hold their base distribution rates constant through May 31, 2024. Specifically, as agreed in the Third Supplemental Stipulation, no proceeding shall commence to adjust the Companies' base distribution rates prior to June 1, 2024.⁹ As discussed in section B below, the limited exceptions to this rate freeze do not permit a reduction in base rates to account for the TCJA or, for that matter,

⁷ PUCO Case No. 17-2280-EL-RDR, Staff's Review and Recommendation (Feb. 1, 2018).

⁸ PUCO Case No. 17-2436-EL-UNC.

⁹ ESP IV, Third Supplemental Stipulation, p. 13; ESP IV Order, p. 25.

an increase in base rates to account for many other potential expense increases. Customers benefit from this rate freeze.

The base distribution rate freezes enacted in the Companies' current and prior ESPs have provided customers the benefits of low, stable and predictable distribution rates since 2009.¹⁰ These stable, more predictable prices support economic development, the economy of Ohio and the well-being of our customers.¹¹ Customers receive protections from increasing costs such as rising labor, materials, or health care under a base distribution rate freeze, as the Companies do not have a mechanism to seek recovery of these applicable incremental expenses. The base rate freeze benefits customers by incenting the Companies to manage costs during the freeze period, which should result in lower test year costs during the base rate case that follows the base rate freeze. The base distribution rate freeze also benefits customers by avoiding the time and rate case expense associated with filing and litigating a base rate case. For these reasons, the Commission has consistently identified the base distribution rate freeze as a benefit of the Companies' ESPs in the ESP vs. MRO test.¹²

Notably, this rate freeze is part of a larger set of benefits to customers, and provisions providing stability for the Companies, that make up ESP IV. In that proceeding, the Companies committed to, and have been implementing, provisions concerning federal advocacy for market enhancements, grid modernization, resource diversification (including environmental stewardship,

¹⁰ See ESP IV Fifth Entry on Rehearing, p. 164 (October 12, 2016) and ESP IV Order, p. 119; ESP III Case No. 12-1230-EL-SSO, Opinion and Order, p. 56 (July 18, 2013) ("ESP III Order"); ESP II Case No. 10-388-EL-SSO, Opinion and Order, p. 44 (Aug. 25, 2010) ("ESP II Order"); ESP I Case No. 08-935-EL-SSO, Second Opinion and Order, p. 18 (March 25, 2009) ("ESP I Order").

¹¹ ESP IV, Direct Testimony of Eileen M. Mikkelsen (Aug. 4, 2014), pp. 5-7.

¹² See ESP IV Fifth Entry on Rehearing, p. 164 ESP IV Order, p. 119; ESP III Order, p. 56 ("laddering of products and continuation of the distribution rate increase freeze will smooth generation prices and mitigate the risk of volatility, which is a benefit to customers."); ESP II Order, p. 44; ESP I Order, p. 18.

battery technology, renewable resources, and carbon emissions reduction), economic development, and low-income assistance.¹³ The Commission has recognized that many of these commitments provide qualitative and quantitative benefits not available via a Market Rate Offer proceeding.¹⁴ In fact, the Commission has found that the \$568 million annual economic impact of retaining the FirstEnergy Corp. headquarters in Akron is an economic benefit of ESP IV.¹⁵ The Commission acted reasonably in approving all of these benefits, including the base distribution rate freeze, for customers. In contrast, making a one-off adjustment to one of these many ESP IV benefits to reflect the TCJA impact would unreasonably disrupt the balance struck in the ESP IV proceeding.

B. Exceptions to the base distribution rate freeze are not applicable to the TCJA.

The only exceptions to the base distribution rate freeze that are permitted under ESP IV are: (1) changes resulting from an emergency under R.C. 4909.16; (2) revenue neutral rate design changes; (3) rate design changes to eliminate subsidies; (4) the addition of a new service offering; and (5) an application filed by the Companies to recover increased costs associated with new or incremental taxes. None of these exceptions apply here.

R.C. 4909.16 grants the Commission authority to make temporary changes to rates in response to an emergency, *i.e.*, when the Commission “deems it necessary to prevent injury to the business or interests of the public or of any public utility of this state in case of any emergency to be judged by the commission.” If an emergency exists, the Commission would have to find by clear and convincing evidence that, absent extraordinary emergency relief, the Companies will be

¹³ See generally ESP IV, Third Supplemental Stipulation.

¹⁴ ESP IV, Fifth Entry on Rehearing), pp. 163-64.

¹⁵ ESP IV, Eighth Entry on Rehearing (Aug. 16, 2017), p. 79.

financially imperiled or their ability to render service would be impaired.¹⁶ If and only if such a showing is made, the Commission could grant temporary relief only at the “minimum level necessary to avert or relieve the emergency.”¹⁷ Additionally, the Commission cannot grant emergency relief under R.C. 4909.16 if the emergency request is filed merely to circumvent, and as a substitute for, permanent rate relief under R.C. 4909.18.¹⁸ These conditions are not satisfied here because there is no emergency and, absent extraordinary relief, the Companies would not be imperiled. The mere adjustment of the federal corporate income tax rate in the TCJA does not constitute an emergency and does not satisfy the requirements for a rate change under R.C. 4909.16.

Moreover, the TCJA does not give rise to rate design changes or involve a new service offering. Any modification to base distribution rates by isolating the impact of the TCJA would not be revenue neutral and thus would not be permitted under the approved base distribution rate freeze. Similarly, there are no rate design subsidies among customers to be eliminated by the TCJA. And no new service is being offered by the Companies because of the TCJA.

Lastly, the Incremental Tax Provision approved by the Commission in ESP II, ESP III and ESP IV permits the Companies to file a separate application to recover increased costs associated with new or incremental taxes, if not collected elsewhere, without violating the agreed-upon distribution rate freeze.¹⁹ This provision is not an existing rider or tariff through which TCJA adjustments could flow. Instead, it is simply a recognition that the Companies may request a rate adjustment to reflect new or incremental tax increases. The Companies made clear in ESP IV,

¹⁶ *In re Akron Thermal, Ltd. Partnership*, Case No. 00-2260-HT-AEM, Opinion and Order at p. 3 (Jan. 25, 2001).

¹⁷ *Id.*

¹⁸ *In the Matter of the Application of Akron Thermal, Limited Partnership for an Emergency Increase in Its Rates and Charges for Steam and Hot Water Service*, Case No. 09-453-HT-AEM (Sept. 2, 2009).

¹⁹ See ESP IV Application filed Aug. 4, 2014, p. 20; ESP III Order, p. 57; ESP II Order, p 17.

over the objection of some intervenors, that the Incremental Tax Provision allowed adjustments only for tax increases and not tax decreases.²⁰ During the ESP IV hearings, the Companies reiterated that if there should be a tax decrease or a reduction in the Companies' taxes that are embedded in base distribution rates, the Companies would not seek to credit customers because the Incremental Tax Provision is asymmetric. Companies' witness Ms. Mikkelsen clearly articulated this during cross examination in the ESP IV hearing:

Q. And you describe the incremental tax provision, and you say it allows the company to file a separate application to commence recovery of any new or incremental taxes paid or collected by the companies and not recovered elsewhere, correct?

A. Yes.

Q. Is that provision intended to address situations where the companies are facing tax increases only?

A. Yes.

Q: So if during the term of the ESP, there should be a tax decrease or reduction in the companies' taxes that are embedded in base rates, would the company not seek to credit customers for that tax reduction?

A: The companies would not seek to credit customers under that circumstance.²¹

The Commission approved the provision as proposed by the Companies without modification.²²

Thus, the Incremental Tax Provision is not a vehicle for passing through TCJA tax reductions to retail customers.

²⁰ ESP IV, Mikkelsen Direct Testimony, pp. 6-7; ESP IV Hearing Transcript, Vol. III, p. 609 (Incremental Tax Provision does not apply to tax decreases); *See* ESP IV, Direct Testimony of David J. Effron (Dec. 22, 2014), p. 7 (Incremental Tax Provision should be symmetrical and not limited to tax increases).

²¹ ESP IV Hearing Transcript, Vol. III, p. 609.

²² ESP IV Order, pp. 29, 121.

Accordingly, none of the exceptions to the Companies' approved base distribution rate freeze provide a mechanism to adjust base distribution rates for the TCJA.

C. The Companies' base distribution rate freeze was fully litigated and approved by the Commission in ESP IV.

The Companies' current base distribution rate freeze was subject to extensive litigation throughout the ESP IV case. Several parties opposed the continuation of the Companies' base distribution rate freeze.²³ Despite this opposition, the Commission approved the Companies' base distribution rate freeze, and in doing so, ruled against the arguments presented in opposition by the other parties in the case. The Commission recognized the benefits of the base distribution rate freeze:

The key provisions in the Stipulations related to distribution rates is the continuation of the base distribution rate freeze for eight years under ESP IV. The extension of the distribution rate freeze will promote stable rates, as base distribution rates will not rise during the term of ESP IV.²⁴

On rehearing, the Commission continued to reject the objections to the Companies' base distribution rate freeze raised by other parties on rehearing.

The Commission finds that arguments raised by OCC/NOAC and OMAEG questioning whether the distribution base rate freeze... [is] in the public interest should be rejected. In the Order, we noted that continuation of the distribution rate freeze will provide rate certainty, predictability and stability for customers. We affirm that finding here. Base distribution rates will remain frozen until June 1, 2024. Elimination of the distribution rate freeze, on the other hand, exposes customers to known expenses which will be recovered, such as rate case expense, and unquantifiable risks that the rate base, rate of return and expenses may be greater than in the current revenue requirement.²⁵

²³ See Initial Briefs filed in ESP IV by Ohio Consumers' Counsel, Ohio Schools Council (OSC), NOPEC, OMAEG.

²⁴ ESP IV Order, p. 92.

²⁵ ESP IV, Fifth Entry on Rehearing, p. 115.

Because the Commission has ruled upon and approved the continuation of the Companies' base distribution rate freeze, there are no changes to base distribution rates to be implemented because of the TCJA.

D. Modifying the Companies' approved base distribution rate freeze would be bad policy.

Any modifications to the base distribution rate freeze would disrupt the balance of interests agreed upon and approved by the Commission in ESP IV. Under the base distribution rate freeze, the Companies generally have agreed to bear the risk of increasing costs for eight years. Absent an emergency, the Commission, signatory parties, and other intervenors would not permit the Companies to increase base rates for an isolated expense item that increases over this eight-year time period. Although the Companies have had the right to request a rate adjustment tied to increasing tax expense since the inception of the Incremental Tax Provision on June 1, 2011, they have not sought to do so, and have continued to be restricted from seeking increases in other non-tax expenses. In addition, the Commission has discretion to deny any request made under the Incremental Tax Provision if determined by the Commission to be unreasonable. As such, it would be wholly inappropriate and contrary to the Commission's decisions in the ESP IV proceeding to require the Companies to adjust base distribution rates because of an isolated reduction in income tax expense.

Additionally, the Commission lacks statutory authority to adjust base distribution rates via single-issue ratemaking outside the ESP process in R.C. 4928.143 or the standard ratemaking process in R.C. 4909.18. Single-issue ratemaking for tax adjustments generally is not authorized.²⁶ The Commission may adopt a single-issue ratemaking provision relating to a utility's distribution

²⁶ See *Pike Natural Gas Co. v. Pub. Util. Comm.*, 68 Ohio St.2d 181, 186, 429 N.E.2d 444 (1981) (rejecting excise tax adjustment clause).

service in an ESP, but must first “examine the reliability of the electric distribution utility’s distribution system and ensure that customers’ and the electric distribution utility’s expectations are aligned and that the electric distribution utility is placing sufficient emphasis on and dedicating sufficient resources to the reliability of its distribution system.” *Id.* This process was followed in the Companies’ ESP IV proceeding, resulting in approval of the base distribution rate freeze through May 31, 2024.²⁷ The customers’ and Companies’ expectations are aligned.²⁸ Ordering a one-off tax adjustment as single-issue ratemaking outside of the ESP process in order to modify single-issue ratemaking that complied with the ESP process is bad policy.

The Companies’ base distribution rates have increased only once over the last twenty years. As a result of S.B. 3, the Companies’ base distribution rates for the market transition period were established based on the unbundled components of distribution service from the Companies’ last preceding rate cases, which the Companies agreed to freeze through December 31, 2007.²⁹ This rate freeze was extended through the end of 2008 by the Companies’ Rate Certainty Plan.³⁰ In the Companies base distribution rate case filed in 2007, the Commission determined that these frozen base distribution rates were generating rates of return of 6.52, 2.50, and 4.82 percent for CEI, Toledo Edison and Ohio Edison, respectively, which was insufficient to provide the Companies

²⁷ See ESP IV, Fifth Entry on Rehearing, ¶ 191. The Commission’s findings were supported by testimony of Company witness Mikkelsen and Staff witness Nicodemus. See Mikkelsen Direct Testimony, pp. 9-11; ESP IV, Direct Testimony of Jacob Nicodemus, pp. 6-10 (Sept. 18, 2015).

²⁸ *Id.*

²⁹ See R.C. 4928.34(A)(2); *In the Matter of the Application of FirstEnergy Corp. on Behalf of Ohio Edison Company, The Cleveland Electric Illuminating Company and The Toledo Edison Company for Approval of Their Transition Plans and for Authorization to Collect Transition Revenues*, Case No. 99-1212-EL-ETP, Opinion and Order, pp. 6, 43-44 (July 19, 2000).

³⁰ *In the Matter of the Joint Application of Ohio Edison Company, The Cleveland Electric Illuminating Company and The Toledo Edison Company for Authority to Modify Certain Accounting Practices and for Tariff Approvals*, Case No. 05-1125-EL-ATA, Opinion and Order, pp. 5, 12 (January 4, 2006). The Companies were authorized to defer up to \$150 million per year in distribution expenses for each year between 2006 and 2008 (*id.* at 8), which order was affirmed on appeal because the accounting deferral did not affect existing rates. *Elyria Foundry Co. v. Pub. Util. Comm.*, 114 Ohio St.3d 305, 2007-Ohio-4164, ¶¶ 32, 34.

reasonable compensation for the service provided.³¹ The base distribution rates approved in Case No. 07-551-EL-AIR, *et al.*, then were frozen pursuant to stipulation in each of the Companies' ESP proceedings.³² The existing base distribution rates are a product of those multiple stipulations and the ESP statute. While it is possible to go back to the last rate case and calculate the TCJA impact based on the approved revenue requirement in that case, it would not be particularly meaningful given the intervening stipulations, rate freezes and ESP orders. As a result, the Commission lacks a sound policy basis for adjusting the Companies' base distribution rates to reflect the impact of the TCJA.

E. Any remaining impacts of the TCJA on the Companies' base distribution rates can be addressed in the Companies' next base distribution rate case.

The Companies have been ordered by the Commission to file a base distribution rate case to be effective June 1, 2024.³³ In light of the base distribution rate freeze in effect and the outstanding obligation to file a new base distribution rate case, it is not appropriate to modify the Companies' base distribution rates at this time. Any remaining impacts of the TCJA on the Companies' base distribution rates can be addressed in the future proceeding.

V. CONCLUSION

The Companies thank the Commission for the opportunity to comment on this important topic. At a high level, the Companies encourage the Commission to consider the impact of the TCJA on each regulated utility individually and to find that applicable savings resulting from the TCJA should be returned by the EDUs subject to the terms and conditions of their approved retail

³¹ *In the Matter of the Joint Application of Ohio Edison Company, The Cleveland Electric Illuminating Company and The Toledo Edison Company for Authority to Increase Rates for Distribution Service, Modify Certain Accounting Practices, and for Tariff Approvals*, Case No. 07-551-EL-AIR, Opinion and Order, p. 19 (Jan. 21, 2009).

³² See ESP I Order, p. 11; ESP II Order, p. 44; ESP III Order, p. 56; ESP IV Order, p. 119.

³³ ESP IV, Fifth Entry on Rehearing, p. 116.

rate plans. Importantly, the Companies already have taken proactive actions to update certain riders estimated to save customers approximately \$40M on an annual basis, and other riders will be reconciled according to their Commission-approved terms. With regard to the Companies' base distribution rates, the Companies will continue to comply with the Commission-ordered rate freeze through May 31, 2024.

Respectfully submitted,

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Summary: Comments electronically filed by Ms. Carrie M Dunn-Lucco on behalf of The Toledo Edison Company and The Cleveland Electric Illuminating Company and Ohio Edison Company