

**BEFORE THE  
PUBLIC UTILITIES COMMISSION OF OHIO**

<b>In the Matter of the Delivery Capital</b>	<b>:</b>	
<b>Recovery Rider Contained in the Tariffs</b>	<b>:</b>	
<b>of Ohio Edison Company, The Cleveland</b>	<b>:</b>	<b>Case No. 17-2009-EL-RDR</b>
<b>Electric Illuminating Company and The</b>	<b>:</b>	
<b>Toledo Edison Company</b>	<b>:</b>	
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**REPLY COMMENTS OF OHIO EDISON COMPANY, THE CLEVELAND  
ELECTRIC ILLUMINATING COMPANY AND THE TOLEDO EDISON COMPANY**

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**INTRODUCTION**

Pursuant to the Attorney Examiner’s Entry of April 20, 2019, Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company (“Companies”) hereby reply to the comments of the Office of the Ohio Consumers’ Counsel (“OCC”) regarding the Compliance Audit of the Companies’ Delivery Capital Recovery Riders (“Rider DCR”) for the year 2017 (“2017 Audit Report”) submitted on May 11, 2018 by Blue Ridge Consulting Services, Inc. (“Blue Ridge”). OCC’s recommendations again are misguided and unwarranted because they ignore the full resolution of tax issues in the Tax Cut/Grid Mod cases and continue to fundamentally misunderstand the capital budgeting process. The Commission should reject OCC’s recommendations as explained below.

**REPLIES TO COMMENTS**

**A. The Stipulation Filed in the Companies’ Tax Cut and Jobs Act/Grid Modernization Cases Resolves All Excess ADIT Issues.**

OCC recommends that the Commission require the Companies to record and amortize a regulatory liability to return to customers through Rider DCR the excess ADIT arising from the

federal Tax Cuts and Jobs Act (“TCJA”).<sup>1</sup> OCC supports its recommendation by asserting that the Stipulation filed in the Companies’ Tax Cut/Grid Mod cases<sup>2</sup> only “resolves some of FirstEnergy’s tax issues” and “even if approved, will not completely resolve the tax issues related to Rider DCR.”<sup>3</sup> According to OCC, Rider DCR “overcharges” must be returned to customers with interest.<sup>4</sup> OCC is wrong for at least three reasons.

First, the Stipulation is comprehensive with respect to the impacts of the TCJA by its very terms to which OCC agreed. The language explicitly states that it includes “resolution as to the refund of all of the savings associated with the TCJA.”<sup>5</sup> Moreover, the Stipulation explains that the full amount of excess accumulated deferred income taxes (“EDIT”) will be returned to customers via a new credit mechanism established for each Company.<sup>6</sup> OCC cannot credibly maintain that any EDIT-related tax issues remain unresolved by the Stipulation, including any impacts on Rider DCR.

Second, the Stipulation explicitly addresses the impact of the TCJA on Rider DCR. Pursuant to the Stipulation, Rider DCR will reflect the inclusion of the normalized and unamortized non-normalized property EDIT balances as of December 31, 2017.<sup>7</sup> The normalized EDIT included in the DCR rate base will be fixed at the December 31, 2017 balance, and not be amortized through the DCR. The non-normalized property EDIT included in the DCR rate base

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<sup>1</sup> Comments on the Audit Report of FirstEnergy’s Charges to Consumers Under the Delivery Capital Recovery Rider Submitted by the Office of the Ohio Consumers’ Counsel, p. 2 (hereafter referred to as “OCC Comments”).

<sup>2</sup> *In the Matter of the Application of Ohio Edison Company, The Cleveland Electric Illuminating Company and The Toledo Edison Company to Implement Matters Relating to the Tax Cuts and Jobs Act of 2017, et al.*, Case No. 18-1604-EL-UNC *et al.*, Stipulation and Recommendation filed November 9, 2018 ( “Original Stipulation”) and Supplemental Stipulation and Recommendation filed January 25, 2019 (“Supplemental Stipulation”), collectively hereafter referred to as “Stipulation”.

<sup>3</sup> OCC Comments p. 2.

<sup>4</sup> *Id.*

<sup>5</sup> Original Stipulation at p. 7.

<sup>6</sup> *Id.* at p.8.

<sup>7</sup> *Id.*

will be updated as the balance is amortized.<sup>8</sup> Accordingly, OCC's arguments that the TCJA impacts on Rider DCR need to be addressed in this proceeding are misguided.

Third, OCC's assertion that there have been EDIT-related Rider DCR "overcharges" to customers resulting from the TCJA is false because OCC overlooks the impact of the Rider DCR revenue caps. Any TCJA-related impacts on Rider DCR would follow the approved Rider DCR reconciliation process, consistent with the Stipulation and the Companies' approved electric security plan, and subject to the applicable approved Rider DCR revenue caps. Even if Blue Ridge's recommendation regarding EDIT was incorporated into Rider DCR, which OCC supports, the Companies' Rider DCR revenue requirements would still be in excess of the approved revenue caps. In other words, the EDIT resulting from the TCJA did not affect the Rider DCR rates that customers were charged. OCC's recommendation to return Rider DCR "overcharges" with interest is therefore without any practical effect and should be rejected.

For these reasons the Commission should reject OCC's EDIT recommendations.

**B. The Companies' Vegetation Management Accounting Treatment is Consistent With Their Last Base Distribution Rate Case.**

OCC recommends that the costs associated with three vegetation management work orders be removed from Rider DCR's revenue requirements, and that a comprehensive audit be performed on the Companies' vegetation management activity during the audit period.<sup>9</sup> OCC asserts "these types of tree-trimming O&M expenses are included in base distribution rates and paid by customers as part of their regular electric bill" and that "[i]nclusion of these costs for collection through Rider DCR results in customers being double-charged through both base distribution rates and Rider DCR."<sup>10</sup>

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<sup>8</sup> *Id.*

<sup>9</sup> OCC Comments at p. 7-8.

<sup>10</sup> *Id.* at p. 8-9.

To the contrary, these costs have not been included as O&M in base rates. As the Companies explained in their initial comments, the Companies' capitalization policy for certain initial clearing activity was implemented in 2004, prior to the Companies last base distribution rate case. Since these types of costs were being capitalized at the time of the Companies' last base rate case, they were not included as O&M expenses in the Companies' current base distribution rates, as OCC claims. Eliminating these costs from the Rider DCR rate base would preclude any recovery of costs for these important activities. Instead of eliminating alleged "double-recovery," OCC's recommendation would result in no recovery. Importantly, the Companies negotiated and agreed to stipulations in their prior electric security plans, which included the commitment to freeze base distribution rates in conjunction with Rider DCR and its associated revenue caps, with the understanding that their capitalization policy for these costs would continue to remain in effect consistent with the last base rate case. Acceptance of OCC's recommendation without allowing the Companies the opportunity for timely recovery or deferral of these costs would contradict the balance of these provisions that were approved by the Commission.

Further, as the Companies have noted, the Commission has found that the Rider DCR rate base should remain consistent with the establishment of rate base during the Companies' last base rate case.<sup>11</sup> OCC also has argued that Rider DCR treatment should follow that of the last base rate case.<sup>12</sup> As noted above, these vegetation management initial clearing activities were, in fact, subject to the same accounting treatment at the time of the last rate case as they

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<sup>11</sup> *In the Matter of the Review of the Delivery Capital Recovery Rider in the Tariffs of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company*, Case No. 11-5428-EL-RDR, Finding and Order, para. 25, August 22, 2012 ("However, the Commission notes that Staff concurred with the Companies that the treatment of ADIT in Rider DCR was intended to be the same methodology approved in the last distribution rate case and that Blue Ridge removed its recommendation.")

<sup>12</sup> See Comments of OCC in Case No. 15-1739-EL-RDR, filed June 23, 2017, p. 6-7; and in Case No. 16-2041-EL-RDR, filed July 7, 2017, p. 9.

are today. Therefore, it is appropriate to continue to include these capitalized costs in Rider DCR rate base.

Finally, the Companies again note that the Commission is empowered to adopt the Commission is empowered to implement whatever system of accounting it reasonably deems appropriate.<sup>13</sup> The Companies developed this policy in conjunction with outside auditors consistent with GAAP, and these activities implement initial clearing that improves service reliability and prolongs the useful service life of distribution assets. The Commission should remain consistent with the last rate case and not eliminate cost recovery of this important program that benefits current and future customers for years to come.

**C. The Companies' Capital Budgeting Process is Not Unreasonable.**

OCC's faulty review of the Auditor's summary of its sample analysis in the 2017 Report leads OCC to mistakenly allege a lack of proper budget planning. Because the Auditor's sample analysis included "overrun" and emergent projects, OCC opines that imprudent costs could be passed along to customers through Rider DCR.<sup>14</sup> OCC recommends that the Commission approve a rebuttable presumption of imprudence for projects that are over budget by 30% or that have no budget.<sup>15</sup> However, OCC continues to take the Auditor's sample analyses out of context and ignores the Auditor's conclusions that the Companies' processes and the amounts for which recovery is sought are not unreasonable.<sup>16</sup>

First, OCC continues to misapprehend the nature of the capital budgeting process for a major electric utility, including the difference between projects or programs and individual work

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<sup>13</sup> See the Companies' Comments at p. 4.

<sup>14</sup> OCC Comments p. 10

<sup>15</sup> *Id.* at p. 10-12.

<sup>16</sup> The Companies incorporate by reference their rebuttal to OCC's past arguments in Reply Comments filed in Case Nos. 15-1739-EL-RDR and 16-2041-EL-RDR on July 24, 2017 and August 7, 2017, respectively.

orders. It simply is not possible to budget at a work order level for “blanket” work and so the Companies budget at an investment reason level. A prime example is new business residential work where the Companies cannot possibly predict at the time the capital budget is finalized precisely where and when a new customer will request service. Further, as the Companies have explained, unlike OCC’s unilateral focus only on how much the cost of individual work orders may exceed the original budget, the Auditor ensures that the underlying policies, procedures and controls—and the total capital budget—are adequate and not unreasonable.<sup>17</sup> And in every instance of further inquiry as to the cause of any given work order exceeding its budget, the Auditor found the Companies’ explanation to be not unreasonable.<sup>18</sup> Further, the Auditor’s overall conclusion states “[b]ased on information reviewed, Blue Ridge concluded that the Companies’ controls were adequate and not unreasonable.”<sup>19</sup> OCC’s allegations of the Companies’ mismanagement of their capital budget planning process should be rejected.

Second, OCC seems not to understand that the work orders in the Auditor’s sample are more complex in nature and thus more prone to budget variances. Blue Ridge uses a cost magnitude sampling technique combined with professional judgment—not random sampling.<sup>20</sup> This cost magnitude sampling technique first segregates work orders by dollar amount so that only work orders above a materiality threshold are sampled for analysis, along with the work orders subjectively selected by Blue Ridge. Such work orders are more likely to be multi-year, multi-phase, complex, emergent, or “blanket” in nature, and are more prone to the many variables which

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<sup>17</sup> As noted on page 26 of the Audit Report, the Commission-approved standard of review in the Rider DCR audit is to confirm that the amounts sought for recovery are not unreasonable based on the facts and circumstances known at the time such expenditures were committed.

<sup>18</sup> 2017 Audit Report, p. 16 (“The Companies’ reasoning for each project’s actual costs exceeding the budget was specific and unique to that project and not unreasonable.”)

<sup>19</sup> *Id.* at p. 43.

<sup>20</sup> *Id.* at p. 60.

can affect actual-to-budget variances. This sampling technique is appropriate for the “deeper dive” analysis that allows Blue Ridge to determine whether processes and controls and outcomes were adequate and not unreasonable for these most challenging and dynamic types of projects. Conversely, OCC treats the sample observations as applicable to the whole work order population as if the sample was a simple random sample, and further only focuses only the conditions where costs exceed the budget instead of looking costs coming in under budget as well as the applicable underlying processes and controls. In contrast to Blue Ridge’s ‘deeper dive’, OCC’s analysis is merely a superficial glimpse at the data and thus leads to inappropriate conclusions and recommendations.

Third, OCC ignores key data supporting the Auditor’s findings and conclusions that the Rider DCR amounts for which recovery is sought are adequate and not unreasonable. For example, OCC picked the Companies’ investment in mobile radio operations to claim that the Companies should have been able to include the activity at the time of annual budget preparation. However, OCC ignored the Auditor’s “deeper dive” reporting that the need was driven by a vendor’s actions, not the Companies’, and that the Companies evaluated alternatives and chose the less costly and more timely solution.<sup>21</sup> OCC further selectively quoted testimony from another proceeding focused on future grid operations to claim that this investment should be ineligible for inclusion within this audit period. But this does not prove that the mobile radio operations are not used and useful *right now* in providing safe and reliable electric service at reasonable prices, rather, it proves that the Companies’ investments are not short-sighted and are not unreasonable based on the facts and circumstances known at the time such expenditures were committed.

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<sup>21</sup> 2017 Audit Report at p. 66.

Finally, as the Companies have noted in reply comments in past audits,<sup>22</sup> the Companies already “share the risk of cost overruns” that OCC again claims its proposed presumption of imprudence standard would provide.<sup>23</sup> The amount of Rider DCR revenue collected by the Companies is subject to approved revenue caps, so the Companies are not insulated from the risk of cost overruns on individual projects. Further, in the Companies’ current situation where their Rider DCR revenue requirements are in excess of the applicable revenue caps, every single work order cost “overrun” is effectively subject to non-recovery through Rider DCR, all else equal. There is no need for OCC’s recommended micro-management solution to a problem that does not exist.

### **CONCLUSION**

The Companies recommend the Commission reject OCC’s recommendations and issue an Order adopting the recommendations contained in the 2017 Audit Report, except for Recommendations No. 10 and No. 17, as set forth in the Companies’ initial comments, and finding that Blue Ridge satisfactorily performed the scope of audit services outlined in the RFP, consistent with the Commission’s Orders in ESP II, ESP III, and ESP IV.

Respectfully submitted,

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<sup>22</sup> See the Companies’ Reply Comments in Case No. 15-1739-EL-RDR, p.4; and Case No. 16-2041-EL-RDR, p. 8.

<sup>23</sup> OCC Comments at p. 10.



ILLUMINATING COMPANY, AND THE  
TOLEDO EDISON COMPANY

## **CERTIFICATE OF SERVICE**

On June 10, 2019, the foregoing document was filed on the Public Utilities Commission of Ohio's Docketing Information System. Service was made to the parties listed below via electronic mail.

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