

STATE OF MARYLAND
PUBLIC SERVICE COMMISSION

*In the Matter of the Petition of the
Maryland Office of People's Counsel to
Investigate the Future of First Energy's
Relationship with Potomac Edison In
Light of Recent Events* *
*
* Case No. 9667
*
*

**INITIAL POST-DISCOVERY BRIEF
OF THE MARYLAND OFFICE OF PEOPLE'S COUNSEL**

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By its very name, this Commission docket concerns the future of FirstEnergy’s relationship with Potomac Edison in light of recent events. Considering that “recent events” relating to the FirstEnergy bribery scandal and implicating Potomac Edison continue to emerge and evolve by the day, Yogi Berra’s famous quip that “the future ain’t what it used to be” has never been so apt.

Indeed, in the short time that has passed since the Commission’s January 19th status conference, numerous developments have transpired that directly impact FirstEnergy and Potomac Edison and go to the heart of the issues that this Commission deemed appropriate for investigation. In just the last two weeks:

- FERC issued an extensive audit report describing significant deficiencies in FirstEnergy Service Company’s cost allocation practices, both in general and connected to FirstEnergy’s criminal conduct. Among dozens of remedial recommendations, FERC proposed that FirstEnergy “critically review and strengthen internal controls” at FirstEnergy and its subsidiaries, “establish and implement procedures” for allocating costs among its companies, and analyze “costs that FirstEnergy and its subsidiaries incurred associated with internal and external lobbying activities.” FirstEnergy accepted these and numerous other FERC recommendations, yet the results remain to be seen.

- FirstEnergy announced in an SEC filing that it had settled shareholder derivative lawsuits relating to the HB6 scandal that will result in six current board members not standing for re-election and may lead to a downsizing of the FirstEnergy board. The settlement was negotiated by the board's "Special Litigation Committee," a four-member group that includes a designee of Carl Icahn.
- A U.S. District Court Judge issued an order in the shareholder litigation requiring FirstEnergy to provide, among other things, "the names of the [FirstEnergy Board] Directors chosen to not run for re-election and the factual basis used to choose those persons" and "the precise nature and extent of the governance reforms, including who will oversee and monitor the implementation of the reforms." FirstEnergy's answer to the judge is due on February 22, 2022.

These are just some of the recent occurrences germane to the issue the Commission set for investigation in this case—FirstEnergy's relationship with Potomac Edison—and they will develop and bring to light issues central to the resolution of this case.

Beyond the imminent revelation of new insights into the scandal and its impact on FirstEnergy and its utilities, what has already been revealed in this investigation demands Commission action. The record in this case shows that FirstEnergy and its shared services company, FirstEnergy Services Company (FESC), have a problematic relationship with Potomac Edison. At virtually every juncture in this investigation, Potomac Edison has stymied efforts to investigate the extent and source of the improper cost allocations, refusing to share documents and information on the grounds that they belong to FirstEnergy. The utility's rationale raises fundamental questions about Potomac Edison's current capability to fulfill its public service obligations to its Maryland customers. As a Maryland public service company, Potomac Edison holds a public franchise imbued with the public interest. Yet the utility has shown significant

subservience during this proceeding to the will of its parent company—a company that has admitted serious criminal wrongdoing. Commission action is required to ensure the utility is vested in fulfilling its primary obligations to furnish electric utility services to its Maryland customers that are safe, adequate, just, reasonable, economical, and efficient.

The record shows that Potomac Edison has little independence from its corporate parent—a disturbing fact given the parent company’s admissions of egregious lawbreaking. For example, Potomac Edison appears to have little or no oversight of its own accounting. Rather, it pays with customer dollars costs that FESC allocates to it under FirstEnergy’s direction. And while Potomac Edison has admitted that FESC passed certain costs associated with FirstEnergy’s criminal conduct in Ohio to Potomac Edison’s customers, it has been unwilling or unable to explain precisely how this occurred or how it came up with the amounts it says customers paid for the bribery scheme.

Potomac Edison’s inability to explain exactly how customers paid for its bribery scheme is not surprising, for the record in this case shows that FirstEnergy or FESC—not Potomac Edison—identified the costs. Potomac Edison’s own representations show that the Maryland utility has been largely frozen out of FirstEnergy’s analysis and findings as to how the improper allocations could have been allowed to happen, how they were subsequently identified, and the approach used to quantify them.

Likewise, Potomac Edison has been unwilling or unable to demonstrate that it has taken steps necessary to ensure it passed no additional improper costs on to its customers beyond those identified exclusively by FirstEnergy and FESC. No systems are in place to

ensure Potomac Edison's and its customers' interests are protected against FirstEnergy or FESC's errors or misconduct.

Potomac Edison's lack of internal controls and FirstEnergy's seemingly absolute dominion over Potomac Edison has made it impossible to ascertain the extent to which Potomac Edison customers have been harmed and the amounts utility customers paid for FirstEnergy's illegal activities. This conclusion is consistent with the findings and nature of several ongoing cases, audits, and investigations in other jurisdictions, including the FERC audit described above and detailed more fully below.

The wide-ranging investigations and proceedings concerning the FirstEnergy scandal have each resulted in their own unique records. But a series of common themes ties them together, namely that (1) FirstEnergy was a very bad actor over an extended period of time, (2) FirstEnergy used and exploited its regulated utilities in furtherance of its unlawful conduct, (3) insufficient controls were in place at the regulated utilities to prevent that malfeasance, and (4) the extent and the details surrounding FirstEnergy's abuse of its utilities is not yet fully known or understood. The instant investigation bears out all these themes.

Compounding the damage that FirstEnergy's conduct has inflicted on its utilities, the scandal has left FirstEnergy vulnerable to severe intrusion into its corporate governance. Shortly after the revelation of the HB6 scandal, FirstEnergy's stock price fell substantially. Thereafter, corporate raider Carl Icahn announced his intention to purchase hundreds of millions of dollars' worth of FirstEnergy stock. Icahn then threatened to engage in a proxy fight with FirstEnergy to secure representation on the FirstEnergy

Board of Directors. And less than a month after Icahn first announced his intended purchase, FirstEnergy capitulated to his demands and entered into a shareholder agreement giving Icahn designees two seats on the FirstEnergy Board along with additional and unique rights not enjoyed by any other FirstEnergy Board member. As noted above, just last week FirstEnergy announced that one of those designees was involved in a shareholder settlement that could result in a reduction of board seats, thereby strengthening the influence of the two Icahn designees.

This Commission remains the last bulwark against the Icahn designees assuming the full powers the Icahn agreement gives them, including the ability to exercise substantial influence over Potomac Edison and all FirstEnergy's utilities. The Commission must review the Icahn agreement under PUA § 6-105 to consider whether the Icahn agreement will benefit Potomac Edison's Maryland customers, will result in no harm to Potomac Edison's Maryland customers, and is consistent with the public interest.

* * *

In this initial post-discovery brief, the Office of People's Counsel will present the information we have learned through discovery and public sources concerning the issues set for investigation, highlight what information remains missing, and proffer recommendations for Commission action. Our investigation raises alarm bells about the relationship between Potomac Edison and its parent company, and we recommend regulatory actions that should be taken immediately based on the available evidence. But key questions remain unanswered that the Commission should address by continuing—and broadening—this important investigation.

Below, this brief will first provide a procedural background of the present case as well as a summary of its substantive discussion. The substantive discussion that follows (1) analyzes the issues surrounding improper cost allocations to Potomac Edison customers, (2) explains how the Icahn Agreement relates to the Commission’s responsibility to review acquisitions enabling persons to exercise “substantial influence” over Maryland utilities, and (3) provides OPC’s recommendations for Commission action.

BACKGROUND AND SUMMARY

FirstEnergy is the corporate parent of Potomac Edison, its wholly owned subsidiary and a regulated Maryland distribution utility. FirstEnergy has acknowledged having engaged in criminal behavior involving, among other things, “conspir[ing] with public officials and other individuals and entities to pay millions of dollars to and for the benefit of public officials in exchange for specific official action for FirstEnergy Corp.’s benefit.”¹ As part of the financial fallout that befell FirstEnergy following disclosure of this scandal, FirstEnergy agreed to provide two seats on its Board of Directors to

¹ *United States of America v. FirstEnergy Corp.*, Deferred Prosecution Agreement at 17, Case No. 1:21-cr-86 (S.D. Ohio 2021) (DPA). The quoted assertion is part of a “Statement of Facts” that begins with the assertion that: “*The United States and FirstEnergy Corp. stipulate and agree that if this case proceeded to trial, the United States would prove the facts set forth below beyond a reasonable doubt.*” The purpose of this scheme was the financial bail-out of certain FE coal and nuclear plants via the passage of Ohio House Bill 6 (HB6). In addition to the Householder payments, FirstEnergy paid millions of dollars to entities linked to the former Chair of the Ohio Public Service Commission apparently to further FirstEnergy’s interests relating to the passage of HB6 and other FirstEnergy legislative and regulatory priorities.

designees of the Carl Icahn Group and gave the Icahn-selected Directors a set of special governance rights afforded to no other Board member.²

In response to these developments, OPC petitioned the Commission to open an investigation into the impacts of this scandal on Potomac Edison ratepayers.³ Potomac Edison responded to the petition by asking that the Commission summarily dismiss it, and—withstanding FirstEnergy’s corrupt conduct—labeled OPC’s concerns as “either baseless or are built upon a misunderstanding (or misstating) of publicly-available facts.”⁴ At the same time, Potomac Edison acknowledged that funds charged to its ratepayers were used as part of FirstEnergy’s efforts to bribe public officials, but claimed to have conducted an internal analysis, and found that “less than \$38,000 of such improperly classified or inadequately documented funds . . . were inadvertently reflected in distribution base rates[.]”⁵ PE suggested that this amount of bribe money was “so small” that it was “not practical to reduce current distribution rates to remove those charges,” and proposed instead to refund the money as part of Potomac Edison’s next rate

² These arrangements are pursuant to a March 16, 2021, “Director Appointment and Nomination Agreement” by and between FirstEnergy Corp. and the Icahn Group. More recently, and as described *infra*, FirstEnergy has entered into an agreement with Blackstone Infrastructure Partners LP, pursuant to which FE will issue \$1 billion of common stock to Blackstone, and it will be afforded the right to nominate a director to the FirstEnergy board of directors for as long as Blackstone maintains the requisite ownership interest in FirstEnergy. For its part, FirstEnergy has agreed to name the Blackstone nominee to any vacant Board seat during the nomination period, and to otherwise support the nominee’s candidacy in any future Board elections.

³ Petition of the Office of People’s Counsel to Investigate the Future of FirstEnergy’s Relationship with Potomac Edison in Light of Recent Events (May 11, 2021) (OPC Petition).

⁴ In the Matter of the Petition of People’s Counsel to Investigate the Future of FirstEnergy’s Relationship with Potomac Edison in Light of Recent Events 1 (June 9, 2021) (Reply of Potomac Edison).

⁵ Reply of Potomac Edison at 9.

case.⁶ Separately, Potomac Edison contended that the Icahn Directors appointed to the FirstEnergy board had not acquired “substantial influence” over FirstEnergy, and, by extension, Potomac Edison, because, among other things, the Icahn board members are subject to the same fiduciary obligations as the other FirstEnergy Directors.⁷

In Order No. 89888, the Commission granted OPC’s request (in part) and opened an investigation “into the future relationship between” FirstEnergy and Potomac Edison,⁸ focusing on “certain issues that either impact Potomac Edison directly, or have a non-minimal likelihood of impacting Potomac Edison.”⁹ The issues set for investigation were:

- a. The extent that any results of the scandal have affected, or might in the future affect, Potomac Edison’s cost to access funds from FirstEnergy’s “money pool”;¹⁰
- b. Whether and to what extent FirstEnergy used, is using, or intends to use any funds from Potomac Edison to pay for the bribes, lobbying costs, legal fees or any other costs associated with the misconduct by FirstEnergy;

⁶ *Id.* According to the response to OPC DR No. 1.4, Potomac Edison has established a “regulatory liability” for the monies to be refunded, the value of which (as of July 31, 2021) was \$96,966.32.

⁷ Reply of Potomac Edison at 16 (“the Icahn Designees are bound by the same fiduciary duties as any other director and must act in the best interests of FirstEnergy and its shareholders in discharging their board responsibilities.”) (footnote omitted).

⁸ Order Granting, In Part, Petition Requesting Investigation, Order No. 89888, P 1 (July 26, 2021).

⁹ *Id.* P 18. In so doing, the Commission noted that it:

clearly has jurisdiction over Potomac Edison’s use of Maryland ratepayer funds and the cost of credit for Potomac Edison. PUA 6-101; 4-102; 4-103(b). Additionally, in approving the merger of Potomac Edison and FirstEnergy, the Commission expressly retained jurisdiction over both applicants to enforce the provisions of the Merger Order.

Id. at n.6.

c. The extent to which the “Icahn Agreement” may potentially cause the Icahn-appointed directors to exercise “substantial influence” over Potomac Edison as set forth in PUA § 6-105.

Id. P 18. In this first phase of the investigation, the Commission permitted OPC and other interested parties four months to conduct discovery on these issues, following which the Commission committed to conducting “a status conference at a future date to assess the results of discovery and whether additional procedural steps are warranted, including the filing of written testimony, a hearing schedule and any post-hearing briefing.” *Id.* P 19.

In the months since the issuance of the Commission’s order, OPC has sought to develop information concerning each of these issues. We will review below what has been produced, but note at the outset that obtaining data has been challenging. While Potomac Edison has claimed to have “turned out its pockets,”¹¹ it is obvious that essential information has yet to be provided.¹² The needed data may in fact reside outside of Potomac Edison’s files, but that does not mean that the information does not exist.

Based upon information provided by the company in this proceeding, as well as publicly available information related to other investigations of FirstEnergy and its distribution utilities, there is good reason to believe that the requisite data are in the

¹¹ Potomac Edison Company’s Opposition to the Office of People’s Counsel’s Motion for Extension of the Discovery Period at 2 (Dec. 10, 2021).

¹² The “internal investigation” that Potomac Edison says supports its \$38,000 refund number has not been produced, nor has the “list” of accounts to be examined in conducting the refund analysis, which Potomac Edison says was provided by a FirstEnergy executive in connection with the conduct of the investigation. Potomac Edison’s Notice of Appeal and Memorandum in Support of Appeal of Proposed Order at 10 & 27 n.52 (quoting Potomac Edison’s Response to OPC DR No. 5.6). While Potomac Edison originally marked its response to OPC DR. No. 5.6 as confidential, it chose to reveal this information in its public pleading.

possession of FirstEnergy or FESC.¹³ FESC provides a broad range of centralized services to Potomac Edison (and FirstEnergy’s other distribution company affiliates) and FESC costs are recovered through billings to the distribution companies. The importance of FirstEnergy and FESC to the matters at issue here cannot be overstated. Literally every single substantive data response provided in this proceeding is sponsored by an individual with a FirstEnergy or FESC job title.¹⁴ But, where useful to it, Potomac Edison asserts that as neither FirstEnergy nor FESC were included in the order opening this investigation, they are not required to produce responsive information.¹⁵ FirstEnergy and FESC have thus wielded their control over Potomac Edison as a sword to provide selectively the information they want to disclose, and their separate corporate identities as a shield to limit the access afforded OPC, intervenors, and, ultimately, the Commission to the information necessary to ventilate these matters and get to the bottom of the truth.

¹³ See *infra* at 12-13, discussing the Motion for an *In Camera* Review to Resolve the FirstEnergy Utilities’ Claim of a Privilege Against Responding to OCC’s Discovery and Motion to Require FirstEnergy Entities to File Notice If They Disclose any Records that They Claim To Be Privileged by Office of the Ohio Consumers’ Counsel, Supplemental Privilege Log Volume 1, Case No. 20-1502-EL-UNC (Jan. 13, 2022).

¹⁴ For example, Potomac Edison has stated in response to a discovery request that the individuals involved in the analysis concluding that Potomac Edison’s rates include \$38,000 in charges relating to the bribery scheme were: (1) Ray Valdes, FESC’s Director of Rates and Regulatory Affairs (2) **[BEGIN CONFIDENTIAL]**

[END CONFIDENTIAL] No person in the direct employ of Potomac Edison is listed as having been involved in the analysis. Potomac Edison has also stated that Eileen Mikkelsen, a former FirstEnergy Vice President who was removed from her position in connection with the Randazzo scandal, provided Valdes the list of charges to review and that Valdes made no independent assessment as to what charges were improper. OPC has been unable to obtain this list or any of Mikkelsen’s other instructions to Valdes concerning the improper charge analysis.

¹⁵ “It bears repeating, however, that the Order pursuant to which OPC issued its data requests granted limited discovery as to Potomac Edison only, *not* FirstEnergy.” Potomac Edison’s Opposition to OPC’s Motion to Compel Responses to Certain Discovery Requests at 4 (Nov. 1, 2021).

Potomac Edison's hiding behind corporate boundaries has made it impossible for OPC to verify the accuracy of Potomac Edison's central claim in this proceeding: that its ratepayers have paid rates that include \$38,000 on an annual basis in charges that contributed to FirstEnergy's bribery scheme. Indeed, it is the other way around: the data we have reviewed and the analyses to which we have had access indicate that the \$38,000 figure may well be understated.

Potomac Edison's separate suggestion that any refunds can be handled in the company's next rate case might be sensible if Potomac Edison had demonstrated that \$38,000 in refunds is in fact all that is at issue. But that showing has not been made.

OPC's efforts to gain information about the extent to which the Icahn directors have acquired "substantial influence" has likewise been met with objections. Potomac Edison takes the position that data requests seeking communications among Icahn and FirstEnergy personnel concerning this subject either "exceed[] the scope of this proceeding" or are privileged.¹⁶

The absence of needed information should not be tolerated. Indeed, it should not have been necessary for the Commission to name FirstEnergy or FESC as specific respondents to this investigation for the requisite information to have been produced. FirstEnergy owns a utility providing service in Maryland and has admitted to the Commission of a serious crime that has impacted Potomac Edison customers. FirstEnergy's failure to "step up" and provide voluntarily any missing documentation is

¹⁶ See e.g., Response to OPC DR No. 1.10.

both disappointing and contrary to its commitment in the Deferred Prosecution Agreement. FirstEnergy there agreed to cooperate in government investigations of the scope and impact of its conduct.¹⁷ FirstEnergy’s press statements affirm that its “core values and behaviors include integrity, openness, and trust.”¹⁸ Potomac Edison stated in a discovery response in this proceeding “that Cooperation with all investigations and other regulatory matters” was a central element of FirstEnergy and Potomac Edison’s plans for restoring both companies’ credit ratings.¹⁹

Equally important, and as we will explain here, information concerning the scope of FirstEnergy’s misconduct and its impact on Potomac Edison (and other FirstEnergy distribution utilities) continues to come to light—both in this proceeding and through related ongoing efforts outside of it. On February 4, 2022, the Office of Enforcement, Division of Audits and Accounting (DAA) at the Federal Energy Regulatory Commission issued a report detailing the results of its audit of FirstEnergy and its subsidiaries’

¹⁷ DPA section 5(A).

¹⁸ FirstEnergy Reaches Agreement to Resolve Department of Justice Investigation (July 22, 2021), https://www.firstenergycorp.com/newsroom/news_articles/firstenergy-reaches-agreement-to-resolve-department-of-justice-i.html

¹⁹ Response to OPC DR No. 1.36. In addition, FirstEnergy’s February 10, 2022, investor presentation entitled, “4Q 2021 Strategic & Financial Highlights,” refers (at 5) to FirstEnergy’s efforts to “build[] a culture where all of us feel valued and understand the importance of doing what is right” and refers to the company’s “dedicat[ion] to helping to restore trust and pride in FirstEnergy by building a company grounded in an unwavering culture of compliance, ethics, integrity, and accountability at every level[.]” The presentation can be accessed at

<https://investors.firstenergycorp.com/investor-materials/webcasts-and-presentations/presentation-details/2022/Fourth-Quarter-2021-Strategic-and-Financial-Highlights/default.aspx> (February 10th Presentation).

compliance with aspects of FERC's accounting regulations.²⁰ FirstEnergy has accepted the majority of the DAA findings and recommendations.²¹

The DAA report shows that the information unearthed in this proceeding raises serious questions that have not yet been fully examined. The FERC auditors document concerns that FirstEnergy (through FESC) is imposing charges on Potomac Edison that are insufficiently supported. And, based on the record in this proceeding, there are concerns that Potomac Edison is paying insufficient attention to those charges before they are included in customer rates. We review the DAA audit's findings *infra*, but highlight at the outset that they include significant shortcomings in internal company controls over political activities and possible concealment of improper expenditures in rates:

Audit staff interviews of FESC employees, reviews of internal emails and messages, and Attachment A – Statement of Facts included in DPA [Deferred Prosecution Agreement] and agreed to by FirstEnergy indicate *the existence of significant shortcomings in FirstEnergy and its subsidiaries' internal controls over financial reporting, including controls over accounting for expenses relating to civic, political, and related activities, such as lobbying activities performed by and on behalf of FirstEnergy and its subsidiaries. Even more concerning, several factual assertions agreed to by FirstEnergy in DPA and the remedies FirstEnergy agreed to undertake, point towards internal controls having been possibly obfuscated or circumvented to conceal or mislead as to the actual amounts, nature, and purpose of the lobbying expenditures made, and as a result, the improper inclusion of lobbying and other nonutility costs in wholesale transmission billing rates.*²²

²⁰ Audit Report, Docket No. FA19-1-000 (Feb. 4, 2022) (DAA Audit Report).

²¹ Those it contests will be set for hearing. DAA Audit Report, Transmittal Letter P 5, Docket No. FA19-1-000 (Feb. 4, 2022) (DAA Audit Report).

²² DAA Audit Report at 48 (emphasis added).

FirstEnergy has accepted the recommendations of the FERC auditors to address this finding.²³

And with respect to FESC billings generally, the auditors conclude that subsidiaries like Potomac Edison receive insufficient details of charges:

Service Company Billing Procedures – Billing information that FESC provided to FirstEnergy’s subsidiaries pertaining to charges for services provided to them was insufficient. Specifically, FESC did not provide detailed information to reflect the services provided and showing the charges classified as direct costs, indirect costs, or compensation for use of capital, with the details of service company accounts by service provided, as required. *As a result, the FirstEnergy subsidiaries misclassified costs charged by FESC.*²⁴

FirstEnergy has accepted recommendations made by the FERC auditors to address this finding.²⁵ These are tantamount to judicial admissions, proof of the facts asserted that cannot be otherwise contested.

For the reasons detailed below, OPC urges that in the next phase of this proceeding, the Commission take the following steps:

- The Commission should broaden the investigation to include FirstEnergy and FESC and permit discovery requests (or subpoenas) directly on these companies. Doing so is the only way to ensure a complete record on whether “FirstEnergy used, is using, or intends to use any funds from Potomac Edison to pay for the bribes, lobbying costs, legal fees or any other costs associated with the misconduct by FirstEnergy.” The further discovery period should be followed by written testimony, a hearing schedule and any post-hearing briefing;

²³ *Id.* at 76-77. FirstEnergy has agreed to “provide responsive factual information” with respect to the results of future investigations, if any, into the requested lobbying-related expenses, but otherwise asserted (undemonstrated) claims of privilege. *Id.* at 77.

²⁴ *Id.* at 6 (emphasis added).

²⁵ *Id.* at 78.

- The Commission should order FirstEnergy and Potomac Edison to show cause as to why the “Icahn Agreement” should not be subject to review under Section 6-105 of the Public Utilities Article;
- The Commission should direct that all refund reports, related analyses, or other documents that FirstEnergy and its subsidiaries have either provided, or have committed to provide to FERC in response to the DAA audit, must also be provided to the Commission, Staff, and OPC, and made available for review by all participants in this proceeding;
- The Commission should direct that the results of all other investigations of FirstEnergy’s scandalous conduct—whether by agencies of the federal or state governments—be submitted to this Commission and be made available for public review and comment;²⁶
- The Commission should direct Potomac Edison to report on the controls it has implemented to ensure that, going forward, there will

²⁶ As explained the DAA Audit Report:

Following the filing of the DOJ complaint, the U.S. Securities and Exchange Commission, the U.S. Internal Revenue Service, the Public Utilities Commission of Ohio, the Ohio Attorney General, and [FERC] commenced investigations of FirstEnergy’s operations. In addition, FirstEnergy initiated its own internal investigation to be overseen by the Independent Review Committee of FirstEnergy’s Board of Directors. As of the date of this report, these investigations have either not been completed, or the findings of these investigations were not available to audit staff during performance of this audit.

DAA Audit Report at 17 (footnote omitted). We note that the DAA Audit Report goes on to state:

FirstEnergy has committed that, in the event that final, conclusive results of one or more of the investigations calls into question the propriety of its past accounting and/or rate determination decisions and customer charges, it will provide notice to the Commission and initiate actions to attain compliance with Commission accounting requirements and make refunds to customers, as appropriate.

Id. at 51.

be full and independent review of all charges FESC imposes on Potomac Edison;

- The Commission should direct Potomac Edison to show cause why its agreement with FESC should not be modified to afford it the opportunity to dispute and not pay improper charges;
- The Commission should direct Potomac Edison to have performed an independent and shareholder-funded audit of all charges imposed on Potomac Edison by FESC and should submit that audit to the Commission; and
- Potomac Edison should be directed to provide, as part of its next rate case, an analysis of the extent to which FirstEnergy’s scandal has impacted its costs of accessing the money pool.

We review the bases for each of these recommendations below.

DISCUSSION

I. The extent to which FirstEnergy has “used, is using, or intends to use any funds from Potomac Edison to pay for the bribes, lobbying costs, legal fees or any other costs associated with the misconduct by FirstEnergy” remains unknown.

It is undisputed that Potomac Edison ratepayer dollars were used in an illegal scheme perpetrated by FirstEnergy, Potomac Edison’s parent, to bribe legislators and regulators in Ohio. Potomac Edison admits that “less than \$38,000 of such improperly classified or inadequately documented funds”²⁷ are reflected in Potomac Edison’s current distribution base rates, approved as part of the company’s last base rate case.²⁸ Despite

²⁷ Reply of Potomac Edison at 9.

²⁸ Potomac Edison contends that the \$38,000 contains two different categories of funds, and that no more than \$9,744.06 of the amounts currently reflected in base rates were used to fund the Ohio bribery scheme. Response to OPC DR No. 3.08, attach. A; Response to OPC DR No. 5.3. According to Potomac Edison, another \$27,844.33 of these funds were paid to [BEGIN CONFIDENTIAL] [REDACTED]

vigorous efforts, we have been unable to verify that the amount of Potomac Edison ratepayer funds used in the base rate test year—June 2017-June 2018— and improperly reflected in the current Maryland base rates totals to less than \$38,000.²⁹

In OPC DR No. 1.1, OPC asked Potomac Edison to “describe the analysis that PE conducted to arrive at this finding” and provide all supporting documentation. In response, Potomac Edison produced an Excel spreadsheet **[BEGIN CONFIDENTIAL]**

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]³¹ **[END CONFIDENTIAL]**

[REDACTED] **[END CONFIDENTIAL]**

²⁹ See, e.g., Reply of Potomac Edison at 9.

³⁰ Maryland PSC Case No. 9490.

³¹ See also Response to OPC DR No.3.8, attach. A. Again, Potomac Edison states in its response to OPC DR No.1.4 that the value of the “regulatory liability” established for the monies to be refunded was \$96,966.32 as of July 31, 2021.

Asked directly about the source material underlying the spreadsheet, Potomac Edison stated that the analysis was performed by an FESC employee, Ray Valdes, but that Valdes did not independently determine which vendors' charges were improperly classified.³² Instead, that information—a list of “accounts”—was “caused to be provided” to him by another FESC employee, Eileen Mikkelsen.³³ Pressed to provide that source material in its original form, PE refused on the grounds that the FirstEnergy internal investigation from which it was derived was protected by FirstEnergy's attorney-client privilege. And, despite repeated requests by OPC, Potomac Edison has consistently also refused to provide any narrative descriptions of the methods or criteria used to generate the list of accounts. Under these circumstances, it is impossible for OPC to say what criteria FESC used to identify suspect payments, and therefore impossible to conclude that all of the improper charges in Potomac Edison distribution rates have been found.³⁴

The Commission has thus far taken Potomac Edison at its word that there is no additional, non-privileged information to be had concerning the foundations of the Mikkelsen/Valdes analysis. As we argued in our Motion for Reconsideration, OPC agrees

³² Potomac Edison's Notice of Appeal and Memorandum in Support of Appeal of Proposed Order, at 27 n.52 (quoting Potomac Edison's response to OPC DR No.5.6).

³³ *Id.* at 10 (citing Potomac Edison's responses to OPC DR No. 4.6 and OPC DR No.5.6).

³⁴ For example, OPC found small charges to “#1 Media” and “Jobob Incorporated,” two vendors elsewhere identified by FirstEnergy as potentially suspect, recorded in Potomac Edison's Accounts 911, 923, and 930.10 expenditures. *See* Compliance Audit of the 2020 Delivery Capital Recovery (DCR) Riders of Ohio Edison Company, The Cleveland Electric Illuminating Company, and The Toledo Edison Company and Expanded Scope, Expanded Scope at 9, tbl. 4, Case No. 20-1629-EL-RDR (Aug. 3, 2021); and Response to SUN DR No. 1.4, Some \$900 of these charges were likely incurred during the test year. *See* Response to SUN DR No. 1.4, attach. G, at 1. It is not clear from the Mikkelsen/Valdes analysis why FESC did not flag these charges for refund. This suggests that the Mikkelsen-Valdes analysis may not be complete even insofar as it sought to summarize charges already known to be related to the bribery scandal and/or Tony George.

with the Commission’s finding in Order No. 90033 that OPC is entitled to “any documentation” relied on by Valdes in conducting the Mikkelsen/Valdes analysis. OPC disagreed with the Commission’s statements indicating that Potomac Edison had provided those materials to OPC, because that is not the case. And, notwithstanding Potomac Edison’s belated clarification that when it said Mikkelsen “caused” Valdes to be provided with a list of vendor accounts, it in fact meant that Mikkelsen caused herself *verbally* to apprise Valdes of the list, to this date OPC has not been provided any information as to the specifics of that communication.

OPC’s belief in the existence of further written materials is well-founded. A privilege log provided by FirstEnergy’s Ohio-based utility subsidiaries to the Office of the Ohio Consumers’ Counsel indicates that FESC and FirstEnergy’s Ohio-based subsidiaries possess emails by and among Mikkelsen, Valdes, and FESC Director of General Accounting Art Richards, [BEGIN CONFIDENTIAL] [REDACTED]

[REDACTED]. [END

CONFIDENTIAL] These emails are described as “reflecting legal advice and work product regarding vendor payments” or “reflecting legal advice and work product regarding refunds” and date from January and February 2021.³⁵ This period coincides with the time period within which the Mikkelsen/Valdes analysis is presumed to have

³⁵ Motion for an *In Camera* Review to Resolve the FirstEnergy Utilities’ Claim of a Privilege Against Responding to OCC’s Discovery and Motion to Require FirstEnergy Entities to File Notice if they Disclose any Records that They Claim to be Privileged by Office of the Ohio Consumers’ Counsel, Supplemental Privilege Log Volume 1 at 12, Case No. 20-1502-EL-UNC (Jan. 13, 2022). The email recipients also include other FirstEnergy/FESC employees whose names appear in the metadata of the Mikkelsen/Valdes analysis Excel file, and who are indicated as having been asked to review its findings.

been conducted and discussed in-house, based on a December 31, 2020 journal voucher recording the audit results³⁶ and Potomac Edison's subsequent establishment in February 2021 of a regulatory liability for misused funds.³⁷

Other documents from the log seem to indicate that identical audits of FirstEnergy's other distribution utilities were performed between July 2020 and April 2021 by Richards. No privilege log has been provided by Potomac Edison, notwithstanding that the same FESC personnel also designed, conducted, and delivered the Mikkelsen/Valdes analysis, and despite OPC's request (in the instructions accompanying its data requests) that a log be provided where relevant. As a consequence, OPC did not have the opportunity to challenge the specific assertions of attorney-client privilege over communications surrounding these vendor payment audits. In short, OPC has thus far received no evidence from Potomac Edison to substantiate the facts and/or value judgments underlying the Mikkelsen/Valdes audit.

At the same time, Potomac Edison has not accommodated efforts by OPC and other parties to obtain sufficient evidence to validate the Mikkelsen/Valdes audit's findings even at a surface level. For example, OPC DR No. 3.3 asks for a record of all cost allocations from FESC to Potomac Edison for the period from January 1, 2017 to December 31, 2020. Potomac Edison provided a four-page list of cost allocations aggregated in lump sum categories according to the services purportedly provided by

³⁶ Response to OPC DR No. 1.4.

³⁷ Reply of Potomac Edison at 9. Response to OPC DR No. 1.4.

FESC (e.g., accounting support). The only information that could be gleaned from such a high-level summary was the total amount of money allocated by category to Potomac Edison over the time period in question. **[BEGIN CONFIDENTIAL]** [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED] **[END CONFIDENTIAL]**. This pattern tracks FirstEnergy’s increased spending in 2020 relating to the bribery scandal.³⁸ Similarly, intervenor Solar United Neighbors of Maryland’s (SUN) SUN DR No. 1.4 requested line-item disclosure of all Potomac Edison payments included in FERC Accounts 911, 921, 923, 930.1, and 930.2. Potomac Edison’s response included unexplained charges in the tens of millions of dollars, aggregated under the label “Non 3rd Party Vendor Activity.” Asked by OPC to provide a breakdown of the transactions and names associated with these Non 3rd Party Vendor Activities, Potomac Edison objected to the request as beyond the scope of the proceeding, explained that most of the entries were for “FirstEnergy employee expense reimbursements (e.g., travel and meals),” and refused to break down the charges in any more detail on the grounds that it would be “very burdensome.” Response to OPC DR No. 4. Notwithstanding the company’s attempt to airbrush away millions of dollars in

³⁸ Affidavit in Support of a Criminal Complaint at 15-16 tbl.1, attachment to Redacted Complaint, *United States v. Borges*, No. 1:20-MJ-00526 (S.D. Ohio July 21, 2020), ECF No. 5.

unexplained charges, Potomac Edison's subsequent response to OPC DR No. 5.10 revealed that [BEGIN CONFIDENTIAL] [REDACTED]

[REDACTED] [END CONFIDENTIAL]. As explained *infra*, FERC's DAA auditors have found—and FirstEnergy has acknowledged—that the absence of adequate support for charges from FESC to Potomac Edison and other FE distribution utilities is a widespread concern.

On the basis of the record to date, this Commission cannot credit Potomac Edison's contention that only \$38,000 of "improperly classified or inadequately documented funds" are reflected in Potomac Edison's current distribution base rates. The evidence that forms the basis of the Commission's decision-making must be "reliable."³⁹ Potomac Edison's representations and discovery responses concerning the \$38,000 figure and supporting spreadsheet are not reliable because they lack a factual foundation. Potomac Edison has failed to show, and apparently cannot show, what vendor charges Valdes was directed to search for, whether he properly implemented that search, and whether the vendor charges for which he was instructed to search represent the entirety of the improperly classified or inadequately documented funds reflected in Potomac Edison's rates.

³⁹ *Md. Dept. of Human Res. v. Bo Peep Day Nursery*, 317 Md. 573, 598 (1989). Substantial evidence "means such relevant evidence as a reasonable mind might accept as adequate to support a conclusion." See also *Am. Radio-Tel. Serv., Inc. v. PSC*, 33 Md. App. 423, 433 (1976) (quoting *Consolidated Edison Co. v. NLRB*, 305 U.S. 197, 229, (1938)).

Under Maryland Rule of Evidence 5-702 and its federal counterpart, Federal Rule of Evidence 702, expert testimony lacking the requisite factual foundation is inadmissible. “Absent [an adequate supply of data or a reliable methodology], the opinion is ‘mere speculation or conjecture.’” *Rochkind v. Stevenson*, 471 Md. 1, 21 (2020) (quoting *Rochkind v. Stevenson*, 454 Md. 277 (2017)). To like effect, Federal Rule of Evidence 702 provides that expert testimony must be “based on sufficient facts or data.”⁴⁰ These common-sense considerations inform the Commission’s evaluation of Valdes’ analysis; the Commission cannot properly credit a cost and rate analysis where the sponsoring utility cannot provide basic information as to the factual and methodological basis underlying said study.

Here, the inability to credit Valdes’ study is compounded by FirstEnergy’s recent admissions in response to the deficiencies in FESC’s cost accounting procedures and documentation detailed in the DAA Audit Report. Nor can the Commission properly credit Valdes’ analysis without violating the due process rights of OPC and other interested parties to cross-examine him as regards the reliability of his analysis, including the underlying factual basis for his study and the reliability of his methodology.⁴¹

OPC’s efforts to inquire into costs beyond those already identified by FESC in the Mikkelsen/Valdes analysis were also unsuccessful.⁴² As discussed *infra* at Section III.1,

⁴⁰ Relatedly, Fed. R. Civ. Procedure 26(b)(2) requires a testifying expert to voluntarily disclose “the facts or data considered by the witness in forming” his opinions.

⁴¹ See, e.g., *Am. Radio-Tel. Serv., Inc. v. PSC*, 33 Md. App. 423 (1976).

⁴² See, e.g., Response to OPC DR No. 1.40 (Potomac Edison objected to OPC’s request for an accounting of internal personnel costs and outside legal and consulting costs incurred by FirstEnergy or its subsidiary

the DAA Audit Report has since identified additional types of costs arising from the bribery scandal which potentially go far beyond the misallocated funds identified by FESC on Potomac Edison’s behalf, but are absent from the record in this proceeding.

Over the course of OPC’s investigation, a picture has emerged of a highly-dependent, wholly-owned subsidiary that knows very little about the costs passed through to it from FirstEnergy and FESC. Potomac Edison objected to or declined to answer data requests about costs resulting from the bribery scandal on the grounds that the requests sought “information outside Potomac Edison’s possession, custody, or control.” *See, e.g.*, Responses to OPC DR. No. 1.2, [BEGIN CONFIDENTIAL] [REDACTED] [END CONFIDENTIAL], SUN DR. No. 1.6. Potomac Edison also professed to have made no effort to assess how the scandal might affect its cost to access funds from the FirstEnergy utilities’ shared money pool (Response to OPC DR. No. 1.30) and [BEGIN CONFIDENTIAL] [REDACTED]

[REDACTED] [END CONFIDENTIAL] It bears repeating that every substantive response to OPC and SUN’s data requests was answered by FirstEnergy

utilities in responding to the bribery scandal as outside the scope of this proceeding); Response to OPC DR No. 1.39 (Potomac Edison refused to answer whether FirstEnergy intends to hold Potomac Edison ratepayers harmless for costs associated with implementing the costs of the Corporate Compliance Program mandated by FirstEnergy’s Deferred Prosecution Agreement on the grounds that the question was “vague, ambiguous, and overbroad”); Response to OPC DR No. 1.25 (Asked to describe any “other costs” incurred in connection with the bribery scandal, Potomac Edison answered with a blanket assertion that “costs were incurred by . . . FirstEnergy” but are not being charged to Potomac Edison).

and/or FESC employees. Not a single substantive response was provided by a person or persons in the direct employ of Potomac Edison.⁴³

There is, more generally, no indication that Potomac Edison ever challenges such charges or that it has the ability to do so independent of FESC's accounting support services. Given these facts, there is legitimate basis for concern that Potomac Edison ratepayers are not adequately protected from improper FirstEnergy/FESC charges. The data that have been produced tell a troubling story. Potomac Edison reimbursed FESC for charges that on their face appear to have nothing to do with Potomac Edison, including for the "Hardworking Ohioans" 501(c)(4) enterprise that was instrumental to the bribery scandal, and the similarly-irrelevant-to-PE "Sustainability Funding Alliance of Ohio." But the list produced for SUN of charges recorded to certain Operations and Maintenance and/or Administrative and General expense accounts is also littered with what appear to be unrecoverable charitable expenditures to entities operating in states outside Potomac Edison's service territory. For example, the response to SUN DR. No. 1.4 includes the following entries recorded to Accounts 911 and 923: \$1,630 to Ohio First Fund Inc.; \$1,668 to the Cleveland State University Foundation; \$207,603 to Cleveland Indians Baseball; \$52,702 to Akron Baseball LLC; \$11,085 to the Greater Abyssinia Baptist Church; and \$4,367 to various chapters of United Way.⁴⁴ Nearly \$110,000 of the charges

⁴³ Even responses authored by "Counsel" appear to have been crafted by FirstEnergy. Counsel to Potomac Edison Jeffrey Trout's LinkedIn page identifies him as "Senior Corporate Counsel at FirstEnergy Corp." <https://www.linkedin.com/in/jeffrey-trout-3a4a656a/>.

⁴⁴ An "Energy and Policy Institute" (EPI) article identifies the Greater Abyssinia Baptist Church and United Way as large donees of FirstEnergy's charity arm, FirstEnergy Foundation Giving. Strings Attached: How utilities use charitable giving to influence politics and increase investor profits,

listed above are from 2017-2018 and may have been incurred during the test year. These entities would appear to have nothing to do with the provision of utility services to Potomac Edison ratepayers.

Other large aggregations of charges, like the Non 3rd Party Vendor Activity, contain no specific attributions. As noted above, OPC's request to disaggregate such unattributed charge categories was rebuffed as "very burdensome," suggesting that a disaggregated representation of those charges is not readily available. Whether Potomac Edison ever saw a disaggregated version is unclear, but Potomac Edison's response to OPC DR No. 5.10, **[BEGIN CONFIDENTIAL]** [REDACTED], **[END CONFIDENTIAL]** raises concerns that such costs may be prematurely stripped of the information necessary to understand them by FESC "cost collector" assignment processes before that information is ever seen by Potomac Edison. OPC asked: "Do the FERC account 921 payments made to Sustainability Funding Alliance for Ohio in 2014 and 2015 appear in PE's response to SUN DR 1-04?" **[BEGIN CONFIDENTIAL]** [REDACTED]

[REDACTED]

<https://www.energyandpolicy.org/strings-attached-how-utilities-use-charitable-giving-to-influence-politics-increase-investor-firstenergy/>.

EPI discovered that some United Way chapters that received funding from FirstEnergy subsequently supported proposals to bail out FirstEnergy's coal and nuclear power plants by submitting comments to FERC in support of Secretary of Energy Rick Perry's proposal to save coal and nuclear plants; and, that the Greater Abyssinia Baptist Church went to bat publicly for FirstEnergy after receiving charitable contributions in excess of \$100,000 and meeting with FirstEnergy's then-CEO Chuck Jones.

[REDACTED]

[REDACTED]

[END CONFIDENTIAL]

Audits conducted by FERC and on behalf of the Ohio Public Utilities Commission (PUCO) have made similar findings which call into question the internal accounting processes at FirstEnergy and FESC, as well as the ability of FirstEnergy’s subsidiaries, including Potomac Edison, to review the costs allocated to them.

As discussed previously in Section I, the DAA Audit Report found that “FESC did not provide [to FirstEnergy’s subsidiaries] the detailed information required by the Commission’s regulations to reflect the services it provided and showing service company accounts for the charges billed and classified as direct costs, indirect costs, or compensation for use of capital.” DAA Audit Report at 59. The report continues: “Audit staff found that, rather than provide detailed billing information as required, FESC provided certain aggregated cost information that made it difficult to discern the basis of costs charged.” *Id.*

A corporate separation audit⁴⁵ commissioned by the PUCO in the wake of the bribery scandal suggests that even if FirstEnergy’s subsidiaries were provided with such

⁴⁵ A Compliance Audit of the FirstEnergy Operating Companies with the Corporate Separation Rules of the Public Utilities Commission of Ohio, Case 17-974-EL-UNC (Sept. 13, 2021) (Corporate Separation Audit).

information, they would not review it. With respect to FirstEnergy’s Ohio-based utility subsidiaries, the Corporate Separation Audit found that they “have little insight into the allocated charges they are receiving from FirstEnergy Services Company” and that there is no system in place to allow the subsidiaries to review or challenge a charge from FESC:

[T]he direct Ohio Companies’ staff play little to no part in maintaining the cost allocation manual. FESC provides accounting services to the Ohio Companies. *It does not appear that any direct Ohio Companies’ staff review the cost allocations they are assigned,* nor does the business services group assigned to serve the Ohio Companies review these allocations on a regular basis. There is no formalized process for disputing an allocated charge.

...

The business services group within FESC provides budgeting services to the Ohio Companies Through interviews we learned that the business services group will dig into any anomaly in actual spending that appears, but do not analyze any items that are close to budgeted spend. This means that a cost that was incorrectly spent but ended up close to budget would not be investigated This process also means that if an inappropriate cost was built into the utility budget from the beginning, it may not be investigated either.

...

During our review, we learned *that the Ohio Companies have little insight into the allocated charges they are receiving from FirstEnergy Services Company.* . . . There is no system in place for the Ohio Companies to review or dispute an allocated charge. Allocated charges are simply passed on to the Ohio Companies with little oversight from Ohio Company staff or even the [FESC] business services group that works directly with the Ohio Companies.⁴⁶

⁴⁶ Corporate Separation Audit at 82-83 (emphasis added).

The report also indicates that proper cost allocators are often not used, in contradiction of FESC’s Shared Services Agreement:

Although the FESC Shared Services Agreement mentions that the Direct Cost allocation factor should be the primary method of charging costs to Ohio Companies, we find this practice being minimally enforced. In numerous interviews, we asked if there was any rule or procedure in place to ensure this happened. Other than verbal reminders from management, *there is no procedure in place to help remind or ensure costs are directly charged as much as possible*. . . . Until a concerted effort is made—especially at the beginning of the accounting period—to question the use of indirect allocators, while promoting the use of direct assignment instead, *it is difficult to say whether the Company has met the requirements of the code*.⁴⁷

And that there are not enough internal controls to prevent cross-subsidization:

While FirstEnergy has maintained a [Cost Allocation Manual], the [Cost Allocation Manual] lacks enough internal controls and oversight regarding the use of cost allocators and costs allocated to Ohio Companies to prevent cross-subsidization.⁴⁸

Finally, the report notes that there is not sufficient oversight of FESC employee time entry:

We find a lack of controls and oversight regarding time entry. There is no reinforcement that [FESC] employees should directly charge their time to a specific affiliate whenever possible. . . . Once time is entered and approved, there appears to be a robust system in place for allocating costs. However, there are minimal checks to monitor whether time is entered accurately.⁴⁹

These failures mean that the Commission cannot know if Maryland customers are being improperly allocated FESC costs. Costs improperly allocated could be costs that no

⁴⁷ *Id.* at 87-88 (emphasis added).

⁴⁸ *Id.* at 90.

⁴⁹ *Id.* at 94.

utility customers—Maryland or customers of other FirstEnergy subsidiaries—should be paying. But the failures also mean that Potomac Edison’s Maryland customers may be paying costs that should be allocated to other FirstEnergy utilities.

Taken together, these findings concerning FESC’s internal processes are illuminating: they help to explain why Potomac Edison was unable to answer any of OPC’s substantive data requests without FESC’s assistance. But they also strongly suggest that Potomac Edison does not have any independent mechanisms separate from FESC to protect Maryland customers from cross-subsidization for costs from misconduct by FirstEnergy or even mundane accounting errors. And even the most mundane accounting errors can significantly impact Maryland customers.

II. Compelling evidence shows that the Icahn Agreement gives the Icahn group and Icahn directors “substantial influence” over Potomac Edison.

With limited exception, OPC’s ability to investigate “[t]he extent to which the ‘Icahn Agreement’ may potentially cause the Icahn-appointed directors to exercise ‘substantial influence’ over Potomac Edison as set forth in PUA § 6-105”⁵⁰ has been frustrated by OPC’s inability to obtain discovery from FirstEnergy or the Icahn Group⁵¹ relating, among other things, to the negotiation of the agreement or the activities of the Icahn Directors and the FirstEnergy Board of Directors and its committees.⁵²

⁵⁰ Order No. 89888 ¶ 18.c.

⁵¹ The Icahn Group consists of Carl C. Icahn, Andrew Teno, Jesse Lynn, Icahn Partners LP, Icahn Partners Master Fund LP, Icahn Enterprises G.P. Inc., Icahn Enterprises Holdings L.P., IPH GP LLC, Icahn Capital LP, Icahn Onshore LP, Icahn Offshore LP, and Beckton Corp. Icahn Agreement, Schedule A. Andrew Teno and Jesse Lynn are the current Icahn Directors.

⁵² OPC’s efforts to compel discovery concerning these matters was unsuccessful. *See* Order No. 89990.

Nevertheless, the combination of public information and limited discovery present a *prima facie* showing that the Icahn Directors possess substantial influence over Potomac Edison as a result of the Icahn Agreement.⁵³

The fundamental facts are not in dispute. Following the federal “Householder indictment”⁵⁴ and revelation of the HB6 bribery scandal, FirstEnergy’s stock price fell substantially.⁵⁵ Its credit rating was reduced to junk bond status.⁵⁶ Then, on February 16, 2021, Carl Icahn, described in the press as “a billionaire activist investor famous for hostile takeovers and shaking up corporate boards” announced his intention to purchase “between \$184 million and \$920 million in FirstEnergy stock.”⁵⁷ Sometime shortly thereafter, Icahn threatened to engage in a proxy fight with FirstEnergy in order to secure

⁵³ Potomac Edison filed a copy of the Icahn Agreement with the Commission on March 31, 2021. A copy of the Icahn Agreement appears at Appendix A to the Letter from Jeffrey P. Trout counsel to Potomac Edison to Andrew Johnson, Executive Secretary Maryland Public Service Commission (Mar. 31, 2021) (Icahn Agreement). The letter also attached SEC Form 8-K indicating the effective date of the Icahn Directors Board memberships.

⁵⁴ Householder was arrested and charged on July 21, 2020. Ohio House Speaker, former chair of Ohio Republican Party, 3 other individuals & 501(c)(4) entity charged in federal public corruption racketeering conspiracy involving \$60 million (July 21, 2020), <https://www.justice.gov/usao-sdoh/pr/ohio-house-speaker-former-chair-ohio-republican-party-3-other-individuals-501c4-entity> (last accessed Feb. 17, 2020). The Householder indictment was publicly filed in federal district court shortly thereafter on July 30, 2020. *United States v. Householder*, Case No. 1:20-CR-077 Indictment (S.D. Ohio filed July 30, 2020).

⁵⁵ Mathew Fox, FirstEnergy plummets 45% in 2 days after investigators tie it to \$60 million bribery scheme that just led to the arrest of Ohio house speaker, Business Insider (July 22, 2020). <https://markets.businessinsider.com/news/stocks/firstenergy-stock-price-alleged-million-bribery-scheme-ohio-house-speaker-2020-7-1029421615>

⁵⁶ Andy Chow, FirstEnergy **CREDIT RATINGS DOWNGRADED to JUNK STATUS**, The Statehouse News Bureau (Nov. 25, 2020), <https://www.statenews.org/government-politics/2020-11-25/firstenergy-credit-ratings-downgraded-to-junk-status>.

⁵⁷ Jim Mackinnon, *Billionaire activist Carl Icahn’s purchase of FirstEnergy stock could lead to utility’s sale, analyst says*, Akron Beacon Journal (Feb. 18, 2021), <https://www.beaconjournal.com/story/news/2021/02/18/activist-investor-icahn-buying-significant-amount-firstenergy-stock/4492146001/>.

representation on the FirstEnergy Board of Directors. And less than a month after Icahn first announced his intended purchase, FirstEnergy capitulated to his demands.⁵⁸ On March 16, 2021, FirstEnergy and the Icahn Group entered into the Icahn Agreement. FirstEnergy agreed to give the Icahn Group, which owned approximately 3.5% of FirstEnergy’s outstanding shares⁵⁹ (an economic investment at the time of OPC’s petition with a market value of around \$707 million),⁶⁰ two seats on the FirstEnergy Board of Directors, and further agreed that the Icahn Directors would possess additional and unique rights not enjoyed by any other FirstEnergy Board member. Pursuant to the Icahn Agreement, FirstEnergy named the Icahn Directors to the FirstEnergy Board of Directors effective March 18, 2021, and they share in and possess ultimate corporate governance authority over FirstEnergy, the entity that wholly owns and controls Potomac Edison.⁶¹

⁵⁸ “The Agreement instead resolves a potential proxy contest among shareholders related to the composition of the FirstEnergy Board of Directors.” Reply of Potomac Edison at 13. *See id.* at n.9 (“*See* [Icahn] Agreement at ¶ 1(a)(v) (‘The Icahn Group agrees not to conduct a proxy contest or engage in any solicitation of proxies, regarding any matter, including the election of directors, with respect to the 2021 Annual Meeting.’)”).

⁵⁹ OPC Petition at 20-21. *See also* Icahn Agreement ¶ 7 (stating the “Icahn Group collectively beneficially owns, an aggregate of 18,967,757 common shares”). Pursuant to ¶ 1(a)(xv) of the Agreement, the two Icahn Directors were each required individually **TO PURCHASE** 100 shares of FirstEnergy stock incident to their becoming FirstEnergy **BOARD** members, and have in fact done so. Jim McKinnon, Icahn's FirstEnergy directors now shareholders in Akron utility, Akron Beacon Journal (Mar. 26, 2021), <https://www.beaconjournal.com/story/business/2021/03/26/new-icahn-directors-now-shareholders-akrons-firstenergy-corp/7011810002/>.

⁶⁰ OPC Petition at 22

⁶¹ FirstEnergy “has not effectuated the voting rights of the Icahn Designees pending completion of the MD PSC review.” Response to OPC DR No. 4.11(b). This limitation, however, has not prevented the Icahn Directors from participating in important actions, including exercising (as part of a committee that also includes three other independent directors) negotiating authority over the shareholder derivative litigation in federal court. We explain *infra*, that the settlement of that litigation, if approved, may lead to governance changes that enhance the extent to which the Icahn directors may exercise substantial influence over FirstEnergy, and, by extension, Potomac Edison.

Consistent with Commission precedent, the Icahn Group, including the Icahn Directors, now possess the ability to exercise substantial influence over Potomac Edison. In analyzing the precise issue of whether the acquisition of a seat on the board of a utility holding company constitutes substantial influence under PUA § 6-105, this Commission answered in the affirmative, finding that “[an investor’s] right to nominate a director to the [parent holding company] . . . is [a] way in which [the investor] will acquire the power to exercise substantial influence over [the holding company].”⁶² That power inheres in the investor’s right to board of director membership separate and apart from all other considerations. “[T]he power to exercise substantial influence here [over the subsidiary utility arises] not from any direct leverage [the investor] could assert vis-à-vis BGE, but from [the investor and its board member’s] ability to influence decisions [the parent holding company] might make regarding the allocation of capital within [the holding company].”⁶³ The same is true with respect to FirstEnergy: the FirstEnergy Board is the ultimate arbiter of capital allocation within the holding company and thus with respect to Potomac Edison.⁶⁴

⁶² Order No. 82719 at 31, *In the Matter of the Current and Future Financial Condition of Baltimore Gas and Electric Company* (Case No. 9173, June 2009).

⁶³ *Id.* at 34.

⁶⁴ See FirstEnergy 2020 annual report at i (providing overview of FirstEnergy’s “capital spend” including distribution rate base), <https://www.firstenergycorp.com/content/dam/investor/files/annual-reports/current.pdf>. FirstEnergy recently “announced a \$2.2 billion increase to its capital investment plan through 2025, which now totals \$17 billion from 2021 to 2025, including \$10 billion in sustainable energy investments.” FirstEnergy Announces Transformative \$3.4 Billion of Equity Financings, Introduces Long-Term Earnings Growth Rate of 6-8% (Nov. 7, 2021), https://firstenergycorp.com/newsroom/news_articles/firstenergy-announces-transformative--3-4-billion-of-equity-fina.html. We are aware of no authority that restricts FirstEnergy’s oversight of Potomac

Potomac Edison continues to “stand[] by its position in its March 31, 2021 filing to the Commission (Maillog #234527) that Commission approval of the Agreement is not required.”⁶⁵ It contends that events happened in the wrong sequence in order for the Icahn Agreement to fall within the Commission’s authority under PUA § 6-105. Potomac Edison argues that because “Icahn was a FirstEnergy shareholder before the Company entered into the Agreement,” the Icahn “Agreement does not involve the ‘acquisition’ of Potomac Edison or any affiliate of Potomac Edison” within the reach of the statute.⁶⁶ In other words, Potomac Edison’s position is that the Commission is powerless to police instances where a person becomes affiliated with an electric utility and immediately thereafter acquires the power to exercise substantial influence over that utility. That argument is unavailing.

As a threshold matter, Potomac Edison’s timing argument is unsubstantiated because Potomac Edison has provided no evidence as to when Icahn became a shareholder of FirstEnergy. OPC was unsuccessful in obtaining discovery as to the circumstances, communications, and negotiations surrounding the Icahn Agreement because that information lies in the hands of FirstEnergy and the Icahn Group—and not Potomac Edison.

Edison’s capital expenditures; to the extent any such internal restriction exists, FirstEnergy can presumably rescind and revise it at will.

⁶⁵ Response to OPC DR No. 1.41.

⁶⁶ Reply of Potomac Edison at 13.

Nevertheless, given the proximity in time of the announcement of investor Icahn’s intended purchase and the execution of the Icahn Agreement, Icahn’s substantial acquisition of FirstEnergy stock and the Icahn Agreement should be seen as a unitary scheme and transaction. This sequence of events fits comfortably within the reach of PUA Section 6-105(2)(e)(1) and the policies underlying the statute. PUA § 6-105(b)(2) provides that it:

is the policy of the State to regulate acquisitions by persons that are not engaged in the public utility business in the State of the power to exercise any substantial influence over the policies and actions of a public service company that provides electricity or gas in the State in order to prevent unnecessary and unwarranted harm to the customers of the public service company.

In order to effectuate that objective, PUA § 6-105(2)(e)(1) prohibits without Commission approval all means of acquiring the power to exercise substantial influence over an electric utility either “directly or indirectly” incident to becoming affiliated with the electric utility by means of stock acquisition.

Section 6-105 applies to “the acquisition of an electric company . . . that operates in Maryland.”⁶⁷ This includes the acquisition of share interests in a parent holding company that owns and controls a Maryland electric utility, as is the case with FirstEnergy, which wholly owns and controls Potomac Edison. Section 6-105(2)(e)(1) provides that:

(e)(1) Without prior authorization from the Commission, a person may not acquire, directly or indirectly, the power to exercise any substantial influence over the policies and actions of an electric company, gas and electric company, or gas company, if the person

⁶⁷ PUA § 6-105(1)(c).

would become an affiliate of the electric company, gas and electric company, or gas company as a result of the acquisition.

The Icahn Group became “affiliated” with FirstEnergy when(ever) it acquired nearly 19 million shares of FirstEnergy’s common stock. Section 6-105 provides that ““affiliate” has the meaning stated in [PUA] § 7-501,” which broadly encompasses “a person that . . . has . . . any economic interest in another person.” PUA § 7-501. Potomac Edison offers a cramped reading of the statute and argues that the direct or indirect acquisition of the power to exercise substantial influence must be simultaneous with the stock transaction that affiliates the newcomer (the person not previously engaged in the public utility business in Maryland) with the electric utility.

Even assuming for purposes of argument that a “direct[]” acquisition of the power to exercise substantial influence is one contemporaneous with the stock acquisition, that does not end the statutory inquiry.⁶⁸ PUA § 6-105(2)(e)(1) is expansive in its reach and likewise prohibits the “indirect[]” acquisition of the power to exercise substantial influence over Potomac Edison incident to the Icahn Group’s acquisition of FirstEnergy stock. As a matter of common usage, “indirectly” means “by a connection that is not immediate” or “in a way that is complicated or not obvious.”⁶⁹ It is evident from Icahn’s course of action that he set out to buy into the company and secure seats on the Board of FirstEnergy as part of a single course of action, and, as is plain, he achieved that

⁶⁸ According to its plain meaning, “directly” could be construed to mean as the direct result of the Icahn acquisition of FirstEnergy’s stock. Based on even the limited information OPC has obtained in this proceeding, there is considerable merit in the argument that the Icahn Agreement was the direct result of the Icahn acquisition.

⁶⁹ *Indirectly*, dictionary.com, <https://www.dictionary.com/browse/indirectly>; *Indirect*, Cambridge Dictionary, <https://dictionary.cambridge.org/us/dictionary/english/indirectly>.

objective by entering into the Icahn Agreement. Whether construed as the direct or indirect acquisition of the power to exercise substantial influence over Potomac Edison, that coordinated scheme falls within the purview of PUA Section 6-105(2)(e)(1) and requires Commission authorization. It is transparently “an attempt by a person not engaged in the public utility business in the State to acquire the power to exercise any substantial influence over the policies and actions of a public service company that provides electricity . . . in the State.”⁷⁰ To construe the statute otherwise defeats its policy and purpose, and would create a loophole capable of evading Commission jurisdiction by the simplest subterfuge in the timing of events.

The Icahn Agreement reflects the contracting parties’ recognition that the Commission might well treat the Icahn Group’s purchase into FirstEnergy and attendant acquisition of FirstEnergy Board seats as a coordinated transaction subject to Commission review pursuant to PUA Section 6-105(2)(e)(1). Paragraph 1(a)(ii) of the Icahn Agreement provides, *in part*, that as long as an Icahn Director serves on the FirstEnergy Board, the Icahn Group “agree that none of them or any of their Affiliates or Associates (each as defined below) will exercise, or take any action that would constitute exercising, substantial influence or control over the Company or any of its subsidiaries.” This is a highly unusual provision and seems to have no other purpose than to try and assuage concerns the Commission may have as regards the Icahn Group’s acquisition of the power to exercise substantial influence over Potomac Edison. The only other state

⁷⁰ PUA § 6-105(b)(2).

with a counterpart provision regulating the attempt to acquire substantial influence over a local utility is Oregon, and FirstEnergy has no utility assets there.⁷¹

Potomac Edison highlighted the provision (Paragraph 1(a)(ii)) when it filed the Icahn Agreement with the Commission and categorically asserted that “[t]he Agreement expressly prohibits the Icahn Group or the Icahn Designees from exercising substantial influence or control over FirstEnergy or any of its subsidiaries.”⁷² Not so. Paragraph 1(a)(ii) contains its own rule swallowing exception, as it *further provides* that “the good faith discharge by the Icahn Designees of their fiduciary duties solely in their role as directors of the Company . . . shall in no event be deemed to constitute the exercise of substantial influence or control over the Company or any of its subsidiaries.” In other words, Paragraph 1(a)(ii) accomplishes nothing other than requiring the Icahn Directors to abide by fiduciary obligations they were already obliged to follow as a matter of pre-existing corporate law.

In addition to its substantive shortcomings, Paragraph 1(a)(ii) is a contractual provision enforceable only by FirstEnergy. Neither the Commission, Potomac Edison, nor its ratepayers can seek to enforce Paragraph 1(a)(ii) because Paragraph 16 of the agreement precludes the assertion of third party beneficiary rights, and states that the Icahn “Agreement is solely for the benefit of the parties hereto and is not enforceable by

⁷¹ ORS § 757.511(1). For an identification of FE’s assets, *see* FE’s SEC Form 10-K dated February 16, 2022. <https://www.sec.gov/ix?doc=/Archives/edgar/data/0001031296/000103129622000013/fe-20211231.htm>.

⁷² Icahn Agreement, Transmittal Letter at 2.

any other persons.”⁷³ OPC DR No. 4.1 asked Potomac Edison whether the Commission, Potomac Edison or its ratepayers could enforce Paragraph 1(a)(ii). Potomac Edison declined to answer, stating that “Potomac Edison notes that the agreement is between the Icahn Group and FirstEnergy Corp, and that it expressly (at paragraph 16) disclaims that it creates any rights in third parties. Potomac Edison also notes that the Commission has jurisdiction over Potomac Edison. The issue described in the data request therefore appears to be a legal one, and Potomac Edison takes no position on it at this time.”⁷⁴

The Icahn Directors’ commitment to act in good faith in accordance with their fiduciary obligations is likewise ineffectual. In Commission Case No. 9173 discussed above, the Commission found that the fiduciary obligations of an acquiring investor board member did not protect against the investor’s exercise of substantial influence over BGE. The same is true here. What the Icahn Group deems in the best interests of FirstEnergy, and the Icahn Group’s substantial share interest in FirstEnergy, may not be in the best interests of Potomac Edison and its ratepayers. For example, the Icahn Directors could believe that FirstEnergy capital is best spent on a major stock buyback, thereby boosting FirstEnergy’s share price (and the value of the Icahn Group’s investment) at a point in time when FirstEnergy’s distribution utilities, including Potomac Edison, were in need of capital funding for improvements needed to benefit ratepayers sooner rather than later. Or, the Icahn Directors could believe that increasing their

⁷³ *Id.* ¶ 1.

⁷⁴ Response to OPC DR No. 4.1.

governance power within FirstEnergy is within FirstEnergy's best interests, as appears to have recently occurred (and is discussed below).

Potomac Edison also argues that “[r]equiring approval from the Commission for the addition of two board members here would set a troubling precedent and call into question whether Commission approval is required *every* time a parent company of a public service company in Maryland seeks to add a member or members to its board.”⁷⁵ This is a red herring. PUA Section 6-105(2)(e)(1) is intended to reach instances where new investors attempt to acquire substantial influence over a Maryland electric utility immediately or proximately incident to that acquisition. That is the case here, but it will not be the case every time a holding company such as FirstEnergy seeks to add a board member. It is, however, the usefulness and flexibility of the statute that it is able to reach newly devised artifices for doing so, such as the Icahn Group's purchase into FirstEnergy leading to, and shortly thereafter resulting in, the Icahn Agreement.

The corporate governance literature explains that agreements that provided shareholders corporate governance rights beyond the ability to vote their shares were generally limited to privately held corporations.⁷⁶ However, in the last decade or so, there has been a major expansion in the use of shareholder agreements in large, publicly traded corporations. Sometimes these agreements are implemented prior to a company's

⁷⁵ Reply of Potomac Edison at 13.

⁷⁶ See, e.g., Jill Fisch, *Stealth Governance: Shareholder Agreements and Private Ordering*, 99 WASH. U.L. REV. (forthcoming 2022) March 2021 draft available at https://scholarship.law.upenn.edu/cgi/viewcontent.cgi?article=3201&context=faculty_scholarship (Fisch); Gabriel Rauterberg, *The Separation of Voting and Control: The Role of Contract in Corporate Governance*, 38 Yale L.J. 1124 (2021).

becoming a public traded entity, and in other instances they are executed at the behest of a large shareholder. The latter is the case here, and is also apparently the case with respect to the Blackstone Group’s recent acquisition of \$1 billion in newly issued FirstEnergy stock.⁷⁷ Because these shareholder agreements are negotiated instruments, they vary in their terms. Nevertheless, they often entitle the large investor to one or more seats on the corporate board of directors. This transforms the traditional nature of shareholder rights. Other common stockholders are limited to their voting rights, which are typically reactive in nature and responsive to board proposals. But by means of the shareholder agreement between the company and its large investor, the large investor enjoys additional and unique corporate governance rights, and through board membership can influence and control the corporation’s policies, objectives and conduct. “The board of directors . . . has primary authority to operate the corporation.”⁷⁸

Seeking to evade the precedent of Case No. 9173, Potomac Edison argues that “[t]he addition of two members to FirstEnergy’s Board—raising the total number of

⁷⁷ The Icahn Agreement has set a troubling precedent, as it signals FirstEnergy’s willingness to sell board seats to major investors. Last November, FirstEnergy “announced it will issue \$1 billion of common stock to Blackstone Infrastructure Partners LP at \$39.08 per share. The company consummated the private placement in December 2021 and has agreed to nominate a director candidate recommended by Blackstone at its 2022 shareholder meeting.” Darren Sweeney, *FirstEnergy touts shareholder settlement as latest step in transformation*, S&P Capital IQ pro (Feb. 11, 2022) <https://www.capitaliq.spglobal.com/web/client?auth=inherit&overridecdc=1&#news/article?id=68867359&KeyProductLinkType=6>. FirstEnergy filed a copy of the FirstEnergy-Blackstone agreement with the Commission on December 30, 2021), Maillog No. 238391. The director nomination provision is set forth in Section 5.5 and, as discussed *supra*, appears to afford Blackstone the right to nominate a director to the FirstEnergy board of directors for as long as Blackstone maintains the requisite ownership interest in FirstEnergy. FirstEnergy has agreed to name the Blackstone nominee to any vacant Board seat during the nomination period, and to otherwise support the nominee’s candidacy in any future Board elections.

⁷⁸ Fisch at 35.

members from 12 to 14—will not alter the Board’s power structure in such a way that permits the Icahn Designees to exercise substantial influence like EDF could.”⁷⁹ But in the *EDF* case the Commission did not engage in head counts, finding instead that where a large investor had one seat on the board of directors, it possessed the ability to substantially influence parent decisions over matters of vital import to the subsidiary Maryland utility, including the allocation of capital or the composition of the utility board of directors.⁸⁰ Anyone who has ever sat on a deliberative voting body, or paid attention to voting bodies, understands that a single vote can be determinative.

Potomac Edison’s head counting likewise elides the fact that the size of board membership can vary over time—as is the case here. FirstEnergy just announced a settlement of shareholder derivative suits relating to the HB6 bribery scandal that will result in six current board members not standing for re-election⁸¹ and may lead to a downsizing of the Board. “FirstEnergy said it has been considering options to reduce the board's size, though it did not state a final number.”⁸² Were FirstEnergy to reduce its

⁷⁹ Reply Potomac Edison at 16. The Board now has 16 seats. <https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/firstenergy-agrees-to-board-refresh-review-of-executive-team-lobbying-activity-68853424>

⁸⁰ As the entity that owns 100% of Potomac Edison, FirstEnergy controls the membership of Potomac Edison’s board of directors. *See* response to OPC DR No. 2.08, attach. B, By-Laws of Potomac Edison, section 3.2.

⁸¹ FirstEnergy SEC Form 8-K (Feb. 10, 2022); <https://d18rn0p25nwr6d.cloudfront.net/CIK-0001031296/3b053861-aeb0-4839-ab1c-166713217bee.pdf>. The settlement was negotiated by the FirstEnergy Board of Directors’ “Special Litigation Committee,” a four-member group that includes Icahn-designee Jesse Lynn. FirstEnergy SEC Form 8-K (June 30, 2021) <https://www.sec.gov/Archives/edgar/data/1031296/000103129621000063/fe-20210629.htm>

⁸² Darren Sweeney, FirstEnergy agrees to board refresh, review of executive team, lobbying activity, S&P Global Marketing Intelligence (Feb. 10, 2022) , <https://www.spglobal.com/marketintelligence/en/news->

Board size from 16 to 10 commensurate with the current member withdrawals, the Icahn Group would enjoy two seats out of ten and need only four votes out of the remaining eight to dictate corporate action, as opposed to the other members, who would need to obtain six votes out of ten in order to oppose the Icahn Directors. The power imbalance is even more pronounced if the Blackstone Group director aligns with the Icahn Directors and forms an institutional investor block of three votes out of ten. The problem is exacerbated as the size of the board is reduced.⁸³

The shareholder derivative suit settlement agreement is subject to the court's approval. On February 11, 2022, federal district court Judge John Adams issued an order asking a number of questions concerning the proposed governance conditions of the proposed settlement that FirstEnergy must answer no later than February 22, 2022. Among other things, the federal district court has directed the parties to provide:⁸⁴

The names of the Directors chosen to not run for re-election and the factual basis used to choose those persons;

The precise nature and extent of the governance reforms, including who will oversee and monitor the implementation of the reforms;

[insights/latest-news-headlines/firstenergy-agrees-to-board-refresh-review-of-executive-team-lobbying-activity-68853424](https://www.firstenergy.com/insights/latest-news-headlines/firstenergy-agrees-to-board-refresh-review-of-executive-team-lobbying-activity-68853424).

⁸³ Concern about expanded power for the Icahn directors if the size of the Board is reduced is not conjecture. The February 10, 2022, investor presentation mentioned *supra* note 19, at 12, states (at slide 8) that the provisions of the settlement of “multiple shareholder derivative lawsuits in Ohio” achieved by the FirstEnergy Board’s “Special Litigation Committee” includes “[a] review of the current executive team to be conducted by a special Board committee” and the understanding that “Six members of the Board, who have served for 5+ years, will not stand for re-election at the 2022 annual shareholder meeting.” February 10th Presentation. The presentation goes on to state (*id.*) that “We had been evaluating various options to reduce the size of the Board, following the addition of seven new directors in 2021, with an eighth from Blackstone to be appointed at the 2022 annual meeting[.]”

⁸⁴ *Miller v. Anderson*, Case No. 5:20CV1743, ECF No. 274, Order and Decision, slip op. at 3 (N.D. Ohio Feb. 11, 2022).

The extent and details of any conclusions reached by the Special Litigation Committee pursuant to its independent review of the facts surrounding this litigation; [and]

The extent and details of any conclusions reached by the Special Litigation Committee pursuant to its independent review of the facts surrounding this litigation.

The answers to these questions are material to this investigation: “the future of FirstEnergy’s relationship with Potomac Edison in light of recent events,” and further demonstrate the need to expand and continue this investigation.⁸⁵

Potomac Edison also ignores the influence and power that the Icahn Directors have as committee members of FirstEnergy’s board committees.⁸⁶ Corporate boards often delegate substantial powers to subordinate committees, and that is the case with FirstEnergy. For example, and as noted *supra*, Icahn Director Lynn serves with three other Board members on FirstEnergy’s Special Litigation Committee, which “ha[s] full and binding authority to determine the Board's actions with respect to pending shareholder derivative litigation.”⁸⁷ As discussed above, the Special Litigation Committee just entered into a settlement that imposes substantial corporate governance changes at FirstEnergy and may well increase the Icahn Group’s voting power on the

⁸⁵ FirstEnergy is required to respond to these questions on February 22, 2022. Assuming the responses provide information relevant to this proceeding, OPC will seek to lodge them with the Commission once they are made public.

⁸⁶ As the Commission held in Order No. 82719 (at 24) “EDF’s power to nominate a director to CEG’s Board of Directors – a director who could serve on or even lead influential committees – compounds EDF’s post-closing influence in a very real and substantial way.”

⁸⁷ Lisa Winston Hicks and Paul Kaleta Elected to FirstEnergy Board of Directors (June 30, 2021), https://www.firstenergycorp.com/newsroom/news_articles/lisa-winston-hicks-and-paul-kaleta-elected-to-firstenergy-board-.html

FirstEnergy Board.⁸⁸ Heightening their ability to exercise substantial influence over Potomac Edison, the Icahn Directors possess special membership rights not enjoyed by any other Board member. Pursuant to Paragraph 1.a(xi) of the Icahn Agreement, FirstEnergy cannot form an Executive Committee without including an Icahn Director, and “once the applicable Regulatory Approvals have been obtained,” which Potomac Edison contends has already transpired, the Icahn Directors must participate in key activities and decisions:

any Board consideration of appointment and employment of named executive officers, mergers and acquisitions of material assets, or dispositions of material assets, or similar business combination transactions, such voting with respect thereto shall take place only at the full Board level or in Board committees of which one of the Icahn Designees is a member[.]

This includes a sale of Potomac Edison or its material assets. Potomac Edison has acknowledged that “no other member of the FE Board has similar written commitments” from FirstEnergy providing such rights.⁸⁹

Potomac Edison likewise seeks to downplay the Icahn Group’s economic interest in FirstEnergy as compared to EDF’s economic interest in Constellation.⁹⁰ This is a distinction without a difference. Assuming that the Icahn Group still holds 18,967,757 shares of FirstEnergy stock, it has (at current market prices) a roughly \$791 million ownership interest in FirstEnergy. Icahn and the Icahn Group have a reputation as one of

⁸⁸ FirstEnergy SEC Form 8-K (Feb. 10, 2022); <https://d18rn0p25nwr6d.cloudfront.net/CIK-0001031296/3b053861-aeb0-4839-ab1c-166713217bee.pdf>.

⁸⁹ Response to OPC DR No. 1.19.

⁹⁰ Reply of Potomac Edison at 13-16.

the foremost institutional investors in the United States (if not internationally), were viewed as a “white knight” coming to the rescue of FirstEnergy, and have a track record of being highly activist investors. Based upon publicly available information, Icahn Enterprises LP has some \$28 billion in assets.⁹¹ Consistent with the Commission’s findings in Order No. 82719, the Icahn Directors enjoy substantial influence over Potomac Edison as members of FirstEnergy by means of their presence on the FirstEnergy Board and sundry Board committees, their access to corporate information, and their attendant ability to influence other Board members and argue for and against various corporate policies and objectives.⁹²

Finally, Potomac Edison claims that “Section 6-105(e)(2) is instructive here” and that “it suggests that the General Assembly contemplated that a transaction that *solely* involves less than 20% of *any* public service company’s board of directors seats would not require Commission approval.”⁹³ Potomac Edison acknowledges that § 6-105(e)(2) does not apply here.⁹⁴ Section 6-105(e)(2) has nothing to do with this matter because it is limited in reach to acquisitions of an electric and gas company in Maryland.⁹⁵ Potomac Edison is an electric utility. At the time § 6-105(e)(2) was enacted BGE was the only “electric and gas company” in the state, and that remains the case today.

⁹¹ Icahn Enterprises LP, <https://ycharts.com/companies/IEP/assets>.

⁹² See Order No. 82719 at 24 and 33

⁹³ Reply of Potomac Edison at 16.

⁹⁴ *Id.*

⁹⁵ PUA § 6-105(e)(2); see also Order No. 82719 at 19 (finding same).

As the Commission explained in Case No. 9173, § 6-105(e)(2) was the product of a settlement agreement that resolved a number of disputes relating to BGE.⁹⁶ Undermining Potomac Edison’s policy argument to extend the reach of § 6-105(e)(2), “[t]he General Assembly considered and rejected amendments to Senate Bill 1013 that would have extended the ‘safe harbor’ to cover investments in the stock of other Maryland utility holding companies.”⁹⁷ The Commission rejected the opportunity to engage in a policy-based extension of the provisions in the *EDF* matter even though that acquisition fell outside the specific reach of § 6-105(e)(2) but concerned BGE.⁹⁸ Instead, the Commission found that—of and by itself—EDF’s right to nominate a director to the holding company board constituted a separate and independent basis to find that EDF would possess the power to exercise substantial influence over the utility.

III. The Commission should proceed by taking immediate regulatory action where appropriate and continuing the investigation to ensure all relevant facts come to light.

Based on the foregoing, OPC has several recommendations for how the Commission should proceed from here. We review the support for each one below.

1. *The Commission should broaden the scope of the investigation to include FirstEnergy and FESC, permit discovery requests concerning the issues set for investigation, and follow the period of discovery by establishing hearing procedures.*

⁹⁶ Order No. 82719 at 5-6, 16-17.

⁹⁷ Order No. 82719 at 19.

⁹⁸ “The amendments adding (e)(2) to PUC § 6-105 left (e)(1)’s baseline ‘substantial influence’ standard untouched, giving us no basis on which to conclude that the ‘safe harbor’ is meant to gut (e)(1) as [the parent holding company] suggests.” Order No. 82719 at 18-19. The same reasoning applies here.

Potomac Edison suggests that this investigation be closed because it involves, at most, a \$38,000 refund, the treatment of which can be addressed in the next Potomac Edison base rate case. As shown here, nothing could be further from the truth. The discovery conducted in this case, and reviewed above, particularly viewed in the context of other related regulatory and judicial proceedings, makes clear that this investigation must be broadened, not closed. The reason is simple: the questions that the Commission set for investigation remain unresolved and cannot be resolved absent additional processes that include the right to seek discovery directly against FirstEnergy and FESC.⁹⁹

Broadening the scope of this investigation makes sense for a number of reasons: First, as we have explained above, questions about the bases for the \$38,000 amount that Potomac Edison says is the total to be refunded have not been answered and will not be answered if Potomac Edison is the only party responsible for providing responses. The discovery responses show that FirstEnergy and FESC directed the review of Potomac Edison rates to purge them of charges for illegal activities. For this reason alone, it is essential to a fair and complete process that OPC and others have an opportunity to seek information from the corporate entities further up the chain.

⁹⁹ As Commissioner Richard noted in his dissent to the Commission's Order 90033, "Potomac Edison and FirstEnergy are both subject to the Commission's jurisdiction. *See, Re FirstEnergy Corporation*, Case No. 9233 (Order No. 83788) 102 MD P.S.C. 11 (2011) at 40. Therefore, the activities of FirstEnergy should not be shielded from review by the Commission[.]" Order No. 90033, Richard, Comm'r, dissenting, at 1 & n.1.

Second, the FERC DAA Audit Report confirms both the need for continued investigation, and that FirstEnergy and FESC are the parties who possess the needed data. The DAA Audit Report shows that there were various categories of payments made to pursue this scheme. But what is lacking in this proceeding is an on-the-record showing that all of those categories have been examined to determine whether any of those dollars ended up in Potomac Edison rates, and to protect against the inclusion of these costs in rates going forward.

As explained above, the DAA Audit Report states that FESC lacks critical internal controls:

Audit staff interviews of FESC employees, reviews of internal emails and messages, and Attachment A – Statement of Facts included in DPA [Deferred Prosecution Agreement] and agreed to by FirstEnergy indicate the existence of significant shortcomings in FirstEnergy and its subsidiaries’ internal controls over financial reporting, including controls over accounting for expenses relating to civic, political, and related activities, such as lobbying activities performed by and on behalf of FirstEnergy and its subsidiaries.¹⁰⁰

Third, the DAA auditors go on to identify, based on information provided by FirstEnergy, various categories of funds that may have been used as part of FirstEnergy’s illegal activities. These funds are separated into internal and external lobbying expenses.

The items in the “External Lobbying” category include:

Payments to Section 501(c)(4) Entities and to Hardworking Ohioans, Inc.: FirstEnergy made payments of approximately \$70.9 million to various 501(c)(4) entities and to Hardworking Ohioans,

¹⁰⁰ DAA Audit Report at 48.

Inc. for lobbying or other nonoperating purposes, or that were not sufficiently supported.¹⁰¹

The DAA goes on to explain that \$1.5 million of the \$70.9 million noted above was “identified as being charged to the [FirstEnergy distribution companies] and the Transmission Companies, \$0.65 million was improperly recorded as General and Administrative costs, while around \$0.85 million was improperly recorded as the cost of electric plant in service.”¹⁰² The materials produced by Potomac Edison in this case show that **[BEGIN CONFIDENTIAL]** [REDACTED]

[REDACTED]
[REDACTED]
[REDACTED] **[END CONFIDENTIAL]**

The auditors next identify another category of spending on activities apparently connected to the illegal scheme:

Payments to Sustainability Funding Alliance of Ohio, Inc. and IEU-Ohio Administration, LLC: From 2010 to early 2019, FirstEnergy made payments to Sustainability Funding Alliance of Ohio, Inc., and IEU-Ohio Administration Company, LLC, two small entities associated with a former Chairman of the PUCO, totaling \$22.8 million. FESC allocated around \$11.9 million of the total payments to FirstEnergy’s [distribution companies] and Transmission Companies as General and Administrative costs, of which \$6.7 million was recorded as electric plant in service and the balance of around \$5.2 million as General and Administrative costs, which were used in customer rate development for certain of those regulated entities. An additional amount of \$9 million, which was paid in part to Sustainability Funding Alliance of Ohio, Inc. under a different vendor number, and in part to IEU-Ohio Administration

¹⁰¹ *Id.* at 50.

¹⁰² *Id.*

Company, LLC, was allocated to the FirstEnergy FPU's located in Ohio.¹⁰³

As concern these payments/charges, the audit report states that “FirstEnergy identified certain of these transactions were either improperly classified, misallocated to certain of the [distribution utilities] and Transmission Companies, or lacked proper supporting documentation and resulted in amounts collected from customers.” *Id.* at 51. The report goes on to state that “FirstEnergy has estimated that around \$185,000 in customer refunds are due, stemming from the \$20.9 million allocated to the [distribution utilities] and Transmission Companies[,]” and that FirstEnergy has “represented that it would make refunds and has already made the necessary accounting entries to correct this issue and prevent the expenses from impacting future rates.”¹⁰⁴ Again, the materials produced by Potomac Edison in this case show that **[BEGIN CONFIDENTIAL]** [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED].¹⁰⁵ **[END CONFIDENTIAL]**

The FERC auditors next identify another category of apparently illegal spending that appears to implicate Potomac Edison ratepayers:

¹⁰³ *Id.* (footnote omitted).

¹⁰⁴ *Id.* at 50-51. The \$20.9 million figure appears to be the combination of the \$11.9 million and \$9 million payments referenced above. While the \$9 million charge is stated to have been allocated to FirstEnergy’s Ohio-based distribution companies, we are unsure which of the distribution utilities were allocated shares of the \$11.9 million payment.

¹⁰⁵ Potomac Edison produced in response to OPC DR No. 1.4 a set of journal entries that include a reference to “Randazzo payments,” which we assume concerns the former PUCO Chair. We do not know whether the dollar amounts associated with those entries are consistent with the amounts identified by the FERC DAA auditors.

Payments to Sixteen Entities Associated With One Person: In coordination with its filing of SEC Form 10-K for the year ended December 31, 2020, FirstEnergy revealed to audit staff in February 2021 that FirstEnergy was investigating payments totaling approximately \$28.8 million made between 2003 and 2020 to sixteen entities associated with one individual. FESC allocated around \$19.7 million of these payments to FirstEnergy’s [distribution utilities], \$1.1 million to the Transmission Companies, \$2.2 million to former generation subsidiaries, and \$5.8 million to FirstEnergy and other nonregulated subsidiaries. FirstEnergy identified certain of these transactions were either improperly classified, misallocated to certain of the [distribution utilities] and Transmission Companies, or lacked proper supporting documentation and resulted in amounts collected from customers. FirstEnergy has estimated that around \$9.6 million in customer refunds are due, stemming from the \$20.8 million allocated to the [distribution utilities] and Transmission Companies. FirstEnergy represented that it would make the refunds and has already made the necessary accounting entries to correct this issue and prevent the expenses from impacting future rates.¹⁰⁶

We have not found reference in the materials produced in this proceeding to “payments to sixteen entities associated with one person,” and do not know whether some (or any) of the \$19.7 million that apparently ended up in distribution utility rates includes Potomac Edison.¹⁰⁷

Turning to the “Internal Lobbying” category, the DAA auditors state that FESC employees did not properly record their time spent on lobbying activities:

¹⁰⁶ DAA Audit Report at 51.

¹⁰⁷ Potomac Edison produced in response to OPC DR No. 1.4 a set of journal entries that include a reference to “Tony George payments,” but we do not know whether (a) “Tony George” is the person associated with sixteen entities, or, (b) even if so, whether the dollar amounts associated with the entries on the data response are consistent with the amounts identified by the FERC auditors. In a recent press report George stated that “I personally never took 28-point-whatever million dollars from anybody.” Jeremy Pelzer, *Audit: FirstEnergy improperly used ratepayer money to fund HB6 dark money efforts*, Cleveland.com (Feb. 4, 2022), <https://www.cleveland.com/news/2022/02/firstenergy-ordered-by-feds-to-refund-customers-for-house-bill-6-lobbying-costs.html>

Audit staff interviewed FESC employees who were classified as registered lobbyists in its Governmental Affairs Department that engaged in lobbying activities on behalf of FirstEnergy and its subsidiaries. Based on interviews pertaining to activities performed by the employees and reviews of their time cards and associated accounting for their labor, audit staff determined that FESC did not record the portion of the costs of labor in its Governmental Affairs Department that was associated with the performance of lobbying activities in Account 426.4, as required by the Commission's accounting regulations. As a result, FESC charged the improperly accounted for costs to FirstEnergy and its subsidiaries. The costs were included in the Transmission Companies' annual wholesale transmission revenue requirements and charged to their customers.

Further, audit staff found that FESC lacked formal procedures and oversight controls to help ensure that lobbying costs were accounted for appropriately. FESC should have had adequate controls in place to prevent such accounting errors. Also, audit staff is concerned about FESC's lack of adherence to its prevailing internal controls and procedures.¹⁰⁸

We have not been able to determine based on the information that has been produced here whether the issues addressed in this passage had an impact on the charges to Potomac Edison ratepayers.

In these circumstances, the Commission should broaden the scope of this investigation to include FirstEnergy and FESC. OPC and the other parties should be given an opportunity to serve discovery on these companies and complete efforts to gain a thorough understanding of the impacts of the scandal on Potomac Edison ratepayers. This period of discovery should be followed by the establishment of a schedule that would include: the filing of written testimony, a hearing schedule and post-hearing briefing.

¹⁰⁸ DAA Audit Report at 51-52.

2. *The Commission should order FirstEnergy and Potomac Edison to show cause as to why the Icahn Agreement should not be subject to Section 6-105 of the Public Utilities Article.*

Consistent with its directives in Case No. 9173, “[t]he Commission [should] order[] production of all documents relevant to the [Icahn Agreement, including Icahn’s purchase of FirstEnergy stock, and all communications between FirstEnergy and the Icahn Group (or any member thereof) relating to these matters] and set a procedural schedule . . . to address the new corporate and economic relationships among [FirstEnergy, the Icahn Group, and Icahn Directors] as well as the effects on [Potomac Edison].”¹⁰⁹ FirstEnergy and the Icahn Group proceeded at risk “without prior authorization”¹¹⁰ from the Commission and cannot properly argue that these matters are a *fait accompli*.¹¹¹ Recognizing the risk of this Commission’s assertion of jurisdiction incident to PUA § 6-105(e)(1), “the Company has not effectuated the voting rights of the Icahn Designees pending completion of the MD PSC review.”¹¹² Fundamentally, the Commission is fully empowered to take all steps necessary to preclude or protect against the Icahn Group’s and Icahn Directors’ acquisition of the power to exercise substantial influence over Potomac Edison.

3. *The Commission should direct that all refund reports, related analyses, or other documents provided to FERC in response to the DAA audit, and*

¹⁰⁹ Order No. 82719 at 11. *See also In the Matter of the Current and Future Financial Condition of BGE*, Order No. 82407, Case No. 9173 (Jan. 16, 2009).

¹¹⁰ PUA § 6-105(e)(1).

¹¹¹ FirstEnergy did not obtain an opinion of counsel with respect to the Commission’s jurisdiction over the Icahn Agreement. *See* Letter (Sept. 22, 2021) (supplementing response to OPC DR No. 1.12).

¹¹² Response to OPC DR No. 4.11.

which concern the FirstEnergy distribution utilities, must also be provided to the Commission and made available for review in this proceeding.

The DAA Audit Report requires that FirstEnergy respond to an extensive set of thirty-eight (38) separate recommendations, certain of which require the submission of additional studies and reports, estimates of possible overcharges, and completion of training requirements.¹¹³ In general, these recommendations relate to improvements that FirstEnergy needs to make to how it imposes charges upon its distribution utilities. The recommendations also include the development of certain “refund analys[es].”¹¹⁴

Some of the responsive information will relate to the ongoing imposition of charges from FirstEnergy and FESC to Potomac Edison. For this reason, OPC asks that the Commission require that all materials prepared in response to these recommendations be filed with the Commission. In addition, OPC and other interested parties must be given an opportunity to review these materials and comment on them. This proceeding should remain an “open” case until all of the requisite filings have been made and comments have been received.

4. *The Commission should direct that the results of all investigations of the conduct of FirstEnergy that led to this proceeding be submitted to the Commission and be made available to the public for review and comment.*

¹¹³ DAA Audit Report at 6-12. First Energy has accepted most of the recommendations. DAA Audit Report, Section V.

¹¹⁴ *E.g.*, Recommendation 9, at 8. The DAA auditors’ recommended actions that FirstEnergy should take include that it “[c]ritically review and strengthen internal controls in FirstEnergy and its subsidiaries.” *Id.* at 52. FirstEnergy states (DAA Audit Report, attach. A at 76) that it “[a]ccept[s]” this recommendation, and that it will undertake the requisite review and strengthening described in the recommendation.

The FERC DAA audit report states that several investigations related to the misconduct of FirstEnergy have been completed or are ongoing:

Following the filing of the DOJ complaint, the U.S. Securities and Exchange Commission, the U.S. Internal Revenue Service, the Public Utilities Commission of Ohio, the Ohio Attorney General, and the Commission commenced investigations of FirstEnergy's operations. In addition, FirstEnergy initiated its own internal investigation to be overseen by the Independent Review Committee of FirstEnergy's Board of Directors. As of the date of this report, these investigations have either not been completed, or the findings of these investigations were not available to audit staff during performance of this audit.¹¹⁵

The DAA Audit Report goes on to state that FirstEnergy must take action before FERC if its accounting is called into question by any investigation:

FirstEnergy has committed that, in the event that final, conclusive results of one or more of the investigations calls into question the propriety of its past accounting and/or rate determination decisions and customer charges, it will provide notice to the Commission and initiate actions to attain compliance with Commission accounting requirements and make refunds to customers, as appropriate.¹¹⁶

There should be no doubt that the results of these ongoing investigations, including the “internal investigation to be overseen by the Independent Review Committee of FirstEnergy's Board of Directors,” may well be relevant to the Commission's consideration here of the “future” of the FirstEnergy-Potomac Edison relationship.¹¹⁷ OPC requests that the Commission direct that FirstEnergy (or Potomac

¹¹⁵ *Id.* at 17 (footnote omitted).

¹¹⁶ *Id.* at 51.

¹¹⁷ *Id.* at 17.

Edison, or both) submit all reports, analyses, or studies that concern the conduct at issue here to the Commission. And, again, OPC and other interested parties should be given the opportunity to review and comment on these materials.

We also ask that the Commission make clear that if the results of these investigations indicate a need for additional actions in Maryland, including with respect to making refunds, that Potomac Edison will so advise the Commission and will implement whatever additional measures are needed.

- 5. Potomac Edison should be required to report to the Commission on the controls it has implemented to ensure that, going forward, there is full and independent review of all charges imposed by FESC.*

This proceeding has in some ways demonstrated the obvious: that FESC plays a significant role in the determination of the charges that end up in Potomac Edison rates. For example, discovery responses show that more than ten years ago, following the completion by FirstEnergy of its acquisition of Allegheny Electric, the Potomac Edison Board of Directors **[BEGIN CONFIDENTIAL]** [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

¹¹⁸ The “Potomac Edison Board of Directors” is something of a misnomer. The response to OPC DR No. 1.43 identifies the Board members as Messrs. Samuel L. Belcher, Steven E. Strah, and K. Jon Taylor. All three are FirstEnergy executives.

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED].¹¹⁹ [END CONFIDENTIAL]

OPC DR. No. 4.3 asked Potomac Edison to identify all instances where Potomac Edison objected to the presented charge, identify the nature of the charge and the objection, the parties involved, and the outcome of the dispute” during the period from January 1, 2012 through December 31, 2020.¹²⁰ The answer is that there were none. While Potomac Edison says that it reviews FESC charges “on a recurring basis,” it is not clear who conducts the reviews. The Potomac Edison refund analysis produced here was

[BEGIN CONFIDENTIAL] [REDACTED]

[REDACTED]

[END CONFIDENTIAL] It is also unclear the extent to which any reviews that are conducted of FESC charges are substantive. In response to a discovery request, Potomac

¹¹⁹ Dunlap’s LinkedIn profile indicates that he is an employee of FirstEnergy, not Potomac Edison. <https://www.linkedin.com/in/daniel-dunlap-a2160829/>.

¹²⁰ Response to OPC DR No. 4.3.

Edison states that while it reviews FESC charges “on a recurring basis,” Potomac Edison has “not formally objected to any FESC charges to PE during the time period identified.”¹²¹ Potomac Edison’s role in all of this is at best unclear. This data response was prepared by Mark A. Myers, who is the “Manager, Ohio Business Services at FirstEnergy Corp.”¹²² In other words, the review by Potomac Edison of FESC charges is being done by a FirstEnergy employee. As discussed *supra* in Section II, the Corporate Separation Audit of FESC and FirstEnergy’s Ohio distribution utilities performed for the PUCO similarly found that the distribution utilities never dispute FESC charges and raised substantial red flags concerning FESC’s charge allocation policies and practices.¹²³

The Commission should have assurance that Potomac Edison is able to conduct thorough review of FESC charges, and that such reviews are being conducted. The FERC DAA Audit Report makes apparent the need for this Commission to address these issues. As noted above, the auditors explain that FESC did not provide sufficient billing details to its subsidiaries:

Audit staff discovered that billing information FESC provided to FirstEnergy’s subsidiaries pertaining to charges for services provided was insufficient. Specifically, FESC did not provide the detailed information required by the Commission’s regulations to reflect the services it provided and showing service company accounts for the charges billed and classified as direct costs, indirect costs, or compensation for use of capital.¹²⁴

¹²¹ *Id.*

¹²² *Id.*

¹²³ Corporate Separation Audit.

¹²⁴ DAA Audit Report at 59.

The report goes on to point out that “FESC’s accounting and billing procedures resulted in the FirstEnergy subsidiaries not having the detailed information required to appropriately account for costs charged by FESC. As a result, the FirstEnergy subsidiaries misclassified some costs charged by FESC.”¹²⁵

The FERC DAA auditors recommend that FirstEnergy:

Revise FESC policies, procedures, and accounting systems so as to provide sufficient billing information to FirstEnergy’s subsidiaries in accordance with the Commission’s regulations.¹²⁶

FirstEnergy has accepted this recommendation. OPC urges that the Commission require FirstEnergy to submit the revisions to its policies, procedures, and accounting systems to the Commission for its review.

6. *Potomac Edison should be directed to show cause why its agreement with FESC should not be modified to afford it the opportunity to dispute and not pay improper charges.*

As discussed above, based upon its discovery response to OPC, it does not appear that Potomac Edison has disputed any charge from FESC going back to January 1,

¹²⁵ *Id.* There is now compelling evidence, and indeed, FirstEnergy has acknowledged, that there are major shortcomings in FirstEnergy and the FESC’s allocation of costs to its distribution utilities, including Potomac Edison. In FirstEnergy’s February 10th Presentation mentioned *supra*, as part of its February 15, 2022, earnings call, FirstEnergy indicates (at slide 31) that it intends to make “accounting changes” and move from “capital to expense” approximately \$90 million in annual “vegetation management” charges and \$60 million in (otherwise unexplained) annual “corporate support” charges. It is difficult to comprehend how FirstEnergy ever believed there was a legitimate basis to include these traditional operation and maintenance and administrative and general costs in utility capital rate base. It is unknown to what extent these improper capital costs are reflected in Potomac Edison’s rates, and how much its ratepayers have been improperly charged as a result.

¹²⁶ *Id.* at 60.

2012.¹²⁷ To like effect, the Corporate Separation Audit found that subsidiaries have minimal oversight of FESC cost allocations:¹²⁸

the Ohio Companies have little insight into the allocated charges they are receiving from FirstEnergy Service Company. . . . There is no system in place for the Ohio Companies to review or dispute an allocated charge. Allocated charges are simply passed on to the Ohio Companies with little oversight from Ohio Company staff or even the business services group that works directly with the Ohio Companies.

Based upon Potomac Edison's response to OPC's discovery request concerning FESC's authorities with respect to Potomac Edison, [BEGIN CONFIDENTIAL] [REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[END CONFIDENTIAL].¹²⁹

¹²⁷ Response to OPC DR No. 4.3. It may well be that Potomac Edison has never disputed any charge from FESC.

¹²⁸ Corporate Separation Audit at 83.

¹²⁹ Response to OPC DR No. 2.10, attach. B-Confidential.

Given FirstEnergy's admitted deficiencies in its response to the DAA audit in FESC's practices, the improprieties it and Potomac Edison have acknowledged in this proceeding, and the corroborative findings in the Ohio Corporate Separation audit, it is essential that Potomac Edison have the right and obligation to protest improper FESC charges, including inappropriately documented charges.

7. *Potomac Edison should be required to have performed an independent and shareholder-funded audit of all charges imposed on Potomac Edison by FESC, and should submit that audit to the Commission.*

In light of the actions that have led to this proceeding, the information that has been produced during the investigation, and the audit reports that have been produced both at FERC and elsewhere, the Commission should direct that Potomac Edison have an annual and independent audit performed of Potomac Edison's review of FESC charges. The audit should be funded by Potomac Edison, and no costs associated with the audit should be passed on to ratepayers. The results of the audit should be filed with the Commission and made available for public review and comment.

8. *The Commission should direct Potomac Edison to address the extent to which FirstEnergy's misconduct has affected the cost of access to the money pool.*

In response to OPC DR No. 1.33, Potomac Edison admitted that its cost to borrow from the Regulated Money Pool increased due to rating agencies' downgrades of Potomac Edison's credit ratings in the wake of the bribery scandal. It stated, however, that "there have been no documents, reports, analyses, or assessments on how the scandal

has or might affect PE's cost to access funds from the Regulated Money Pool,"¹³⁰ and refused to engage with questions about what measures it had taken or might take to hold ratepayers harmless for such increased costs, asserting that items pertaining to short-term debt outside the test year would be reviewed in Potomac Edison's 2023 distribution rate case.¹³¹ To the extent that the Commission decides not to pursue this matter further in this proceeding, OPC asks that Potomac Edison be directed to provide, as part of its 2023 distribution rate case filing, a report, analysis, or assessment as to whether (and, if so, how) the scandal has affected the cost of Potomac Edison's access to money pool funds.

CONCLUSION

The record developed in this proceeding and the continually evolving public record reveal that the inquiries that the Commission set forth as the subject of this investigation cannot be answered without additional Commission action. The Commission must ensure that Potomac Edison's customers are made whole and are insulated from any future misallocations from FirstEnergy. It must also ensure that the Icahn Group's substantial influence will benefit Potomac Edison's customers, not harm them, and be consistent with the public interest. The Commission should take appropriate regulatory action now and also expand this investigation so that pieces missing from the complete picture can be found, evaluated, and acted upon.

¹³⁰ Response to OPC Dr No. 1.30.

¹³¹ Response to OPC DR No. 1.34.

The concerning nature of the relationship between FirstEnergy, FESC, and Potomac Edison raises questions beyond those which were apparent at the start of this investigation. Potomac Edison’s utter lack of ability to meaningfully review and challenge cost allocations, together with evidence of erroneous cost allocations—as well as FirstEnergy’s fundamental reluctance to cooperate with this investigation intended to protect Marylanders—demands that the Commission take additional action on behalf of Potomac Edison’s Maryland customers.

For all of the reasons detailed above, OPC respectfully requests that the Commission implement each of its recommendations.

Respectfully submitted,

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February 18, 2022

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that on this 18th day of February, 2022, the foregoing “Post-Discovery Brief of the Office of People’s Counsel” was either hand-delivered, e-mailed or mailed first-class, postage prepaid to all parties of record to this proceeding.

/s/ Irene N. Wiggins

Irene N. Wiggins

Assistant People’s Counsel