BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Regulation of the Purchased Gas Adjustment Clauses Contained within the Rate Schedules of Northeast Ohio Natural Gas Corporation and Orwell Natural Gas Company.	:	Case No. 12-209-GA-GCR Case No. 12-212-GA-GCR
In the Matter of the Regulation of the Uncollectible Expense Riders of Northeast Ohio Natural Gas Corporation and Orwell Natural Gas Company.	:	Case No. 12-309-GA-UEX Case No. 12-312-GA-UEX

NORTHEAST OHIO NATURAL GAS CORPORATION AND ORWELL NATURAL GAS COMPANY'S APPLICATION FOR REHEARING AND REQUESTS FOR CLARIFICATION, AND IN THE ALTERNATIVE, MOTION TO STAY THE ENFORCEMENT OF CIVIL FORFEITURES PENDING AN APPEAL TO THE OHIO SUPREME COURT

Pursuant to 4903.10, Ohio Revised Code ("RC"), and Rule 4901-1-35, Ohio Administrative Code ("OAC"), Northeast Ohio Natural Gas Corporation ("NEO" or "Northeast") and Orwell Natural Gas Company ("Orwell")(together, the "Companies") respectfully file this Application for Rehearing of the Public Utilities Commission of Ohio's ("Commission") November 13, 2013 Opinion and Order (the "Opinion and Order"). This Application for Rehearing requests an Order on Rehearing finding that the Commission's November 13, 2013 Opinion and Order is unreasonable and unlawful for the following reasons:

A. **The Commission's order requiring a new RFP process is ambiguous and unreasonable and should be clarified or modified to permit the Companies to purchase both local and interstate gas production in-house.**

B. **The Opinion and Order regarding the effective audit periods is ambiguous and unreasonable and should be clarified or modified on rehearing.**

i The Opinion and Order should be clarified or modified to include a finding that identifies the specific dates of the Audit Periods for NEO and Orwell.

ii. The Opinion and Order should be clarified or modified to include a finding that adjusts the disallowed JDOGM fees and the Cobra Pipeline processing fees in accordance with the Commission's audit period.

C. The Commission's disallowances of local production gas costs are unlawful and unreasonable.

i. The Commission's adoption of the Staff's repricing methodology is unreasonable and unlawful.

ii. The Commission erred because it evaluated the fairness of prices based on the profits of an unregulated marketer, which constitutes de facto regulation of unregulated markets.

iii. The Commission erred by disallowing all of JDOGM's agency fees because the Commission approved the Staff's repricing of local production, which repricing already discounted the Companies' agency fees to JDOGM.

D. The Commission's order of management performance audits is unlawful and unreasonable for several reasons.

i. The Commission's Opinion and Order subjects non-party affiliated entities to investigative audits, which violates those non-parties' due process rights.

ii. The Commission cannot pierce the corporate veil of the Companies and their affiliated entities.

iii. The Commission impermissibly exceeded its jurisdiction by ordering investigative audits of unregulated entities.

iv. The Commission failed to set forth "the specific matters to be audited, investigated, or subjected to hearing" as required by RC 4905.32.

v. The Commission erred by authorizing the Staff to order investigative audits beyond the scope of RC 4905.302(C)(2), which statute "strictly limit[s]" the scope of investigative audits.

vi. To the extent that the Commission has ordered NEO and Orwell to pay for its affiliated entities' audits, the Opinion and Order unlawfully pierces the corporate veil of the Companies.

vii. The Commission erred by ordering investigative audits pursuant to RC 4905.302 to companies that are not "gas companies" as defined by 4905.03.

E. The Commission erred by assessing civil forfeitures in the context of a GCR case.

i. The Commission's assessment of civil forfeitures against the Companies is unlawful and unreasonable because the Commission is not authorized to assess forfeitures in GCR hearings.

ii. The Commission's assessment of forfeitures against the Companies violates their due process rights.

iii. In the alternative, if the Commission denies the Companies' Application for Rehearing with respect to the assessment of civil forfeitures, the Companies move the Commission to stay the enforcement of the civil forfeitures pending an appeal to the Ohio Supreme Court.

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December 13, 2013

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NORTHEAST OHIO NATURAL GAS CORPORATION AND ORWELL NATURAL GAS COMPANY'S MEMORANDUM IN SUPPORT OF THE APPLICATION FOR REHEARING AND REQUESTS FOR CLARIFICATION, AND IN THE ALTERNATIVE, MOTION TO STAY THE ENFORCEMENT OF CIVIL FORFEITURES PENDING AN APPEAL TO THE OHIO SUPREME COURT

I. INTRODUCTION.

The Commission's November 13, 2013 Opinion and Order ("Opinion and Order") in this proceeding is unreasonable and unlawful. Northeast Ohio Natural Gas Corporation ("NEO" or "Northeast") and Orwell Natural Gas Company ("Orwell")(together, the "Companies") seek rehearing to correct the errors in the Opinion and Order as set forth in this Application for Rehearing. Specifically, the Companies seek rehearing on issues related to the Commission's decisions to adopt the Staff's repricing methodology, order management and performance audits of the Companies' and their affiliated entities, and assess civil forfeitures against the Companies. In coming to these conclusions, the Commission has exceeded its jurisdiction by taking action far beyond the powers granted to the Commission by the Ohio General

Assembly. Additionally, the Companies request that the Commission clarify aspects of the Opinion and Order relating to the Companies' future purchases of gas and the length of the audit period in this proceeding. Clarification on these issues will allow the Companies, the Staff, and the Ohio Consumers' Council ("OCC") to work together to address the disallowances in the Opinion and Order and create a gas purchasing plan for the Companies in the future.

II. LAW AND ARGUMENT.

A. The Commission's order requiring a new RFP process is ambiguous and unreasonable and should be clarified or modified to permit the Companies to purchase both local and interstate gas production in-house.

The Opinion and Order should be clarified or modified to permit the Companies to purchase local and interstate gas production in-house. In the Opinion and Order, the Commission found that the Companies must "immediately commence a new RFP process" for the purchasing of local and interstate gas production. (Opinion and Order at 26-27). It is unclear whether, as an alternative, the Commission would permit the Companies to purchase local gas production using in-house employees of the Companies as the Commission required during the time period beginning seventy days from the date of the Opinion and Order until a new successful bidder is chosen. (*Id.*).

At the hearing, the Staff and the OCC argued that the Companies purchased local production gas in-house prior to 2008, and that those prices were reasonable. (Opinion and Order at 29, 33). The Staff explained in their Post-Hearing Brief that "[b]y purchasing gas directly from local producers, NEO and Orwell previously reduced their dependence on interstate purchases, which also reduced the amount customers paid in purchased gas costs." (Staff Br. at 3). Likewise, the OCC stated that "[w]hen local

production was purchased in-house the price for local production was less than the price for interstate gas." (OCC Br. at 16). Additionally, if the Companies are permitted to purchase gas in-house, the Companies will be able to reduce its purchase-price by eliminating any premium charged by the winning bidder of an RFP. As a result, the overall price of delivered gas should be reduced if the Companies purchased gas in-house rather than issuing a new RFP for a purchasing agent. Thus, the Companies respectfully request clarification or a modification of the Opinion and Order to permit the Companies to immediately purchase local and interstate gas for its Gas Cost Recovery ("GCR") customers in-house as an alternative to issuing a new RFP.

B. The Opinion and Order regarding the effective audit periods is ambiguous and unreasonable and should be clarified or modified on rehearing.

i. The Opinion and Order should be clarified or modified to include a finding that identifies the specific dates of the audit periods for NEO and Orwell.

In the Companies' Post-Hearing Brief, the Companies argued that the Staff improperly extended the dates of the audit period beyond the Commission-approved timeframe. (Opinion and Order at 45). Specifically, Commission's January 23, 2012 Entry in this proceeding ordered that the time period for NEO's audit was from March 1, 2010, to February 29, 2012, and the time period for Orwell's audit was from July 1, 2010, to June 30, 2012. (Opinion and Order at 46). The Commission found that "all ordered financial adjustments must be recalculated by Staff to only account for the effective time periods of the prescribed audit periods" as provided in the January 23, 2013 Entry.

The need for clarification of this issue arises because Staff Witness Sarver testified that there is a difference between an "audit period" and a "reporting period." At

the hearing, Staff Witness Sarver explained that the dates of the Audit Period "confuse[] people" because they "represent the effective period that's listed on the cover page of each of the GCR filings." (Tr. Vol. III, Sarver 752:15-18). Mr. Sarver explained that the *reporting period* of a financial audit actually lags six months behind the audit period. (*Id. at* 752:18-21). Under Staff's accounting practices, the Staff audited the purchased gas costs for NEO beginning in September 2009, which is actually six months prior to the beginning date of the audit period ordered by the Commission. (*Id. at* 751:8-19). Thus, based on Staff Witness Sarver's testimony, the two year reporting period of NEO's audit is September 1, 2009 through August 31, 2011 *i.e.* only the months in that period would be evaluated in the GCR. The Staff's accounting practice is confirmed in NEO's Financial Audit from the prior audit period filed with the Commission on November 24, 2010 in Docket No. 10-209-GA-GCR. In that case, the audit period wass March 1, 2008 through February 28, 2010; however, the reporting period was November 30, 2007 through August 31, 2009. (Companies Br. at 13).

Further complicating the issue, the Commission's Order set the timeframe for the Orwell audit period as July 1, 2010 through June 30, 2012. (Opinion and Order at 46). The corresponding reporting period for this audit should therefore be February 1, 2010 through January 31, 2012. However, Orwell's reporting period does not lag behind the audit period by six months; the audit period and reporting period in this instance are concurrent. (Commission Ordered Ex. 1). The Companies cannot reconcile these dates with Mr. Sarver's statement regarding the six month lag between the reporting period and the audit period.

Based on Staff Witness Sarver's testimony relating to the NEO and Orwell's audit periods, the recalculation of the effective audit periods would be as follows:

NEO: September 1, 2009 through August 31, 2011.
Orwell: February 1, 2010 through January 31, 2012.

Using these time periods, there is a need for clarification under the Staff's effective period because the period from February 1, 2010 to June 30, 2010 was already addressed in Orwell's prior GCR case.

On the other hand, if the Commission intended to account only for the months identified in the January 23, 2013 Entry, the recalculation of the effective audit period would be as follows:

NEO: March 1, 2010 through February 29, 2012.
Orwell: July 1, 2010 through June 30, 2012.

There is a need for clarification with respect to these dates since the dates identified in the Opinion and Order would exclude the six months included in Staff's reporting period that occurred prior to March 1, 2010 for NEO. Accordingly, the Companies respectfully request that the Commission clarify the time frame of the audit period by identifying the dates which should be evaluated for the purposes of this gas cost recovery case.

ii. The Opinion and Order should be clarified or modified to include a finding that adjusts the disallowed JDOGM fees and the Cobra Pipeline processing fees in accordance with the Commission's audit period.

The Companies also request clarification regarding whether the financial adjustments to the Cobra fees and JDOGM disallowance are limited to the audit period. Based on the Commission's Order at page 46, the Commission found that "*all* financial adjustments must be recalculated by Staff" to account for the effective audit periods.

With respect to Cobra's processing fees on the Churchtown system, the Commission ordered NEO to disallow $145,363 and make an "adjustment to NEO's GCR in this amount in the customer's favor, and that this adjustment should be applied in the first GCR filing following the Opinion and Order." (Opinion and Order at 45). The $145,363 adjustment was based on Staff Witness Sarver's testimony that 581,457 Dth of local gas was purchased by NEO on the Churchtown system during the audit period. (Opinion and Order at 43.). However, the audit period used by Staff to determine the volume of gas purchased on the Churchtown system is September 1, 2009 to May 31, 2012, which is the Staff' audit period that the Commission instructed the Staff to adjust. (Staff Ex. 2 at RS Ex. 7). The Companies request clarification or modification of the Order to align the disallowance of the processing fees with the Commission's adjusted audit period.

Additionally, the Commission found that the premiums paid to JDOGM should be disallowed and an adjustment to the GCR should be made in the customers' favor for NEO of $583,417.80 and for Orwell of $224,991.60. (Opinion and Order at 42). The adjustment is based on the Staff's incorrect audit period; not the audit period approved by the Commission (Tr. Vol. III at 671). Although the Companies dispute the reasonableness and lawfulness of the disallowance, in the event the Commission affirms the disallowance, the Companies request clarification or modification of the Order to align the disallowance of the JDOGM fees with the Commission's adjusted audit period.

C. The Commission's disallowances of local production gas costs are unlawful and unreasonable.

i. <u>The Commission's adoption of the Staff's repricing methodology is unreasonable and unlawful.</u>

The Commission failed to address the Companies' arguments related to the Staff's unreasonable repricing methodology detailed in the Companies' Post Hearing Brief and Reply. The Companies incorporate by reference those arguments from their Post Hearing Brief and Reply and will summarize the main points herein.

First, the Staff's determination of the Staff's Alternative Premium NYMEX Plus is unreasonable and unsupported in the record. The Staff recommended repricing the local production for the audit period based on the following inputs:

Local Producers	Avg. NYMEX for the Audit Period[1]	Staff Alternative Premium NYMEX Plus	JDOG Premium NYMEX Plus	Difference
Cobra[2]	$3.834	$0.50	$1.091	$0.591
NEO non-Cobra[3]	$3.82	$0.70	$1.61	$0.91
Orwell[4]	$4.01	$0.25	$1.46	$1.21

According to Mr. Sarver, the "average NYMEX for the Audit Period" represents the weighted average cost of purchasing the volumes during the Audit Period each month based on the NYMEX price at the time. (Tr. Vol. III; Sarver 722:21-23). However, Mr. Sarver recognized that the "prevailing pricing in the market is going to be set by the Appalachian Index and the Dominion Transmission Index." (Tr. Vol. III; Sarver 720:16 – 721:9). Even with this knowledge, Staff witness Sarver ignored the "prevailing pricing in the market" and based his repricing on the NYMEX. On the other hand, the Companies' witness Dr. Overcast evaluated the Companies purchase based on the Dominion Transmission Index during the audit period, which is the uncontroverted best index to evaluate "prevailing prices."

[1] These represent the weighted average cost of purchasing the NYMEX based on the volumes purchased each month and the NYMEX price for the corresponding month. (Sarver 723:2-12).
[2] Local producers that are physically connected to the Cobra pipeline. (Sarver 722:2-3).
[3] Any producer that NEO purchased from who is not physically connected to Cobra. (Sarver 722:6-7).
[4] Local producers that feed into Orwell. (Sarver 722:10).

Additionally, the Commission did not address the Staff's unsupported basis for the Staff's adjustment to the prices paid to John D. Oil and Gas Marketing ("JDOGM"). Turning to the column "Staff Alternative Premium NYMEX Plus" in the table above, Staff repriced the premium to be paid to JDOGM during the current Audit Period based on contracts between JDOGM and local producers in the prior audit period. (Tr. Vol. III; Sarver 725:4-13). The Audit Report states: "In its determination of the prices paid to local producers, Staff started with the NYMEX based price paid to the producer using the contracts and pricing sheets provided in the 2012 audit." (Staff Ex. 1; Audit Report at 14).

Referring to the second row in above table, Mr. Sarver explained:

> So if I start at – with Cobra $3.83 which is just the average, but if I start and go to the staff audit report and I turn to page 15, and I look at the table at the top of that page and I look to see what local producers were paid under the contracts that were provided in the 2010 case, it would show me that Cobra producers are paid a weighted average of $3.37 which is 45 cents less than their weighted average NYMEX. So when I'm looking at these alternatives, I have to look at what the producers were paying to determine what amount needs to be added on to them. (Sarver 725:1-17).

The table in the Audit Report at page 15 is reproduced here:

Systems	Avg. NYMEX Price	Weighted Avg. Price Paid to Producers	Volumes Billed to Companies by JDOG Dth	Weighted Difference
Cobra	$3.834	$3.376 Dth	953,472 Dth	$(0.458)
Non-Cobra	$3.82	$4.40 Mcf[5]	280,003 Mcf	$0.580
Orwell	$4.01	$4.11 Mcf	63,693 Mcf	$0.10

[5] In the Audit, the Weighted Average Price Paid to Producers for Non-Cobra was listed as measured in Dth. Mr. Sarver testified that this unit should be changed to Mcf. No conversion from Dth to Mcf was needed. (Sarver 726:10-11).

(Staff Ex. 1; Audit Report at 15). The weighted average prices paid to local producers are the weighted average prices that JDOGM paid to local producers in the prior audit period, which are based on contracts between JDOGM and local producers. (Tr. Vol. III; Sarver 726:16-25). The weighted difference in the fourth column represents the difference between the weighted average price paid to local producers during the prior audit period and the weighted average NYMEX price in the current audit period.

The Staff failed to explain in the audit, testimony, or their briefs the significance of the weighted difference calculation or its relationship to the Staff Alternative Premium NYMEX Plus. Because the Staff could not explain it, the Commission had no evidence in the record to rely on to support the Staff's methodology. Indeed, the Commission failed to address this issue in the Opinion and Order. As the Companies argued in their Post Hearing Brief, it appears that the Staff's estimation for JDOG's premium is unsupported and unrelated to the weighted difference calculation. Following Mr. Sarver's example using the Cobra calculations, the weighted average price paid to local producers in the prior audit period was 45 cents less than the weighted average price of NYMEX quantities in the current audit period. The Commission did not find any correlation between the 45 cent "weighted difference" and the Staff's 50 cent Alternative Premium NYMEX Plus.

Similarly, if Non-Cobra prices are examined based on the Staff's repricing, the methodology is equally unsupportable in the record. For example, the weighted average price paid to local producers in the prior audit ($4.40 Mcf) is *higher* than the weighted average NYMEX price ($3.82), resulting in a 58 cent weighted difference. With regard to Non-Cobra gas, the Commission has accepted the Staff's repricing that

has JDOGM paying more to local producers than the weighted average NYMEX price despite the fact that Staff witness Sarver testified that "local production costs should not exceed the costs of interstate supplies." (Staff Ex. 2; Sarver Direct 13-17). The Staff never reconciled these inconsistent positions in its repricing. Without explanation, the Staff allowed a 70 cent premium for Non-Cobra local production. The repricing is simply a guess. The Commission failed to address this obvious deficiency in the Staff's repricing methodology.

Moreover, the Commission's findings that approve of the Staff's repricing methodology require a public utility to turn over contracts that belong to an unregulated entity. (Opinion and Order at 37). The PUCO is a creature of statute and has no authority to act beyond its statutory powers. *Disc. Cellular, Inc. v. Pub. Utilities Comm'n*, 112 Ohio St. 3d 360, 373 2007-Ohio-53 ¶51. Revised Code Sections 4905.04 and 4905.05 only empower the Commission to regulate public utilities and railroads within Ohio. The Commission found it "reasonable and appropriate" for the Staff to use the JDOG's outdated contracts from the prior audit to determine the agency premiums earned by JDOGM in the current audit period. (*Id.*). In this regard, the Commission found it more reasonable to use outdated contracts than it was to rely on Dr. Overcast's current prices on the Dominion Transmission Index. The Commission made this finding because the Companies "refused" to turn-over JDOGM's contracts with JDOGM's local producers. (*Id.*). However, the Commission does not have regulatory authority over JDOGM or its unregulated local producers. As such, the Commission approved the Staff's repricing methodology under the unlawful premise that the Companies were somehow in control of JDOGM's contracts or had the power to access those contracts.

The Commission's findings against the Companies therefore exceed the jurisdiction of the PUCO by penalizing a public utility for not producing information that is not subject to the Commission's jurisdiction.

ii. The Commission erred because it evaluated the fairness of prices based on the profits of an unregulated marketer, which constitutes de facto regulation of unregulated markets.

The Commission lacks authority to regulate the profits of an unregulated gas marketer. In the Companies' Post-Hearing Brief and Reply Brief, the Companies argued that by repricing gas purchased from a marketer, the Staff inserted itself into the market by questioning the profits of an unregulated gas marketer rather than questioning whether a regulated entity's purchases are reasonable. The Companies argued that the Staff's proposed repricing could have a chilling effect on the market by signaling price ceilings to marketers. While the Commission recognized that the Companies' made these arguments, the Commission failed to make a specific finding in response to them.

Simply put, it is against public policy in Ohio to evaluate the Companies' GCR rate based on an evaluation of an unregulated gas marketer's assumed profit margins. By adopting the Staff's methodology, the Commission has determined that Companies' gas costs were too high because an unregulated marketer made too much money selling the Companies gas. This results in the effective regulation of the profits of unregulated entities. The Staff's methodology forces the Commission to interfere with the unregulated side of the natural gas market by finding, as the Commission did, that the margin between the marketer's purchase price for gas and sale price for gas is too great. Basing the Commission's decision on marketers' prices is a *de facto* cap on marketers' profits, which is clearly outside the jurisdiction of the PUCO.

iii. The Commission erred by disallowing all of JDOGM's agency fees because the Commission approved the Staff's repricing of local production, which repricing already discounted the Companies' agency fees to JDOGM.

In the Opinion and Order, the Commission found that the premiums paid to JDOGM should be disallowed and an adjustment to the GCR should be made in the customers' favor for NEO of $583,417.80 and for Orwell of $224,991.60. (Opinion and Order at 42). By disallowing all of the fees paid to JDOGM and adopting the Staff's recommended repricing, the Commission has disallowed more premium payments than were actually paid to JDOGM. The result of this extra disallowance is that the Companies are forced to adjust the GCR in the customers' favor more for agency fees than the customers initially paid for agency fees during the audit period.

This "double disallowance" occurred because the Staff's repricing methodology already discounted agency fees paid by customers. In the Staff's Post-Hearing Brief, the Staff explained that it was "appropriate for the Companies to pay JDOGM some premiums for its services." (Staff Br. at 10). The Staff calculated "alternative premiums," which the Staff found reasonable. (Staff Br. at 11-12). The Staff discounted the premium paid to JDOGM in the table on page 11 of the Staff's Post-Hearing Brief, which table is reproduced here:

Local Producers	**Staff Alternative Premium NYMEX Plus**	**JDOG Marketing Premium NYMEX Plus**	**Difference**
Cobra	$0.50	$1.091	$0.591
NEO non-Cobra	$0.70	$1.61	$0.91
Orwell	$0.25	$1.46	$1.21

Based on the Staff's repricing, the Actual Adjustment to the GCR would reflect the Staff's Alternative Premium. Consequently, the "Difference" between JDOGM's premium and the Staff's premium has already been discounted from the Staff's AA. (Staff Br. at 10-12). If the Commission requires the Companies to adjust their GCRs by using the Staff's AA, plus the full disallowance of JDOGM's premiums, then there will be a double disallowance on the difference.

The Staff's Reply Brief recognizes the mathematical error present in the Opinion and Order. The Staff argued that the "Commission should *either* disallow all fees paid to JDOGM for purchases of local production *or* adopt Staff's repricing for local production." (Staff Reply at 6)(*emphasis added*). Not both. To have the Companies adjust the GCR accounting for a full disallowance of JDOGM premiums and the Staff's AA, the Companies' customers will be reimbursed twice the amount that customers initially paid for all volumes of gas by the amount of the "Difference" in the Staff's table above.

D. The Commission's order of management performance audits is unlawful and unreasonable for several reasons.

The Commission's Opinion and Order found that "an investigative audit of the Companies and all affiliated and related companies should be undertaken by an outside auditor." (Opinion and Order at 57). With respect of the scope of the audit, the Commission found that "[t]he outlines and extent of the investigative audit shall be proposed by Staff based on the evidence of record from this audit." (*Id.*). The Commission also found that, pursuant to RC 4905.302(C)(3)(b), the Commission has good cause to impose the costs of the investigative audit on NEO and Orwell.

The Commission's Opinion and Order relating to the ordered investigative audits is unlawful and unreasonable for several reasons. First, the Commission's Opinion and Order purports to subject non-party affiliated entities to a Commission directed investigative audit, which violates the non-parties' due process rights. Second, the Commission cannot pierce the corporate veil of the Companies and their affiliated entities. Third, the Commission impermissibly exceeded its jurisdiction by ordering investigative audits of unregulated entities. Fourth, the Commission failed to set forth "the specific matters to be audited, investigated, or subjected to hearing" as required by RC 4905.32. Fifth, the Commission erred by authorizing the Staff to order investigative audits beyond the scope of RC 4905.302(C)(2), which statute "strictly limit[s]" the scope of investigative audits. Sixth, to the extent that the Commission has ordered NEO and Orwell to pay for its affiliated entities' audits, the Opinion and Order unlawfully pierces the corporate veil of the Companies. Seventh, the Commission erred by ordering investigative audit pursuant to RC 4905.302 to companies that are not "gas companies" as defined by 4905.03.

i. <u>The Commission erred by subjecting NEO and Orwell's affiliated entities to investigative audits because the affiliated entities have not had an opportunity for notice and hearing in this matter, which violates their due process rights.</u>

In the Companies' Reply Brief, the Companies argued that the Commission could not order the investigative audits of non-parties because the non-parties were deprived of their due process rights to be heard at the Commission. (Opinion and Order at 56). In response to this argument, the Commission failed to opine on the legality of the investigative audits in the context of due process, and instead, the Commission ordered investigative audits of the non-parties and proclaimed that "any parties named to be part

of this investigative audit will be given notice of the proceeding and the opportunity to participate in any hearings, the opportunity to present evidence on any subject to be examined at the hearing." (Opinion and Order at 55-56). Essentially, the Commission told the non-party affiliates that they will be entitled to due process in the next proceeding, but not this one.

The non-party affiliates (to the extent they are known) were deprived of their due process rights. By requiring management and performance audits of non-party affiliates arising from a hearing where they were not named as parties, not given notice of or the opportunity to participate any hearings or briefing, not given the opportunity to present or cross-examine witnesses, and not permitted to present evidence in their defense, the Commission has violated the due process rights of the Companies' non-party affiliates guaranteed by the United States and Ohio Constitutions. The Fourteenth Amendment of the United States Constitution provides that state governments may not "deprive any person of life, liberty, or property, without due process of the law. The Ohio Constitution guarantees "due course of law" which is virtually the same as the Due Process Clause of the Fourteenth Amendment of the United States Constitution. Section 16, Article I of the Ohio Constitution.[6] *In re Hua,* 62 Ohio St.3d 227, 258, 405 N.E.2d 255 (Ohio 1980).

The United States Supreme Court has established that the "deprivation of life, liberty or property by adjudication (must) be preceded by notice and opportunity for hearing appropriate to the nature of the case." *Hua* at 258, citing *Mullane v. Central Hanover Trust Co.*, 339 U.S. 306, 313, 70 S.Ct. 652, 94 L.Ed. 865 (1950). "'The

[6] Because the "due course of law" provision of the Ohio Constitution is virtually the same as the "due process" clause of the Fourteenth Amendment, Ohio courts often look to the opinions of the United States Supreme Court decided under the Fourteenth Amendment in defining the rights guaranteed under Article I of the Ohio Constitution. *State ex rel. Heller v. Miller*, 61 Ohio St.2d 6, 399 N.E.2d 66 (1980).

formality and procedural requisites for the hearing can vary, depending upon the importance of the interests involved and the nature of the subsequent proceedings.'" *Id.* quoting *Boddie v. Connecticut*, 401 U.S. 371, 378, 91 S.Ct. 780, 786, 28 L.Ed.2d 113 (1971). In cases where important decisions affecting substantial rights turn upon controverted issues of fact, the "due process" right to an adjudicatory hearing would be meaningless unless the parties whose rights may be affected are allowed full opportunity to present their own evidence, to confront and cross-examine adverse witnesses, and to present oral argument in support of their respective positions. *Goldberg v. Kelly*, 397 U.S. 254, 267-271, 90 S.Ct. 1011, 1020-1022, 25 L.Ed.2d 287 (1970).

There is no question that these due process requirements apply to decisions by the Commissions and the hearings conducted before them. For example, in *Vectren Energy Delivery of Ohio, Inc., v. Public Utilities Commission of Ohio,* 113 Ohio St.3d 180, 2006-Ohio-1386 at ¶ 53, 863 N.E.2d 599 ("*Vectren*"), the Ohio Supreme Court held that that the Commission did not violate a gas provider's due process rights during a gas-cost-recovery proceeding where the provider had received, among other things, a full hearing before the committee and actual notice of the same. The provider was permitted to present evidence to the Commission, including calling its own witnesses, cross-examining other parties' witnesses and filing exhibits, and was "able to argue its position through the filing of post hearing briefs and challenge the PUCO's findings through an application for rehearing." *Id.*

Unlike the gas provider in *Vectren*, the non-party affiliates have not been afforded due process. Certainly, at a minimum, non-parties to a gas-cost-recovery proceeding

being subjected to orders of the Commission should be entitled to notice of and participation in any hearings. However, the Companies' non-party affiliates have had no notice of the hearings on the issues, no opportunity to present evidence, and no opportunity to participate in this briefing. Moreover, the Commission did not even identify the non-party affiliates that will be required to have investigative audits. (Opinion and Order at 57). Accordingly, the Commission's finding imposing investigative audits on the Companies' non-party affiliates should be overturned by the Commission because the Commission's Opinion and Order violates the non-party affiliates' due process rights.

ii. The Commission's Order is unlawful and unreasonable because it holds the Companies' sister corporations liable for the Companies' acts.

The Commission's Opinion and Order is unlawful and unreasonable because it holds the non-party affiliates responsible for the alleged misdeeds or actions of their sister companies. It is well established that, absent piercing of the corporate veil, a parent company or corporation is not liable for the acts of its subsidiaries. *U.S. v. Bestfoods,* 524 U.S. 51, 61 118 S.Ct. 1876, 141 L.Ed.2d 43 (1998); *Belvedere Condominium Unit Owners' Assn. v. R.E. Roark Cos., Inc.* (1993), 67 Ohio St.3d 274, 617 N.E.2d 1075, *Dombroski v. WellPoint, Inc.,* 119 Ohio St.3d 506, 2008-Ohio-4827, 895 N.E.2d 538.

Similarly, sister corporations are separate entities not liable for the acts of the other. *Minno v. Pro-Fab, Inc. 121 Ohio St. 3d*, 905 N.E.2d 613, 2009-Ohio-1247, ¶ 11-12. This is true even where the corporations have common shareholders or are controlled by the same or substantially the same owners. *Id.* at ¶ 12 ("the common shareholder ownership of sister corporations does not provide one sister corporation

with the inherent ability to exercise control over the other. Any wrongful act committed by one sister corporation might have been instigated by the corporation's owners, but it could not have been instigated by the corporation's sister").

Thus, the fact that the non-party affiliates share officers and directors with Orwell and NEO is irrelevant. Separate legal identities of related corporations must be respected even where directors and officers serve in various capacities in multiple entities. *CSAHA/UHHS Canton, Inv. v. Aultman Health Foundation,* 5th Dist. No 2012CA00303, 2012-Ohio-897, ¶ 110. The purported actions of NEO and Orwell alone are not enough to implicate the non-party affiliates or provide the good cause necessary to subject them to costly and time consuming audits that those affiliates will potentially fund without any opportunity to pass those costs onto customers. The Commission should order on rehearing that the Companies' non-party affiliated entities not be subject to investigative audits.

iii. The Commission impermissibly exceeded its jurisdiction by ordering investigative audits of unregulated entities.

To the extent the Commission Opinion and Order authorized the audits of the Companies' affiliated unregulated entities, the Opinion and Order is unlawful because it impermissibly exceeded its statutory jurisdiction. The PUCO is a creature of statute and has no authority to act beyond its statutory powers. *Disc. Cellular, Inc. v. Pub. Utilities Comm'n*, 112 Ohio St. 3d 360, 373 2007-Ohio-53 ¶51. RC 4905.04 and RC 4905.05 empower the Commission to regulate public utilities and railroads within Ohio. In the Opinion and Order, the Commission ordered investigative audits of all of the Companies' affiliated and related parties. (Opinion and Order at 57). The Commission did not limit the scope of the investigative audits to entities regulated by the

Commission. Because the Commission did not identify the parties that will be audited, the Companies cannot be sure of Commission's intent. If the Commission intended to authorize the investigative audits of any of NEO or Orwell's affiliated companies that are not public utilities located within Ohio, the Commission's Opinion and Order is unlawful and should be modified to comply with Ohio law.

iv. The Commission failed to set forth "the specific matters to be audited, investigated, or subjected to hearing" as required by RC 4905.302(C)(5).

The Commission's Opinion and Order fails to comply with RC 4905.302(C)(5), which statute requires the Commission to "set forth the reasons showing good cause [for the audit] and the specific matters to be audited, investigated, or subjected to hearing" for gas companies with 15,000 or fewer customers. Orwell is a gas company with fewer than 15,000 customers. (Staff Ex. 1; Audit Report at 8). Therefore, the Commission must specify the matters to be audited, investigated, or subjected to hearing in this Opinion and Order, which the Commission failed to do. Instead, the Commission ordered the Staff to decide "the outlines and extent of the investigative audit . . . based on the evidence of record from this audit." The Commission's broad delegation of power to the Staff is not specific by any means and fails to comply with RC 4905.302(C)(5).

Additionally, to the extent that the Commission intended to order an investigative audit of Brainard Natural Gas Company pursuant to RC 4905.302, the Commission's order is unlawful because it fails to satisfy RC 4905.302(C)(5). Like Orwell, Brainard is a natural gas company with 15,000 or fewer customers. Accordingly, the Commission has failed to show good cause or specify the matters to be audited, investigated, or

subjected to hearing in this Opinion and Order. The Commission has, therefore, improperly ordered the investigative audit of Brainard Natural Gas Company.

v. The Commission erred by authorizing the Staff to order investigative audits beyond the scope of RC 4905.302(C)(2), which statute "strictly limit[s]" the scope of investigative audits.

In the Opinion and Order, the Commission authorized the Staff to determine the "outlines and extent" of the investigative audit. (Opinion and Order at 57). The Commission's delegation of power to the Staff is impressible under RC 4905.302(C)(2), which provides:

> The commission shall not require that a management or performance audit pertaining to the purchased gas adjustment clause of a gas or natural gas company, or a hearing related to such an audit, be conducted more frequently than once every three years. Any such management or performance audit and any such hearing *shall be strictly limited* to the gas or natural gas company's gas or natural gas production and purchasing policies. No such management or performance audit and no such hearing shall extend in scope beyond matters that are necessary to determine the following:
>
> (a) That the gas or natural gas company's purchasing policies are designed to meet the company's service requirements;
>
> (b) That the gas or natural gas company's procurement planning is sufficient to reasonably ensure reliable service at optimal prices and consistent with the company's long-term strategic supply plan;
>
> (c) That the gas or natural gas company has reviewed existing and potential supply sources.

The Commission's Opinion and Order permits the Staff to propose an audit based on any evidence in the record of this proceeding. The evidence introduced by the OCC and the Staff in this GCR proceeding went far beyond the scope of a management and performance audit. To the extent that the Commission has authorized the Staff to initiate investigative audits that have a broader scope than the scope set forth in RC

4905.302(C)(2), the Commission's Opinion and Order is unreasonable. To be sure that Ohio law is followed, the Commission should modify the Opinion and Order to comply with RC 4905.302.

vi. To the extent that the Commission has ordered NEO and Orwell to pay for its affiliated entities' audits, the Opinion and Order unlawfully pierces the corporate veil of the Companies and violates Chapter 49 of the Revised Code.

The Opinion and Order states that the Commission found that "good cause exists to warrant imposing the costs of the ordered audit upon the Companies." (Opinion and Order at 57). The Opinion and Order is not clear as it pertains to the audit that the Companies will pay for. The Commission clearly intended for the "Companies" (NEO and Orwell) to pay the costs of their own audit. (Opinion and Order at 57). However, it is unclear if the Commission intended the Companies to pay for the audits of the Companies' affiliated entities. Throughout the ordering paragraphs on pages 56 and 57 of the Opinion and Order, the Commission referenced the impending "audit" in the singular, as if it is a single audit for all of the related entities of the Companies. If the Commission intended for the Companies' to pay the costs of the audit for all of the related entities, the Commission's Opinion and Order is unlawful and unreasonable.

First, the Commission will unlawfully pierce the corporate veil to hold the Companies liable for their related entities. As stated above, sister corporations are separate entities not liable for the acts of the other. *Minno v. Pro-Fab, Inc. 121 Ohio St. 3d*, 905 N.E.2d 613, 2009-Ohio-1247, ¶ 11-12. By ordering the Companies to pay for audits of their sister entities, the Commission has unlawfully pierced the Companies' corporate veil. The Commission's finding is unlawful under Ohio law.

Second, RC 4905.302 "strictly limits" the scope of a management and performance audit. The Commission's Order violates 4905.302(C)(2) by imposing the costs of non-party affiliated entities upon the Companies. A Commission ordered management and performance audit may only review: 1) a gas company's purchasing policies; 2) a gas company's procurement planning; and 3) a gas company's review of existing and potential supply sources. RC 4905.302(C)(2). The laws regulating management and performance audits do not authorize one gas company (*i.e.* NEO) to audit another gas company (*i.e.* Brainard Natural Gas Company). Additionally, management and performance audits ordered pursuant to RC 4905.302(C)(2), as the Commission did here, cannot extend to companies that are not gas companies, as explained below.

vii. The Commission erred by ordering investigative audits pursuant to RC 4905.302 to companies that are not "gas companies" as defined by 4905.03.

The Commission's Opinion and Order authorized an investigative audit pursuant to RC 4905.302 for the Companies' related entities that are not "gas companies" as defined by 4905.03. (Opinion and Order at 57). The Commission is not empowered by the General Assembly to authorize a management and performance audit of companies other than "gas companies" and "natural gas companies" pursuant to RC 4905.302. Specifically, RC 4905.302 references "gas companies" and "natural gas companies" as defined by RC 4905.03. Although the Commission did not identify all of the parties to be audited, the Companies have affiliated regulated entities that are not gas companies that may be subjected to the audit. To the extent the Opinion Order authorizes the audits under RC 4905.302 of entities that are not "gas companies" and "natural gas companies," the Commission's Opinion and Order is unreasonable and unlawful.

E. The Commission erred by assessing civil forfeitures in the context of a GCR case.

i. The Commission's assessment of civil forfeitures against the Companies is unlawful and unreasonable because the Commission is not authorized to assess forfeitures in GCR hearings.

The Revised Code and the Commission's Rules do not contemplate the assessment of forfeiture in a GCR proceeding. Section 4905.54 of the Revised Code provides the Commission with the power to "assess a forfeiture of not more than ten thousand dollars for each violation or failure against a public utility...that after due notice fails to comply with an order, direction or requirement of the commission that was officially promulgated."

The procedural framework for GCR cases is set forth in section 4905.302. Specifically, R.C. 4905.302(C) provides that the Commission establish rules for the purchased gas adjustment clause, including investigative procedures, including periodic reports, audits, and hearings to examine the accuracy of the gas costs reflected in the company's GCR rates. Commission rules specify how these audits and hearings are to be conducted. *See* O.A.C. § 4901:1-14-07.

Neither the Commission's rules nor R.C. 4905.302(C) provide for GCR cases to be anything other than a vehicle for analyzing NEO and Orwell's gas utility procurement policies and practices. This framework specifically limits the scope of the Commission's inquiry and analysis. Despite these clear limitations on the purpose and scope of GCR proceedings, the Commission has improperly transformed these proceedings into an enforcement mechanism for assessing forfeitures on NEO and Orwell. Nothing in the Ohio Revised Code or the Commission's rules provides for forfeiture in a GCR case

under R.C. 4905.54. Accordingly, the Commission's assessment of forfeitures is unreasonable and unlawful.

ii. The Commission's assessment of forfeitures against the Companies violates their due process rights.

Due process considerations in the Fourteenth Amendment of the United States Constitution and Section 16, Article I of the Ohio require that NEO and Orwell be provided with notice of these alleged violations and be provided the opportunity to present their own evidence in their defense and to confront and cross-examine adverse witnesses, and support their positions before being deprived of a property right via fines and penalties. *See Vectren Energy Delivery of Ohio, Inc., v. Public Utilities Commission of Ohio, 113 Ohio St.3d 180, 2006-Ohio-1386 at ¶ 53, 863 N.E.2d 599.* The fact that a GCR case is pending did not provide NEO and Orwell with notice of claims of violations unrelated to the GCR proceedings.

If the Commission has reasonable grounds that the Companies are in violation of the Ohio Revised Code, the Commission's Rules or a Commission order, the Commission can raise those issues in the appropriate docket and provide the Companies with notice of the allegations against them. By doing so, the Companies would have a right to notice of the claims alleged and an opportunity to defend themselves – an opportunity not afforded in this GCR proceeding.

Moreover, the Commission has notice provisions for forfeitures in the context of motor carrier issues that provide parties with appropriate notice prior to being assessed forfeitures. See OAC 4901:2-7 *et seq.* These rules rightly provide notice to parties to a Commission case with any violations that will be charged against the party. The process set forth in OAC 4901:2-7 is far different than process provided to the

Companies. The GCR proceedings were initiated on January 4, 2012. On February 23, 2013, the Staff filed their Audit Report, which did not request that the Commission order civil forfeitures. On July 1, 2013, the Staff and the OCC filed testimony in this case. Neither the Staff nor the OCC requested that the Commission assess forfeitures in their testimony. From July 8, 2013 through July 10, 2013, the Commission held an evidentiary hearing. Rebuttal testimony was presented on July 22, 2013. The first request for forfeitures was made by the OCC after the completion of the evidentiary hearings when the OCC filed their Post Hearing Brief on October 19, 2013. Contrary to the Commission's findings, the Companies did not have an opportunity to fully address these issues at the hearing because they did not have notice of any requested forfeitures until after the evidentiary record had closed. Consequently, the Companies respectfully request that the Commission order on rehearing that the civil forfeitures against the Companies be dismissed.

iii. In the alternative, if the Commission denies the Companies' Application for Rehearing with respect to the assessment of civil forfeitures, the Companies move the Commission to stay the enforcement of the civil forfeitures pending an appeal to the Ohio Supreme Court.

The Opinion and Order issued civil forfeitures against NEO for $26,000 and Orwell for $50,000. (Opinion and Order at 62). The Commission directed the Companies to pay the civil forfeitures within 30 business days of this Opinion and Order. (*Id.*). As noted in the Opinion and Order, the Companies objected to the assessment of civil forfeitures in the context of a GCR proceeding. (Opinion and Order at 61). Because the Companies have contested the Commission's order of the civil penalties, the Companies respectfully request that the Commission stay the order directing the Companies to pay the civil forfeiture until the record in this case is closed. In the event

that the Companies choose to appeal the decision of the Commission to the Ohio Supreme Court, the Companies respectfully request that the Commission stay the order to pay civil forfeitures until the record in the appeal to the Ohio Supreme Court is closed.

III. CONCLUSION.

For the foregoing reasons, the Companies urge the Commission clarify its directions regarding the audit period and the Companies' ability to purchase gas in-house in the future. In addition, the Companies respectfully request that the Companies grant rehearing regarding the Staff's repricing methodology, the Commission ordered management and performance audits, and the Commission ordered civil forfeitures.

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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing was served this 13th day of December, 2013 by electronic mail upon the following:

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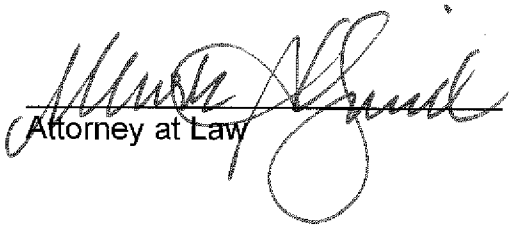

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Summary: Application For Rehearing electronically filed by Mark Yurick on behalf of Northeast Ohio Natural Gas Corporation and Orwell Natural Gas Company