

**BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO**

In the Matter of the Commission-Ordered)
Investigation of Marketing Practices in the) Case No. 14-568-EL-COI
Competitive Retail Electric Service Market)

**APPLICATION FOR REHEARING AND MEMORANDUM IN SUPPORT OF IGS
ENERGY**

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APPLICATION FOR REHEARING OF IGS ENERGY.

Pursuant to R.C. 4903.10, Interstate Gas Supply, Inc. (“IGS”) hereby seeks rehearing of the Finding and Order (“Order”) issued by the Public Utilities Commission of Ohio (“Commission”) in this proceeding on November 18, 2015. In reliance on Ohio Administrative Code (“OAC”) 4901:1-21-05, the Order determined that beginning January 1, 2016, no competitive retail electric service (“CRES” or “supplier”) contract labeled as a fixed-price contract may include a clause that would allow the CRES provider to pass-through additional charges to customers—regardless of whether the customer is a residential, commercial, or industrial customer. The Order also directed Commission Staff to incorporate new definitions into Rule 4901:1-21-05. As specified further in the attached memorandum in support, the Order is unlawful and unreasonable in the following respects:

1. The Order is unlawful and unreasonable inasmuch as it departs from the express language of OAC 4901:1-21-05 to prohibit pass-through provisions in fixed-price contracts.
2. The Order is unlawful and unreasonable inasmuch as it prohibited suppliers from including pass-through clauses in fixed-price contracts with commercial and industrial contracts. The Order unjustly and unreasonably determined that such provisions are misleading, deceptive, or unconscionable.

3. The Order's proposed definition of "fixed-price" is unjust and unreasonable. The Order would require fixed-price contract prices to be provided only on a kilowatt hour basis for all customers. Suppliers provide commercial and industrial customers prices that contain several components that cannot be specified in a kilowatt hour price.
4. The Order is unlawful and unreasonable inasmuch as the determination that suppliers may not invoke change in law provisions in fixed-price contracts without obtaining affirmative customer consent is arbitrary, unfair, and unworkable.
5. To the extent that the Order is intended to apply to contracts entered into prior to the date of the Order, it violates the Ohio Constitution's prohibition against retroactive application of laws and thus unlawful and unreasonable. Because the Order was issued over a year and a half after this proceeding was opened, the Order is also arbitrary, unjust, and capricious.
6. The Order is unlawful and unreasonable to the extent it did not grant IGS's Motion to Intervene

The reasons for this application for rehearing are stated further in the attached memorandum in support. IGS respectfully requests that the Commission grant this application for rehearing and correct the errors identified herein.

Respectfully submitted,

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MEMORANDUM IN SUPPORT

I. INTRODUCTION

Competitive retail electric service providers convey value to their customers through a diverse range of products and services. One type of product is a fixed-price contract. In these contracts, suppliers (particularly for large commercial and industrial customers) often include clauses that provide the option to pass through additional costs to customers that may result from unforeseen or unexpected circumstances such as a change in law or regulatory change. In so doing, the supplier can offer a customer the lowest price possible, with the understanding that if rare regulatory events occur that impose unforeseeable additional charges, then those costs will be passed on to the customer. The ability of a supplier to offer these types of contracts is directly at issue in this proceeding.

This proceeding originated following the events of January 2014. Due to unseasonably cold temperatures that occurred during January 2014, PJM Interconnection LLC (“PJM”) allocated to an unusually high amount of balancing and operating reserve (“BOR”) charges to suppliers—approximately \$600 million, or five times the normal amount during that month. This unexpected event caused suppliers to

incur millions in unhedgeable costs. Although some suppliers may have had the right to flow through these costs, only a handful—in fact, it was likely only FirstEnergy Solutions (“FES”)—attempted to pass these costs onto their customers.

On April 9, 2014, after learning about FES’ decision to flow through polar BOR charges, the Commission opened this investigation and solicited comments and reply comments regarding the legitimacy of pass through clauses. Then, the Commission did nothing for nearly a year and a half. Much occurred in that time. FES decided against flowing through polar vortex costs to mass market customers (residential). And FES stopped providing service to mass market customers altogether. Thus, the primary impetus for this proceeding evaporated overnight.

After this eighteen month delay, on November 18, 2015 the Commission issued the Order that is the subject of this Application for Rehearing. The Order determined that suppliers may not include pass-through language in contracts with a fixed-priced label. The Order relies exclusively on OAC 4901:21-05. And the Order determined that its holding is applicable to all customer classes—residential, commercial, and industrial—regardless of their sophistication.

The Order, however, indicated that regulatory changes may leave a supplier with an uneconomic contract with no opportunity for redress. Thus, the Order determined that suppliers may include in fixed-price contracts regulatory change/change of law provisions that would allow the supplier to renegotiate a contract with the customer’s affirmative consent. To the extent that affirmative consent is not reached, the customer may default to the standard service offer or enter a contract with an alternative supplier—without penalty:

The Commission recognizes that circumstances may occasionally arise over which a CRES provider has no control and no ability to hedge, such as a regulatory change in law. The Commission finds it would be inappropriate to require CRES providers in those circumstances to remain bound by an uneconomic contract with no opportunity for redress. Not only would such a requirement be inequitable for a CRES provider, but could affect consumers as well, as it could result in CRES providers charging much higher rates in fixed-price contracts in attempt to hedge, or elimination of fixed-price contracts from the market.

Consequently, the Commission believes that the fixed means-fixed axiom should be balanced by continuing to permit regulatory-out clauses that would be available for CRES suppliers in very limited circumstances, which must be delineated in plain language in the clause. Regulatory out clauses allow a supplier to revise a contract by proposing new contract terms to the customer. If the customer affirmatively consents to the new terms, the contract would remain in place with the new terms. However, customers could affirmatively reject or passively reject the proposed terms by inaction. A customer rejecting the terms would then be permitted to pursue another CRES provider or the default service without being subjected to any penalty. The Commission further finds that regulatory-out clauses must be clearly and conspicuously stated in the contract; that any acronyms in the regulatory out clause must be defined within the contract; and that the clause must specify to a reasonable extent the circumstances under which it could be invoked.

The Order determined that the above guidelines represent the Commission's "going forward" interpretation of its rules. The Order indicated that suppliers have until "January 1, 2016, to bring all marketing for contracts being marketed into compliance with the 'fixed-means-fixed' guidelines set forth in this Finding and Order."¹

The Order further determined that the Rule 4901-21-05 is ambiguous and therefore requires clarification and modification. To that end, the Order directed that additional definitions be incorporated into the rule related to fixed price and variable price. The Order stated that fixed price should be defined as "[a]n all-inclusive per kWh price that will remain the same for at least three billing cycles or the term of the contract,

¹ Order at 13.

whichever is longer.”² The Order stated that variable price should be defined as “[a]n all-inclusive per kWh price that can change, by the hour, day, month, etc., according to the terms and conditions in the supplier's disclosure statement.”³ Finally, the Order stated that introductory price should be defined as “[f]or new customers, an all-inclusive per kWh price that will remain the same for a limited period of time between one and three billing cycles followed by a different fixed or variable per kWh price that will be in effect for the remaining billing cycles of the contract term, consistent with terms and conditions in the supplier's 'disclosure statement.’”⁴

As discussed further below, the Order is unlawful, unreasonable, arbitrary, and capricious; thus, the Commission should reverse the Order and correct the errors identified herein. And, as discussed in the Motion for Stay submitted by the Retail Energy Supply Association (“RESA”), IGS urges the Commission to stay the January 1, 2016 implementation date identified in the Order. Due to the unresolved issues identified in this Application for Rehearing, as well as the pending rulemaking proceeding being undertaken by Staff, the January 1, 2016 implementation date is unworkable and will lead to customer and CRES provider confusion—to the detriment of the competitive market.

II. ARGUMENT

A. The Order is unlawful and unreasonable inasmuch as it departs from the express language of OAC 4901:1-21-05 to prohibit pass-through provisions in fixed-price contracts

² Order at 13-14.

³ *Id.* at 14.

⁴ *Id.*

In reliance on Rule 4901:1-21-05, the Order determined that no contract labeled fixed-price may include a clause that allows the supplier to pass-through to the customer additional charges identified in the contract. As discussed below, contrary to the Order, that section contains provisions that authorize a supplier to include a pass-through clause so long as it is disclosed to the customer. Thus, the Order unlawfully rewrote OAC 4901:1-21-05 outside of a rulemaking process and without obtaining approval of the modification from the Joint Committee on Agency Rule Review ("JCARR").

OAC 4901:1-21-05(C), provides that it is a misleading, deceptive, and unconscionable sales practice to fail to comply with provision (A), (B),⁵ or (C) of the rule. Provision (A) contains specific requirements for offers to residential and small commercial customers.⁶ The specific language of that portion of the rule, however, indicates that suppliers may include a properly disclosed pass-through clause.

As is relevant to this Application for Rehearing, provision (A) indicates that an offer must include the following items, some of which may identify a pass-through clause:

⁵ Provision B states "A CRES provider's promotional and advertising material that is targeted for **residential and small commercial customers** shall be provided to the commission or its staff within three business days of a request by the commission or its staff." Provision (B) relates to the transmission of advertising materials to residential and small commercial customers, so that provision is not relevant to this proceeding.

⁶ "(A) Each competitive retail electric service (CRES) provider that offers retail electric generation service **to residential or small commercial customers** shall provide, in marketing materials that include or accompany a service contract, sufficient information for customers to make intelligent cost comparisons against offers they receive from other CRES providers."

(1) For fixed-rate offers, the cost per kilowatt hour for generation service and, if applicable, transmission service.

(2) For per cent-off discounted rates, an explanation of the discount and the basis on which any discount is calculated.

(3) For variable rate offers, a clear and understandable explanation of the factors that will cause the price to vary, including any related indices, and how often the price can change.

(4) For flat-monthly rate offers, a specific listing of the rate to be charged per month for the duration of the contract.

(5) The amount of any other recurring or nonrecurring CRES provider charges.

(6) A statement that the customer will incur additional service and delivery charges from the electric utility.

(7) A statement of any contract contingencies or conditions precedent.⁷

The rule specifically requires disclosure of recurring and nonrecurring charges and any contract contingencies or conditions precedent, but it does not indicate that such charges cannot be included in a fixed-rate contract. Each of these provisions could each be utilized to include a pass-through provision.

A recurring or non-recurring charge describes a charge in *addition* to a fixed-rate in a contract. Clearly, the rule envisions that a supplier may enumerate certain terms in their contract that would allow for the pass through of certain non-recurring charges.

Likewise, Webster's dictionary defines contingency as an event that may but is not certain to occur.⁸ A pass-through clause often identifies events such as additional wholesale charges or changes that may or may not occur, which would require the imposition of additional charges at the supplier's election. Similarly, Webster's

⁷ OAC 4901:1-21-05(A) (emphasis added).

⁸ <http://www.merriam-webster.com/dictionary/contingency>

dictionary defines condition precedent as a “condition whose fulfillment must precede the vesting of an estate, the taking effect of a contract, *or the accruing of a right.*”⁹ Thus, a condition precedent could describe the passage of an event, regulatory change, or legal change that would accrue a right to pass-through additional identified costs to the customer.

The fact that the rule requires the disclosure of recurring and non-recurring charges and any contract contingencies or conditions precedent charges is an admission that such charges may be included in a fixed-price supplier contract. In other words, it would defy reason to require a supplier to disclose the above-mentioned contractual terms in a fixed-rate contract if they were not permitted to be included in the contract in the first instance. The Order ignores the existence of these portions of rule—effectively deleting these portions without explanation. Because each of the above-mentioned contractual terms would permit the use of a pass-through clause, the Order unlawfully and unreasonably determined that fixed-rate contracts cannot include a pass-through clause.

Finally, it is important to consider that the Commission’s determination regarding the validity of pass-through clauses may have unintended negative consequences. While this investigation is focused on the pass-through of additional unanticipated costs, the Order’s holding is equally applicable to the pass-through of unanticipated credits. For example, the Commission recently issued an order in Ohio Power Company’s electric security plan case, which directed the utility to bill customers directly for transmission charges. These transmission charges were already included in many of

⁹ <http://www.merriam-webster.com/dictionary/condition%20precedent> (emphasis added)

the supplier contracts. To the extent that a supplier had a fixed-price contract with a pass-through clause related to a regulatory change, the supplier would not be permitted to pass through to the customer the reduction that resulted from the utility billing the customer directly for transmission charges.

To be clear, IGS does not oppose further consideration of new disclosure requirements pertaining to pass-through clauses in residential and small commercial contracts. But those changes should be considered in a separate rulemaking proceeding that provides suppliers with sufficient time to implement any changes.

B. The Order is unlawful and unreasonable inasmuch as it prohibited suppliers from including pass-through clauses in fixed-price contracts with commercial and industrial contracts. The Order unjustly and unreasonably determined that such provisions are misleading, deceptive, or unconscionable

The only section of OAC 4901:1-21-05 that is applicable to mercantile customers is provision (C). That section provides that a supplier may not engage in unfair, misleading, and deceptive, or unconscionable sales acts, and includes a list of enumerated prohibited acts. The enumerated acts, however, are applicable to interactions with residential and small commercial customers, as well as promotional materials not typically provided to commercial and industrial customers.¹⁰ Thus, the Order implicitly determined that entering into a fixed-price contract that contains a pass-through clause to a commercial or industrial contract is unfair, deceptive, and unconscionable. That determination is unjust and unreasonable.

As discussed above, the rule currently allows inclusion of pass-through clauses in fixed-rate contracts with residential and small commercial customers. It cannot follow

¹⁰ Rule 4901:1-21-05-(C)(8) is limited to advertising or marketing offers. Commercial and industrial customers normally receive customized pricing that would not fall under the rule.

that it is misleading, deceptive, and unconscionable to include pass-through clause with more sophisticated customers.

Moreover, if a pass-through clause is included and properly disclosed in a contract with a commercial or industrial customer that otherwise contains a fixed-price for electricity (or perhaps a fixed-price for the energy portion of the bill), it would be unjust and unreasonable to determine that a supplier has done wrongdoing. Commercial and industrial customers are sophisticated purchasers of electricity. It is clear by this proceeding and others that commercial and industrial customers are represented by counsel and review terms and conditions in their contract closely. Yet, the Order assumes that these customers do not read the terms and conditions in their contracts or understand a pass-through clause. If a customer understands that a contract contains a pass-through provision and the nature of the costs related to the clause, it cannot follow that the supplier has mislead or deceived the customer.

Commercial and industrial customers are not shy to file complaints before this Commission when a supplier attempts to pass a cost that is allegedly outside the terms and condition of the contract. Rather than place limitations on the types of contracts that willing sellers and willing sophisticated buyers may enter, the Commission should rely on the dispute resolution process that exists today and works well.

C. The Order's proposed definition of "fixed-price" is unjust and unreasonable. The Order would require fixed-price contract prices to be provided only on a kilowatt hour basis for all customers. Suppliers provide commercial and industrial customers prices that contain several components that cannot be specified in a kilowatt hour price

The Order appears to have identified three labels that must be placed on a contract: fixed, variable, and introductory. The Order proposed the following definitions:

- **Fixed Price:** An all-inclusive per kWh price that will remain the same for at least three billing cycles or the term of the contract whichever is longer
- **Variable Price:** An all-inclusive per kWh price that can change, by the hour, day, month, etc., according to the terms and conditions in the supplier's disclosure statement
- **Introductory Price:** For new customers, an all-inclusive per kWh price that will remain the same for a limited period of time between one and three billing cycles followed by a different fixed or variable per kWh price that will be in effect for the remaining billing cycles of the contract term, consistent with terms and conditions in the supplier's 'disclosure statement

With respect to commercial and industrial customers, the Order's determination is unjust and unreasonable, and, as a practical matter, it is unworkable given the structure of the pricing provided to these classes of customers.

Initially, commercial and industrial customers do not typically enter into contracts for an all-inclusive price per kWh—they often don't want them. While a portion of a commercial or industrial customer contract may include a fixed-price, these customers enter into a host of differing sophisticated contractual arrangements depending on their load factor, time of use, and appetite for risk. For example, some have contracts that are fixed for a certain block of kilowatts and with the remainder of the customer's usage tied to an index price. Other customers may receive a fixed price for the energy portion of their bill with a pass-through clause for the capacity portion. Other customers may have two-different blocks of fixed-price energy for different times of day. These are just a few contractual structures that exist that defy classification into the three definitional buckets identified in the Order.

A more workable framework would allow suppliers to structure their contracts for commercial and industrial customers in any way the customer desires, without adding labels that will only create customer and supplier confusion.

That being said, IGS would not object to a requirement that when a contract with a commercial and industrial customer includes the words “fixed”, the contract should identify in close proximity that additional charges may apply under specific circumstances clearly identified in the contract. For example, if a supplier offers a fixed-price for energy with a capacity pass through, the contract could identify that the “customer will pay 6 cents per kilowatt hour with capacity pass-through as defined in terms and conditions” or “customer will pay 6 cents per kilowatt hour and customer will pay capacity charges based upon the customer’s peak load contribution” or “customer will pay 6 cents per kilowatt hour subject to pass-through of charges identified in terms and conditions.” Such a paradigm would strike the appropriate balance between ensuring proper disclosure of contract terms while preserving the ability to provide innovative products and services that fit specific customer needs.

D. The Order is unlawful and unreasonable inasmuch as the determination that suppliers may not invoke change in law provisions in fixed-price contracts without obtaining affirmative customer consent is arbitrary, unfair, and unworkable

The Order recognized that suppliers may enter fixed-price contracts and incur unexpected costs due to regulatory orders or changes in law. In light of this risk, the Order determined that suppliers may, in limited circumstances, obtain affirmative customer consent to renegotiate the terms of a contract. But, if such consent is affirmatively denied or passively not provided, the customer may elect an alternate supplier or revert to default service without penalty. As discussed below, the process specified in the Order unjustly and unreasonably eliminates the value of a change in law/regulatory change provision in a supplier contract.

In the event that a regulatory order or change requires a supplier to incur unexpected costs, there is little likelihood that the supplier may obtain affirmative consent from a customer. By allowing the customer to terminate a contract without the imposition of a penalty, a customer has every incentive to seek an offer from an alternative supplier. This is especially true if the price for energy declines after the customer enters into the contract.

If the customer does in fact terminate their relationship with their supplier, it may have a detrimental impact on the supplier's hedging portfolio—rendering prior wholesale contracts uneconomic. For example, assume that supplier enters into a three year contract with a 5 megawatt demand customer with an 80% load factor and hedges the customer's energy requirements for the duration of the contract. If a change in law occurs after one year, the supplier will be left holding a forward energy contract for two remaining years that will have to be liquidated into the market. For every \$1 per mwhour that the market price is less than the contract price, the supplier may lose \$70,000. Such a result would be fundamentally unfair to the supplier if the regulatory change/change in law provision is properly disclosed in the contract.

Rather than requiring affirmative consent, the Commission on rehearing should allow suppliers to include provisions in their contracts that allow the pass-through of additional unexpected costs that result from regulatory orders or changes in law, subject to providing customer notice. Such provisions should be clearly disclosed and be limited to the pass-through of costs that are actually incurred.

E. To the extent that the Order is intended to apply to contracts entered into prior to the date of the Order, it violates the Ohio Constitution's prohibition against retroactive application of laws and thus unlawful and

unreasonable. Because the Order was issued over a year and a half after this proceeding was opened, the Order is also arbitrary, unjust, and capricious

Although the Order indicated that suppliers must bring their contracts into compliance with the Order by January 1, 2016, it did not specifically exempt pass-through clauses in existing contracts. As discussed below, it would be unlawful, unjust, unreasonable, arbitrary, and capricious to prohibit suppliers to invoke pass-through clauses in existing contracts.

Initially, “[s]ection 28, Article II of the Ohio Constitution provides that ‘[t]he general assembly shall have no power to pass retroactive laws.’ *State v. Cook*, 83 Ohio St.3d 404, 410 (1998). The Ohio Constitution prohibits retroactive application of statutes to impair vested rights in existing contracts or create new burdens. *Id.* at 410-412. This limitation applies to administrative rules. *Fraternal Order of Police v. Hunter*, 49 Ohio App. 2d 185, 195 (1975). Ohio courts have held that “[r]etroactive application of administrative rules is particularly disfavored when substantive rights are involved.” *Martin v. Ohio Dept. of Human Serv.*, 130 Ohio App. 3d 512, 524 (1998) (Ct. Appeals, Second Dist., Champaign Co.). The Order, if applied retroactively to existing contracts, would impair suppliers’ substantive rights to pass-through costs specifically enumerated in their contracts with customers. That would violate precedent and the Ohio Constitution’s prohibition against retroactive application of law and regulation.

In this instance, retroactive application of the new regulation would be arbitrary and capricious, given that the Commission opened this proceeding and then did nothing for eighteen months. During that time, suppliers continued to enter

into fixed-price contracts with pass-through clauses. Had the Commission not unduly delayed its Order, the number of contracts potentially impacted by the Order would be significantly less. Thus, the retroactive application of the Order to existing contracts would also be arbitrary and capricious.

F. The Order is unlawful and unreasonable to the extent it did not grant IGS's Motion to Intervene

The Order granted the intervention of several customer parties, but did not specifically address IGS's Motion to Intervene, which was filed on May 9, 2014.¹¹ IGS assumes that the Order's failure to grant IGS's Motion was an oversight, but, to the extent that it was not, the Order is unlawful and unreasonable.

For purposes of considering requests for leave to intervene in a Commission proceeding, the Commission's rules provide that:

Upon timely motion, any person shall be permitted to intervene in a proceeding upon a showing that: (1) A statute of this state or the United States confers a right to intervene. (2) The person has a real and substantial interest in the proceeding, and the person is so situated that the disposition of the proceeding may, as a practical matter, impair or impede his or her ability to protect that interest, unless the person's interest is adequately represented by existing parties.¹²

Further, R.C. 4903.221(B) and Rule 4901-1-11(B), OAC, provide that the Commission, in ruling upon applications to intervene in its proceedings, shall consider the following criteria:

- (1) The nature and extent of the prospective intervener's interest;
- (2) The legal position advanced by the prospective intervener and its probable relation to the merits of the case;
- (3) Whether the intervention by the prospective intervener will unduly prolong or delay the proceedings;
- (4)

¹¹ Order at 2.

¹² Rule 4901-1-11(A), OAC.

Whether the prospective intervener will significantly contribute to full development and equitable resolution of the factual issues.

As discussed in IGS's Motion to Intervene, Comments, and this Application for Rehearing, IGS has a real and substantial interest in the resolution of this proceeding. As IGS stated in its Motion to Intervene, "IGS has a substantial interest in this proceeding, insofar as the resolution of this proceeding may impact the products that competitive retail electric service ("CRES") providers offer to customers, as well as CRES providers' marketing practices."¹³

IGS has direct, real, and substantial interests in this proceeding. IGS's intervention has not unduly delayed this proceeding. Further, IGS is so situated that without IGS' ability to fully participate in this proceeding, its substantial interest will be prejudiced. Others participating in this proceeding do not represent IGS's interests. Inasmuch as others participating in this proceeding cannot adequately protect IGS's interests, it would be inappropriate to determine this proceeding without IGS's participation. Finally, the Supreme Court of Ohio has held that intervention should be liberally allowed for those with an interest in the proceeding.¹⁴

Accordingly, on rehearing, the Commission should grant IGS's Motion to Intervene.

III. CONCLUSION

For the reasons stated herein, IGS requests that the Commission grant this application for rehearing and correct the errors identified in the Order. Moreover, IGS

¹³ Motion to Intervene and Memorandum in Support of IGS at 5.

¹⁴ *Ohio Consumers' Counsel v. Pub. Util. Comm.*, (2006) 111 OhioSt.3d 384, 388.

urges the Commission to grant the Motion for Stay filed by RESA to ensure that changes to supplier disclosure requirements are made in a manner that can be appropriately incorporated into contracts—January 1, 2016 simply does not provide sufficient time, given the uncertainty surrounding the additional compliance requirements adopted in the Order. Any changes that are ultimately made to OAC 4901:1-21-05 should be made within a separate rulemaking proceeding and implemented after final approval by JCARR.

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CERTIFICATE OF SERVICE

The undersigned hereby certifies that a copy of the foregoing *Application for Rehearing and Memorandum in Support of IGS Energy* was served this 18th day of December 2015 via electronic mail upon the following:

/s/ Joseph Olikier

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Summary: Application for Rehearing and Memorandum in Support of IGS Energy electronically filed by Mr. Joseph E. Olikier on behalf of IGS Energy