BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Commission's Investigation of Submetering in the State of Ohio.	:	Case No. 15-1594-AU-COI

DIRECT ENERGY SERVICES, LLC AND DIRECT ENERGY BUSINESS, LLC'S MEMORANDUM CONTRA TO THE JOINT APPLICATION FOR REHEARING OF THE SECOND ENTRY ON REHEARING FILED BY OHIO POWER COMPANY AND DUKE ENERGY OHIO, INC.

I. INTRODUCTION

Pursuant to Ohio Administrative Code ("OAC") Rule 4901-1-35, Direct Energy Business, LLC and Direct Energy Services, LLC submit this Memorandum Contra to arguments raised in the Joint Application for Rehearing of the Second Entry on Rehearing filed by Ohio Power Company and Duke Energy Ohio, Inc. (jointly "Utilities") in this matter on July 21, 2017 ("Joint Application for Rehearing").[1] In its June 21, 2017 Second Entry on Rehearing ("Second EOR") in this matter, the Public Utilities Commission of Ohio ("Commission") established a zero percentage threshold for the Relative Price Test set forth in its December 7, 2016 Finding and Order ("December 7, 2016 Order"). In its December 7, 2016 Order, the Commission proposed to extend to landlords, condominium associations, submetering companies, and other similarly-situated entities the historical test it uses to determine whether an entity is a public utility (known as the *Shroyer Test*[2]). The Commission proposed to revise the third prong of the *Shroyer Test* to create a rebuttable presumption that an entity is a public utility by comparing

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[1] There are several applications for rehearing of the Second Entry on Rehearing currently pending.

[2] *In re the Matter of the Complaints of Inscho v. Shroyer's Mobile Homes*, Case No. 90-182-WS-CSS, et al., (Feb. 27, 1992) ("*Shroyer*" or "*Shroyer Test*").

utility rates to what the charges are to end use customers and identifying a threshold percentage above which the pricing of the entity will subject it to regulation as a public utility.

After consideration of comments from interested stakeholders, the Commission adopted a threshold percentage of zero to serve as the baseline test. Once the rebuttable presumption is triggered through the use of the Relative Price Test, a reseller may demonstrate that it falls under a Safe Harbor (resulting in avoidance of Commission jurisdiction) if it: (1) is passing through its annual costs of providing a utility service charged by a local public utility and competitive retail service provider (if applicable) to its submetered residents at a given premises; or (2) its annual charges for a utility service to an individual submetered resident do not exceed what the resident would have paid the local public utility for equivalent annual usage, on a total bill basis, under the local public utility's default service tariffs.

The Utilities' Joint Application for Rehearing submits that the Safe Harbor should be modified to avoid the potential problem of a reseller evading the purpose of the Relative Price Test through an affiliate retail supplier.[3] To avoid this potential issue, the Utilities recommend that the two branches of the Safe Harbor be modified to be conjunctive. The Utilities' further argue that a "no markup" restriction be imposed for both the reseller and any retail supplier affiliates.[4] The Utilities' also advocate that the Commission should specify that the price paid by the reseller to the retail supplier (affiliated or non-affiliated) should be calculated on a net basis (which would factor in fees/other payments).[5]

Direct Energy Business, LLC and Direct Energy Services, LLC ("Direct Energy") are retail suppliers in the state of Ohio and serve electric and natural gas customers in Ohio's

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3 Joint Application at 2.
4 Joint Application at 2.
5 Joint Application at 2.

investor-owned utility territories. Retail suppliers like Direct Energy may supply the energy to the landlord or building owner and the landlord/building owner in turn bills its tenants for the power purchased for the property. The prices retail suppliers offer to their customers (whether those customers are residential customers or building owners) are not regulated by the Commission. As conveyed in its comments filed in this proceeding,[6] Direct Energy has concerns regarding the negative retail market impacts that may result if the Commission regulates landlords and building entities as public utilities based on a comparison of their retail end user prices to utility rates. This is because the price offers of retail suppliers to landlords and/or building entities are based on the usage and consumption of the building which does not translate to pure residential costs or usage. The PUCO's Second EOR adequately addresses that concern by establishing a disjunctive two-branch Safe Harbor that would render a reseller outside the Commission's jurisdiction if it passes through its annual costs of providing a utility service charged by a local public utility or retail supplier (if applicable) to its submetered residents at a given premises.

Direct Energy finds the Relative Price Test and Safe Harbor established in its Second EOR to be a reasonable and appropriate way for the Commission to evaluate the reasonableness of a submetering company's charges. Consequently, Direct Energy opposes the Utilities' proposed modifications to the Safe Harbor and Relative Price Test as they would result in inappropriate regulation of retail supplier pricing by the Commission.

II. BACKGROUND

The Commission's Second EOR established a zero percentage threshold for the Relative Price Test and a Safe Harbor for a reseller once the rebuttable presumption is triggered under the

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6 Comments of Direct Energy dated January 13, 2017 at 2.

third prong of the *Shroyer Test.*[7] More specifically, the Commission established in its Second EOR that:

> A [r]seller will overcome the rebuttable presumption and thus will not be subject to Commission jurisdiction under the third prong of the *Shroyer Test* if the Reseller demonstrates that (1) the Reseller is simply passing through its annual costs of providing a utility service charged by a local public utility and competitive retail service provider (if applicable) to its submetered residents at a given premises; or (2) the Reseller's annual charges for a utility service to an individual submetered resident do not exceed what the resident would have paid the local public utility for equivalent annual usage, on a total bill basis, under the local public utility's default service tariffs.

Second EOR at 15. The Commission clarified that the Relative Price Test and Safe Harbor will apply only to submetered residential customers.[8]

The Commission directed that electric, gas water and sewer distribution utilities work with Commission Staff to "develop a website tool or other mechanism to provide submetered residential customers with an estimated calculation of what the customer would have paid the local public utility for equivalent usage, on a monthly total bill basis, under the utility's default service tariffs."[9] A submetered residential customer could review his or her bill and compare the reseller's utility service charge against what the customer would have paid the local public utility. If the submetered customer is paying the reseller more than what he or she would have paid the local public utility, then the rebuttable presumption is triggered and the reseller is presumed to be a public utility under the third prong of the *Shroyer Test.* However, the reseller

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[7] To determine public utility status of an entity, the Commission has historically applied the *Shroyer Test.* Pursuant to this three-part test, the Commission considers the following three factors: (1) Has the landlord manifested an intent to be a public utility by availing itself of special benefits available to public utilities such as accepting a grant of a franchised territory, a certificate of public convenience and necessity, the use of eminent domain, or use of the public right of way for utility purposes?; (2) Is the utility service available to the general public rather than just to tenants; (3) Is the provision of utility service ancillary to the landlord's primary business?

[8] Second EOR at 15.

[9] Second EOR at 15.

will avoid Commission jurisdiction under the *Shroyer Test* if it can demonstrate that it falls within one of the Safe Harbor provisions detailed above.

The Commission advised that in calculating the reseller's charges under the Relative Price Test, a submetered customer should include any administrative fees or similar charges, but exclude any charges for common areas. For common areas, the Commission will not assert jurisdiction over a reseller in instances in which a reseller is passing through its costs of providing a utility service charged by a local public utility and retail supplier (if applicable) to its submetered residents. Thus, the Commission determined that the rebuttable presumption "will be invoked where the [r]eseller charges the submetered residential customer more than the customer would have paid the local public utility under the default service tariff for the equivalent usage on a total bill basis."[10] If, however, a reseller would fail to rebut that presumption, it would be classified as an unlawfully operating public utility and be subject to Commission regulation.

Numerous stakeholders filed applications for rehearing of the Second EOR on June 21, 2017. As explained below, Direct Energy takes issue with the Utilities' proposals, reflected in their applications for rehearing, because they would: (1) result in unprecedented regulation of retail supplier pricing; and (2) hamstring the ability of retail suppliers to develop market-based pricing and/or customer-specific pricing tailored to the specific needs of a reseller.

III. ARGUMENT

The Commission should deny the Utilities' proposals because they would result in regulation of retail supplier pricing which is unlawful and unsupported by Commission precedent. In their Joint Application on Rehearing, the Utilities argue that the "Safe Harbor is

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[10] Second EOR at 18.

fundamentally flawed because an affiliate of the submetering entity can charge any price it wishes and avoid the price protection ostensibly intended by the Relative Price Test."[11] The Utilities call for elimination or modification of the Safe Harbor and support the Commission evaluating public utility status on a case-by-case basis.[12]

The Utilities assert that the Safe Harbor is flawed because it permits a reseller to pass through to its customers the amount it paid for utility services, even if that price exceeds the comparable retail price.[13] As currently structured, the Safe Harbor is triggered by either the first or second branch of the test. The Utilities claim that resellers may evade falling under the Commission's jurisdiction through use of an affiliate retail supplier. To eliminate the potential that a reseller overpays for utility services from an affiliate retail supplier and avoids Commission jurisdiction via the Safe Harbor provision, the Utilities recommend that the two branches of the Safe Harbor be modified to be conjunctive. The Utilities propose that a reseller would operate in the Safe Harbor only if it "(1) passes through charges it pays for utility service without markup *and* (2) those charges do not exceed the comparable rate level of the local public utility."[14]

Direct Energy submits that it would be unreasonable to make the two branches of the Safe Harbor conjunctive. Significantly, this approach would result in defacto regulation of retail

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[11] Joint Application for Rehearing at 4.

[12] Applications for Rehearing are governed by Section 4903.10, Ohio Revised Code ("O.R.C.") and OAC Rule 4901-1-35. Those authorities direct that applications for rehearing be granted only where a Commission order is "unreasonable," "unlawful," or "unjust or unwarranted." The Second EOR is not "unreasonable," "unlawful," or "unjust or unwarranted" as it relates to the Safe Harbor and Relative Price Test and the Utilities failed to demonstrate otherwise. As discussed in this Memorandum Contra, the adoption of the Utilities' proposed modifications to the Relative Price Test and Safe Harbor would be unlawful and unreasonable, as their proposed restrictions rise to the level of Commission regulation of retail supplier pricing. Thus, the Commission should deny the Utilities' proposed modifications to the Relative Price Test and Safe Harbor provision set forth in the Second EOR.

[13] Joint Application for Rehearing at 4.

[14] Joint Application for Rehearing at 5.

supplier pricing which is both illegal and would negatively impact the competitive market.[15] Retail suppliers, like Direct Energy, may supply the energy to the landlord or building owner through negotiated contracted prices. In a submetering context, the landlord or building owner is the commercial customer of the retail supplier. Since retail supplier prices are not regulated, the retail supplier can offer a price to the commercial customer that is based on market factors and takes into consideration the individual circumstances of the customer. The pricing between the retail supplier and the commercial customer is then negotiated and set forth in a contract between the two entities. The pricing arrangement between the retail supplier (affiliated or unaffiliated) and the commercial customer is presumably reasonable as it is a negotiated arrangement set forth in a contract. If a landlord or building owner must ensure that the retail price charged to the end-user customer must be constrained by the utility rate, then that will negatively impact how the retail supplier may elect to structure the price to its commercial customers. The cost and usage factors associated with large commercial usage are not a 1:1 translation to residential, leading to a commercial expectation of residential pricing which does not match their usage profile.

The Utilities also assert that even if the two branches of the Safe Harbor are applied conjunctively, the result would be that the reseller could charge up to the level of the equivalent local utility rates. They submit that resellers would still enjoy significant profit levels and that this issue should be fixed by imposing a "no markup" restriction on both a reseller and its retail

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[15] The Commission does not have the statutory authority to set competitive retail provider rates or design products but the Commission does have the authority to: (1) set minimum standards related to unfair, deceptive, and unconscionable acts and practices regarding marketing, solicitation, sale of power and administration of contract; (2) hear and initiate complaints against retail providers; and, (3) determine whether a service previously approved as competitive is no longer competitive. See Section 4928.10, 4928.16, and 4928.06, Ohio Revised Code. Similarly, Chapter 4929 which establishes the Commission's regulatory authority over competitive retail natural gas service suppliers does not empower it to set retail contract rates or terms of service. Further, Section 4929.02(A)(7) establishes state policy to eliminate rate making by the Commission for natural gas supplies under Chapters 4905 and 4928 of the Revised Code.

supplier affiliate.[16] In short, the Utilities would like the Commission to impose price restrictions on both the reseller and retail supplier affiliate, prohibiting them from marking up prices paid for utility services sold. This means that a retail supplier affiliate would have to charge the price it paid for the commodity without markup.

If the Commission imposes a "no markup" restriction on affiliate retail suppliers, as suggested by the Utilities, it would constitute direct regulation of retail supplier pricing. Moreover, Direct Energy expects that affiliate retail suppliers would not be sustainable if they were constrained to providing services to resellers at a charge no more than the price it paid for the commodity. Certainly, it is not feasible for a business to operate if it cannot markup a product or service as businesses have administrative and other costs to cover. Such a result would be an inappropriate restriction on retail supplier pricing and the Commission has no authority to impose such a restriction. The imposition of a "no markup" restriction would negatively impact the competitive market and, ultimately, harm end-user customers who will not receive the benefit of a negotiated, market-based retail price.

The Utilities take their argument even further by claiming that an unaffiliated retail supplier could assist a reseller in circumventing Commission jurisdiction through "kickback" payments. The Utilities argue that the Commission should direct that the price paid by the reseller to an affiliated or unaffiliated retail supplier for purposes of the Relative Price Test be calculated on a "net basis." The Utilities provide the following example of its proposed "net basis" calculation: "if a reseller pays $100 for a service it resells to a retail customer but the retail

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16 Joint Application for Rehearing at 6.

supplier pays a $20 fee to the reseller, the net price the reseller paid would be $80 – which could not be marked up when it resells to retail customers."[17]

The website tool or other mechanism to be developed by Commission staff for residential customers to calculate an estimate of what they would have paid their local public utility for equivalent service will assist residential customers in conducting the Relative Price Test. The residential customer will have an opportunity to obtain information regarding payments between the retail supplier and reseller if it files a complaint against a reseller. Direct Energy is not opposed to the Relative Price Test being calculated on a "net basis" so long as the Safe Harbor would operate if a reseller (1) passes through charges it pays for utility service without markup *or* (2) those charges do not exceed the comparable rate level of the local public utility. Maintaining the Commission's disjunctive two-branch Safe Harbor provision will ensure that the Safe Harbor extends to resellers that contract with a retail supplier for not only commodity services but any customer-specific services that may not be offered by a local public utility.

In summation, the Commission did not err by establishing the Relative Price Test and Safe Harbor provisions as set forth in its Second EOR. The Commission's approach is a reasonable way to evaluate the reasonableness of a submetering company's charges and it should not be altered. There is simply no legal or record support for the Commission extending its jurisdiction over the terms of retail supplier pricing, as urged by the Utilities. It is critical that the Commission deny the Utilities' proposed modifications to the Relative Price Test and Safe Harbor provision to protect the competitive retail market.

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[17] Joint Application for Rehearing at 6.

IV. CONCLUSION

For the reasons discussed above, Direct Energy requests that the Commission reject the Utilities' Joint Application for Rehearing.

Respectfully submitted,

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Date: July 31, 2017

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CERTIFICATE OF SERVICE

I certify that an accurate copy of the forgoing Memorandum Contra has been filed with the Public Utilities Commission of Ohio on July 31, 2017, and electronically served upon all parties of record via the PUCO's electronic filing system. In addition, I certify that a service copy of the foregoing document was sent by or on behalf of the undersigned counsel on July 31, 2017 to the following parties of record via electronic transmission.

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Summary: Memorandum Direct Energy Services, LLC and Direct Energy Business, LLC's Memorandum Contra to the Joint Application for Rehearing of the Second Entry on Rehearing Filed by Ohio Power Company and Duke Energy Ohio, Inc. electronically filed by Mr. Scott R. Dismukes on behalf of Stoner, Sarah Ms. and Eckert Seamans Cherin & Mellott, LLC and Clearfield, Daniel Mr.