BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO

In the Matter of the Complaint of The Suburban Fuel Gas, Inc.,	)	
Complainant,	)	
vs.	)	Case No. 86-1747-GA-CSS
Columbia Gas of Ohio, Inc.,	)	
Respondent.	)	

POST-HEARING BRIEF OF RESPONDENT COLUMBIA GAS OF OHIO, INC.

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I. Introduction

This case involves a complaint by The Suburban Fuel Gas, Inc. (Complainant or Suburban) against Columbia Gas of Ohio, Inc. (Respondent or Columbia). The complaint was originally filed on August 29, 1986. It alleged, without specificity, that Columbia had violated various enumerated provisions of the Ohio utility statutes.

On September 23, 1986, Columbia moved to dismiss on the grounds that Suburban lacked standing to challenge Columbia's rates, charges, or practices, and that the complaint was so lacking in detail that it failed to state reasonable grounds for complaint. In an entry issued on October 9, 1986, the Attorney Examiner essentially agreed with the latter contention, and directed Suburban to file a more definite statement of the facts which constituted the basis of its complaint.

On October 22, 1986, Suburban filed an amended complaint, again alleging that Columbia had violated various provisions of the Ohio utility statutes. On November 12, 1986, Columbia moved to dismiss the amended complaint, again citing Suburban's lack of standing and failure to provide sufficient detail. Columbia also argued that certain issues raised in the amended complaint were beyond the jurisdiction of the Commission.

On January 6, 1987, the Commission denied Columbia's motion to dismiss, and directed Columbia to answer the amended complaint. Columbia filed its answer on January 27, 1986. In an entry issued on Fe uary 2, 1987, the Attorney Examiner found that reasonable grounds for complaint had been stated, and set the matter for hearing. The Office of Consumers' Counsel (OCC) was later granted leave to intervene.

The hearing was held on May 7, 1987. Although Suburban had alleged that Columbia's actions had adversely affected its operations, it presented no testimony by any of its own officers, agents, or employees. Instead, its case in chief consisted solely of testimony by Columbia officials Ronald G. Parshall and Michael J. Law, who were called by Suburban as on cross-examination. Mr. Parshall is Columbia's Bowling Green Area Manager, while Mr. Law is an Industrial Marketing Engineer in Columbia's Findlay Division.

For its direct case, Columbia presented the prepared, written testimony of Thomas F. D[illegible]vers, Columbia's Vice President, Rates and Depreciation, as well as additional testimony by Mr. Law. Columbia also elicited testimony from Suburban's Executive Vice President, A. Scott Rothey, who was called by Columbia as on cross-examination.

At the conclusion of the hearing, the Attorney Examiner directed that Suburban submit its initial brief by June 5, 1987, and that Columbia and OCC submit their initial briefs by June 19, 1987. By subsequent entries, those dates were extended to June 12, 1987, and July 7, 1987. This brief is submitted in accordance with the revised schedule established by the Attorney Examiner.

II. Argument

In its post-hearing brief, Suburban repeatedly argues that Columbia has blatantly violated numerous provisions of its tariffs and the Ohio utility laws. A careful examination of the record, however, reveals just the opposite. When one disregards Suburban's rhetorical excesses and innuendoes, corrects the various mischaracterizations, and carefully analyzes the applicable case law, it becomes abundantly clear that Columbia has violated neither its tariffs nor the relevant statutory provisions. On the contrary, Columbia's rates, charges, and practices have been both reasonable and lawful, and fully consistent with its obligations as a public utility.

Columbia will respond in detail to each of the substantive arguments set forth in Suburban's post-hearing brief. To place those arguments in the proper perspective, however, it is first necessary to briefly review the present environment in the natural gas industry.

A. The Impact of Increased Competition in the Natural Gas Industry

Although Suburban has devoted lengthy portions of its post-hearing brief to a summary of the evidence, the facts in this case are essentially undisputed. Columbia and Suburban are both natural gas distribution companies, providing service to retail customers at various locations within this state. In certain geographic areas, Columbia and Suburban are competitors, and the legal arguments presented by Suburban have focused on

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various rates, charges, and practices affecting competition between the two companies.

The potential ramifications of those arguments, however, go well beyond any questions involving competition between Columbia and Suburban. If adopted, Suburban's arguments could materially alter the basic policies established in the Commission's generic transportation guidelines, and significantly change the manner in which the state's utilities market their products and services. As a result, Suburban's arguments cannot be viewed in isolation; they must be viewed in the broader context of the sweeping changes taking place throughout the natural gas industry, and this Commission's response to those changes.

Since 1978, when Congress deregulated the wellhead price of natural gas, a combination of regulatory changes and market forces has dramatically increased competition in the industry, all the way from the wellhead to the burner tip. As the Federal Energy Regulatory Commission (FERC) put it in Order No. 436, "competition in the natural gas industry today is proliferating." Order No. 436, mimeo, at IV. A. 145, 50 Fed. Reg. 42408, 42453 (October 18, 1985), FERC Stats. & Regs. ¶30,665, 33 FERC ¶61,007. As a result, local gas distribution companies, which were once considered natural monopolies, now face intense competition from alternate fuels, such as electricity and fuel oil; from unregulated gas producers; and, as the record in this case shows, from other natural gas distribution companies.

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The advent of increased competition in a regulated industry has created something of a paradox. At the same time local gas distribution companies are facing increased competition from a variety of sources, they remain subject to stringent price controls and other regulatory restrictions. Those restrictions were developed at a time when the purpose of regulation was to supplant competition, and not to encourage it. They were neither designed for nor intended to be used in a competitive environment, where rapid, flexible response to changing market conditions is essential to economic survival.

This paradox has led both state and federal regulators to rethink traditional regulatory concepts, and to approve new, innovative rates and other arrangements to enable utilities to better cope with increased competition. In Order No. 436, for example, FERC broke with past precedent and authorized "selective discounting" of interstate transportation rates in competitive situations. In PUCO Case No. 85-800-GA-COI, this Commission followed suit, authorizing the use of "downwardly flexible" intrastate transportation rates. Investigation of Gas Transportation, PUCO Case No. 85-800-CA-COI (Entry on Rehearing, August 13, 1986). This Commission has also approved a number of other innovative arrangements, including sales and transportation rates based upon the price of competing alternate fuels, Ohio Gas Co., PUCC Case No. 86-2193-GA-AEC (December 23, 1986); West Ohio Gas Co., PUCO Case No. 87-741-GA-AEC (June 16, 1987); a variety of arrangements whereby incremental gas supplies are earmarked for specific customers, Cincinnati Gas & Electric Co., PUCO Case

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No. 86-743-GA-AEC (August 5, 1986); River Gas Co., PUCO Case Nos. 86-1768-GA-UNC and 86-2050-GA-UNC (January 20, 1987), and pre-granted, or "blanket" approval of various transportation arrangements. See, e.g., Dayton Power & Light Co., PUCO Case No. 84-46-GA-AEC (January 31, 1984); East Ohio Gas Co., PUCO Case No. 87-95-GA-AEC (May 27, 1987).

Each of those innovative rates or other arrangements represented a significant departure from past practice, and each might have been considered unduly discriminatory or otherwise impermissible in earlier years. Nevertheless, in each instance, the Commission obviously concluded that the arrangement was justified by competitive conditions, and that each was reasonable and lawful under the circumstances. The existence of competition cannot, of course, justify a departure from the requirements of the statutes, but it does underscore the need for the Commission to adopt reasonable and flexible interpretations of the statutes which recognize current competitive conditions. As the Commission recently said in considering a similar competitive situation in the telephone industry:

> The evolution of competition in certain segments of the telecommunications industry warrants this Commission exercising its jurisdiction in regulating such segments in a more flexible and streamlined manner than traditional regulation.

Investigation into Regulatory Framework for Telecommunications Services, PUCO Case No. 84-944-TP-COI (April 9, 1985) at 13. In approving the innovative rates and other arrangements described earlier, the Commission has indicated that a similar approach is appropriate for the gas industry. The Commission should continue

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to follow that approach, for only in tnat manner can it enable the state's gas utilities to cope with the demands of a rapidly changing marketplace, while maximizing the benefits of competition for Ohio consumers.

B. Columbia's Basic Marketing Philosophy and its Response to Increased C petition

The record shows that Columbia has responded vigorously to both the threats and opportunities posed by increased competition, fully utilizing the innovative tools approved by the Commission. In doing so, Columbia has been guided by its basic marketing philosophy, which was articulated at the hearing by Columbia Vice President Thomas F. Devers. In essence, that philosophy is to provide a variety of services that meet the energy needs of its customers at prices which are competitive with alternate fuels and competing suppliers of natural gas (Columbia Ex. 1, at 3).

In marketing its product and services, Columbia places its greatest emphasis on the retention of existing loads, because it recognizes that load retention is essential to its overall marketing success and least-cost strategy. This is true because all of Columbia's customers contribute to its fixed costs, and whenever the Company loses an existing customer to a competitor, the fixed cost contribution of that customer is ultimately borne by the remaining customers. For this reason, Columbia is prepared to defend its existing load from any market raider, and believes that through a combination of flex rates and innovative arrangements, it can meet all competition for its existing

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customers (Columbia Ex. 1, at 3).

Although Columbia places its greatest emphasis on load retention, it realizes that its success also depends upon securing new loads. A major marketing strategy of Columbia is increasing throughput each year. As a result, Columbia will aggressively pursue new markets as they develop. It will be a strong competitor, but will compete in a fair and reasonable manner (Columbia Ex. 1, at 3).

It is not, however, Columbia's policy to raid the existing customers of neighboring gas companies (Columbia Ex. 1, at 3). The Company recognizes that the duplication of utility facilities is ordinarily uneconomic and contrary to the best interests of consumers (Id., at 3-4). As a result, Columbia has not attempted to take the existing customers of other utilities, including Suburban, and there is nothing in the record of this case that indicates otherwise (Id.; Tr. 200).

Unfortunately, the same thing cannot be said of some of Columbia's competitors. Suburban, in particular, has been more than willing to duplicate Columbia's facilities in order to raid its existing markets.

The case of Equity Meats, which is located near North Baltimore, provides an excellent example. Suburban began serving Equity Meats in 1985 (Tr. 207). At the time it initiated service, Equity Meats was a customer of Columbia, and Suburban knew that to be the case (Tr. 207-8). In an effort to deny that this constituted market raiding, Suburban claims that the portion of the load solicited by Suburban was burning propane at the time

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(Suburban Brief, at 42). A short time later, however, Equity Meats informed Columbia that it intended to stop taking gas service from Columbia and purchase all of its gas requirements from Suburban (Columbia Ex. 1, at 5). It subsequently provided a sworn affidavit verifying that it had received a competing offer from Suburban for the remainder of its load (Complainant's Ex. 14). Columbia undoubtedly would have lost the load to Suburban, had it not offered Equity Meats a special agency purchase and transportation arrangement (Complainant's Ex. 12; See Section C, infra).

A similar duplication of facilities by Suburban occurred in the case of D. S. Brown Company. Suburban initiated service to D. S. Brown in January 1987 (Tr. 208). D. S. Brown was also a customer of Columbia at the time (Tr. 208). In another effort to deny that it was raiding Columbia's markets, Suburban cites the fact that D. S. Brown was then burning fuel oil instead of natural gas (Suburban Brief, at 42). The fact remains, however, that Columbia had a pipeline connection with the customer; it had an active service at those premises; and Columbia was fully prepared to match any competing offer received by the customer (Tr. 126, 208; Complainant's Ex. 16).

In conjunction with its efforts to serve D. S. Brown, Suburban also sought an ordinance which would have enabled it to serve selected portions of the Village of North Baltimore (See Complainant's Ex. 16). Columbia was, and is, providing natural gas service to the Village and its inhabitants (Complainant's Ex. 11).

Despite Suburban's assertions to the contrary (Suburban Brief, at 41-42), these activities constitute market raiding under any commonly accepted definition of the term. Columbia has not, and will not, stand idly by while competitors duplicate its facilities in order to take its existing customers (Columbia Ex. 2; Tr. 199-200). Columbia strongly defends its existing loads against market raiding, and in doing so, fully utilizes the opportunities afforded by the Commission's transportation guidelines (Columbia Ex. 1, at 3).

C. Columbia's CTAPA Program

One of the cornerstones of Columbia's response to increased competition has been its CTAPA (Competitive Transportation and Agency Purchase Agreement) program. The purpose of this program is to enable Columbia to retain existing loads that would otherwise have been lost, and to acquire new loads that have not previously been served by a gas distribution company (Columbia Ex. 1, at 4). Under this program, Columbia purchases supplemental gas supplies as agent for participating customers, and transports those supplies to the customer's facilities (Id.). The customer pays the cost of the gas (delivered to Columbia's city gate), an agency fee of $.05 per Mcf, and a delivery charge which compensates Columbia for transporting the gas (Id.). Where firm backup service is required, the delivery charge includes a supplemental charge which reflects the cost of providing that service (Id.).

As its name implies, the CTAPA program is used in competitive situations where the load would not otherwise be

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served by Columbia. This includes situations where the customer would utilize an alternate fuel, such as electricity, fuel oil, or propane, as well as instances where the customer would take service from a competing gas distribution company or producer (Id.).

The CTAPA program also provides positive benefits for Columbia's remaining customers, who are not eligible for this service. The non-excise tax portions of the agency fee and supplemental charge are credited to Columbia's gas cost recovery (GCR) rate, thereby lowering the cost of gas to tariff customers, and the CTAPA customers also contribute to Columbia's fixed costs. Without the program, those costs would be borne by the remaining customers. The program has no adverse impact on any customer, because the gas supplies for CTAPA customers are taken from incremental purchases not needed for system supply (Id., at 5).

In addition, the CTAPA program is fully consistent with the basic marketing philosophy articulated by Mr. Devers. It is used to retain existing load and to compete fairly for new markets, but it is neither designed for nor utilized to raid the existing markets of competitors (Id., at 4-5).

The first CTAPA agreement was used to prevent the loss of Equity Meats to Suburban (Id., at 5; Complainant's Ex. 13). Since then, Columbia has entered into several other CTAPA agreements, which have enabled Columbia to retain additional loads that otherwise would have been lost, and to acquire new loads not previously served by a gas utility (Columbia's Ex. 1, at 4). For example, Columbia entered into CTAPA agreements with C & C Fabrication and Dayspring Assembly of God Church, both of which were new customers who otherwise would have taken service from Suburban (Complainant's Ex. 8, 9, and 10; Tr. 118). Columbia has also offered CTAPA agreements -- which Suburban refers to as "12 month, fixed-rate contracts" -- to the tenants of the Woodland Mall, including Elder-Beerman and J. C. Penney Co. (Complainant's Ex. 6, Tr. 138-9, 140-1, 147). Those agreements, like the contracts with C & C Fabrication and the Dayspring Assembly Church of God, were needed to meet competition posed by Suburban (Tr. 138-139).

These agreements have all been approved by the Commission. The agreement with Equity Meats was approved in Case No. 86-1781-GA-AEC. The contract with C & C Fabrication was approved in Case No. 87-504-GA-AEC. In Case No. 87-159-GA-AEC, involving a CTAPA agreement with Madison County Hospital, the Commission issued pre-granted, or "blanket" approval of all similar agreements, thus eliminating the need for further applications. That blanket approval applied to the CTAPA agreement with the Dayspring Assembly of God Church (Columbia Ex. 3), as well as the agreements with Elder-Beerman and J.C. Penney, which had not yet been executed at the time of the hearing.

Suburban has challenged virtually every aspect of the CTAPA program on a variety of grounds. In doing so, however, Suburban carries a particularly heavy burden, because the Commission has already approved each of these agreements, finding their terms to be just and reasonable.

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1. Approval by the Commission

The most dubious argument advanced by Suburban in this proceeding is its contention that Columbia improperly transformed the CTAPA program from one which was "intended" to permit only the retention of existing load to one that also allowed Columbia to obtain new customers in competitive situations. Suburban specifically accuses Columbia of abusing the program and playing "word games" that failed to apprise the Commission that CTAPA agreements would be used for the acquisition of new loads (Suburban Brief, at 28, 44-45). That contention is simply unfounded.

The CTAPA program was designed for all "competitive situations where the load would not otherwise be served by Columbia" (Columbia Ex. 1, at 4; Tr. 165). That language, which clearly encompasses the acquisition of new loads, was specifically used in Columbia's application for blanket approval of the program. (Columbia Ex. 4, at 3; Tr. 170). Suburban claims that Columbia misled the Commission by referring to loads that might otherwise be "lost", but new loads, like existing ones, can be "lost" to a competing supplier. Moreover, any suggestion that Columbia misled the Commission is effectively refuted by the Commission's <u>own description</u> of the CTAPA program, which was set forth in Columbia's last GCR order:

> In this program, COH acts as an agent to purchase and arrange transportation for a pool of gas in a manner similar to the SIAP Program, except that COH agrees to provide the gas at a fixed price for a one-year period and its use is limited to: (1) retain existing loads, (2) reacquire former load, and (3) <u>acquire new load where competition</u>

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> exists from alternate fuel sources and suppliers...(emphasis supplied).

Columbia Gas of Ohio, PUCO Case No. 86-21-GA-GCR (March 3, 1987) at 22. That order, which was issued fourteen days before the Commission granted blanket approval of the CTAPA program in Madison County Hospital, PUCO Case No. 87-159-GA-AEC (March 17, 1987), unequivocally shows that the Commission knew precisely what it was approving, and that it authorized the use of CTAPA agreements to acquire new loads.

2. Adherence to Tariffs

Suburban next suggests that the implementation of the CTAPA program violated R.C. §§4905.30 and 4905.32, which generally require that utilities file tariff schedules with the Commission and adhere to the rates, terms, and conditions set forth in those tariffs. That argument apparently overlooks the fact that CTAPA customers are not served under a tariff; they are served under special contracts which are filed and approved under R.C. §4905.31. That section creates a specific exception to the general requirements of R.C. §4905.30 and 4905.32; it expressly allows utilities to provide service under "reasonable arrangements" that deviate from the utility's tariffs, subject, of course, to Commission approval. Although Suburban repeatedly implies that there is something wrong with using special contracts to serve small-volume customers who would otherwise be served under the general service tariff (Suburban Brief, at 11, 43), neither R.C. §4905.31 nor the decisions of this Commission provide any basis for such a limitation. Such arrangements are clearly permissible, provided that they establish a classification of service based upon any "reasonable consideration." R.C. §4905.31(D). In approving the CTAPA agreements, the Commission has clearly found that they are based upon reasonable considerations.

The crux of Suburban's complaint on this issue is that Columbia has, on occasion, billed customers under CTAPA agreements, pending formal approval by the Commission (Suburban Brief, at 30-32). This occurs in competitive situations (Tr. 153-54), and simply recognizes the realities of the marketplace. CTAPA customers, by definition, are those who would otherwise take service from a competing supplier (Columbia Ex. 1, at 4). In such situations, rapid response is absolutely essential. If Columbia had been required to wait for formal Commission approval prior to offering the CTAPA rate, it undoubtedly would have lost each of the customers in question. It would make no sense whatsoever for the Commission to provide innovative arrangements that enable utilities to cope with increased competition, only to impose procedural requirements that effectively nullify those arrangements.

Nor do the relevant statutory provisions dictate such a result. There is nothing in R.C. §4905.31 that prohibits a utility from temporarily offering service under a special arrangement, pending Commission approval. This is particularly true where, as here, the arrangements in question were fully consistent with the Commission's transportation guidelines enunciated in PUCO Case No. 85-800-GA-COI. In fact, the statute

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imposes no time limits for filing. Should the Commission ultimately disapprove any of these contracts, the customer would obviously be liable for the full tariff rate, and its billings would be subject to adjustment. In the meantime, however, "the only penalty imposed for failing to file such contracts with the Commission is that the contracts shall not be lawful," Cookson Pottery Co. v. Public Utilities Commission, 161 Ohio St. 498, 505, 120 N.E.2d 98, 102 (1954) (emphasis supplied), and the only consequence of that is that the contracts are not enforceable in a court of law. See, Lake Erie Power & Light Co. v. Telling-Belle Vernon Co., 57 Ohio App. 457, 14 N.E.2d 947 (1937). There is no basis, either in R.C. §4905.31 or elsewhere, for imposing any further penalties, sanctions, or adverse findings. See Cookson, 161 Ohio St. at 505-6, 120 N.E.2d at 102-3.

This issue, moreover, is clearly moot, because all applicable requirements of R.C. §4905.31 have clearly been satisfied. That statute requires only two things: special contracts must be "filed with" and "approved by" the Commission. In the case of each CTAPA agreement at issue in this proceeding -- Equity Meats, C & C Fabrication, and Dayspring Assembly of God Church -- the contract has been filed with and approved by the Commission. Once approved by the Commission, such agreements are valid ab initio. Suburban's argument is accordingly without merit and should therefore be rejected.

3. Discrimination

Suburban further claims that the CTAPA program is unlawfully discriminatory, and therefore violates R.C. §§4905.32, 4905.33, and 4905.35, because it is available only to selected customers. That argument is flawed for several reasons.

To begin with, CTAPA customers are served under special contracts, not under Columbia's tariffs (See Section 2, supra), and the statutory prohibitions on discrimination do not apply to special contracts. As the Supreme Court said in Cookson Pottery v. Public Utilities Commission, 161 Ohio St. 498, 120 N.E.2d 98 (1954) (where the utility had originally provided all of its service under special contracts):

> The filing of such contracts with and their approval by the commission did not obligate the utility to serve customers other than those with which it had contracts, but when the utility filed a schedule of rates [i.e., a tariff] subject to the approval of the commission, the utility thereby, for the first time, became obligated to serve without discrimination all applicants within its area with its type of service at the rates fixed by the schedule.

161 Ohio St. at 506, 120 N.E.2d at 103. Since Columbia has not held itself out to provide CTAPA service under a tariff or schedule that applies to all customers (Tr. 162), it has no legal obligation to provide such service to customers other than those with whom it has CTAPA agreements.

Assuming, however, arguendo, that the statutes in question apply to special contracts, the CTAPA program would not constitute unlawful discrimination. Any classifications or differences in treatment resulting from the program are clearly permissible under the applicable provisions of Ohio law.

It is well established that the law does not prohibit all discrimination by public utilities. R.C. §4905.35 forbids only "undue" or "unreasonable" preferences or advantages, while R.C. §4905.33 prohibits only receiving a greater or lesser compensation for providing a "like and contemporaneous service under substantially the same circumstances and conditions." R. C. §4905.32 contains a similar provision, which bars utilities from granting refunds, privileges, or facilities, except as they are uniformly extended to all customers "under like circumstances for like or substantially similar, service."

The general rule in this regard was set forth in <u>Buckeye Lake Chamber of Commerce v. Public utilities Commission</u>, 161 Ohio St. 306, 119 N.E.2d 51 (1954):

> ...[A] utility may, without being guilty of unlawful discrimination, classify its customers on any reasonable basis and make separate rates for each class.

161 Ohio St. at 311, 119 N.E.2d at 54. In <u>F. & R. Lazarus Co. v. Public Utilities Commission</u>, 162 Ohio St. 223, 122 N.E.2d 783 (1954), the Court added that:

> ...[N]ot all discrimination in rates is unjust. In order to constitute an unjust discrimination, there must be a difference in rates under substantially similar conditions as to service, and it is not an undue preference to make to one patron a rate lower than that made to another, where there exist differences in conditions affecting the expense or difficulty of performing the service which fairly justify a difference in rates.

162 Ohio St. at 230, 122 N.E.2d at 786. In other words, the Ohio utility laws require similar treatment only where the customers are similarly situated.

Although the Court's language in F. & R. Lazarus Co. might have implied that classifications or rate differentials are permissible only when based on differences in the underlying cost of service, subsequent decisions have shown that this is clearly not the case. The Court has repeatedly upheld classifications based upon factors other than costs. In American District Telegraph Co. of Cincinnati v. Public Utilities Commission, 40 Ohio St. 2d 83, 320 N.E.2d 664 (1974), for example, the Court upheld the use of "banded" telephone rates, in which rate differentials are based upon the value of service, and not the cost of providing it. In County Commissioners Association v. Public Utilities Commission, 63 Ohio St. 2d 243, 407 N.E.2d 534 (1980), the Court upheld a rate classification that recognized the unique status and financial plight of public schools. And in City of Cleveland v. Public Utilities Commission, 63 Ohio St. 2d 62, 406 N.E.2d 1370 (1980), the Court upheld an energy conservation rate, which was available only to customers whose homes met certain insulation and other energy conservation standards. In rejecting the contention that the energy conservation rate violated R.C. §§4905.33 and 4905.35, the Court reiterated and expanded upon the principle enunciated in F. & R. Lazarus Co.:

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> Obviously, not all rate differentiations are unlawful... R.C. §4905.31(D) authorizes "[a] classification of service based upon the quantity used, the time when used, the purpose for which used, the duration of use, and <u>any other reasonable consideration</u>." (emphasis in original).

63 Ohio St. 2d at 67-68, 406 N.E.2d at 1376.

A classification based on competitive conditions is clearly reasonable. For that reason, state regulatory agencies have repeatedly held that a utility may, without being guilty of undue discrimination, charge different rates in specific areas, or to particular customers, where such rates are necessary to meet competition from alternate suppliers. <u>Pacific Gas & Electric Co.</u>, 22 P.U.R. 3d 209 (Cal. P.U.C. 1958); <u>Michigan Gas Utilities Co.</u>, 57 P.U.R. 4th 699 (Mich. P.S.C. 1984); <u>Pacific Power & Light Co.</u>, 80 P.U.R. N.S. 1 (Ore. P.U.C. 1949). In the <u>Pacific Power</u> and <u>Pacific Gas & Electric</u> cases, the California and Oregon Commissions allowed electric utilities to charge lower rates in specific geographic areas where they faced competition from other electric companies. In <u>Michigan Gas Utilities</u>, the Michigan Commission approved a discounted rate for customers who had the capability to use oil or other alternate fuels, in order to prevent the loss of those loads. In doing so, the Commission specifically rejected the argument that the discounted rate was discriminatory because the ability to utilize alternate fuels was not related to the cost of providing service:

> A review of court decisions from other jurisdictions supports the principle that rate discrimination is illegal only when it is not based on a difference in cost of service or other rational basis. [Citations omitted]. A distinction between customers

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> that can burn only natural gas and customers that can readily switch to alternative fuels is not an irrational distinction. The distinction is particularly justified when the purpose is to retain industrial load to reduce the burden upon ratepayers who cannot readily switch.

57 P.U.R. 4th at 704. In Pacific Power & Light Co., the Oregon Commissioner articulated the basic rationale for permitting a utility to charge different rates in competitive situations:

> ...[T]he existence of competition at one point and not at another has, in itself, been deemed to destroy that similarity of circumstances and conditions without which such discrimination would not exist.

80 P.U.R. N.S. at 3. In other words, a utility may charge different rates or provide different services in competitive situations, because customers who are vulnerable to competition are not similarly situated, and do not receive service under substantially the same circumstances and conditions, as the utility's remaining, or "captive" customers.

The FERC recognized these principles in Order No. 436, where it authorized "selective discounting" of interstate transportation rates. The stated purpose of selective discounting was to permit "differences in prices because of business factors, such as competitive circumstances." Order No. 436, mimeo, at IV. A. 150, 50 Fed. Reg. at 42454. Expanding upon that purpose, FERC explained that:

> [C]ompetition in the natural gas industry today is proliferating. In these circumstances, it makes little sense to withhold from pipelines the basic weapon other businesses have to wage the competitive battle: the ability to lower prices to beat the competition.

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<u>Id</u>., at IV. A. 145-46, 50 Fed. Reg. at 42453. In fact, selective discounting was intended for use in precisely the same circumstances in which Columbia uses its CTAPA agreements. FERC indicated that it was confident that:

> ...pipelines will always seek to charge the ceiling [transportation] rate in order to maximize profit and will only discount when necessary <u>to make a sale that would not otherwise be made</u> (emphasis supplied).

<u>Id</u>. at IV. A. 140, 50 Fed. Reg. at 42452.

Since selective discounts, by definition, were to be available only to particular entities, various parties argued that they were unduly discriminatory, and constituted <u>per se</u> violations of Section 4(b) of the Natural Gas Act (15 U.S.C. §717c(b)). That section prohibits any "undue preference or advantage" or any "unreasonable differences" in rates or services. After considering those arguments at length, FERC rejected them, finding that selective discounts were not <u>per se</u> unduly discriminatory, assuming that the same discounts were provided to customers who were similarly situated. A key factor in that decision was the fact that the Commission had imposed conditions assuring that selective discounting would have no adverse impact on the remaining customers who were not eligible for the discounts.

The same arguments were raised on appeal, and the Court of Appeals likewise rejected the claim that selective discounts, in and of themselves, were unduly discriminatory. <u>Associated Gas Distributors v. FERC</u>, No. 85-1811 (D. C. Cir. June 23, 1987). The Court began by noting that " 'the mere fact of a rate

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disparity' is not enough to constitute unlawful discrimination." Id., slip op. at 50. It then considered and rejected the specific argument that discounts in competitive situations, which are inherently based on "value of service" considerations, are unlawfully discriminatory:

> The judicial acceptance of such price differentials is longstanding. For nearly 100 years, for example, the courts have interpreted the anti-discrimination provisions of the Interstate Commerce Act to allow the ICC to approve differentials justified exclusively by competition.

Id., slip op. at 55. The Court went on to reject the remaining challenges to selective discounting.

In its generic transportation guidelines issued in Investigation of Gas Transportation, PUCO Case No. 85-800-GA-COI (Entry on Rehearing, August 13, 1986), this Commission adopted an approach similar to that taken by FERC in Order No. 436. It specifically authorized selective discounting in the form of "downwardly flexible" intrastate transportation rates. Those rates were obviously intended for use in competitive situations. It was pursuant to those guidelines that the CTAPA agreements were approved. In expressly authorizing the use of such rates, the Commission implicitly found that they are not, in and of themselves, unduly discriminatory in violation of either R.C. §4905.33 or §4905.35.

Taken together, the foregoing judicial and regulatory authorities firmly establish that a utility rate, charge, or program is not unlawfully discriminatory merely because it is available only in competitive situations. This is particularly

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true where the program has no adverse impact upon the remaining customers to whom it is not available. For those reasons, Columbia's CTAPA program, which benefits all of Columbia's customers, is not unlawfully discriminatory, and does not violate R.C. §§4905.32, 4905.33, or 4905.35, merely because it is available only in competitive situations where the load would not otherwise be served.

In response, Suburban will undoubtedly contend that Columbia's arguments on this issue are invalid in situations where a company has attempted to beat, rather than meet, its competitor's prices. It is true, of course, that the CTAPA rates are lower than Suburban's tariff rates, but that does not vitiate Columbia's arguments on this issue. In the first place, rates designed to beat competition are not necessarily discriminatory in the regulatory context. In Order No. 436, for example, FERC made it clear that selective discounts could be used to beat competition. Order No. 436, mimeo, at IV. A. 145-46, 50 Fed. Reg. at 42453. Furthermore, even though the CTAPA rates are lower, they already reflect the full cost to Columbia of providing the service (Columbia Ex. 1, at 6). Even if Columbia deemed it appropriate to charge higher rates, the Commission's transportation guidelines, as currently written, do not permit flexing above the full-margin transportation rate. Investigation of Gas Transportation, PUCO Case No. 85-800-GA-COI (Entry on Rehearing, August 13, 1986). Under these circumstances, the CTAPA rates cannot be considered unduly discriminatory simply because they are somewhat lower than Suburban's tariff rates.

In addition to its general attack on Columbia's CTAPA agreements, Suburban also accuses Columbia of specific instances of discrimination in the implementation of the program. In particular, it faults Columbia for offering a CTAPA agreement to Dayspring Assembly of God Church, while not offering a similar agreement to the Bowling Green Church of God, and claims that Columbia has failed to explain why Dayspring Assembly is the only church in the area which enjoys the CTAPA rate (Suburban Brief, at 20-21, 36, 40).

The explanation is obvious from the record. To begin with, the CTAPA program had not yet been developed when Columbia initiated service to the Bowling Green Church of God (Tr. 94). The failure to offer a nonexistent program to a prospective customer can hardly be considered undue discrimination. Furthermore, the Bowling Green Church of God did not fall within the class of customers who are eligible for CTAPA agreements. That program, at the risk of being repetitive, is available only in "situations where the load would not otherwise be served by Columbia" (Columbia Ex. 1, at 4). This particular customer agreed to pay the applicable regional rate and take service from Columbia even in the absence of a CTAPA agreement (Tr. 94). There is nothing in either R.C. §4905.33 or §4905.35 that requires Columbia to offer a special arrangement, which was specifically designed to meet competition, in a situation where it is clearly not required for that purpose.

Dayspring Assembly of God, on the other hand, had received a competing offer from Suburban, which it was fully prepared to accept (See Complainant's Ex. 10). It was offered a CTAPA agreement for precisely the same reason that other customers have been offered such agreements: the load would not otherwise have been served by Columbia (Columbia Ex. 1, at 4). It is presently the only church in the area which enjoys that rate because there are no other churches who would otherwise take service from a competitor (Tr. 136). If there were such churches, they would also be offered CTAPA agreements (Tr. 137).

Suburban also criticizes Columbia because the CTAPA rate can be increased or decreased under the agreements with C & C Fabrication and Dayspring Assembly Church of God, whereas the rate in the Equity Meats contract can only be decreased (Suburban Brief, at 40). Once again, the reason is obvious: Equity Meats declined to sign the contract without the indicated change. Such minor variations are bound to occur in competitive situations, and they can hardly be considered undue discrimination. Indeed, the need to accommodate such variations is one of the principal reasons CTAPA customers are served under special contracts rather than a tariff. Even if the variation cited by Suburban were deemed significant, it would be fully justified by the fact that Equity Meats was an existing customer which Columbia was trying to retain (Columbia Ex. 1, at 5), whereas C & C Fabrication and Dayspring Assembly of God were new customers, which had not previously been served by a gas utility (Tr. 118), and which made no such demand.

In short, there is no basis, either in the record or the applicable case law, for concluding that the CTAPA program is unduly or unlawfully discriminatory. Neither the program in general, nor its application in specific cases, has violated the prohibitions on undue discrimination set forth in R. C. §§4905.32, 4905.33, and 4905.35. Suburban's arguments on this point are without merit and should be rejected.

4. Furnishing Service for Less Than Actual Cost

Suburban further contends that the entire CTAPA program should be re-evaluated and discontinued because it violates the prohibition, set forth in R.C. §4905.33 (cited by Suburban as R.C. §4905.35), against furnishing service for less than actual cost for the purpose of destroying competition. That contention is flatly contradicted by the record.

According to Mr. Devers, who was the only rate expert to testify on the subject, the CTAPA rates are based on the full cost of service, including the full-margin general service transportation rate (Columbia Ex. 1, at 5; Tr. 185). He stated unequivocally that the CTAPA program does not involve the provision of service for less than actual cost (Columbia Ex. 1, at 6), and there is nothing in the record that refutes that testimony.

In an apparent effort to do so, Suburban implies that the CTAPA rate is understated because it does not include the state excise tax on the cost of gas (Suburban Brief, at 26). That argument is nothing more than a red herring. The Commission has always excluded that portion of the excise tax from Columbia's transportation rates (Tr. 184-85), for the obvious reason that the excise tax does not apply to transportation volumes owned by an end-user. That is true whether the volumes are acquired directly by the end-user, or, as in the the case of CTAPA, by the utility as agent for the customer (Tr. 182). Moreover, even if the excise tax were applied to CTAPA volumes, Columbia would still not be furnishing service for less than actual cost, because the CTAPA agreements specifically require the <u>customer</u> to reimburse Columbia for any such tax liability (Complainant's Ex. 8 and 10, ¶5 of the Agreements; Complainant's Ex. 13, ¶6 of the Agreement).

Suburban's real complaint regarding this issue is premised upon what <u>might</u> happen if Columbia exercised its right under the contracts to flex its CTAPA rates downward in order to retain the loads (<u>See</u> Suburban Brief, at 46-47). That argument is both speculative and premature, since there is no suggestion in the record that Columbia has flexed its transportation rates downward for any of the CTAPA customers involved in this case. Those customers are paying the full cost of service, including full-margin transportation rates. As a result, this issue is not ripe for decision, and there is no need to decide it in the context of this proceeding.

If, however, the Commission deems it appropriate to do so, Columbia submits that the CTAPA rates would not violate R.C. §4905.33, even if competition required flexing those rates downward. Suburban apparently assumes that the term "actual cost" in that section refers to average, or fully distributed costs. This is clearly not the case. When a firm sells its product for less than cost for the purpose of destroying competition, it is engaging in predatory pricing, Sunshine Books v. Temple University, 697 F.2d 90, 92 (3rd Cir. 1982), and the obvious purpose of R.C. §4905.33 is to prohibit predatory pricing by regulated utilities, just as the antitrust laws prohibit predatory pricing by unregulated firms. There is considerable disagreement over precisely what constitutes predatory pricing, but the principal economic test, both for antitrust and regulatory purposes, is whether the firm is selling below its marginal, or variable, cost, and not whether it is selling below its average costs. Northeastern Telephone Co. v. American Telephone & Telegraph Co., 651 F.2d 76, 88-91 (2d Cir. 1981), cert. denied, 455 U. S. 943 (1982); FERC Order No. 436, mimeo, at IV. A. 138; 50 Fed Reg. at 42452. As a result, the meaning of "actual cost" for purposes of R.C. §4905.33 is clearly the marginal, or variable, cost. This is particularly true in the case of a program like CTAPA, which involves incremental loads that would not be served by Columbia in the absence of the program (Columbia Ex. 1, at 5-6). The Commission recognized this in Case No. 85-800-GA-COI, when it authorized the use of transportation rates that are "downwardly flexible" from the tariff or contract rates, which are ordinarily based on the utility's average costs. If R.C. §4905.33 prohibited charging less than average costs in competitive situations, the Commission could not have approved the use of downwardly flexible rates.

The testimony of Mr. Devers specifically indicated that even if it became necessary to flex the transportation rates downward in order to retain the loads, Columbia would not charge

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less than a "floor rate" which included the cost of gas, the agency fee, and an amount sufficient to cover the variable costs of providing the service (Columbia Ex. 1, at 6; Tr. 185-86). As a result, there is simply no basis in the record for concluding that Columbia has, or will, furnish service to CTAPA customers for less than the actual cost of providing it. Nor is there any basis for finding that any flexing that might be necessary to retain existing CTAPA customers would be done for the purpose of destroying, rather than meeting, competition from alternate suppliers. On the contrary, the record establishes just the opposite (Columbia Ex. 1, at 4, 6; Columbia Ex. 2). For those reasons, Suburban's argument that the CTAPA program violates the predatory pricing provisions of R.C. §4905.33 is simply unfounded.

5. <u>Restructuring of Competitive Programs</u>

In its final argument related to CTAPA, Suburban argues that "special marketing programs," as it calls them, should be confined to competition from unregulated suppliers and other "special situations" (Suburban Brief, at 47-49). These special situations, according to Suburban, should include only instances where competition would have a "serious adverse effect on either a utility or its remaining customers" (<u>Id.</u>, at 49). This is far more than an attack on Columbia's CTAPA program; it is a request for a fundamental restructuring of the Commission's generic transportation guidelines and its basic policies concerning competition. Columbia does not believe that such a restructuring

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is warranted, and even it it were, this case is clearly not the proper vehicle to accomplish it.

The Commission's transportation guidelines have a direct and substantial impact on all segments of the Ohio gas industry, as well as the consuming public. For that reason, they were adopted only after extensive public input, including comments by gas utilities, end-users, and producers. In view of the potential impact, it would be inappropriate to make significant changes in the guidelines, particularly changes as sweeping as those proposed by Suburban, without affording all affected parties the opportunity to be heard. From a practical standpoint, this clearly cannot be done in the context of this case.

Even if it were appropriate to make such changes in an individual complaint case, Suburban's proposed changes are not justified by record in this case, because they are based on underlying assertions or premises that are unsupported -- and in some cases contradicted -- by the evidence presented at the hearing.

The first of these premises is the implication that Columbia should not be permitted to use special transportation arrangements to compete with Suburban, because Suburban "is operating more efficiently than [Columbia], as evidenced by its lower tariff rates" (Suburban Brief, at 48). This is sheer nonsense. A regulated gas utility's rates are affected by a variety of factors, including the number of customers it serves, the load factors and geographic locations of those customers, the

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age and condition of its physical plant, its expenditures on maintenance and pipeline safety, the timing of rate cases, the operation of the gas cost recovery mechanism, the number of PIP customers it serves, and a host of other items. A snapshot comparison of two utilities' tariff rates says little or nothing about their relative efficiencies or the quality of service they provide to their customers.

The second unsupported assertion is Suburban's claim that permitting Columbia to respond to competition selectively, using CTAPA, rather than systematically, by lowering all of its rates, will frustrate the purpose of competition and deny Columbia's customers, as a whole, the benefits of competition with Suburban (Suburban Brief, at 48). That contention mirrors the arguments of those who urged FERC to prohibit selective discounting and require that all discounts be provided on a uniform basis. After careful consideration, FERC rejected those arguments, finding that selective discounting would provide "greater social and economic gains" than price uniformity. Order No. 436, mimeo, at IV. A. 143, 50 Fed. Reg. at 42453. The reasons for that conclusion were summarized in the Court of Appeals opinion:

> [FERC] saw substantial benefits from such discounts: cheaper fuel supplies for the price-elastic customers receiving the discounts; reduced revenue shortfalls for pipelines that would otherwise lose the business altogether; and protection for non-favored customers from rate increases that would otherwise occur if pipelines lost volume through inability to respond to competition.

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Associated Gas Distributors v. FERC, No. 85-1811 (D.C. Cir., June 23, 1987), slip op. at 53. FERC recognized that these benefits would seldom be achieved if discounting were permitted only on a uniform basis. Unless the pipeline was facing a severe loss of throughput, the high cost of uniform discounting would ordinarily lead it to forego such discounts, and the price-elastic customers, as well as their potential revenue contribution, would be lost, with the result of higher rates to all of its customers. As a result, FERC found that "[t]he captive customer will gain less from required uniform discounting than when selective discounting is possible." Order No. 436, mimeo, at IV. A. 144, 50 Fed. Reg. at 42453. This Commission obviously came to the same conclusion in Case No. 85-800-GA-COI, where it authorized selective discounting in the form of downwardly flexible intrastate transportation rates.

The same considerations are present here. Despite Suburban's assertions to the contrary, the CTAPA program provides all of the benefits cited by FERC in Order No. 436. It provides cheaper fuel supplies for the "price-elastic customers" -- i.e., the CTAPA customers who would otherwise not be served by Columbia. It also reduces the revenue shortfall to Columbia that would otherwise occur if the loads were lost to competitors, thereby protecting the captive customers from rate increases that would be necessary if CTAPA customers were not contributing to Columbia's fixed costs (See Columbia Ex. 1, at 5). This, contrary to Suburban's claims, clearly enables the captive customers to share in the benefits of competition. Furthermore,

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the CTAPA program, unlike selective discounting, provides an additional benefit to the captive customers: the non-excise tax portions of the agency fee and supplemental charge are credited to Columbia's GCR, thereby lowering the cost of gas to captive customers. Those credits further enhance the benefits of competition for those customers.

Suburban further suggests that the CTAPA program may increase rates in the long run, because it will destroy competition, and because the "costs associated with such competitive pricing" must be recovered from the remaining customers if Columbia is to remain in business (Suburban Brief, at 48). That contention ignores the fact that there are no such "costs" which are not currently being recovered from the CTAPA customers, since the CTAPA rates presently reflect the full cost of that service (Columbia Ex. 1, at 5). If it ever became necessary to flex those rates downward, and if Columbia subsequently sought to recover the lost revenues in a rate case, there would be ample opportunity at that time to consider the reasonableness of the proposal. Furthermore, there has been no showing that CTAPA will destroy competition. On the contrary, the record is replete with evidence indicating that Columbia continues to face intense competition, from alternate fuels as well as Suburban (See, e.g., Complainant's Ex. 16).

Finally, Suburban suggests that transportation programs such as CTAPA should be used only to compete with unregulated competitors, or in situations where competition would have a "serious adverse effect" on the utility or its remaining

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customers. (Suburban Brief, at 49). Although such an arbitrary limitation would obviously benefit Suburban by insulating it from competition from Columbia, there is nothing in either the Commission's transportation guidelines or the record in this case which justifies such a change.

For those reasons, Columbia submits that Suburban's proposed changes should be rejected, and the CTAPA program, which benefits all of Columbia's customers, should not be modified as a result of this proceeding.

D. Columbia's Line Extension Policies

Suburban has also raised various questions concerning Columbia's line extension policies. Those questions have focused upon the circumstances under which the Company will extend its distribution mains to serve new industrial or commercial customers without requiring a line extension deposit. The Company's policies in that regard were described in detail by Mr. Devers.

1. Columbia's Existing Practices and Tariff Provisions

In deciding whether to extend its distribution mains at Company expense, Columbia begins with a cost-benefit analysis of the proposed project. This is done by calculating a "maximum allowable investment," based on the prospective customer's projected consumption, in order to determine the level of investment that can be supported by the anticipated revenues (Columbia's Ex. 1, at 6; Tr. 192). If the projected consumption shows that the required investment is economically justified, Columbia will extend its mains without requiring a deposit

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(Columbia Ex. 1, at 6).

If the customer's projected consumption does not, in and of itself, justify the required extension, Columbia then examines other factors, such as potential load growth from other customers who might be served from the main extension, as well as competition from alternate energy suppliers, to determine whether the extension is economically justified at Company expense (Id., at 6-7). These determinations, which are based on the Company's sound business judgment, are made on a case-by-case basis (Id., at 6). If Columbia determines that the project is economically justified, it proceeds to extend its mains (Id., at 7). If not, the prospective customer must enter into a line extension agreement and deposit all or part of the cost of the proposed extension with Columbia (Id.).

This policy is just and reasonable because it fairly balances the interests of the Company and both its existing and prospective customers (Columbia Ex. 1, at 7). On the one hand, the Company should not be forced to make uneconomic extensions of its mains, unless the prospective customer is willing to deposit the cost of the extension. On the other hand, it would be unfair to force the prospective customer to deposit the full cost of a necessary line extension where all or part of the required investment is justified at Company expense (Id.). Columbia's policy satisfies both of those concerns.

Suburban claims that Columbia has violated Section 34 of its Rules and Regulations, and has therefore violated R.C. §4905.30 and 4905.32, by failing to require line extension deposits from C & C Fabrication, the Woodland Mall, and other unnamed customers, as "required" by its tariff (Suburban Brief, at 34). Although Suburban has glossed over the underlying legal issue, that argument presupposes that the tariff "requires" Columbia to collect a deposit equal to the full cost of every main extension used to serve commercial or industrial customers. Neither Columbia nor the Commission has ever interpreted the line extension tariff in that manner, and Columbia submits that this interpretation is clearly erroneous.

In support of its position that deposits are always required, Suburban cites certain testimony of Mr. Parshall (Tr. 44-45, 60). Columbia objected to that line of questioning at the hearing (Tr. 41-42), and submits that this testimony is inadmissible and should be stricken from the record. The construction of a utility tariff presents a question of law, Saalfield Publishing Co. v. Public Utilities Commission, 149 Ohio St. 113, 77 N.E.2d 914 (1948), and despite Mr. Parshall's extensive knowledge and experience in the gas industry, he was not qualified to offer legal conclusions.

The meaning and effect of a utility tariff must be ascertained, not from the testimony of witnesses, but from "the language employed, the connection in which used, and the evident purpose of such provisions." Saalfield Publishing Co., paragraph one of the syllabus. Suburban's interpretation of Columbia's line extension tariff effectively disregards all three of those factors.

The language employed in Section 34 of the Rules and

Regulations reads as follows:

> Where a main extension is <u>requested</u> for commercial or industrial purposes and such main extension is determined by the Company to be economically feasible, the applicant or applicants <u>may</u> enter into a line extension agreement and shall deposit with the Company the estimated cost of such extension (emphasis supplied).

That language contrasts sharply with the language of the preceding paragraph, which states that:

> Where a main extension is <u>necessary</u> to provide service availability to plots of lots or real estate subdivisions and such main extension is not deemed justified at the Company's expense, the owners or promoters of such plots of lots or real estate subdivisions <u>shall</u> enter into a line extension agreement and shall deposit with the Company the estimated cost of such extension (emphasis supplied).

In other words, the section involving extensions for commercial or industrial purposes does not apply in all situations where such an extension is <u>necessary</u>; it applies only where the extension is <u>requested</u> by the customer. The only instance in which it is necessary for a customer to "request" a line extension for purposes of that tariff is where the Company is unwilling to make the extension without a deposit, because the cost is not deemed justified at Company expense. In that case, the tariff gives the customer an option. If it chooses to do so, it "may" enter into a line extension agreement and assure that the main is extended by depositing the estimated cost of the extension with the Company. The tariff language has no application, however, where the Company decides to extend the main at its own expense because the cost of doing so is economically justified. That point is demonstrated by both the "language employed" in the tariff and the "connection in which [it is] used." Saalfield Publishing Co., paragraph one of the syllabus.

That conclusion is bolstered by an examination of the "evident purpose" of the line extension tariff. That purpose, according to the Commission, is "to avoid burdening existing customers with costs for lines which might not be economically justified..." Durieux v. Columbia Gas of Ohio, PUCO Case No. 77-323-GA-CSS (May 11, 1979), at 4. The line extension tariffs serve no evident purpose, and should not be deemed applicable, in instances where the cost of the line is economically justified, and the line is therefore constructed at the Company's expense.

In addition, a utility's tariffs should be interpreted in light of the statutory scheme for regulating public utilities. See, Norman v. Public Utilities Commission, 62 Ohio St. 2d 345, 406 N.E.2d 492 (1980). Two aspects of that scheme militate against the tariff interpretation advanced by Suburban. First, as Suburban has repeatedly noted, the statutes prohibit undue or unreasonable discrimination by utilities. Columbia's line extension tariff clearly permits it to extend its mains to new residential subdivisions where the expenditure is deemed justified at Company expense. If the tariff were interpreted to deny Columbia the opportunity to extend it mains to new commercial or industrial customers under the same circumstances, it might well be deemed unduly discriminatory.

Second, the statutes allow the Commission to regulate, but not manage, utilities. Elyria Telephone Co. v. Public

Utilities Commission, 158 Ohio St. 441, 448, 110 N.E.2d 59, 63 (1953). Decisions concerning the proper level of investment in new facilities, such as distribution mains, are better left to a utility's management, subject to review by the Commission in subsequent rate proceedings.

In the case of C & C Fabrication, the calculation of the maximum allowable investment showed that C & C's projected load, in and of itself, justified the cost of the extension (Tr. 204). In the case of the Woodland Mall, it was necessary to consider other factors, such as potential growth in the area and the existence of competition from alternate energy suppliers (Columbia Ex. 1, at 6; Tr. 187). In both cases, however, the extensions were deemed justified at Company expense.

2. Suburban's Line Extension Policies

The most anomalous aspect of this argument is that Suburban's conduct, as opposed to its rhetoric, shows that it doesn't even believe its own argument. This is one instance in which a party's actions truly speak louder than its words.

Suburban's line extension tariff was patterned after Columbia's, and Mr. Rothey conceded that the two tariffs are "substantially similar" (Tr. 211). In fact, the relevant language concerning extensions for commercial and industrial purposes is absolutely identical (Compare Complainant's Ex. 4, Section 34, with Columbia Ex. 5, Section 12).

Yet despite Suburban's insistence that the tariff language requires Columbia to collect a deposit before extending its mains, Suburban has clearly offered to extend its own mains

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without a deposit. For example, when Suburban [illegible]peting with Columbia to serve the Wood County Children's Resour e Center (Tr. 55-58), Suburban offered to extend its mains by more than 100 feet without asking for a deposit (Tr. 212).

In deciding whether to extend its mains without a deposit, Suburban, like Columbia, begins with a cost benefit analysis to determine whether the projected load justifies the proposed main extension (Tr. 212-13). It also considers potential growth from additional loads that might be served from the extension (Tr. 213). That was one of the factors it considered in offering to extend its mains to the Children's Resource Center (Id). In short, Suburban considers essentially the same factors, and follows essentially the same policies, as Columbia does in administering its own main extension program.

This is not to say that Columbia may violate its tariffs simply because Suburban has done so. The point is only that Suburban cannot have it both ways. Suburban has obviously adopted two different interpretations of the same tariff: one for purposes of its arguments in this case, and the other for purposes of its own operations. It has undoubtedly chosen the correct interpretation in its day-to-day operations, and that interpretation should be adopted by the Commission for purposes of this proceeding.

3. Impact of Suburban's Interpretation

This argument is particularly troubling because it, like so many of Suburban's arguments, has ramifications that go well beyond the parameters of this case. If adopted, Suburban's

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argument would require Columbia to collect a deposit equal to the full cost of every main extension needed to serve a new commercial or industrial customer. It would significantly and unnecessarily increase the cost of obtaining gas service for every new automobile factory, steel mill, shopping mall, gasoline station, or corner store that is not located on an existing distribution line. That is unquestionably the wrong approach to take at a time when the state is actively fostering economic development by seeking new business and industry (See Columbia Ex. 1, at 7).

Nor is there any need to adopt such an approach. As the foregoing discussion demonstrates, Columbia's existing line extension policies are fair, reasonable, and fully consistent with the applicable tariff language. For those reasons, Suburban's arguments on this point are without merit and should be rejected by the Commission.

E. Columbia's Marketing Incentives

Another important aspect of Columbia's response to competition has been the offering of certain marketing incentives. In order to attract new load, Columbia has sometimes installed customer service lines (or house piping, which consists of the piping between the meter and the appliances), or reimbursed the customer for the expenses of such lines or piping (Columbia Ex. 1, at 7). It has also agreed to reimburse customers for certain equipment costs (Tr. 138), and in one isolated case, it waived its regulator fee (Tr. 22-23). These incentives, like the CTAPA program, are used only in situations where the Company's best judgment indicates that the load would not otherwise be served by Columbia (Columbia Ex. 12, at 7). Functionally, they are no different than heat pump rebates, free installation of custom calling services, or other incentives offered by other public utilities.

The benefits of these incentives are obvious. By attracting new loads, these incentives, like the CTAPA program, produce increased contributions to fixed costs which benefit all of Columbia's customers. Furthermore, the costs of these incentives are fully absorbed by Columbia shareholders, and are not passed on to Columbia's customers (Columbia Ex. 1, at 7; Tr. 153, 186-87).

Nevertheless, Suburban has attacked the marketing incentives on a variety of grounds. In particular, Suburban claims that they violate R.C. §4905.32 because they are contrary to Columbia's tariffs; that they violate R.C. §4905.33 and 4905.35 because they are discriminatory; and that they violate R.C. §4905.33 because Columbia is furnishing service for less than cost for the purpose of destroying competition (Suburban Brief, at 32-41). The short answer to these contentions is that the marketing incentives do not involve the provision of a utility service, and the statutes cited by Suburban do not apply.

It has long been clear that the state's public utility laws apply only to public utility services. The general rule, which is followed throughout the nation, was set forth in Floyd & Co. v. Cincinnati Gas & Electric Co., 96 Ohio App. 133, 120 N.E.2d 596 (1954):

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> The fact that a business or enterprise is, generally speaking, a public utility does not make every service performed or rendered by it a public service... [I]t may act in a private capacity, as distinguished from its public capacity, and in doing so is subject to the same rules as a private person.

96 Ohio App. at 140, 120 N.E.2d at 601-2. See also, 73B C.J.S. 150, Public Utilities, §11; 64 Am. Jur. 2d 550, Public Utilities, §1. The sale of telephone directory advertising, for example, constitutes a "private endeavor," and not a public utility service, because utilities are under no "public duty" to provide such advertising. Richard A. Berjian, D. O., v. Ohio Bell Telephone Co., 54 Ohio St. 2d 147, 154-55, 375 N.E.2d 410, 415 (1978). As a result, the public utility laws do not apply to such sales. R.C. §4905.32 does require that directory advertising charges be set forth in telephone companies' tariffs (and they are not); R.C. §§4905.33 and 4905.35 do not require that such advertising be provided on a non-discriminatory basis; and R.C. §4905.33 does not prohibit the furnishing of such advertising at less than actual cost.

The same thing is true of the installation, maintenance, and repair of customer service lines. The Commission has repeatedly held that those activities do not constitute a public utility service, even when provided by a public utility. Keeling v. Cincinnati Gas & Electric Co., PUCO Case Nos. 84-374-GA-CSS (May 1, 1984); Kemme v. Cincinnati Gas & Electric Co., PUCO Case No. 82-1362-GA-CSS (December 22, 1982). For that reason, those activities, like telephone directory advertising, fall outside the ambit of the Ohio utility laws, and the provisions of R.C. §§4905.32, 4905.33, and 4905.35 do not apply.

This is also true of the remaining marketing incentives provided by Columbia, including reimbursement for equipment costs. Since the tariffs place the responsibility for such matters upon the customer (Complainant's Ex. 4), Columbia has no public utility obligation to provide such services, and if it chooses to do so, the statutory provisions cited by Suburban are likewise inapplicable.

Even assuming, however, for the sake of argument, that the statutes in question are applicable, there is still no basis for concluding that the marketing incentives violate those statutes. In particular, these practices are not inconsistent with R.C. §4905.32, because they do not violate Columbia's existing tariff provisions. A tariff is essentially a contract between a utility and its customers. Its principal function is to set forth the respective obligations of the parties, and in particular, to define the scope of the public utility obligation. Under Columbia's tariffs, that obligation does not include the responsibility to provide service lines, house piping, or appliances (Complainant's Ex. 4, Sections 22, 27 and 28). There is nothing, however, in the tariff that prohibits Columbia from furnishing additional assistance above and beyond its minimum obligations, provided that it does so in a reasonable and non-discriminatory manner. Such actions no more "violate" the tariff than waiving a security deposit in hardship cases, or refraining from disconnecting service on cold winter days.

Nor are these practices unlawfully discriminatory in violation of R.C. §§4905.33 and 4905.35. As Columbia noted in response to a similar argument involving the CTAPA program, the law does not prohibit all discrimination; it forbids only undue or unreasonable preferences or advantages that fail to provide similar treatment of customers who are similarly situated. Classifications are permissible when based upon reasonable considerations. The marketing incentives, like the CTAPA program, are available in competitive situations where the load would not otherwise be served, and the authorities cited in Section II-C-3 of this Brief show that rates, charges, and programs are not unduly discriminatory merely because they are available only in competitive situations. For those reasons, the marketing incentives do not violate R.C. §§4905.33 and 4905.35.

Suburban also cites various minor differences among the incentives offered to different customers as evidence of alleged discrimination (Suburban Brief, at 40). Those differences, however, as Suburban has recognized, were determined on the basis of the competitive situations (Id.), and if anything, they simply underscore the need for flexible responses in meeting competition. There has been no showing that such differences constitute undue or unreasonable discrimination in violation of the statutes.

Finally, there has been no showing that the marketing incentives violate the provisions of R.C. §4905.33, which prohibit furnishing free service or service for less than actual cost for the purpose of destroying competition. As noted earlier, that section clearly contemplates the furnishing of a utility service, such as selling or transporting natural gas, and not the furnishing of equipment, such as service lines or house piping. Suburban implies that the furnishing or use of facilities violates this section whenever the cost of those facilities is not fully reflected in rates (Suburban Brief, at 26). This is obviously incorrect. There are numerous instances in which utilities must construct and utilize new plant facilities, even though the associated costs have not been (and may never be) fully reflected in rates. There is no evidence in the record of this case showing that Columbia has furnished any utility service for less than actual cost. Nor is there any evidence that any of Columbia's activities, including its marketing incentives, were intended to destroy, rather than meet competition.

For those reasons, Suburban has failed to show that Columbia's marketing incentives violate R.C. §4905.32, §4905.33 or §4905.35. In addition, Suburban has largely ignored the most important aspect of that program: it is funded solely by Columbia's shareholders. As FERC recently noted in Order No. 436, "[r]egulat should be limited when it comes to the specification of how stockholders' funds are used." Mimeo, at IV. A. 143, 50 Fed. Reg. at 42453. The marketing incentives are reasonable; they benefit Columbia's customers, and they should not be prohibited as a result of this proceeding.

F. Suburban's Lack of Standing

At the outset of this proceeding, Columbia moved to dismiss on the grounds that Suburban lacked standing to pursue the claims set forth in its complaint. In denying that motion, the Commission held, apparently for the first time, that the "self-complaint" provisions of R.C. §4905.26 allow a utility to challenge another utility's rates, charges and practices. With all due respect, Columbia urges the Commission to reconsider that holding.

A review of both the evidence and the arguments presented by Suburban makes it even more apparent that Suburban is attempting to raise the rights of third parties. Two examples illustrate the point. Suburban strenuously argues that J.C. Penney should have been able to derive certain information from Columbia's tariffs, and repeatedly implies that the Bowling Green Church of God should have been offered a CTAPA agreement (Suburban Brief, at 35-36). If the standing doctrine means anything at all, Suburban cannot maintain a complaint on behalf of Columbia's customers, such as J. C. Penney or the Bowling Green Church of God. For that reason alone, Suburban's complaint -- and particularly those portions dealing with alleged discrimination or the alleged failure to incorporate certain items in the tariffs -- should be dismissed.

III. Conclusion

In setting this case for hearing, the Commission carefully delineated its intended role in this type of controversy. Referring to an earlier case involving a dispute

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between a regulated telephone company and an unregulated competitor, the Commission explained that:

> The Commission's primary interest was in securing the best possible service for the public, and not in refereeing a contest between competitors. It is to the extent that Suburban's allegations against Columbia could affect service to the public that the complaint touches the function of the Commission.

Entry dated January 6, 1987, at 10. A careful examination of the record shows that Suburban, which has the burden of proof, Grossman v. Public Utilities Commission, 5 Ohio St. 2d 189, 214 N.E.2d 666 (1966), has failed to show that any of the challenged rates, charges, or practices have adversely affected service to the public.

Columbia's CTAPA program benefits the CTAPA customers by providing them with lower-priced gas, and it benefits the remaining customers by providing increased fixed cost contributions from loads that would not otherwise be served, as well as the agency fees and supplemental charges, which are credited to Columbia's GCR. It has no adverse impact on any of Columbia's customers.

The same thing is true of Columbia's line extension policies, which fairly balance the interests of both Columbia's existing and prospective customers. Where an extension is economically justified, Columbia will extend its distribution mains at Company expense. Where it is not, the prospective customer is required to deposit the estimated cost of the extension. In that manner, both groups are protected from unfair or unreasonable charges, and neither is adversely affected.

This is also true of Columbia's marketing incentives. All customers benefit from the attraction of new loads and the resulting increase in contributions to fixed costs. Once again, there is no adverse impact upon Columbia's customers, since the costs of the incentives are fully absorbed by Columbia shareholders.

Nor has there been any showing that these practices have adversely affected service to Suburban's customers. They are clearly no worse off, because Columbia has not even attempted to duplicate Suburban's facilities in order to raid its existing markets. It is true, of course, that Suburban has lost certain new customers to Columbia, but such losses are a natural and inevitable result of competition. Suburban clearly had no vested interest in serving those customers, and if it chose to invest in new facilities without a commitment from the customer to take service, Suburban, and not its customers, should be forced to bear the loss.

In any competitive situation, there will be successes and failures, winners and losers. Whatever its merits, Suburban's complaint in this case was undoubtedly prompted by Columbia's success in the marketplace. Columbia should not be penalized for that success. Columbia has responded firmly to the competition posed by Suburban, including its efforts to raid Columbia's existing markets, but it has done so in a reasonable and lawful manner which maximizes the benefits of competition for all of its customers, while adversely affecting none of them.

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For the foregoing reasons, Columbia submits that Suburban has failed to sustain its burden of proving that Columbia's actions have been unjust, unreasonable, or unlawful, and that its complaint should therefore be dismissed in its entirety.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing Post-Hearing Brief was served upon the parties listed below by regular U. S. Mail this 7th day of July, 1987.

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United States Court of Appeals

FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 85-1811

ASSOCIATED GAS DISTRIBUTORS, PETITIONER

v.

FEDERAL ENERGY REGULATORY COMMISSION, RESPONDENT

AIR PRODUCTS AND CHEMICALS, INC., et al.,
ALGONQUIN GAS TRANSMISSION COMPANY,
ALABAMA-TENNESSEE NATURAL GAS COMPANY,
AMERICAN BAKERS ASSOCIATION,
AMERICAN GAS ASSOCIATION,
AMERICAN PUBLIC GAS ASSOCIATION,
AMERICAN PAPER INSTITUTE, INC.,
ARKLA, INC.,
AMOCO PRODUCTION COMPANY,
ARCO OIL AND GAS COMPANY,
ASHLAND EXPLORATION, INC.,
ARMSTRONG WORLD INDUSTRIES,
ASSOCIATED GAS DISTRIBUTORS,
ASSOCIATION OF TEXAS INTRASTATE
NATURAL GAS PIPELINES,
ATLANTA GAS LIGHT COMPANY,
BALTIMORE GAS AND ELECTRIC COMPANY,
BROOKLYN UNION GAS COMPANY,

Bills of costs must be filed within 14 days after entry of judgment. The court looks with disfavor upon motions to file bills of costs out of time.

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Cabot Corporation,
Carolina Utility Customers Association, Inc.,
Cascade Natural Gas Corporation,
Central Illinois Light Company,
Champlin Petroleum Company,
Chemical Manufacturers Association,
Chevron U.S.A. Inc.,
Cities Service Oil and Gas Corporation,
Citizens Energy Corporation,
City of Wilcox, Arizona and Arizona Electric Power Cooperative, Inc.,
Columbia Gas Distribution Companies,
Columbia Gas Transmission Corporation,
Columbia Nitrogen Corporation and Nipro, Inc.,
Commonwealth of Kentucky Public Service Commission,
Conoco, Inc.,
Consolidated Edison Company of New York, Inc.,
Consumers Power Company and Michigan Gas Storage Company,
Delhi Gas Pipeline Corporation,
Department of Public Service Commission of the State of New York,
Diamond Shamrock Exploration Company,
El Paso Natural Gas Company,
Entex, Inc.,
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Florida Gas Transmission Company,
Foothills Pipe Lines (Yukon) Ltd.,
Gas Distributors Information Service,
State of Louisiana,
Tenneco Oil Company,
Tenngasco Corporation,
Texas Eastern Transmission Corporation,
Texaco, Inc.,
Texas Gas Exploration Corporation,
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Transcontinental Gas Pipe Line Corporation,
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Trunkline Gas Company,
Weirton Steel Corporation,
Westcoast Transmission Company Limited,
West Virginia Consumer Advocate,
Wisconsin Power & Light Company,
Union Oil Company of California,
Valero Transmission Company,
United Distribution Companies,
UGI Corporation,
Kansas Power and Light Company,
State of Michigan and Michigan Public Service Commission,
South Jersey Gas Company,
Washington Gas Light Company,
Arizona Public Service Company,
Sun Exploration and Production Company,
Bethlehem Steel Corporation, Intervenors

And Consolidated Case Nos. 85-1812, 85-1813, 85-1818, 85-1821, 85-1830, 85-1836, 86-1001, 86-1006, 86-1007, 86-1008, 86-1016, 86-1017, 86-1018, 86-1019, 86-1020, 86-1022, 86-1023, 86-1024, 86-1029, 86-1030, 86-1031, 86-1032, 86-1034, 86-1035, 86-1036, 86-1038, 86-1042, 86-1046, 86-1047, 86-1048, 86-1049, 86-1050, 86-1051, 86-1053, 86-1054, 86-1055, 86-1056, 86-1063, 86-1066, 86-1067, 86-1076, 86-1081, 86-1083, 86-1085, 86-1086, 86-1087, 86-1088, 86-1089, 86-1090, 86-1092, 86-1094, 86-1095, 86-1097, 86-1098, 86-1099, 86-1100, 86-1102, 86-1103, 86-1153, 86-1154, 86-1155, 86-1226, 86-1235, and 86-1246

Petitions for Review of Orders of the Federal Energy Regulatory Commission

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Argued October 14 and 15, 1987

Decided June 23, 1987

William W. Brackett, with whom *Daniel F. Collins* and *G. Mark Cook* were on the brief for ANR Pipeline Co., et al., petitioners in Nos. 86-1055 and 86-1067. *Terry O. Vogel, Jeffrey M. Goldsmith*, and *William M. Lange* entered appearances.

Roberta L. Halladay, with whom *Jerome C. Muys* and *C. William Cooper* for United Distribution Companies, petitioners in No. 86-1006 and intervenors in Nos. 85-1811, 86-1016, 86-1067, 86-1087, and 86-1153; *William Warfield Ross* and *Daniel Koffsky* for Consumers Power Co., petitioner in No. 86-1047 and intervenor in No. 85-1811, and *Thomas Patrick* and *Karen Cargill* for The Peoples Gas Light and Coke Co. and North Shore Gas Co., petitioners in No. 86-1155 and intervenors in Nos. 85-1811 and 86-1153, were on the joint brief. *Janet M. Robins* for Consumer Power Co., et al. and *Mark McGuire* for The Peoples Gas Light and Coke Co., et al. also entered appearances.

John T. Miller, Jr. for Elizabethtown Gas Co., petitioner in No. 85-1836.

Robert A. Nelson, Jr. for Northwest Gas Co., with whom *Donald K. Darkner* and *Daniel F. Stenger* for CP National Corp. and *Thomas F. Brosnan* for Washington Natural Gas Co. were on the joint brief for petitioners in No. 86-1097.

Kenneth J. Nieses for Laclede Gas Co., petitioner in No. 86-1001 and intervenor in No. 85-1811.

David B. Robinson, with whom *William J. Guste, Jr.*, Attorney General, State of Louisiana, and *Theodore L. Jones* for State of Louisiana, petitioners in No. 86-1053 and 86-1051 and intervenor in No. 85-1811; *Patrick J. Nugent, James M. Costan*, and *Elisa J. Grammer* for Association of Texas Intrastate Natural Gas Pipelines, intervenor in No. 85-1811; *J. Paul Douglas*, with whom

Brian J. Heisler and *Kevin Sweeney* for Amoco Gas Co., petitioner in Nos. 86-1081 and 86-1154 and intervenor in Nos. 85-1811, 86-1016, and 86-1055; *C. Burnett Dunn* for Oklahoma Natural Gas Co., intervenor in Nos. 85-1811, 86-1067, 86-1088, and 86-1153; and *William I. Harkaway* for Consolidated Edison of NY, Inc., petitioner in No. 86-1094 and intervenor in No. 85-1811, were on the joint brief. *Timothy Keegan* for Association of Texas Intrastate Natural Gas Pipelines, *Diane Siler* for the State of Louisiana, and *Barbara M. Gunther* and *Steven I. Kalish* for Consolidated Edison of NY, Inc. also entered appearances.

Edward J. Grenier, Jr., with whom *William H. Penniman, Glen S. Howard, Gail S. Gilman, James P. Rathvon*, and *James M. Bushee* for the Process Gas Consumers Group and the American Iron & Steel Institute, petitioners in Nos. 86-1007 and 86-1008 and intervenors in Nos. 85-1811, 86-1226, 86-1235, and 86-1246; *Nicholas W. Fels* and *David N. Heaps* for Air Products & Chemicals, Inc., et al., intervenor in Nos. 85-1811, 86-1016, and 86-1017; *Stephen A. Herman* and *John G. Froemming* for the Fertilizer Institute and American Bakers Association, intervenors in Nos. 85-1811, 86-1016, and 86-1017; *Rigdon H. Boykin* and *Thomas E. Hirsch, III* for American Paper Institute, petitioner in No. 86-1089 and intervenor in Nos. 85-1811, 86-1016, and 86-1017; and *John W. Hardwicke* for Maryland Industrial Group, intervenor in Nos. 85-1811, 86-1016, and 86-1017 were on the joint brief.

Thomas G. Johnson, with whom *M.G. Brookshier* and *Charles McCloes, Jr.*, for Shell Offshore, Inc. and Shell Western Electric and Power Inc., petitioner in Nos. 86-1016, 86-1017, and 86-1018 and intervenor in Nos. 85-1811, 85-1812, and 85-1813; *Harris S. Wood* and *Michael G. Maloney* for Arco Oil & Gas Co., intervenor in Nos. 85-1811, 85-1087, and 86-1153; *Thomas J. Eastment* and *Charles M. Darling IV* for Ashland Corp., petitioner in No. 86-1092 and intervenor in No. 85-1811; *Roscoe C. Elmore* for Cabot Corp., intervenor in No.

(Friendly, J.) ("the [judicial] hackles bristle still more when a financial penalty is assessed for action that might well have been avoided if the agency's changed disposition had been earlier made known, or might even have been taken in express reliance on the standard previously established"). *Cf. Boyce Motor Lines, Inc. v. United States*, 342 U.S. 337, 340 (1952) (requirement of adequate notice for criminal enforcement of administrative regulations). Moreover, if the Commission approves plans of compliance so vague that enforcement is impaired, its posture will be essentially that found fatally defective in *MPC II*: it will have authorized blanket certificate transportation under rules not adequately grappling with the potentially discriminatory effects.

The Commission's oracular procrastination (a blend of Delphi and Fabius) makes challenges to the specifics of "first come, first served" unripe. These challenges include assertions that the policy (1) gives inadequate attention to contractual commitments or to "dependency" as bases of distinction; (2) unduly threatens the security of supply of LDCs; and (3) disregards equities based on prior payments for pipeline capacity. *See, e.g.*, Brief of Interstate Pipeline Group at 35-36; Brief of Associated Gas Distributors at 39-41. One intervenor also poses a carefully reasoned attack on the Commission for its failure to consider alternatives such as an auction system. *See* Brief of Baltimore Gas & Elec. Co. at 19-20. Though the point is much closer, the Commission's vagueness and lack of commitment are such that even this attack appears unripe. The ripeness doctrine seeks to

> prevent the courts, through avoidance of premature adjudication, from entangling themselves in abstract disagreements over administrative policies, and also to protect the agencies from judicial interference until an administrative decision has been formalized and its effects felt in a concrete way by the challenging parties.

Abbott Laboratories v. Gardner, 387 U.S. 136, 148-49 (1967). As the Commission confined its disposition of the issue to some general remarks in its supporting statement, our involvement in the merits at this stage would defy these principles.

III. Rate Conditions

With the stated intention of imposing on pipelines more of the risk and responsibility for their own business decisions, the Commission has established a system of flexible rates. *See* 18 C.F.R. §§ 284.7, 284.8(d), 284.9(d).[10] Tariffs are to provide for ceilings and floors, with the pipeline free to charge anywhere within that band. Each maximum rate is to be based on what is typically known as "fully allocated cost," *i.e.*, a rate such that, if the pipeline carries projected volume at the specified unit price, it should exactly recover all costs allocable to the relevant service for the period. *See* 18 C.F.R. § 284.7(c)(3). Minimum rates are to be based on average variable cost. *See* 18 C.F.R. § 284.7(d)(4)(ii). The maximum rates are to vary depending on whether the service is in a peak or off-peak period, and on whether it is firm or interruptible service. A pipeline discounting any service from the maximum rate must, within 15 days of the close of the billing period, report the maximum rate for the transaction, the rate actually charged, the shipper's identity, and any corporate affiliation between pipeline and shipper. 18 C.F.R. § 284.7(d)(5)(iv).

[10] These sections govern permissible rates for transportation by interstate pipelines under § 7 blanket certificates and under § 311. Rates charged by intrastate pipelines under § 311 are required to be "fair and equitable." *See* NGPA § 311(b)(2)(A), 15 U.S.C. § 3371(b)(2)(A) (1982); 18 C.F.R. §§ 271.101-.1106 (1985). Order No. 436 also requires intrastate pipelines to adhere to the restrictions on reservation fees that Order No. 436 imposes on interstate pipelines' transportation. *See* 18 C.F.R. § 284.123(b).

Pipelines may charge a "reservation fee" for firm service. Otherwise shippers could request whatever volume they liked, without cost and regardless of intent to use. As requests would vastly exceed capacity, the pipeline could not rationally plan capacity allocation. *See* J.A. 457-60. Apart from the reservation fee, pipelines are required to charge on a "volumetric" basis, *i.e.*, a simple charge per unit actually transported, without a "demand charge" or "minimum bill."

A. *Absence of Finding that Prior Rates Were Unlawful.*

The Interstate Pipeline Group objects that the Commission did not make specific findings that any rates charged by individual pipelines were unlawful before imposing the new rate conditions. The Commission is not required to make individual findings, however, if it exercises its § 5 authority by means of a generic rule. *See, e.g., Wisconsin Gas Co. v. FERC*, 770 F.2d 1144, 1165-68 (D.C. Cir. 1985), *cert. denied*, 106 S. Ct. 1967 (1986). The pipelines seek to distinguish *Wisconsin Gas* on the ground that it "involved specific findings as to a single billing term," to wit, minimum bill provisions that included variable costs. (Minimum bills charge for specific portions of contract demand even as to gas that is not taken; the Commission believed that inclusion of variable costs in such bills imposed an unjustifiable restriction on customer choice of gas supply and improperly sheltered pipelines from competition.) The distinction is irrelevant. What justified the generic approach in *Wisconsin Gas* was the Commission's conclusion that *any* tariff violating the rule would have such adverse effects on the interstate gas market as to render it "unjust and unreasonable" within the meaning of § 5. That is precisely what the Commission has concluded here.

The pipelines may be claiming that the Commission's failure to adduce evidence meeting the standards of adjudication breaches the substantial evidence require-

ment of § 19 of the NGA, 15 U.S.C. § 717r (1982). Again *Wisconsin Gas* is dispositive. There the court reaffirmed the court's conclusion in *American Public Gas Ass'n v. FPC*, 567 F.2d 1016 (D.C. Cir. 1977), that § 19's reference to "substantial evidence," located as it is in the provision guiding judicial review, does not dictate the procedure to be employed in FERC's notice-and-comment rulemakings. *Wisconsin Gas*, 770 F.2d at 1167-68.

Finally, the pipelines' complaint may be that the Commission adopted its new rate criteria without "factual" submissions tracing a relationship between rate practices formerly permitted and the evils that it sought to correct. There may be circumstances in which such a claim would prevail. In *Electricity Consumers Resource Council v. FERC*, 747 F.2d 1511, 1514 (D.C. Cir. 1984), for example, this court declared that "mere reliance on an economic theory cannot substitute for substantial record evidence and the articulation of a rational basis for an agency's decision." In fact, however, the court in *Electricity Consumers* was persuaded that the Commission had "inexplicably distorted" the theory that it claimed to apply. *Id.* Here the pipelines point to no such inexplicable distortion.

Promulgation of generic rate criteria clearly involves the determination of policy goals or objectives, and the selection of means to achieve them. Courts reviewing an agency's selection of means are not entitled to insist on empirical data for every proposition on which the selection depends. *Wisconsin Gas* made that clear. For example, in the rulemaking proceeding parties had objected that curtailment of the minimum bill would result in the pipelines shifting costs to its most captive customers. The Commission responded in part with a prediction that "the increased incentive to compete vigorously in the market would eventually lead to lower prices for all consumers." 770 F.2d at 1161. The court accepted this without record evidence, presumably because it viewed the prediction as at least likely enough to be within the Commission's authority. Clearly nothing in *Electricity Consumer's* reference to "economic theory" was intended to invalidate agency relience on generic factual predictions merely because they are typically studied in the field called economics. Agencies do not need to conduct experiments in order to rely on the prediction that an unsupported stone will fall; nor need they do so for predictions that competition will normally lead to lower prices.

In support of this objection the pipelines do not identify any factual proposition, relied on by the Commission, that they regard as requiring additional support. Accordingly, the objection cannot succeed.

B. *Allowance of Discounting Generally.*

Several petitioners object that the Commission's allowing pipelines to discount from the maximum rates is in effect an approval of "undue preference[s]" and "undue discrimination" in violation of §§ 4 and 5 of the NGA. But "the mere fact of a rate disparity" is not enough to constitute unlawful discrimination. *Cities of Bethany v. FERC*, 727 F.2d 1131, 1139 (D.C. Cir.), *cert. denied*, 469 U.S. 917 (1984). The reporting system will enable the Commission to monitor behavior and to act promptly when it or another party detects behavior arguably falling under the bans of §§ 4 and 5. This provision for flexibility conforms to Congress's intention in the NGA to allow a vital role for private contracting between the parties. *See United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 332, 338-39 (1956); *see also Sea-Land Service, Inc. v. ICC*, 738 F.2d 1311, 1316-19 (D.C. Cir. 1984) (rejecting proposition that "contract rates," based on individual contract but available to similarly situated shippers of like commodities, are automatically violative of nondiscrimination principle). Accordingly, given the Commission's broad latitude to choose between rulemaking and adjudication, *see SEC v. Chenery Corp.*,

332 U.S. 194 (1947),[11] we could find the provisions illegal only if they carried such a risk of allowing undue discrimination or preferences as to be arbitrary and capricious. We do not find the risk so high.

The Associated Gas Distributors call our attention to the problem of discounts in favor of a pipeline's gas trading affiliate. We recognize that such transactions may carry more than the usual risk of undue discrimination. *Cf.* NGPA § 601(b)(1)(E), 15 U.S.C. § 3431(b)(1)(E) (1982) (imposing a special limit on pipeline recovery of cost of gas purchased from affiliate). But we see no reason to think that such a discount should be *per se* unduly discriminatory. If a pipeline gives its gas trading affiliate discounts identical to those given to unaffiliated parties in identical circumstances, the discount would not be unlawful merely on account of the affiliation. Accordingly, the risk of such discounts proving invalid is insufficient to justify invalidation of the rule.

C. *Potential Discrimination Between Bundled and Unbundled Transportation.*

Other petitioners suggest that the Commission's rate regulations are invalid because they sanction undue discrimination between unbundled transportation and the transportation component of a bundled sales transaction. That the criteria governing permissible rates in the two categories are different, however, does not establish discrimination between them. Most notably, the petitioners point to no reason to suppose that, as a whole, unbundled transportation service will recover a lower proportion of its costs than will the transportation component of unbundled sales. Indeed, the rate provisions specify that the maximum rates for each subcategory of unbundled transportation are to be designed to recover "solely those costs which are properly allocated to the service to which

[11] *See also supra* part II.B.3.

the rate applies." 18 C.F.R. § 284.7(d)(4)(i). That the pipelines may offer discounts does not alter the case. They do so at their own risk, *see especially id.* at § 284.7 (c)(5)(iii) (disallowing any rate seeking to recover losses from a prior period); pipeline managements will presumably aim at a pricing strategy that will, in fact, fully recover costs allocable to unbundled transportation. We cannot evaluate the rule on the basis of an assumption that they will not succeed. (We address below a claim that the rate provisions disable pipelines from full recovery of unbundled transportation costs.)

The claim of discrimination in favor of unbundled transportation contains a more subtle argument (or at least the seeds of such an argument): even though such rates may recover exactly the cost of service (just as for the transportation component of sales service), perhaps the flexibility afforded pipelines will in effect give unbundled transportation an advantage over sales service. The possibility is hardly one that we may rule out *a priori*. But we think it a problem that the Commission should be free to solve if and when it develops. As the Commission points out, the historical problem has been that unbundled transportation rate provisions put it at a *disadvantage* as against sales service. J.A. 318 No one appears to dispute that finding. It seems wholly suitable for the Commission to experiment with one rate structure in this specialized area; if it proves a triumphant success, the Commission will doubtless have opportunities to extend it to sales.

D. *Selective as Opposed to Uniform Discounts.*

Some parties accept the concept of price discounting but argue that the Commission should allow only "uniform" discounting (in effect requiring a pipeline to promulgate in advance the criteria under which it would provide discounts). The Commission, however, made the

judgment that such a rule would unduly stifle discounting. J.A. 478-83. It saw substantial gains from such discounts: cheaper fuel supplies for the price-elastic customers receiving the discounts; reduced revenue shortfalls for pipelines that would otherwise lose the business altogether; and protection for non-favored customers from rate increases that would ultimately occur if pipelines lost volume through inability to respond to competition. J.A. 483.

For much the same reasons that courts allow administrative agencies the leeway to choose between rulemaking and adjudication (variability of circumstances, difficulties of foresight), we think that the Commission was within its power to allow pipelines a parallel choice. But, just as courts insist on a degree of agency consistency, *see, e.g., Local 32, American Federation of Gov't Employees v. FLRA*, 774 F.2d 498, 502 (D.C. Cir. 1985), we expect that the Commission will exact from the pipelines as much consistency of application as is necessary for both to be in conformity with §§ 4 and 5.

E. *Consistency of "Value-of-Service" Discounting with MPC II.*

The American Public Gas Association and others contend that the general consent to selective discounting violates this court's decision in *Maryland People's Counsel v. FERC ("MPC II")*, 761 F.2d 780 (D.C. Cir. 1985). The attack is directed especially to Commission suggestions—in supporting statements, not the rule itself—that discounting intended to meet competition from alternative fuels or indeed from other pipelines is not *per se* unduly discriminatory. J.A. 476.

Petitioners misconceive the scope of *MPC II*. Pipelines were using their market power in the transportation market to discriminate (indirectly) in the sale of gas, a commodity that Congress had concluded was produced under roughly competitive conditions. In the sale of such a commodity there is no economic justification for [illegible] ing different prices based on the purchasers' differing access to substitutes (*i.e.*, their price elasticity of demand). Indeed, if a product is produced under competitive conditions, such price discrimination cannot occur unless a bottleneck with market power stands between it and the customers. By contrast, pipeline transportation service is marked by a degree of natural monopoly, J.A. 305-06, 352, 481 (*i.e.*, longrun average costs decline in the relevant range of production). *See* 2 A. Kahn, *The Economics of Regulation: Principles and Institutions* 119-23 (1971). In such an industry, "value-of-service" ratemaking (*i.e.*, rates varying on the basis of differing demand characteristics) has an established place,[13] though not an uncontested one.[14] The equitable argument in favor of such differentials is that they may benefit captive customers by making a contribution to fixed costs that otherwise would not be made at all. (The efficiency argument is that such differentials will raise total volume closer to the level it would attain if all sales were priced at marginal cost.)

[13] *See* E. Gellhorn & R. Pierce, *Regulated Industries* 185-89 (1987).

[14] *See* Tye & Leonard, *On the Problems of Applying Ramsey Pricing to the Railroad Industry with Uncertain Demand Elasticities*, 17A Transportation Research 439 (1983); Tye, *Ramsey Pricing and Market Dominance Under the Staggers Rail Act of 1980*, 24 Transportation Research Forum 667 (1983); Meyer & Tye, Toward Achieving Workable Competition in Industries Undergoing a Transition to Deregulation (March 19, 1987) (unpublished). We do not understand these critics to attack rate differentials where application of some apparently egalitarian principle, such as an equal revenue-to-variable-cost ratio, would result in prices for some customers or commodities above what the profit-maximizing monopolist would charge. *See* Tye, *Ramsey Pricing and Market Dominance Under the Staggers Rail Act of 1980*, 24 Transportation Research Forum at 669-70; Henderson, *Price, Discrimination Limits in Relation to the Death Spiral*, 7 Energy Journal (No. 3) 33, 37 (1986).

These justifications were missing in *MPC II*. There the court found that the then-existing blanket certificate regulations allowed pipelines to deny captive consumers access to the spot market for gas, while providing it for the non-captives. 761 F.2d at 788. This allowed pipelines to preserve the revenues attributable to transportation of gas to fuel-switchable customers, while continuing to sell their inventory of overpriced gas to captive customers. The Commission advanced an argument that the pipelines' receipt of transportation revenues would redound to the benefit of captive customers—an argument that sounds like the one advanced above. The court said no. First, we said that the Commisison had offered no reason to think that the captives could not enjoy the fuel switchables' contribution to fixed costs even if the Commission conditioned the program on equal access for captive consumers—precisely what the Commission has done here. *Id.* Second, we pointed out that the Commission had nowhere answered the petitioners' argument that the captives' loss through lack of access to the wellhead market would greatly exceed their gain through the fuel-switchables' contribution to fixed costs. *Id.* Here, of course, the Commission is providing access to the spot market. Thus the facts here obviate our two reasons for rejecting the Commission's argument on contributions to fixed costs.

To read *MPC II* as a rule that price differentials based on demand conditions are always unduly discriminatory would render the decision a defiant and unreasoned exception to the general pattern. The judicial acceptance of such price differentials is longstanding. For nearly 100 years, for example, the courts have interpreted the anti-discrimination provisions of the Interstate Commerce Act to allow the ICC to approve differentials justified exclusively by competition. *See, e.g.*, *Texas & Pacific Ry. v. ICC*, 162 U.S. 197, 218-19 (1896); *Dresser Industries, Inc. v. ICC*, 714 F.2d 588 (5th Cir. 1983) (review under three different anti-discrimination provisions); *National Gypsum Co. v. United States*, 353 F. Supp. 941, 946-49

(W.D.N.Y. 1973) (enumerating cases following this view). Indeed, the Supreme Court has even struck down an ICC finding of unlawful discrimination where it appeared to be based on an absolute rule that competitive conditions could never justify a rate differential. *Eastern-Central Motor Carriers Ass'n v. United States*, 321 U.S. 194 (1944).

We have answered the claims that the rate provisions of Order No. 436 put it in violation of our mandate in *MPC II*. This is not to say, of course, that the Commission is free to uphold every price distinction based on different demand elasticities. It has long been contended, for example, that rate differentials based exclusively on competition between transporters with similar cost functions may end up forcing captive customers to bear disproportionate shares of fixed costs without any offsetting gain in efficiency. *See, e.g.*, 1 A. Kahn, *The Economics of Regulation: Principles and Institutions* 159-81, esp. 170 (1970). The contention is not self-evidently true: if the demand of buyers with access to competing carriers is at all price elastic, the price reductions they enjoy will raise their demand close to competitive levels. In any event, the Commission may properly defer its ultimate resolution of these issues to another day and another proceeding. *Cf. American Commercial Lines, Inc. v. Louisville & Nashville R.R.*, 392 U.S. 571 (1968) (finding broad discretion in ICC to choose format in which to resolve issues of price discounting in competition between railroads and barge-truck combinations).

F. *Impact of Discounting on Pipeline Solvency.*

Petitioners ANR Pipeline Company and Colorado Interstate Gas Company fault the regulations for allowing the pipeline to discount below the ceilings but never to charge more. To the Commission's defense that the discounting mirrors the world of unregulated firms, they respond that in such a world the circumstances where

market conditions force a firm to discount are likely to be matched by ones allowing the charge of a premium. (In equilibrium firms will earn a normal profit.) Here, they argue, the rules parallel only the downside of the unregulated market. As a result, they say, return will necessarily be less than in other industries with corresponding risks, in violation of *FPC v. Hope Natural Gas Co.*, 320 U.S. 591, 603 (1943).

We can imagine a rate methodology under which this contention would be sound. Suppose that a pipeline has a capacity for transporting 120,000 units a year, that each year's share of fixed costs amounts to $90,000, and that variable costs are $.10 per unit. In an initial rate case, the Commission projects volume at 100,000 units, and thus sets a maximum price of $1.00 per unit ($.90 as a share of fixed costs and $.10 for variable costs).

While those rates are in effect, suppose the firm in fact carries 100,000 units at $1.00, but, spotting market opportunities, carries another 10,000 units at $.20 per unit for customers who would switch to alternative fuels if the transportation charge rose above $.25 per unit. (If the pipeline knew that $.25 was the switchover point, it would charge that, but it may not know exactly.)

In the next rate case, suppose the Commission projects use at 110,000 units, and accordingly sets the maximum price at $.92 per unit ($.10 for variable costs and $.82 ($90,000/110,000) for fixed costs). Such a rate would be sufficient to recover costs only if the pipeline carried 110,000 at the maximum rate; but the evidence overwhelmingly suggests that it will not be able to do so—the extra 10,000 units of business were due to the discount. Unless some change in circumstance saves the pipeline, revenue will be $94,000 ($92,000 for 100,000 units transported at the maximum rate plus $2,000 for 10,000 units at $.20), against costs of $101,000 ($90,000 fixed and $11,000 variable).

We see no reason, however, to suppose that the Commission intends such calculations. Its only statement relating to projections, 18 C.F.R. § 284.7(c)(3), indicates the contrary:

> The pipeline's revenue requirement allocated to firm and interruptible services should be attained by providing the projected units of service in peak and off-peak periods at the maximum rate for each service.

In its commentary, the Commission pointed to this passage as proof of its agreement with MPC's suggestion that "revenue projections in rate filings [should] assume that all sales and transportation volumes will be charged at the maximum rate." J.A. 484. Thus, it appears that "rate" in § 284.7(c)(3) refers to the maximum unit price, not to projected throughput. This would appear to undermine any fear that the Commission might employ the dubious procedure hypothesized above.

* * * *

Thus we find no legal defect in the rate provisions of Order No. 436.

IV. Contract Demand ("CD") Adjustment

Local distribution companies require a firm supply of gas. Typically they have looked to pipeline sales service to fill this need. Firm sales contracts give the customer the right to demand, and obligate the pipeline at all times to stand ready to deliver, a certain quantity of gas per day, generally known in the industry as "Contract Demand" or "CD." Once the arrangement receives the necessary certificate under § 7 of the NGA, the LDC's entitlement and the pipeline's obligation acquire a legal existence independent of the contract and persist until the Commission issues formal approval of "abandonment." *See California v. Southland Royalty Co.*, 436 U.S. 519 (1978); *Panhandle Eastern Pipe Line Co. v. Michigan Consolidated Gas Co.*, 177 F.2d 942, 945 (6th Cir. 1949). For a "full requirements" customer, relying on a single pipeline, the CD will amount to its entire anticipated gas needs; "partial requirements" customers, as the name suggests, rely on more than one pipeline.

"Demand charges" are based on CD and are payable regardless of the customer's actual use; having thus committed itself to partial payment for the gas covered by its CD, a customer pays only a "commodity charge" when it actually takes gas.[14] Thus, if the demand charge is $1 and the commodity charge $3, the customer will switch to an alternative supply only when the alternative's total cost (transportation and gas) is under $3, even though (in a sense) gas at $3.50 would be a better bargain. (It is better only "in a sense" because the customer gets a security of supply from its pipeline supplier that it does not get in the spot market.) The relation with a regular pipeline supplier thereby constrains the customer's practical freedom to take advantage of open access to the wellhead market. The higher the CD in relation to its total usage, and the higher the demand charge as a proportion of total price, the more severe is the constraint.

To make the customers' access meaningful, Order No. 436 provides customers a limited right to unilaterally modify their contracts with pipelines who elect to operate under the Order. It entitles any party with a firm sales contract on the date the pipeline becomes subject to Order No. 436[15] to (a) convert specified percentages of

[14] Order No. 436 largely retains this two-tiered rate structure, with firm transportation customers paying a "reservation" fee for the guaranteed right to call on a certain amount of the pipeline's capacity and a "volumetric" fee to cover the variable cost of providing the service actually called for. *See supra* part III.

[15] A pipeline becomes subject to the provisions of Order No. 436 for these purposes when it accepts a blanket certifi-