

# EMERGENCY RATE MAKING FOR OHIO PUBLIC UTILITIES

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## I. INTRODUCTION

Until recently, the statute conferring emergency rate making authority upon the Public Utilities Commission of Ohio was seldom applied. Though it has been part of Ohio law in substantially the same form for sixty-five years, the Ohio supreme court has considered its provisions only a few times, and most of the cases were decided in the period between 1920 and 1948. During the past several decades, until 1973, the Commission was not even requested to invoke its emergency authority except as a vehicle for rescuing small utilities which had delayed too long in assessing and updating their financial programs. Throughout the late 1950's and 1960's the larger utilities had no reason to request emergency relief—their budgets reflected record profits, five of them enjoyed top bond ratings, and economies of scale achieved by building large facilities resulted in decreasing electric rates.

However, the double-digit inflation of the 1970's created extraordinary financial pressures upon Ohio's electric companies. Caught between rising operating costs on one hand, and increased demands for service on the other, those companies have found it more difficult to attract capital needed to provide expanded service, or even maintain existing service. They have therefore requested and received temporary authority to increase rates. The statute under which the commission may grant such emergency relief is § 4909.16 of the Ohio Revised Code,<sup>1</sup> commonly known as the emergency statute. Under prevailing economic conditions, this section will remain an important legal tool. This article is intended as a guide to present law and policy related to the emergency statute. It offers an analysis of the Ohio supreme court's interpretation of § 4909.16, an indication of the probable limits of the Commission's jurisdiction under the statute and case law, an examination of Commission practices under the statute,

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\* Commissioner, Public Utilities Commission of Ohio. The views expressed herein do not necessarily represent the official position of the Commission. The author expresses deep appreciation to Samuel Price, second year law student at The Ohio State University, College of Law, for his invaluable assistance in research, drafting, editing and preparation of this article.

<sup>1</sup> All references are to the Ohio Revised Code unless specified otherwise.

and a summary of recent applications of the statute by the Commission.

## II. JURISDICTION AND AUTHORITY UNDER THE STATUTE

The emergency statute was enacted as § 4 of the Public Utilities Act of 1911,<sup>2</sup> and was first codified as § 614-32 of the General Code. In 1953, the legislature revised the wording for stylistic purposes when it recodified the statute as § 4909.16 of the Ohio Revised Code; however, the present version remains identical in substance with the original enactment.<sup>3</sup> The statute now reads:

[w]hen the public utilities commission deems it necessary to prevent injury to the business or interests of the public or of any public utility of this state in case of any emergency to be judged by the commission, it may temporarily alter, amend, or, with the consent of the public utility concerned, suspend any existing rates, schedules, or order relating to or affecting any public utility or part of any public utility in this state. Rates so made by the commission shall apply to one or more of the public utilities in this state or to any portion thereof, as is directed by the commission, and shall take effect at such time and remain in force for such length of time as the commission prescribes.

The language of the statute places only the most general limitations on the Commission's discretion in determining what circumstances justify an emergency order. Circumstances must be such that, in the Commission's judgment, some injury to the business or interests of the public or of a public utility will result unless the Commission acts. Some would argue that dictum from the concurring opinion of Chief Justice Marshall in *City of Columbus v. PUCO*<sup>4</sup> limits the Commission's power to find an emergency based on a company's

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<sup>2</sup> Public Utilities Act § 34, 102 Laws of Ohio 549, 559 (1911).

<sup>3</sup> As originally enacted the statute reads:

The commission shall have power, when deemed by it necessary to prevent injury to the business or interests of the public or any public utility of this state in case of any emergency to be judged by the commission, to temporarily alter, amend, or with the consent of the public utility concerned suspend any existing rates, schedules or order relating to or affecting any public utility or part of any public utility in this state. Such rates so made by the commission shall apply to one or more of the public utilities in this state or to any portion thereof as may be directed by the commission, and shall take effect at such time and remain in force for such length of time as may be prescribed by the commission.

*Id.*

<sup>4</sup> 103 Ohio St. 79, 133 N.E. 800 (1921).

inability to meet its operating expenses. That case, however, was decided without a majority opinion, and in fact, the supreme court has always upheld the Commission when its finding of emergency was the crux of the case.

For example, in *Manufacturers Light & Heat Co. v. PUCO*,<sup>5</sup> the Commission granted an emergency rate increase because the utility company's financial data showed that its revenues were insufficient to cover operating expenses. However, after further hearings four months later, the Commission rescinded its order on grounds that the company had failed to show that the emergency still existed. The company appealed, arguing that the evidence of record would not support rescission of the emergency order, but the supreme court affirmed without considering the adequacy of the record. The court held that "[u]nder the provisions of [§ 4909.16] the determination of whether an emergency exists, warranting a temporary alteration of rates, and the length of time such altered rates shall remain in effect are within the judgment and sound discretion of the Public Utilities Commission."<sup>6</sup> This holding is based on the court's earlier decision in *City of Cambridge v. PUCO*.<sup>7</sup> In that case the court held, as in *Manufacturers*, that the determination of an emergency lies within the sound discretion of the Commission, and that the Commission's own regulatory lag and the inability of a utility company to pay its fixed charges were factors upon which the Commission could reasonably base a finding of emergency.<sup>8</sup>

### III. EMERGENCY JURISDICTION OVER MUNICIPAL UTILITY RATES

The Commission's emergency jurisdiction is limited in respect to utility rates established by municipal corporations, but the cases do not precisely define the limitation. The supreme court has held that in some circumstances the Commission may temporarily alter the terms of utility contracts between municipal corporations and utility companies, but it remains undecided whether the power to make such alterations may be applied to the utility rates. To describe the limitation as clearly as the cases allow requires a brief overview of the various authorities granting regulatory powers to the cities.

The General Assembly first gave the cities unilateral rate mak-

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<sup>5</sup> 163 Ohio St. 78, 125 N.E.2d 183 (1955).

<sup>6</sup> *Id.* at 80, 125 N.E.2d at 184-85.

<sup>7</sup> 159 Ohio St. 88, 111 N.E.2d 1 (1953).

<sup>8</sup> *Accord*, *City of Jackson v. PUCO*, 159 Ohio St. 123, 111 N.E.2d 7 (1953).

ing powers by the Act of March 11, 1853,<sup>9</sup> which authorized city councils to fix rates for natural gas service. As amended, the statute (now § 743.26) also grants authority to fix electric and water rates. The Act of April 5, 1854,<sup>10</sup> provides that if an electric company or gas company assents in writing to a regulatory ordinance, the city may not require the company to furnish service at rates lower than the ones specified in the ordinance “during the period of time agreed on,” not to exceed ten years. The supreme court has held that the company’s assent, given pursuant to this section, creates a contract between it and the municipal corporation.<sup>11</sup> The Act of April 20, 1904<sup>12</sup> empowers cities to grant the use of their public ways to hot water and steam heating companies for laying conduits, and to regulate rates for hot water and steam heat. By 1911 utility service had grown into a matter of more than local concern, and the General Assembly passed the Public Utilities Act,<sup>13</sup> which established the Ohio Public Service Commission (superseded two years later by the Public Utilities Commission),<sup>14</sup> and which included the original version of § 4909.16. The same act, however, included a section to protect existing municipal regulatory powers from encroachment by the newly established state commission.<sup>15</sup> That section is now codified as § 4909.40, which reads as follows:

*Chapters 4901., 4903., 4905., 4907., 4909., 4921., 4923., and 4925. of the Revised Code do not apply to any rate, fare, or regulation prescribed by any municipal corporation granting a right, permission, authority, or franchise to use its streets, alleys, avenues, or public places for street railway purposes, or to any prices so fixed under sections 715.34, 743.26, and 743.28 of the Revised Code, except as provided in sections 4909.34, 4909.35, 4909.36, 4909.38, and 4909.39 of the Revised Code [emphasis supplied].*<sup>16</sup>

<sup>9</sup> 51 Laws of Ohio 360, 373 (1853).

<sup>10</sup> 52 Laws of Ohio 30 (1854) (now § 743.28).

<sup>11</sup> *Ohio River Power Co. v. City of Steubenville*, 99 Ohio St. 421, 124 N.E. 246 (1919).

<sup>12</sup> 97 Laws of Ohio 504, 507 (1904) (now § 715.34).

<sup>13</sup> 102 Laws of Ohio 549 (1911).

<sup>14</sup> 103 Laws of Ohio 804 (1913).

<sup>15</sup> Public Utilities Act § 49, 102 Laws of Ohio 549, 563 (1911).

<sup>16</sup> For purposes of this discussion, §§ 4909.34, 4909.35, 4909.36, 4909.38, and 4909.39, referred to in § 4909.40, may be summarized as follows. At any time within one year before the expiration of an existing contract made between a city and a gas or electric company pursuant to §§ 715.34, 743.26 and 743.28, the city may enact a new ordinance to fix a new rate for an ensuing period, pursuant to the same sections of Title 7. Within sixty days after passage of such an ordinance, the company affected may complain to the Commission. By filing its complaint the company agrees to continue serving the public during the term of the ordinance

In addition to the power to regulate utility rates unilaterally, the cities also have the power to contract for utility service. They may make contracts for gas or electric service under the Act of May 14, 1878,<sup>17</sup> and for gas and water service under the Act of May 1, 1852.<sup>18</sup> Finally, the cities have express constitutional authority to contract for all utility services under Article XVIII, § 4 of the Ohio Constitution, adopted in 1912. That section provides as follows:

Any municipality may acquire, construct, own, lease and operate within or without its corporate limits, any public utility the product or service of which is or is to be supplied to the municipality or its inhabitants, and may contract with others for any such product or service. The acquisition of any such public utility may be by condemnation or otherwise, and a municipality may acquire thereby the use of, or full title to, the property and franchise of any company or person supplying to the municipality or its inhabitants the service or product of any such utility.

The supreme court has limited the Commission's power to review the contracts between municipal corporations and utility companies upon constitutional grounds. In *Link v. PUCO*,<sup>19</sup> the city of Cleveland passed an ordinance setting a rate for steam heating service, and the company assented to the rate. A group of citizens then petitioned the Commission to investigate the reasonableness of the rate pursuant to what is now § 4909.36. Although § 4909.36 is one of the sections exempted from the restriction imposed by § 4909.40, the Commission dismissed the petition for lack of jurisdiction. The citizens appealed, and the supreme court affirmed, holding that the statute authorizing the petition was inconsistent with Article XVIII, Section 4 of the state constitution, that the company's assent to the rate fixing ordinance had created a contract protected by that section, and that the Commission therefore has no jurisdiction to review the rates set in the contract.

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complained of. The newly enacted rate takes effect notwithstanding the company's complaint, unless the company chooses to continue charging the same rate as under the expiring contract. If the Commission finds that the new ordinance would be unfair or unreasonable or would provide the company with insufficient compensation for its service, then it must fix a just and reasonable rate to remain in effect for two years or for the time of the new ordinance, whichever period is longer. Otherwise the Commission may confirm the rate fixed by the ordinance. A water company may petition the Commission to fix a rate for water service within a municipal corporation if the city fails to enact a new rate within sixty days after the expiration of the rate fixing ordinance under which the company had been serving.

<sup>17</sup> 75 Laws of Ohio 161, 354-58 (1878) (now § 743.38).

<sup>18</sup> 50 Laws of Ohio 274, 290 (1852) (now § 4933.04).

<sup>19</sup> 102 Ohio St. 336, 131 N.E. 796 (1921).

In *City of Akron v. PUCO (Akron I)*,<sup>20</sup> the city passed an ordinance to fix a natural gas rate, and the gas company accepted. Later the city asked the Commission to act under the emergency statute to set a lower rate, alleging "an emergency due to the depression." On the company's motion the Commission dismissed for lack of jurisdiction, and again the supreme court affirmed, citing *Link*. The opinion implies that the holding rests not only on Article XVIII, Section 4 of the state constitution, but also on Article II, Section 28, which forbids impairment of the obligation of contracts.<sup>21</sup>

Thus, the limitation on the Commission's emergency powers, as applicable to the alteration of municipal utility rates, is partly statutory and partly constitutional. The statutory limitation precludes alteration of prices fixed for natural gas, electricity, water, hot water or steam heat pursuant to §§ 715.34, 743.26 and 743.28. The constitutional limitation, when applicable, precludes alteration of contracts generally.

In *City of Akron v. PUCO (Akron II)*<sup>22</sup> however, the supreme court held that the constitutional limitations will not prevent the temporary alteration of express contract terms pursuant to the emergency statute where such alterations are essential to the public health and welfare. *Akron II* embodies the supreme court's broadest construction of the Commission's emergency powers. In that case, the Commission held a hearing after giving notice to every incorporated municipality and every natural gas company in the state to investigate the adequacy of the state's natural gas supply. It found that projected increased use of natural gas for heating purposes, which would exceed the companies' ability to meet the demand, would create a gas shortage for the next winter. The Commission, relying on the emergency statute, issued an order temporarily prohibiting any gas company from supplying newly installed space-heating equipment. The city of Akron appealed the Commission's order. On appeal, the city stipulated that the record

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<sup>20</sup> 126 Ohio St. 333, 185 N.E. 415 (1933).

<sup>21</sup> *Id.* at 337, 185 N.E. at 416: "[T]he state cannot extend its police powers . . . so as to interfere with vested contract rights."

Article II, Section 28 provides:

The general assembly shall have no power to pass retroactive laws, or laws impairing the obligation of contracts; but may, by general laws, authorize courts to carry into effect, upon such terms as shall be just and equitable, the manifest intention of parties, and officers, by curing omissions, defects, and errors, in instruments and proceedings, arising out of their want of conformity with the laws of this state.

<sup>22</sup> 149 Ohio St. 347, 78 N.E.2d 890 (1948).

supported the findings and order, that the state's natural gas supply would probably be inadequate to meet the coming winter's demand, and that the order was reasonable and necessary as an emergency measure to protect the public health, safety and welfare. The only issue on appeal was the city's contention that insofar as the order purported to alter service connection regulations established by contract between the city and the gas company, the order violated Article XVIII, Section 4 of the state constitution and the contract clauses of both state and federal constitutions. The court affirmed the Commission's order. It held that where the parties, one a municipal corporation and one a utility company, were both entities created for public purposes, and where their contract affected the public welfare, their contract must be construed as including all legislative regulations later adopted as essential to the health, safety and welfare of the people. Therefore, no constitutional bar to its enforcement existed where the appellant conceded that it was a necessary measure for dealing with a state-wide emergency.<sup>23</sup>

Whether, in an emergency of similar exigency and scope, the commission may alter the *price* terms of municipal utility contracts remains undecided. Dicta in *City of Cincinnati v. PUCO* may be read as supporting the position that § 4909.40 prohibits the Commission from altering rates fixed by municipal ordinance for any type of utility company specified in §§ 715.34, 743.26, or 743.28, regardless of whether the company has accepted the ordinance so as to create a contract.<sup>24</sup> The supreme court, however, has more consistently taken

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<sup>23</sup> The *Akron II* case is important in another respect. A long line of cases holds that the Commission is the legislature's creature and may exercise no powers except those delegated by statute. See *Penn Central Transp. Co. v. PUCO*, 35 Ohio St. 2d 97, 298 N.E.2d 587 (1973). Nevertheless the necessary logical implication of the holding in *Akron II* is that under the emergency statute the Commission has at its disposal implied powers not expressly conferred. The statute expressly empowers the Commission to "alter, amend, or, with the consent of the utility concerned, suspend any existing rates, schedules, or order relating to or affecting any public utility or part of any public utility in this state." Relying on the word *order*, the Commission clearly may alter temporarily any of a utility's rules and regulations which it has previously approved. But the Commission's order affirmed in *Akron II* uniformly affected the service-connection regulations of every gas company in the state, and the court never even considered whether the regulations thus affected were the subject of an "existing-order." Moreover, of all the regulations affected by the Commission's order, those which had been established by contracts between gas companies and municipalities could not possibly have been the subject of existing orders, except for regulations which perhaps had come before the Commission under §§ 4909.34, 4909.35, 4909.36, 4909.38 and 4909.39. In *Akron II*, therefore, the court's holding clearly recognizes that the Commission's jurisdiction under the emergency statute is broader than the power which the statute confers by its express terms.

<sup>24</sup> 149 Ohio St. 570, 80 N.E.2d 150 (1948). In that case a gas company complained to the Commission under what is now § 4909.34 against a newly enacted regulatory ordinance which

the position that the company's assent to a regulatory rate takes the rate out of the purely regulatory realm, in which § 4909.40 limits the Commission's emergency powers. Instead, the assent creates a contract, and the Commission's actions are governed by constitutional limitations and *Akron II*. For example, in *Akron I*, cited with approval in the *Cincinnati* case, the appellee urged the court to affirm the Commission's dismissal for lack of jurisdiction on the ground that § 614-47 (now § 4909.40) prohibited the Commission from altering the municipal contract rate, but the court said "section 614-47 is of no help in this case as we view it. It is simply a reiteration of the spirit of the Constitution." And again, "[i]f a public utility agrees to furnish its product to the municipality at the regulatory rate, and there is a meeting of the minds and an acceptance, then the regulatory rate becomes [the] contract rate," and was therefore unreviewable on purely constitutional grounds.<sup>25</sup> Likewise, in *Akron II*, without mentioning the city's statutory power to regulate rates, the court stated that the contracts between the city and the company had been made "by virtue of authority conferred by Section 4, Article XVIII of the State Constitution."<sup>26</sup> This dicta from *Akron II* is consistent with the first proposition of the syllabus in *Link*, which states:

Section 4, Article XVIII of the Ohio Constitution, is self-executing and no action of the legislature is essential to empower a municipality and a public utility company to enter into a valid contract for the product or service of such utility company to be supplied to the municipality and its inhabitants.<sup>27</sup>

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it did *not* accept, because the new rate was lower than the old. While the complaint was pending, the old rate continued in effect, beyond the expiration of the old ordinance, by operation of what is now § 4909.38. The company asked the Commission to increase *that* rate pursuant to the emergency statute, alleging financial difficulties. The Commission granted a temporary emergency rate increase, and the city appealed, arguing that what is now § 4909.40 denied the Commission jurisdiction. The court affirmed the Commission, holding that the interim rate was an existing rate fixed by operation of law, and not by a subsisting ordinance, and that it therefore lay outside the protection of § 4909.40. The court's holding expressly overrules *City of Cleveland v. PUCO*, 126 Ohio St. 91, 183 N.E. 924 (1932), thereby settling an old dispute as to whether such an interim rate is an "existing rate" within the terms of the emergency statute.

In the dictum referred to the court states that "[s]ection [4909.40] prevails and precludes the commission from exercising jurisdiction where there is a valid and operative ordinance under which a utility is furnishing its products or services to users within the municipality . . . ." 149 Ohio St. at 574, 80 N.E.2d at 152.

<sup>25</sup> 126 Ohio St. 333, 337, 185 N.E. 415, 416 (1932).

<sup>26</sup> 149 Ohio St. 347, 353, 78 N.E.2d 890, 894 (1948).

<sup>27</sup> 102 Ohio St. 336, 131 N.E. 796 (1921). *See also* *Phelps v. Logan Natural Gas & Fuel Co.*, 101 Ohio St. 145, 128 N.E. 58 (1920); *cf.* *Ohio River Power Co. v. City of Steubenville*, 99 Ohio St. 421, 124 N.E. 246 (1919).



These precedents, taken together, suggest two conclusions. First, once a utility company accepts the terms of a municipal ordinance, the rate is no longer a regulatory one "fixed under sections 715.34, 743.26, and 743.28 of the Revised Code," but is rather a rate fixed pursuant to the city's constitutional contractual powers. Second, such a rate therefore lies outside the protection of § 4909.40 and is susceptible to temporary alteration by the Commission pursuant to the emergency statute, on the authority of *Akron II* and within its limitations.

The issue of the scope of the Commission's emergency powers relative to municipal utility rate has lain dormant since *Akron II* in 1948. However, it remains an important consideration for the Commission to reckon with in fashioning regulatory policies in matters of state-wide concern requiring orders of uniform application. The issue may well arise, for example, in connection with the commission's presently effective orders for emergency curtailment of natural gas service, some of which are now on appeal before the supreme court.<sup>28</sup> On the other hand, the issue has not presented difficulty in dealing with the financial problems of particular utilities, because most municipal ordinance contracts include provisions for termination by either party upon specified notice.

#### IV. POLICY AND PRACTICES UNDER THE EMERGENCY STATUTE

From its diverse experience in administering the emergency statute, the Commission has developed certain broad policies to govern its consideration of emergency rate requests. In four emergency orders issued during the 1950's, the Commission granted emergency rate increases based on findings of rate base and rate of return, without making the extensive investigation and property valuation that would have been required if the application had been filed under

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<sup>28</sup> *Ohio Bakers Ass'n. v. PUCO*, Ohio supreme court Docket No. 75-493 (filed June 3, 1975); *Ohio Mfrs. Assn. v. PUCO*, Ohio supreme court Docket No. 75-435 (filed May 20, 1975); *Ohio Mfrs. Assn. v. PUCO*, Ohio supreme court Docket No. 75-971 (filed Oct. 14, 1975).

As this article went to press, the supreme court issued its decision in Docket Nos. 75-435 and 75-493, *consolidated sub. nom. Ohio Mfrs. Assn. v. PUCO*, 45 Ohio St. 2d 86, 341 N.E.2d 585 (1976). The appellants contended that the authority of the commission under § 4909.16 to issue orders with regard to energy emergencies was pre-empted by the legislation creating the temporary Energy Emergency Commission, which was granted overlapping authority, and that § 4909.16 was repealed by implication. The court ruled that the contention was baseless, that the authority was hierarchical, and that there was no basis for the claim of repeal by implication. The PUCO's orders in both cases were affirmed.

the regular rate-making statutes. In the first of the four cases, the Commission granted higher natural gas rates on the sole ground that the applicant's present rate of return was inadequate and would further diminish with an expected increase in the wholesale price of gas.<sup>29</sup> This is the only case in which the Commission ever found an emergency consisting solely of an inadequate rate of return; the other three similar decisions include a boilerplate finding "[t]hat from the evidence adduced at said hearing the Commission finds that the rates presently in effect provide a wholly inadequate rate of return, which will not provide sufficient revenue to enable Applicant to render reasonably adequate service at a reasonable cost."<sup>30</sup> With the inclusion of this finding, these three orders ostensibly satisfy the statutory criterion that emergency relief must be found "necessary to prevent injury to the business of interests of the public or of [a] public utility." Even so, the language of these decisions suggests that the deciding factor in each case was the applicant's percentage rate of return, and in that respect these cases are exceptional.

The Commission's policy, firmly established in later cases, has been to stress the differences between emergency rate proceedings and permanent rate cases. In a permanent rate case the applicant's rate of return is the main issue, and the Commission has to determine that issue according to the procedures specified in the regular rate making statutes. The central issue in an emergency case, on the other hand, is not rate of return, but how to protect the applicant from the injurious effects of its particular financial circumstances, so that its ability to provide adequate service will not be impaired.<sup>31</sup>

Until the last few years most emergency rate applications came from small utility companies staffed with a handful of employees and serving at most a few hundred customers. Generally, the applicant had simply waited too long to file for a permanent rate increase and

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<sup>29</sup> Lake County Gas Co., PUCO Case No. 24,030 (Aug. 3, 1953).

<sup>30</sup> Natural Gas Co. of W. Va. at 1, PUCO Case No. 24,225 (Mar. 30, 1954); Natural Gas Co. of W. Va. at 2, PUCO Case No. 24,227 (Mar. 30, 1954); Manufacturers' Light & Heat Co. at 2, PUCO Case No. 24,334 (Feb. 9, 1954). The finding in Case No. 24,225 *supra* was "wholly inadequate revenues" instead of "a wholly inadequate rate of return."

<sup>31</sup> See, e.g., Ottoville Mutual Tel. Co., PUCO Case No. 73-356-Y at 4 (Nov. 13, 1973). The Commission stated:

Before embarking on a discussion of the applicant's theory, the Commission notes that because the terms "rate base" and "rate of return" have very precise statutory meanings, such issues are properly considered in an application for a permanent rate increase filed pursuant to Section 4909.18 Revised Code and, as a general rule, have no place in the emergency case.

had suddenly found itself unable to pay its fixed charges, or even to pay its operating costs. The Commission's policy in such cases has always been to keep the applicant on its feet during the pendency of its permanent rate case by granting emergency rates high enough to stave off an operating deficit and allow it to pay the interest on its debt.<sup>32</sup> Where emergency cases have been brought by small mutual telephone companies, owned by the customers who had voted to apply for increased rates, the Commission has granted the applications in full,<sup>33</sup> or has reserved only minor issues to be heard in the concurrent permanent cases.<sup>34</sup> On the other hand, the Commission has denied relief where the applicant's accounting procedures had produced a paper deficit,<sup>35</sup> where the period of time to which the applicant's financial evidence related was unrepresentative of the applicant's operations in general,<sup>36</sup> where the evidence of record simply did not show that the applicant would be operating at a loss,<sup>37</sup> or where the applicant had requested emergency rates for the admitted purpose of recouping the losses it had incurred in a particularly bad year.<sup>38</sup> The Commission has also ruled that no emergency existed where the prospect of an operating deficit had arisen because the applicant's parent company had decided not to continue subsidizing the applicant's operations.<sup>39</sup>

The emergency application of the Ottoville Mutual Telephone Company in 1973 presented typical emergency circumstances.<sup>40</sup> The applicant was a small rural telephone company that served about 750 customers in northwestern Ohio under tariff rates that had been in force for fourteen years. Historically, the company's capital structure had been based on membership fees paid by the customer. In 1968 the management polled its subscribers and found that they favored a comprehensive service upgrade that would provide all customers with

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<sup>32</sup> Madison Water Works, Inc., PUCO Case No. 74-721-WW-AEN (Mar. 5, 1975); Minford Tel. Co., PUCO Case No. 72-800-Y (Feb. 23, 1973); Forest Hills Util. Co., PUCO Case No. 36,771-A (Sept. 29, 1970).

<sup>33</sup> Farmers Mut. Tel. Co., PUCO Case No. 74-648-Y(E) (Feb. 21, 1975); Arthur Mut. Tel. Co., PUCO Case No. 73-568-Y (Dec. 11, 1973); Ottoville Mut. Tel. Co., PUCO Case No. 73-356-Y (Nov. 13, 1973).

<sup>34</sup> Bascom Mut. Tel. Co., PUCO Case No. 74-240-Y (July 15, 1974).

<sup>35</sup> Harbor Hills Serv. Co., PUCO Case No. 75-30-WW-AEM (May 9, 1975); Madison Waterworks, Inc., PUCO Case No. 30,563 (Feb. 20, 1962).

<sup>36</sup> Howard Antle and Gene Fitch, dba Burr Oak Serv. Co., PUCO Case No. 74-317-Y (Mar. 12, 1975).

<sup>37</sup> Chocktaw Util. Inc., PUCO Case No. 74-87-Y(E) (June 7, 1974).

<sup>38</sup> Brimfield Water Co., PUCO Case No. 73-631-Y (Dec. 14, 1973).

<sup>39</sup> Valley Util. Co., PUCO Case No. 73-207-Y (Aug. 17, 1973).

<sup>40</sup> Ottoville Mut. Tel. Co., PUCO Case No. 73-356-Y (Nov. 13, 1973).

single-party service. Thereupon the company obtained a \$410,500 loan from the Rural Electrification Administration (REA) and began a construction program. In 1969 the management applied to the Commission for a permanent rate increase, but when it became apparent that much of the new construction would not be completed in time to be considered in the company's permanent rate case, the management withdrew its application. In 1971, while still operating under rates set in 1959, the company began to feel the grave effects of increased costs which were directly attributable to the capital investment required to upgrade service. These included increased taxes, increased labor and maintenance costs, and the cost of the debt which the company had assumed under its REA loan. These costs had severely weakened the applicant's financial position. In both 1971 and 1972 the applicant suffered net losses. In 1972 the company tried to extricate itself from these difficulties by borrowing an additional \$109,500 from the REA, but the company's pro forma operating statement showed that it would suffer another loss of about \$20,000 in 1973. Realizing the company's inability to meet its operating expenses and interest charges, and that its credit would probably be impaired, the management filed concurrent applications for emergency rate relief and for a permanent rate increase. In its emergency application the company asked only for an increase sufficient to provide it with funds to pay for its operating expenses and the interest on its loans until its permanent rate application could be decided. The Commission granted the application.

In so doing the commission laid down standards which it has consistently followed in subsequent requests for emergency rate relief. First, the Commission noted that in an emergency case the commission's staff does not make its own independent investigation of the applicant's financial position as it does in permanent rate cases. In the absence of such an independent analysis, the evidence submitted by the applicant must "clearly and convincingly demonstrate that a situation exists which warrants an exercise of the Commission's emergency powers." Second, the Commission said that emergency relief is a remedy "extraordinary in nature," and restated its long standing policy that emergency increases should be granted only when such relief "is the only reasonably practical mechanism available to prevent injury to the applicant utility's business and to the public interest." Third, the Commission warned that it would not permit the emergency statute to become a vehicle for circumventing the regular rate making procedures established by § 4909.18 and that

it would "look askance at emergency applications which request the identical relief sought in a [concurrently filed] permanent application . . . ." To protect the integrity of the rate-making process, the Commission said it would "fix the amount of temporary relief at the minimum level which, under the exigent circumstances constituting the emergency, will avert the impending injury to the interests of the applicant and of the public."<sup>41</sup>

The first large utility in recent years to be granted emergency rates was United Telephone Company of Ohio.<sup>42</sup> The circumstances leading to the decision are unique to the company but the facts upon which the Commission based its finding of an emergency served to pave the way for subsequent applications filed by major electric companies. United's precarious financial position developed from its 1968 merger with eight small independent telephone companies, after which the company had set about improving and extending its service with the goal of providing one-party service to all its customers. To finance necessary construction and the replacement of outdated equipment, the company had issued four bond series between 1969 and 1972 under indentures requiring that the company maintain a net income equal to two times the total annual interest on its outstanding bonds.

The Commission had set rates for United in 1970, but in 1971 the company had filed under the emergency statute for an increase, alleging that the existing rates would not yield the revenues that the Commission had found to be reasonable a year earlier. The Commission denied the emergency application but reopened the 1970 case to reconsider its decision. After a hearing, the Commission issued an order two years later that left the 1970 decision undisturbed. Five days after this decision United filed a new emergency application, alleging that rising costs had eroded its earnings in 1971 to 1973 to the point that its net income no longer met the requirements of the company's outstanding bond indentures. Without emergency rate relief, the company would be unable to issue additional bonds in order to raise capital for necessary construction and upgraded service. Moreover, its bond rating would probably decline, leading to higher interest rates on long-term debt and a higher rate of return on its invested capital. The increased cost of capital would have to be charged to the customers, but the resulting revenues would simply be

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<sup>41</sup> *Id.*, at 2-3.

<sup>42</sup> United Tel. of Ohio, PUCO Case No. 73-178-Y (Aug. 1, 1973).

absorbed in the increased cost of financing rather than being utilized to improve services. Under these circumstances, although the company had never sustained a deficit, its financial condition was still so unfavorable that injury to its business and impairment of its ability to serve the public would result unless the Commission acted. The Commission approved an emergency rate increase, reasoning that “[i]f the public must, in any case, pay a higher price for applicant’s services, the increase should be imposed now, so that it can support the additional financing which, in turn, will provide the customers with better service for their money.”<sup>43</sup> In granting the company’s application, the Commission followed the policy that was restated in the *Ottoville* order. It limited relief to “the minimum amount which, under the *exigent* circumstances constituting the emergency, will avert the impending injury to the interests of applicant and of the public.”<sup>44</sup> Accordingly, the Commission subtracted from the total additional revenues requested the amount United expected to pay in dividends to its parent company, and allowed United to collect the difference through increased rates.

In 1974, a year after the *United* decision, unprecedented inflation spawned emergency requests from six of the seven major Ohio electric companies. In the five cases in which emergency relief was granted,<sup>45</sup> the financial circumstances resembled those of *United*. In each case inflationary costs had deeply eroded the applicant’s net earnings until the company could no longer issue new bonds to finance essential maintenance and construction or to convert existing short term debt to long-term debt. One company’s bond rating had already been down-graded and the ratings of the others were due to be reviewed. In each case, the applicant had already pared planned construction to the minimum and alleged that service interruptions would become longer and more frequent. The Ohio Power Company stated that unless it proceeded with its minimum construction program, it would have to stop accepting new customers. The Ohio Edison Company showed that further construction deferrals would result in restriction of service during periods of peak load. Further-

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<sup>43</sup> *Id.*, at 5.

<sup>44</sup> *Id.*

<sup>45</sup> Columbus & Southern Ohio Elec. Co., PUCO Case Nos. 74-760-EL-AIR, 74-813-EL-AIR (Mar. 5, 1975); Ohio Edison Co., PUCO Case Nos. 73-509-Y, 73-510-Y, 73-847-Y (Feb. 18, 1975); Dayton Power & Light Co., PUCO Case No. 74-238-Y (Jan. 15, 1975); Toledo Edison Co., PUCO Case Nos. 73-706-Y, 73-905-Y, 73-906-Y (Jan. 15, 1975); Ohio Power Co., PUCO Case No. 74-580-Y (Jan. 13, 1975).

more, each company had minimized operating expenses prior to seeking emergency relief. The Dayton Power and Light Company had reduced its labor force and instituted a voluntary early retirement program. It had also instituted cost-control programs, improved its inventory controls, deferred maintenance expenditures on facilities not essential for service, reduced advertising, reduced the size of its transportation fleet, and reduced its charitable contributions. Despite such measures, costs had risen. The Ohio Power Company showed that its operating costs had increased more than seventy percent in two years. In each of these cases the Commission found, as in *United*, that emergency rate relief was the only means to insure that the applicants would be able to arrange necessary financing on reasonable terms. Accordingly, in each of the five cases, the Commission granted what it found to be the minimum amount of additional revenues that would prevent deterioration of the quality of the applicant's services. It also required that each applicant be prepared to refund with interest any additional amount which the commission might later find to be unreasonable after considering the evidence in the applicant's concurrent permanent rate case.

In three other applications filed by two major electric companies, the applicants alleged that their failure to realize authorized rates of return had reduced their ability to attract capital investment and made the acquisition of long-term debt more expensive. In those cases the Commission found that the *Ottoville* criteria had not been met and denied the applications. These decisions included the following explanation:

[W]hen considered in light of the financial difficulties facing the other major electric utilities who have been before the Commission for emergency relief in recent months, the conditions alleged in this motion, even if true, do not constitute a pressing need for temporary rate relief. Applicant is not approaching any legal limitations on its ability to issue either short or long-term debt, nor is there any expectation that [it] will be unable to issue stock on realistic terms. Thus, it is clear that the extraordinary measure of temporary rate relief is not the only practical mechanism available to applicant to obtain funds required to continue to provide adequate service. This has been an absolute requirement in all prior emergency cases and the Commission finds nothing in the instant motion which would justify a departure from this well-established precedent.<sup>46</sup>

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<sup>46</sup> Cincinnati Gas & Elec. Co., PUCO Case No. 74-845-EL-AIR, at 3 (Apr. 4, 1975); Cincinnati Gas & Elec. Co., PUCO Case No. 75-70-EL-AIR, at 3 (Apr. 1, 1975); Cleveland

The applicants had also argued that since their rates of return had fallen below the rates previously approved by the Commission, the Commission's refusal to grant emergency rate increases would amount to unconstitutional confiscation of the applicant's property. In addressing this contention, the commission had occasion to re-emphasize the essential differences between emergency rate proceedings and permanent rate proceedings.

The fact that the rate of return authorized in a prior case is not now being realized by a utility does not render the rates presently in effect confiscatory. The central concept of ratemaking theory contemplates exactly such a result. The return allowed is calculated after determining the proper level of allowable annual expenses and is fixed at a level which will permit the utility to . . . carry on its operations [successfully], assuming economical management. There is no guarantee that such a rate of return will be realized indefinitely. This provides incentive for management efficiency and is the essence of proper regulation. No due process safeguards are violated [simply] because when a utility's operations are [affected] by increasing costs of doing business beyond management's control, the company is expected to . . . come before this agency [again] for analysis of its financial condition, which is precisely what this applicant has done through its pending [permanent] application. Thus, the instant motion [requesting emergency rates] raises the issue which is, in fact, the heart of the subject matter of the permanent case.<sup>47</sup>

These denials of emergency relief demonstrate the Commission's reluctance to increase rates pursuant to its emergency authority unless the utility's ability to provide adequate service is in imminent jeopardy.

The Commission's policies governing emergency rate relief may be summarized as follows: A company's percentage rate of return is not per se an issue in emergency rate proceedings. Whether an existing rate is confiscatory must be decided under the regular ratemaking procedures that the legislature has provided for that purpose. A company's inability to meet its fixed charges or its operating expenses is grounds for requesting emergency relief, and if the Commission finds such relief appropriate it will order a rate which will enable the

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Elec. Illum. Co., PUCO Case No. 74-571-Y, at 3 (Apr. 1, 1975).

<sup>47</sup> Cincinnati Gas & Elec. Co., PUCO Case No. 74-845-EL-AIR, at 3-4 (Apr. 4, 1975); Cincinnati Gas & Elec. Co., PUCO Case No. 75-70-EL-AIR, at 3-4 (Apr. 1, 1975); Cleveland Elec. Illum. Co., PUCO Case No. 74-571-Y at 3-4 (Apr. 1, 1975).



company to meet its financial obligations and continue operations pending its permanent rate application. Even if a company's revenues cover its fixed charges and operating expenses, it may still have grounds for requesting an emergency rate if rising costs have eroded its earnings so as to render impossible the issuance of new debt and equity on reasonable terms, thus jeopardizing substantially the quality of utility service. In such a case, if the Commission finds emergency relief appropriate, it will order a rate which will allow the company to compete for new capital and will protect the quality of the company's service from further deterioration pending the company's permanent rate application. These emergency rate-making standards are now on review before the supreme court in *Amherst v. PUCO*<sup>48</sup> and *Coalition of Concerned Utility Users v. PUCO*,<sup>49</sup> and decisions in those cases may affect the Commission's practices.

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<sup>48</sup> Ohio supreme court Docket No. 75-535 (filed June 16, 1975).

<sup>49</sup> Ohio supreme court Docket No. 75-611 (filed July 7, 1975). As this article went to press, the supreme court issued its decision in this case. *Coalition of Concerned Utility Users v. PUCO*, 45 Ohio St. 2d 151, 341 N.E.2d 839 (1976). The PUCO's order granting emergency rate relief to the Columbus and Southern Ohio Electric Company was affirmed.