

**BEFORE
THE PUBLIC UTILITIES COMMISSION OF OHIO**

In the Matter of the Review of Ohio Edison)
Company, The Cleveland Electric Illuminating)
Company, and The Toledo Edison Company's) Case No. 17-974-EL-UNC
Compliance with R.C. 4928.17 and Ohio)
Admin. Code Chapter 4902:1-37.)

INITIAL COMMENTS OF THE RETAIL ENERGY SUPPLY ASSOCIATION

The Retail Energy Supply Association (RESA) offers the following comments to the Final Report of SAGE Management Consultants, LLC filed on May 14, 2018 (Sage Report).

The comments expressed in this filing represent the position of RESA as an organization but may not represent the views of any particular member. Founded in 1990, RESA is a broad and diverse group of twenty retail energy suppliers dedicated to promoting efficient, sustainable and customer-oriented competitive retail energy markets. RESA members operate throughout the United States delivering value-added electricity and natural gas service at retail to residential, commercial and industrial energy customers. More information on RESA can be found at www.resausa.org.

I. INTRODUCTION

RESA members have a unique relationship with FirstEnergy Corp., the sole shareholder of both the Ohio Companies and FirstEnergy Solutions (FES).¹ In order to offer competitive retail electric service (CRES) in the Ohio Companies' service areas, RESA members are subject to the Ohio Companies' Supplier Tariff.² FES offers CRES services in competition with RESA members. FES is also subject to the Supplier Tariff, but its affiliation with the companies that

¹ These comments generally follow the conventions used in the Sage Report to refer to FirstEnergy subsidiaries. "Ohio Companies" means Ohio Edison, Toledo Edison, and CEI, collectively.

² See Ohio Edison Co., P.U.C.O. No. S-2. All Ohio Companies operate under the same supplier tariff.

administer this tariff creates an opportunity for inside dealing and special treatment. The statutes and rules requiring electric distribution utilities (EDUs) and their affiliates to “function independently of each other” prohibit affiliated entities from acting on this opportunity.³

The Ohio Companies operate under a corporate separation plan and code of conduct that highlights the separate corporate identities of the Ohio Companies and FES. Structural separation of regulated and unregulated businesses into separate legal entities is merely a first step. Meaningful corporate separation requires structurally separate entities to also *function* independently. The Ohio Companies and FES do not function independently. They are alter egos of FirstEnergy Service Company, and the Service Company manages FirstEnergy subsidiaries for the benefit of the parent company, FirstEnergy Corp. FirstEnergy’s subsidiaries are interdependent, not independent.

The Sage Report offers a starting point for reforming the Ohio Companies’ corporate separation plan and code of conduct. While some of the specific findings are questionable, RESA agrees with the auditor’s recommendations. These recommendations, however, do not go far enough. In addition to prohibiting co-branding and co-marketing among the Ohio Companies and their affiliates with the “FirstEnergy” name and logo, the Commission should order the Ohio Companies to suspend any further sales or marketing through the Smart Mart program. The ultimate fate of that program can be decided in the context of RESA’s pending complaint.⁴

The Commission should also order a financial review to determine whether the Ohio Companies have properly charged FES for all fees payable under the Supplier Tariff. The fact that FES has been a dominant player in its affiliates’ service area, but has paid only a “negligible” amount in supplier fees, warrants further investigation.

³ O.A.C. 4901:1-37-04(A)(1).

⁴ See Complaint, Case No.18-0736-EL-CSS (filed April 25, 2018).

The Sage Report necessarily looks backward, but the Commission should also look forward. One of the primary goals of the PowerForward initiative is to create a “marketplace that allows for innovative products and services to arise organically and be delivered seamlessly to customers by the entities of their choosing.”⁵ The Commission has recognized that this sort of innovation is “more likely to succeed in the competitive marketplace than in a regulated environment.”⁶ Competitive markets and corporate separation go hand-in-hand. Competitors in the PowerForward marketplace “could include EDU affiliates with appropriate corporate separation safeguards to eliminate the possibility of competitive advantage.”⁷ The Ohio Companies have demonstrated not only the “possibility” of competitive advantage, but its inevitability when corporate separation requirements are ignored.

II. COMMENTS

The following comments should not be considered a comprehensive review of either the Sage Report or the Ohio Companies’ compliance with their corporate separation plan or code of conduct. The auditors were charged with reviewing compliance with only a fraction of the applicable rules. The auditors have made findings and recommendations, but it is ultimately up to the Commission to determine whether the Ohio Companies are in compliance. The comments below merely reflect RESA’s takeaway from the report within the confines of the limited period available to submit comments.

A. Ohio law requires structural and functional separation of EDUs and their affiliates.

All of the major EDUs in Ohio are subsidiaries of holding companies. All of these holding companies also own (or at one time owned) subsidiaries that offer competitive retail electric services. The statutes and rules governing corporate separation are intended to ensure

⁵ *PowerForward: A Roadmap to Ohio’s Electricity Future*, Public Utilities Commission of Ohio, at 9.

⁶ *Id.* at 23.

⁷ *Id.*

that suppliers affiliated with an EDU do not receive special advantages that are withheld from unaffiliated suppliers. To this end, R.C. 4928.17(A) provides:

[N]o electric utility shall engage in this state, either directly or through an affiliate, in the businesses of supplying a noncompetitive retail electric service and supplying a competitive retail electric service, or in the businesses of supplying a noncompetitive retail electric service and supplying a product or service other than retail electric service, unless the utility implements and operates under a corporate separation plan[.]

Ohio EDUs continue to enjoy a monopoly in the provision of “noncompetitive retail electric service.” The word “unless” in R.C. 4928.17(A) suggests that an electric utility may also offer “competitive retail electric service” and/or “a product or service other than retail electric service” *if* the utility implements and operates under a corporate separation plan.” But R.C. 4928.17(A) goes on to say that the corporate separation plan must be “consistent with” several requirements, including a requirement that “[t]he plan provides, at a minimum, for the provision of the competitive retail electric service or the nonelectric product or service through a fully separated affiliate of the utility[.]” R.C. 4928.17(A)(1). Thus, an electric utility *may not* offer a “competitive retail electric service” or “a product or service other than retail electric service” (which means the same thing as “nonelectric product or service”). An *affiliate* of an electric utility may offer these services, but only after the electric utility implements and operates under a corporate separation plan.

The Ohio Companies filed their corporate separation plan in Case No. 09-462-EL-UNC. The plan was approved by stipulation Case No. 10-388-EL-SSO. No amendments to the plan have been made nor any waivers granted.

The purpose of the Ohio Companies’ plan is “to ensure corporate separation of its noncompetitive retail electric service from the competitive retail electric service (and products or services other than retail electric service) offered by certain of its affiliates, and to ensure compliance with Ohio Administrative Code (O.A.C.) Sections 4901:1-37 et seq. and Ohio

Revised Code (R.C.) Section 4928.17.”⁸ Under the plan, FES “remains a separate affiliate and is marketed as such.”⁹ The plan contemplates the provision of shared services by the Service Company, with Service Company personnel designated “as either corporate support services employees, utility services employees, or competitive services employees.”¹⁰

Although R.C. 4928.17(A)(1) effectively limits an electric utility’s service offerings to noncompetitive services, the Ohio Companies’ plan allows the utilities to continue to provide “a limited number of products and services other than retail electric service pursuant to existing tariff provisions.”¹¹ These “grandfathered” products and services are described in the “special customer services” provision of the Ohio Companies’ tariff; the plan characterizes these products and services as “other utility-related services, programs, maintenance and repairs related to customer-owned property, equipment and facilities.”¹²

The plan also describes the Ohio Companies’ intention to jointly advertise and market their affiliation *with their parent company* under the “FirstEnergy” trademark.¹³ The plan does *not* authorize the utilities to jointly advertise or market with unregulated affiliates. “In order to ensure compliance with corporate separation rules and regulations the Companies do not plan to joint advertise or joint market with any unregulated competitive affiliate, and if that position changes, they will advise the Commission.”¹⁴

⁸ Application, Corporate Separation Plan, Case No. 09-462-EL-UNC (June 1, 2009) at 2.

⁹ *Id.* at 6.

¹⁰ *Id.* at 3.

¹¹ *Id.* at 6.

¹² *Id.*

¹³ *Id.* (“The Companies may use its parent company trademark “FirstEnergy” to jointly advertise and/or jointly market. For example, the parent company trademark may appear by itself, on company clothing, badges, or equipment, or it may appear along with the name of the respective operating company (see logos on Attachment 2).”

¹⁴ *Id.*

O.A.C. Chapter 490:1-37-04 proscribes rules to implement R.C. 4928.17. Electric utilities must maintain structural safeguards to ensure that separate corporate entities and employees of these entities “function independently of each other.” 4901:1-37-04(A)(1) and (3). Electric utilities and their affiliates must maintain separate accounting. *Id.* at (B). Financial arrangements among a utility and its affiliates are subject to restrictions against a utility’s assumption of the debts or liabilities of affiliate or becoming a guarantor or surety of an affiliate. *Id.* at (C) The rules also address 11 specific topics to be addressed in the utility’s code of conduct. *Id.* at (D). The Commission may order the filing of an amended corporate separation plan on its own initiative or at the request of any party. R.C. 4928.17(D).

B. The Ohio Companies do not function independently of their affiliates.

The Ohio Companies and their affiliates must “function independently of each other.”¹⁵ The Ohio Companies are affiliated by common ownership and control with, among others, FirstEnergy Corp., the Service Company, and FES. Employees of these affiliates must also “function independently of each other.”¹⁶

To “function independently,” each legal entity must act in its own best interests. The Ohio Companies must function as “wires-only” distribution utilities, ensuring adequate service at a reasonable cost. FES must function as a CRES supplier, competing in the market under the same rules applicable to RESA members. The Service Company should have no external business agenda. The Service Company “is intended to provide shared and common services to all FirstEnergy subsidiaries such as information technology, accounting, security, and the like.”¹⁷

The Ohio Companies and their affiliates are managed in a way that is directly at odds with any reasonable notion of corporate separation. Contrary to functioning “independently of

¹⁵ O.A.C. 4901:1-37-04(A)(1).

¹⁶ *Id.*

¹⁷ Sage Report at 34.

each other,” FirstEnergy subsidiaries are managed directly or indirectly by the Service Company. The Service Company does not serve FirstEnergy subsidiaries; the subsidiaries serve the Service Company. The Service Company does in fact have an external business agenda, and that agenda is to serve the interests of the parent company, FirstEnergy Corp. The parent company’s executives have a fiduciary obligation to maximize shareholder value. The parent company serves investors, *not* the Ohio Companies.

The holding company model of ownership and management is not necessarily incompatible with corporate separation. Holding companies are common in deregulated markets. But when separate subsidiaries engaged in both regulated and unregulated businesses are managed under the same umbrella, a rigorous code of conduct becomes even more important. Again, holding companies serve their public shareholders. It is in shareholder’s financial interest to privatize gains through unregulated businesses while socializing losses to ratepayers of unregulated subsidiaries. Ratepayers on the hook for “credit support” collected by the Ohio Companies and redistributed to FirstEnergy Corp. know this better than anyone.

The Sage Report explains how putting the Service Company in charge of both regulated and unregulated businesses compromises the independence of both. Leaders of both the CRES retail sales function and regulated utility operations are employed by the Service Company. “Attendance by the FES CRES retail sales executive at meetings with other Service Company executives focused on regulated utility operations is problematic. It makes separation of regulated and competitive information highly challenging.”¹⁸ The auditors characterize this management structure as “highly inappropriate.”¹⁹

Lower-level Service Company employees also routinely interact with both the Ohio Companies and FES. For example, “FirstEnergy Corp. has centralized its communications

¹⁸ *Id.* at 34.

¹⁹ *Id.*

function, including for the Ohio Companies and FES competitive retail electric service (CRES).”²⁰ A single person handles all transmission-related communications, from rebuilds and new lines to “regulatory issues such as the Ohio electric security plan” and media support for the annual FES participation in the PJM Interconnection (PJM) capacity auction.”²¹ A five-person Financial and Web Communications group handles financial communications and social media for both the utilities and FES.²² A separate five-person Customer Communications unit “manages the regulated customer communications support for the Energy Efficiency Group, the Pennsylvania Smart Meter Program, and FirstEnergy Products.”²³ Until recently, the manager of this group “personally provide[d] communications support to FES,” and a web specialist in the group is currently “focused on the FirstEnergy Products Smart Mart web presence” while also “support[ing] the FES website.”²⁴

The same executives that manage FirstEnergy Corp. also manage the other FirstEnergy subsidiaries, regulated and unregulated alike. To RESA’s understanding (and we are happy to be corrected if wrong), most if not all executives and senior managers of the major subsidiaries are Service Company employees. Because senior management wears two or more hats, it is not surprising to learn that most Service Company personnel also wear multiple hats. The Service Company has devoted a great deal of effort to blurring the distinction between the regulated and unregulated businesses it manages by stamping these businesses with the “FirstEnergy” name and logo.

²⁰ *Id.* at 91.

²¹ *Id.* at 91-92.

²² *Id.* at 92.

²³ *Id.* at 93.

²⁴ *Id.*

C. The joint use of the “FirstEnergy” name and logo confers an unfair advantage.

The Sage Report finds that FES’s former success in the CRES market “may be related to its FirstEnergy name” and the implied endorsement by the FirstEnergy Ohio Companies. The Report recommends “[r]emoving FirstEnergy from the name of FirstEnergy Solutions to eliminate affiliate bias.”²⁵ RESA agrees with this recommendation. The Companies’ approved corporate separation plan forbids them from advertising their affiliation with a CRES provider. FES is an affiliated CRES provider. As the auditors note, “it is impossible” to not make a connection between the Companies and FES due to the common use of the “FirstEnergy” name and logo.²⁶

The Companies will claim that it is not *they* who are promoting an affiliation; it is their parent company and “FirstEnergy” trademark owner who makes branding decisions, and the Companies have no control over these decisions. This argument overlooks the fact that both the Companies and their affiliates are controlled by the Service Company. The same people who make branding decisions about the Companies also make those decisions for affiliates. To the extent an affiliate is directing the Companies to brand and market in violation of their code of conduct, the Commission has authority to order the affiliate to cease the unlawful conduct. *See* R.C. 4928.18(B) (conferring jurisdiction to hear complaint for code of conduct violation by “an electric utility or its affiliate”). Moreover, regardless of who *owns* FirstEnergy’s intellectual property, the Commission can certainly restrict the *use* of that intellectual property by Commission-regulated EDUs and Commission-licensed CRES providers.

²⁵ *Id.* at 97-98.

²⁶ *Id.* at 98.

D. The Ohio Companies are unlawfully providing nonelectric products and services through Smart Mart.

FES is exiting the electric supply market. The Ohio Companies are now venturing into the competitive market for nonelectric products and services through their Smart Mart website. These products and services include “smart thermostats and smart light bulbs (with cameras, speakers, or Wi-Fi boosters)” as well as “appliance warranties and electrician referrals.”²⁷ Executives in this program tout the importance of using the FirstEnergy name with FirstEnergy Products, saying FirstEnergy is a “trusted supplier” and the “FirstEnergy brand is prominent.”²⁸

Smart Mart is the brainchild of a business unit called “FirstEnergy Products” (FEP). “FEP is not a legal entity. It is a business unit operated by the FirstEnergy Service Company (Service Company) on behalf of the Ohio Companies and other FirstEnergy utility operating companies.”²⁹ FEP “is being ramped up” and the Service Company recently “replicated the FES support model for FEP.”

As the Commission is well aware, Service Company costs are allocated to the Ohio Companies and recovered in rates. One must presume that if the Service Company is operating Smart Mart “on behalf of” the Ohio Companies, then the Service Company’s cost to operate this venture is being, or will be, recovered from ratepayers. This is a blatant and unlawful subsidy. RESA members offer or plan to offer the very same products and services. RESA members cannot compete with providers that enjoy ratepayer-funded subsidies.

The Service Company also acts as a conduit for the unlawful flow of subsidies to FES. “Retail Operations now has two clients – FES Retail Sales and FEP. The FES sales plan comes from the Vice President of FES Retail Sales and Marketing and the FEP sales plan comes from

²⁷ *Id.* at 94.

²⁸ *Id.* at 98.

²⁹ *Id.* at 65.

the Vice President of Marketing and Product Development (both vice presidents report to the Senior Vice President, Marketing and Branding).³⁰ Moreover, “this group will respond to a FES request for a product to bundle for a CRES sales offering.”³¹ This is precisely the type of inside dealing the corporate separation rules prohibit.

The Sage Report states that the Ohio Companies offer Smart Mart products and services under a tariff, but the auditors do not identify the tariff. It appears the auditors merely took the Ohio Companies at their word. The Ohio Companies’ “special services tariff,” also referenced in their corporate separation plan, does not authorize the provision of goods or services remotely resembling any Smart Mart offerings. The tariff states:

C. Special Customer Services: The Company may furnish customers special customer services as identified in this section. *No such special customer service shall be provided except where the Company has informed the customer that such service is available from and may be obtained from other suppliers.* A customer’s decision to receive or not receive special customer services from the Company will not influence the delivery of competitive or non-competitive retail electric service to that customer by the Company. Such special customer services shall be provided at a rate negotiated with the customer, but in no case at less than the Company’s fully allocated cost. Such special customer services shall only be provided when their provision does not unduly interfere with the Company’s ability to supply electric service under the Schedule of Rates and Electric Service Regulations.

Such special customer services include: design and construction of customer substations; resolving power quality problems on customer equipment; providing training programs for construction, operation and maintenance of electrical facilities; performing customer equipment maintenance, repair or installation; providing service entrance cable repair; providing restorative temporary underground service; providing upgrades or increases to an existing service connection at customer request; performing outage or voltage problem assessment; disconnecting a customer owned transformer at customer request; loosening and refastening customer owned equipment; determining the location of underground cables on customer premises; disconnecting or reconnecting an underground pedestal at customer request; covering up lines for protection at customer request; making a generator available to customer during construction to avoid outage; providing pole–hold for customer to perform some activity; opening a transformer at customer request for customer to install an underground elbow;

³⁰ *Id.* at 94-95.

³¹ *Id.* at 94.

providing a “service saver” device to provide temporary service during an outage; resetting a customer-owned reclosure device; providing phase rotation of customer equipment at customer request; conducting an evaluation at customer request to ensure that customer equipment meets standards; or upgrading the customer to three phase service.³²

The Sage Report characterizes these special services as “jobbing and contracting services.”³³

“The J&C work groups act as electrical contractors and perform customer paid work outside of their regular utility work.”³⁴ This type of work is a far cry from the products and services offered through Smart Mart. The Smart Mart goods and services unquestionably constitute “a product or service other than retail electric service,” and must therefore be offered, if at all, through a “fully separate affiliate.” R.C. 4928.17(A)(1). The EDUs may not offer these services “directly or indirectly.” *Id.* at (A).

E. The Commission should review whether the Ohio Companies appropriately charged FES under the Supplier Tariff.

The Ohio Companies’ Supplier Tariff provides standard policies and procedures for customer enrollment, billing, wholesale settlements, and other activities associated with retail energy supply. The Supplier Tariff requires CRES suppliers to pay various fees, including a \$5 switching fee for each new enrollment, a \$5 fee for responding to requests for historical usage, and a \$53 per hour fee for special services.

The Sage Report offers reason to question whether the Ohio Companies required FES to pay the same fees charged to unaffiliated CRES providers. Notwithstanding the outsized market share enjoyed by FES, the supplier fees paid by FES were “immaterial for financial reporting purposes and not listed as transactions on the Ohio Companies’ FERC Form 1s.”³⁵ Whether the

³² See Ohio Edison Company, P.U.C.O. No. 11, Original Sheet 4, Page 13 of 21, Section X.C., effective January 23, 2009.

³³ Sage Report at 65.

³⁴ *Id.* at 89.

³⁵ *Id.* at 68.

amount paid was “immaterial” does not answer whether the amount actually paid bears any relation to what should have been paid. The “highly inappropriate” relationship between the Service Company and FES deserves greater scrutiny.

III. CONCLUSION

The Commission should adopt the findings and recommendations of the Sage Report and take the additional actions requested here.

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Respectfully submitted,

/s/ Rebekah J. Glover

Mark A. Whitt (0067996)

Rebekah J. Glover (0088798)

WHITT STURTEVANT LLP

88 E. Broad St., Suite 1590

Columbus, Ohio 43215

Telephone: (614) 224-3946

Facsimile: (614) 224-3960

whitt@whitt-sturtevant.com

glover@whitt-sturtevant.com

*Attorneys for Retail Energy Supply
Association*

(All counsel consent to service by e-mail)

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing was served by electronic mail this 31st day
of December, 2018, to the following:

scasto@firstenergycorp.com
dakutik@jonesday.com
radoringo@jonesday.com
maureen.willis@occ.ohio.gov
joliker@igsenergy.com
mnugent@igsenergy.com
gkrassen@bricker.com
dstinson@bricker.com
thomas.lindgren@ohioattorneygeneral.gov

/s/ Rebekah J. Glover
One of the Attorneys for the Retail Energy Supply
Association