Due Process and the Automatic Fuel Adjustment Clause

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Notes

Due Process and the Automatic Fuel Adjustment Clause

Utility regulation and rapidly rising utility rates\(^1\) have been subjects of increasing controversy in recent years.\(^2\) One of the most controversial aspects of utility regulation is the “fuel adjustment clause,” under which utilities pass rising fuel costs to their consumers without the prior approval of the state regulatory commission.\(^3\)

The rate schedules of public utilities are ordinarily creatures of the regulatory process. Typically a state utility commission sets rates upon the basis of the utility's cost of production and investment, allowing a return on investment comparable to that earned by other businesses with corresponding risks. The determination is made on the basis of evidence presented during a public hearing, and changes in the rate schedule ordinarily cannot be made in the absence of such a hearing.\(^4\) However, a

\(^1\)In 1974 alone, electric power rates nationwide increased by an average of 55 percent. See Schiffel, Electric Utility Regulation: An Overview of Fuel Adjustment Clauses, PUB. UTIL. FORT., June 19, 1975, at 23.


\(^3\)The focus of this note is on the automatic fuel adjustment procedure that operates outside the regulatory process. This procedure allows the utility to increase rates with every billing period without any form of prior approval from the state utility commission. However, a few state legislatures or their state utility commissions have initiated fuel adjustment procedures that are subject to commission review and prior hearing, and as such, do not raise the constitutional questions which are the central subject of this note. See, e.g., IND. CODE § 8-1-2-42(b) (1976) (fuel adjustment only after prior hearing). California, Montana, New Jersey and Florida have procedures similar to that of Indiana.

States where the fuel adjustment appears to operate without a prior hearing include: Alabama, Alaska, Arizona, Arkansas, Connecticut, Delaware, District of Columbia, Georgia, Idaho, Illinois, Kentucky, Massachusetts, Nevada, New Mexico, New York, Ohio, Oregon, South Carolina, South Dakota, Vermont, Virginia, Washington and Wisconsin.

For a discussion of the operation of fuel adjustment in each state, see Trigg, Escalator Clauses in Public Utility Rate Schedules, 106 U. PA. L. REV. 964 (1958). See also 74 OP. ATT'r GEN. FLA. 309 (1974).

The fuel adjustment clause may be expressly authorized by statute. See, e.g., IND. CODE § 8-1-2-42(b) (1976). Most often, the clause is adopted by the state regulatory agency pursuant to its general ratemaking powers. See Note, The Fuel Adjustment Clause and Its Role in the Regulatory Process, 47 Miss. L.J. 502, 507 (1976).

\(^4\)There has long been uncertainty as to whether ratemaking is an exercise of state power that requires a hearing. In Morgan v. United States, 298 U.S. 468 (1936), the Supreme Court
utility with a fuel adjustment clause incorporated into its rate schedule is allowed to increase its rates without following the normal ratemaking procedures. The fuel adjustment clause, in effect, allows the rate schedule to be altered outside the administrative process and in the absence of public participation. The proponents of the automatic fuel adjustment clause maintain that it is the most efficient method of coping with rapidly increasing fuel costs. It is argued that one of the purposes of fuel adjustment is to reduce the

held that because ratemaking involves a determination of what rates are just and reasonable, the setting of rates by an administrative agency is a quasi-judicial exercise requiring a fair hearing. Morgan further held that quasi-judicial ratemaking proceedings must provide for the “taking and weighing of evidence, determinations of fact based upon the consideration of the evidence, and the making of an order supported by such findings . . . .” Id. at 480. One year later in Ohio Bell Tel. Co. v. Public Util. Comm’n, 301 U.S. 292 (1937), the Court held that because utility regulatory commissions have been delegated such broad discretionary powers in ratemaking, the fourteenth amendment requires a fair hearing to decide most ratemaking matters. Despite these two cases, several state courts have found that ratemaking is a legislative determination which does not require a public hearing. See, e.g., Wood v. Public Util. Comm’n, 4 Cal. 3d 288, 481 P.2d 823 (1971).

The most recent Supreme Court expression on the subject is found in United States v. Florida East Coast Ry. Co., 410 U.S. 224 (1973), which apparently limits the scope of Morgan. A divided Court, speaking through Mr. Justice Rehnquist, held that the Interstate Commerce Commission was not required to hold an adjudicative-type hearing prior to the fixing of railroad rates that were to be national in scope. The Court noted that the ratemaking by the Commission involved factual inferences “apparent to anyone” and that it was an exercise of “basically legislative-type judgment” not involving an adjudication of a particular set of disputed facts. Id. at 246. However, the Court did imply that any ratemaking determinations “designed to adjudicate disputed facts in particular cases” must be done pursuant to an adjudicative hearing. Id. at 245.

The setting of rates for electric utilities is distinguishable from the method that is employed to set national railroad rates. Unlike the determination of railroad rates, which primarily involves policy judgments and undisputed facts, there are numerous factual controversies surrounding the setting of utility rates, including the valuation of the utility’s investment, the various costs that are reasonably incurred to render service, and the appropriate rate of return on the investment. See generally C. PHILLIPS, THE ECONOMICS OF REGULATION (rev. ed. 1969). Because disputable facts are common to such ratemaking, the Florida East Coast decision would seem to compel an adjudicative hearing prior to setting utility rates. While the Supreme Court has not explicitly addressed this issue since Ohio Bell, this note will proceed on the assumption that ratemaking for electric utilities involves the adjudication of disputed facts, and that consequently, rates must be set pursuant to an adjudicative hearing.

A typical fuel adjustment formula may read:

Whenever the weighted average cost of fuel is greater or less than 27.0¢ per million BTU by any amount, there shall be a corresponding increase or decrease per kilowatt-hour billed at the rate of 0.0121¢ . . . for each 1.000 per million BTU departure from said standard cost, adjusted to the nearest 0.0005¢.


See note 3 supra.

It is not the purpose of this note to offer the complete set of economic justifications for fuel adjustment but rather to analyze the procedural framework for its implementation. The substantive case for fuel adjustment is adequately made elsewhere. See, e.g., Schiffel, Electric Utility Regulation: An Overview of Fuel Adjustment Clauses, PUB. UTIL. FORT., June 19, 1975; Trigg, Escalator Clauses in Public Utility Rate Schedules, 106 U. Pa. L. Rev. 964 (1958).
number of costly formal rate hearings\(^8\) and to meet the adverse economic incidents of "regulatory lag."\(^9\)

The use of the fuel adjustment clause has not escaped criticism. It is argued that the use of the fuel adjustment clause functions as a disincentive to the economical operation and purchase of fuel supplies by the utility since it may fully recover any costs it incurs.\(^10\) Other criticisms of the fuel adjustment clause are that it represents an abdication of the state's regulatory function,\(^11\) has an inflationary effect upon the economy, results in undesirably frequent changes in the rate schedules, ignores other ratemaking factors, such as competition and public benefit, usually considered by a utility commission in setting rates, and segregates and emphasizes one factor in ratemaking while ignoring possible savings and efficiencies that may have occurred in other portions of the utility's operation.\(^12\) A final criticism, the focus of this note, is that the increase in rates without a hearing violates the consumers' right to a prior hearing as guaranteed by the due process clause of the fourteenth amendment.\(^13\)

**The Property Interest**

The initial question is whether the due process clause has any relevance to the adjustment of utility prices. The requirements of procedural due


> When prices are rising, the time that necessarily elapses between the date when earnings fall below the permissible minimum rate of return and the date when the commission enters its order allowing increased rates, is a time which the utility earns less than a fair and reasonable return.

> The inevitable delay between the happening of an event that entitles a party to legal relief and the date when he gets relief makes it impossible in some kind of cases for law and equity to do complete justice.

\(^10\) This argument is based on the assumption that since the utility is allowed to pass on the total cost of fuel automatically, utilities may purchase expensive fuel or allow its procurement expenses to increase without corresponding decreases in profits. It assumes that the fuel adjustment clause allows the utility to operate on a "cost-plus" basis insulating the utility from normal business risks by shifting all the risks of utility business onto the consumer. See *The Fuel Adjustment Capers*, 39 Consumer Rptr. 836, 839 (1974).

\(^11\) The use of automatic fuel adjustment delegates ratemaking power to private parties; delegation of power to private bodies who may exercise that power to their own advantage has been found to be constitutionally objectionable. See, e.g., *Carter v. Carter Coal Co.*, 298 U.S. 238 (1936); *Blementhal v. Board of Medical Examiners*, 57 Cal.2d 228, 368 P.2d 101 (1962); *State v. Allstate Ins. Co.*, 231 Miss. 869, 97 So.2d 372 (1957).

\(^12\) The constitutionality of this delegation to utilities is beyond the scope of this note; for a survey of the constitutional issues raised by delegation to private parties, see Liebman, *Delegation to Private Parties in American Constitutional Law*, 50 Ind. L.J. 650 (1975).

process apply only to deprivations of interests encompassed by the fourteenth amendment's protection of "liberty and property." Before a due process analysis may properly proceed, it must be determined whether utility consumers have a cognizable "property" interest in anything affected by the use of the fuel adjustment clause.

Recent doctrinal developments demonstrate that the concept of property is no longer confined to the traditional categories of "real estate, chattels, or money." Today the concept of property encompasses such varied interests as "reasonable expectations," statutory rights, the pursuit of a trade, educational benefits and the use of property. However, to have a cognizable property interest the individual must have "more than an abstract need or desire for it;" one must also have a "legitimate claim of entitlement to it."

One source of cognizable property interests to which a person may claim entitlement is a state statute conferring valuable social benefits. As part of their regulatory schemes most states have enacted statutes which guarantee to the utility consumer the right to fair and reasonable utility rates. The increase in rates by the use of the fuel adjustment clause

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reside. No State shall make or enforce any law which shall abridge the privileges and immunities of citizens of the United States; nor shall any State deprive any person of life, liberty, or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws.

14See, e.g., Board of Regents v. Roth, 408 U.S. 564, 569 (1972).
15The standard for determining the existence of such an interest was set out in Board of Regents v. Roth:
16But, to determine whether due process requirements apply in the first place, we must look not to the "weight" but to the nature of the interest at stake. We must look to see if the interest is within the Fourteenth Amendment's protection of liberty and property.
408 U.S. at 570-71 (emphasis in original).
17Id. at 572.
20See Goldsmith v. United States Bd. of Tax Appeals, 270 U.S. 117 (1926) (right of a certified public accountant to practice before the Board of Tax Appeals); Freitag v. Carter, 489 F.2d 1377 (7th Cir. 1973) (right to obtain a chauffeur's license); Hornsby v. Allen, 326 F.2d 605 (5th Cir. 1964) (right to obtain a retail liquor license to sell).
23Board of Regents v. Roth, 408 U.S. 564, 577 (1972).
24Id.
FUEL ADJUSTMENT CLAUSE

involves state action\textsuperscript{26} that may adversely affect these important statutory rights. Specifically, the mistaken, unjustified or fraudulent application of the fuel adjustment clause\textsuperscript{27} to raise the consumers' utility rates has the effect of forcing them to pay "unfair and unreasonable" rates\textsuperscript{28} in degradation of their property interest in fair and reasonable rates.

The due process clause has been often used to protect against the wrongful deprivation of state statutory benefits. In Goldberg v. Kelly\textsuperscript{29} the Supreme Court held that welfare recipients were entitled to a hearing before termination of welfare payments despite the fact that the recipients had not shown that they were in fact entitled under the statute to the payments.\textsuperscript{30} The Court held that the due process clause demands a predeprivation hearing at which the welfare recipient is given an opportunity to demonstrate his entitlement under the statute. An analogous situation is the consumer faced with an increase in utility rates by the use of the fuel adjustment clause. As the welfare recipient must be afforded the opportunity to demonstrate misapplication of state power in denying a statutory benefit, the utility consumer must be afforded the opportunity to

\textsuperscript{26}In Jackson v Metropolitan Edison Co., 419 U.S. 345 (1974), the Supreme Court held that the termination of utility service without notice and a hearing for nonpayment of service is not "state action" giving rise to a cause of action under 42 U.S.C. § 1983 (1970). However, the Court noted that when dealing with an exercise of power which traditionally has been associated with the state, a finding of state action will be appropriate. Id. at 352-53. Ratemaking, unlike the termination of utility services, has long been viewed as a state legislative function which may be delegated and as being subject to the limitations of the due process clause. For early expressions of this principle, see Brass v. North Dakota ex rel. Stoeser, 153 U.S. 391 (1894); Budd v. New York, 143 U.S. 517 (1892); Munn v. Illinois, 94 U.S. 113 (1877).

In Jackson, the Court further indicated that a utility practice may be state action if the state puts its "own weight on the side of the proposed practice by ordering it." 419 U.S. at 537. The use of the fuel adjustment clause is ordinarily ordered by the state utility commission. For examples of such orders, see In re Southern Cal. Edison Co., 94 P.U.R. 3d 252 (Calif. 1972); In re Green Mountain Power Corp., 94 P.U.R.3d 417 (Vt. 1972); In re Potomac Elec. Power Co., 84 P.U.R.3d 250 (D.C. 1970).

Finally, because Jackson involved the actions of privately owned utility company, its holding is doubly inapposite to those publicly owned utilities which operates with a fuel adjustment clause. Cf. Craft v. Memphis Light, Gas & Water Div., 534 F.2d 684 (6th Cir. 1976) (publicly owned and operated utility must meet requirements of the due process clause before terminating service to a customer).

While the typical application of the fuel adjustment clause is neither fraudulent, mistaken or unjustified, the potential for abuse clearly does exist where power may be executed for one's own advantage. It is precisely the prevention of those possible abuses that the due process clause seeks to ensure. See Rendleman, The New Due Process: Rights and Remedies, 63 Ky. L.J. 531, 556 (1975).

An increase in utility rates via the fuel adjustment cause not prompted by a commensurate increase in the cost of fuel or by an inflationary adjustment is "unfair and unreasonable" in that the marginal revenues generated by the fuel adjustment surcharge do not absorb increased fuel costs but rather increase the net revenues of the utility, inflating the reasonable rate of return allowed the utility by the state regulatory commission.

\textsuperscript{29}937 U.S. 254 (1969).

\textsuperscript{30}Id. at 267. See also Bishop v. Wood, 426 U.S. 341 (1976) (city ordinance may create property interest within the meaning of the fourteenth amendment).
demonstrate that the proposed increase in rates is unjustified and deprives him of his statutory interest in fair and reasonable utility rates.

Recent limitations on the Goldberg doctrine indicate that the right to a hearing is illuminated by reference to the state statutory framework which created the property interest and particularly by any accompanying statutory language which prescribes the manner in which the interest is to be protected or terminated. The consumer interest in fair and reasonable rates has typically been created by statute, incident to a general scheme of regulating utilities and their rates. While these statutes generally do not explicitly address the use of the fuel adjustment clause, they do provide that utility rates are to be set pursuant to a hearing. The fact that the entitlement to fair and reasonable rates was created incident to a regulatory scheme which generally prescribes some form of hearing prior to the adjustment of utility rates would indicate that the property interest created is to be adjusted only incident to such a hearing.

The consuming public's legal standing with respect to the rate schedule should not differ significantly from that of the utility's stockholders. It is well settled that the utility has a constitutionally cognizable property interest in the rate schedule which is protected under the due process clause. Since consumers and utilities continue to be viewed as "adversaries" for the purpose of ratemaking, it would be anomalous to consider the utility's interest in rate schedules as "property" but to treat the consuming public's interest in that same rate schedule as something less than property. Furthermore, the interest in fair and reasonable rates is comparable to the statutory right to continued utility service, an interest

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32 See note 3 supra.
33 See note 25 supra & text accompanying.
34 The Supreme Court in Bishop v. Wood, 426 U.S. 341 (1976), adopted the view that while a state may create a property interest, it may also prescribe and limit the procedural incidents which safeguard that property interest. Bishop is inapposite to the adjustment of utility rates by fuel adjustment clause because, unlike the statutory right involved in Bishop, the statutes creating the entitlement to fair and reasonable rates are not expressly conditioned by any procedural limitations. See note 25 supra. Nor can the utility commission limit the property right created by the state legislature by adopting limited procedural rights without explicit statutory authority from the state legislature. Cf. Kent v. Dulles, 357 U.S. 116 (1958) (administrative power to adjust constitutional interests cannot be implied).
35 Because ratemaking may reduce the value of the utility's property, the Fourteenth Amendment protects the utility's interest in the adjustment of rates. See, e.g., Mississippi Power & Light Co. v. Jackson, 9 F. Supp. 564 (S.D. Miss. 1935) (notice and hearing must be given to the utility before any change in rates); Georgia Power & Light Co. v. Georgia Pub. Serv. Comm'n, 8 F. Supp. 603 (W.D. Ga. 1934) (unreasonable reduction of utility's rate of return is denial of property without due process).
36 At least one court has recognized the argument for similar treatment of the utility and the consumer in ratemaking: It might be urged with some realism on the side of the consumer that unreasonableness of an order or rate means also one that is confiscatory as to the rate payer who is forced to pay a rate which is excessive, extortionate or beyond the value
which has also been found by several courts to be "property" for due process purposes.\textsuperscript{37}

The judicial proclivity to label an interest as property has not been immune to considerations of public policy.\textsuperscript{38} It is certainly proper to inquire whether the interest sought to be brought within the ambit of the fourteenth amendment is so important that some form of hearing should be granted to protect against wrongful deprivation. Here the right to fair and reasonable utility rates as guaranteed by statute seems no less important than many of the other interests that have been afforded due process protection by the courts.\textsuperscript{39} Clearly the fact that utility service has become a necessity of life for the American consumer is relevant.\textsuperscript{40} The relative importance of fair and reasonable utility rates becomes even more striking when the cost of utility service is measured against other household expenditures. In 1974 the average household spent over six percent of its budget on utility services;\textsuperscript{41} by 1980 utility expenditures in the United States are expected to reach over $150 billion annually.\textsuperscript{42} Control over such

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of the service rendered . . . . Under such a rationale the Commission is bound at the extremes on each side (the rate payer and the utility) by constitutional safeguards against confiscation, \textit{thus giving each the same standards and safeguards.} Public Serv. Comm'n v. Indianapolis, 235 Ind. 70, 85 n.1, 131 N.E.2d 308, 514 n.1 (1956) (emphasis in original).
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The Supreme Court has refrained from deciding whether a claim to continued utility service is property for due process purposes. See Jackson v. Metropolitan Edison Co., 419 U.S. 345, 359 (1974).

\textsuperscript{3}See, e.g., Lines v. Fredricks, 400 U.S. 18 (1970), where the Court refused to label a bankrupt's unpaid vacation pay as "property" under the Bankruptcy Act and thereby to force the bankrupt to turn over the vacation pay to the trustee in bankruptcy. In allowing the bankrupt to retain the pay the Court sought to pursue a policy which gives the bankrupt a "new opportunity in life and [a] clear field for future effort, unhampered by the pressure and discouragement of preexisting debt." \textit{Id. at 20.}

See also, Rendlemann, \textit{The New Due Process: Rights and Remedies}, 63 Ky. L.J. 531, 558-59 (1975): "In dealing with questionable or hazy state property interests, the social welfare purpose is an analytical variable with a sounder basis in reality than chameleon conclusions like possession."


enormous expenditures cannot, consistently with sound public policy, escape the protections of the fourteenth amendment.  

Admittedly, concluding that consumers do have a cognizable property interest in the utility rate schedule is not without conceptual difficulty. However, by focusing on the state guarantees of fair and reasonable utility rates and acknowledging the relative importance of utility service in the modern context, the reach to the protections of the due process clause is not strained.

**How Much Due Process Is Due?**

Once it is established that a cognizable property interest is affected, the next determination concerns the specific procedures required to protect the consumers' right to fair and reasonable rates. In making that determination the focus turns to three factors: the severity of loss incident to the deprivation of fair and reasonable rates, the weight of governmental and producer interests justifying either no action or summary action and the "functional appropriateness" of the procedure for protecting the consumers' interests.

The impact upon the consumer from paying excessive utility bills undoubtedly can be severe. Not only does the excess payment divert income from the purchase of other necessities, but the additional cost increases the probability that the consumer will not be able to pay the

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4See generally Reich, New Property, 73 YALE L.J. 733 (1964).
4Four federal district courts have faced this issue squarely and have unanimously resolved that the consumer has no property right in existing rate schedules. See Georgia Power Project v. Georgia Power Co., 409 F. Supp. 332 (N.D. Ga. 1975); Hartford Consumer Activists v. Hausman, 381 F. Supp. 1275 (D. Conn. 1974); Sellers v. Iowa Power & Light Co., 372 F. Supp. 1169 (S.D. Iowa 1974); Holt v. Yonce, 370 F. Supp. 374 (D.S.C. 1973), aff'd sum., 415 U.S. 969 (1975). The courts were also unanimous in their failure to consider the statute as a source of property interests and in their failure to consider the increasing importance of utility service to the modern household.

The four holdings may be inappropriate for present analysis because they involved consumer challenges to the practice of granting interim rate increases pending a full hearing on the merits for the rate increases. For the purposes of the due process clause, the critical difference between the interim rate increase and the fuel adjustment clause is that in the former the full hearing for the consumer is merely delayed, whereas by the nature of the automatic fuel adjustment clause the consumer never gets his "day in court."

4Courts now routinely look to the potential harm to the individual as an initial measure of the types of procedural protections that must be afforded the individual. See Mitchell v. W.T. Grant Co., 416 U.S. 600 (1974); Bell v. Burson, 402 U.S. 555, 540 (1971) ("procedures adequate to determine a welfare claim may not suffice to try a felony charge").


4See generally Note, Specifying the Procedures Required by Due Process: Toward Limits on the Use of Interest Balancing, 88 HARV. L. REV. 1510 (1975).
monthly bill, thereby subjecting him to the termination of an indispensable utility service. The potential harm, however, is probably not as severe as the near total deprivation of household income that was threatened in Goldberg v. Kelly and in Sniadach v. Family Finance Corp. Consequently, the due process model may demand fewer procedural safeguards in fuel adjustment cases because greater weight will be accorded to the countervailing state interests in bypassing the normal panoply of procedural protections.

The state evidences two distinct objectives in the continued use of the fuel adjustment clause. First, the state utility commission manifests a concern for the interests of that state’s utilities in whose financial stability the public has a vital stake. The “market” demands that the utility companies be allowed to increase their prices as their costs of production increase, thereby maintaining a reasonable rate of return on the shareholder's investment even in times of inflation. A utility facing net revenue erosion from increased fuel costs is not an attractive investment or market risk. Declining utility profits hinder the procurement of the vast sums of equity and debt financing necessary for the maintenance and expansion of the utility's power systems. Diminishing profits also adversely affect the utility's credit ratings, which in turn increase the cost of the financing which is available. These increased costs are eventually borne by the consumers in the form of higher utility rates. Hence, by ordering the use of the fuel adjustment clause, the state is attempting to protect the financial integrity of the utility in order to insure the longrun maintenance of the state's utility delivery system at the lowest cost to the consumer.

While termination procedures vary considerably among utilities, the usual practice is that the consumer's service must be terminated eventually if his account remains in arrears. See Shelton, The Shutoff of Utility Services for Non-Payment, 46 WASH. L. REV. 745 (1971). Nor is the consumer entitled to a hearing before his service is terminated. Jackson v. Metropolitan Edison Co., 419 U.S. 345 (1974).

Sniadach held that a debtor's wages could not be garnished in the absence of procedures consistent with the due process clause because such garnishment imposes a "tremendous hardship on wage earners with families to support." Id. at 340.

Although the “balancing test” articulated in Sniadach and Goldberg has been somewhat limited by the later analysis in Board of Regents v. Roth, 408 U.S. 564 (1972), and Fuentes v. Shevin, 407 U.S. 67 (1972), the state's interest in relieving itself of administrative burdens necessarily enters into the analysis. See Note, Specifying the Procedure Required by Due Process: Toward Limits on the Use of Interest Balancing, 88 HARV. L. REV. 1510 (1975). See also Matthews v. Eldridge, 424 U.S. 319, 335 (1976) (due process analysis requires consideration of fiscal and administrative burdens that the procedural requirement would entail).


Second, the use of the fuel adjustment clause also helps to minimize state administrative burdens. Given the frequent adjustment in rate schedules associated with rapidly rising fuel prices, formal ratemaking hearings in place of the automatic adjustments would probably require most states to expand their utility regulatory staffs. Where the fuel adjustment clause operates outside the regulatory process, its use cuts regulatory expenses and decreases the frequency with which both the state and the utility must prepare for the more expensive formal rate proceedings.

To suggest that the state has an interest, even a strong interest, in the continuation of the fuel adjustment clause outside the regulatory process is not, of course, dispositive of the consumer's due process interests. Substantive and administrative interests of a state in the maintenance of a given procedure are not sufficient justifications for failing to provide a hearing on matters of such importance to the individual; the weight of state interests merely shapes the form that the hearing will take. What the fourteenth amendment demands is that the state provide a procedural model that is functionally appropriate for protecting the legitimate interests of the individual and that accommodates governmental interests without sacrificing the individual's "day in court." The procedure suggested below seeks to find that balance.

A SUMMARY HEARING MODEL

The consumer's interest in the ratemaking process is limited to insuring that only fair and reasonable rates are maintained by the utility and the state. Only if the fuel adjustment is mistakenly or fraudulently

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57 Cf. Stanley v. Illinois, 405 U.S. 645 (1972) (administrative convenience alone does not justify an irrebuttable presumption); Reed v. Reed, 404 U.S. 71 (1971) (statutory preference of a class of persons in order to eliminate the need for a hearing is the type of arbitrary legislative choice forbidden by the fourteenth amendment).
58 The lesson of Mitchell v. W.T. Grant Co., 416 U.S. 600 (1974), and Fuentes v. Shevin, 407 U.S. 67 (1972), is that absent "unusual or emergency circumstances" the determination as to the necessity of the change in status quo must be made incident to a hearing. It is unlikely that the steady inflation of fuel costs creates such an emergency as to justify the abandonment of the administrative process. The justification for wholly summary action lies in the necessity to act immediately, and its use has been limited to prevention of such evils as epidemics, distribution of putrid foods or adulterated drugs, the sale of worthless securities and the conduct of bank officers which might jeopardize the interests of depositors. See Freedman, Summary Actions by Administrative Agencies, 50 Ctr. L. Rev. 1 (1972). When the utility faces an actual emergency because of a sudden erosion of its profits due to increased costs, most states have provided a special procedure for interim relief where rates are increased pending a full hearing on the merits. See, e.g., Ind. Code § 8-1-2-113 (1976). Yet even the change of rates in an "emergency" is not immune to the requirements of an adequate hearing. Public Serv. Comm'n v. Indianapolis Rys., 225 Ind. 30, 72 N.E.2d 434 (1947). For the distinction between fuel adjustment and interim rates as it affects the due process analysis, see note 44 supra.
59 See notes 27-28 supra & text accompanying.
applied by the utility can unfair and unreasonable rates result from its use. Consequently, the consumer’s interest is adequately protected by insuring that no mistake or fraud occurs in the fuel adjustment clause.\textsuperscript{60}

The procedural device necessary to prevent the evils of mistake and fraud is the pre-rate increase hearing before the state utility commission, limited in scope to the sole issue of fuel cost adjustment.\textsuperscript{61} The hearing should be held on the record after notice and an opportunity for participation has been given to all interested parties. The opportunity for participation means that the consumer or his representative should be given the right to inspect the evidence offered by the utility and to cross-examine the witnesses of the utility. The opportunity to cross-examine the utility witnesses could expose any attempt by the utility to misuse the fuel adjustment process by purchasing fuel from a subsidiary at an artificially high price and then attempting to pass that price on the consumer. Cross-examination would also reduce the utility’s opportunity to pass improper, extraneous costs that were not intended to be incorporated into the fuel adjustment process.\textsuperscript{62} Concomitantly the consumer must be allowed to offer evidence in rebuttal or in explanation of his interest.\textsuperscript{63} Resort to these devices should decrease the possibility that error will occur in the use of the fuel adjustment clause to increase utility rates.\textsuperscript{64}

**CONCLUSION**

The due process clause protects not only traditional property interests but also shelters modern interests and rights that are valuable to the individual. Given the growing importance that utility service plays in the American household, the statutory right to fair and reasonable utility rates is no less deserving of procedural protection than many of the consumer

\textsuperscript{60}See notes 48-49 \textit{supra} & text accompanying.

\textsuperscript{61}The Indiana legislature, in response to criticism of the automatic nature of the fuel adjustment clause, amended the regulatory procedure to require summary hearings before the fuel adjustment rate becomes effective. Before the hearing the public counselor is empowered to examine the books of the petitioning utility and oppose any increase thought to be unjustified. Presumably a consumer may participate in the summary hearings. \textit{See Ind. Code} § 8-1-2-46(b) (1976). There is no requirement that a record of the proceeding be kept.

\textsuperscript{62}For example, in 1974 one electric utility used the automatic fuel adjustment procedure to improperly pass on $1.8 million of expenses. \textit{See} Schiffel, \textit{Electric Utility Regulation: An Overview of Fuel Adjustment Clauses}, PUB. UTIL. FORUM., June 19, 1975, at 27. Had a hearing been held prior to the adjustment of the rates, the utility commission could have discovered that the utility was improperly passing on costs other than those incurred for fuel.


\textsuperscript{64}It has been a long-standing judicial assumption that this model of fact-finding is the superior form of ascertaining the truth and reducing the incidence of error. Fuentes v. Shevin, 407 U.S. 67 (1972); \textit{Joint Anti-Fascist Refugee Comm. v. McGrath}, 341 U.S. 123, 160-84 (1951) (Frankfurter, J. concurring).

For a complete discussion of the values served by adversary hearings, see Kadish, \textit{Methodology and Criteria in Due Process Adjudication—A Survey and Criticism}, \textit{66 Yale L.J.} 319 (1957).
interests which have found constitutional protection in Goldberg v. Kelly and its progeny. Accordingly, before utility rates may be increased consistent with the limitations of the due process clause, the consumer or his representative must first be provided with the opportunity to challenge the increase.

It is quite likely that with the frequent need to resort to fuel adjustment, very few consumers will avail themselves of the opportunity to challenge their public utility in such a proceeding. Consumers, however, are not without their representatives in utility matters. The public counselor, the state attorney general's office, large industrial consumers and public interest groups are all potential participants in the fuel adjustment hearings. Moreover, the mere fact that one may choose not to exercise procedural protections afforded by the due process clause is no justification for withholding the opportunity to exercise those rights. Furthermore, the possibility that the utility may be called upon to support the increase in rates factually and may be subject to cross-examination will induce it to come prepared to offer the most accurate and complete information available concerning changes in the cost of fuel, regardless of the fact that consumer participation is not routine.

Requiring summary hearings before allowing rate changes caused by fuel cost increases does not interfere with the promotion of the governmental interests discussed earlier. Legitimate increases in fuel costs continue to be passed to the consumer with only a short delay caused by the hearing. The financial integrity of utilities will not be undercut by this

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66 Given the number and diversity of the consumer's interests in other goods and services, it is unlikely that the monthly adjustment of rates, to which the consumer may have already become "desensitized," will generate sufficient concern to mobilize him to participate in the hearing. But even assuming that some consumers will be so motivated, they likely will lack the requisite expertise for participation in the hearing in a meaningful fashion. To effectively cross-examine the utility witness, one must be conversant with accounting principles as well as be capable of reading and understanding fuel purchase contracts. Further, the likelihood of individual consumer participation is diminished by a cost barrier to the extent that effective participation requires the employment of any attorney or an accountant.


68 The attorney general's office in a number of states has been active in proceedings before the state utility commission. See, e.g., Florida ex rel. Shevin v. Yarbrough, 257 So.2d 891 (1972); In re Massachusetts Elec. Co., 12 P.U.R.4th 65 (Penn. 1975).

69 Because rate hikes increase their cost of production, many industrial users or their associations have opted to oppose rate increases. See, e.g., In re Southern Natural Gas Co., 12 P.U.R.4th 119 (F.P.C. 1975); Ex parte Alabama Textile Mfrs. Ass'n, 238 Ala. 228, 215 So.2d 447 (1968); In re Michigan Power Co., 12 P.U.R.4th 139 (Mich. 1975).

70 For examples of consumer group participation in rate proceedings, see Citizens for Allegan County v. FPC, 414 F.2d 1125 (D.C. Cir. 1969); In re Southern California Edison Co., 100 P.U.R. 3d 257 (Calif. 1973); In re Consolidated Edison of New York, Inc., 8 P.U.R. 4th 475 (N.Y. 1975) (over twenty interest groups intervening).

71 See text accompanying note 56 supra.
delay of a few days or weeks. While the hearing undoubtedly will add administrative expenses, the fact that the hearings are summary in nature and limited in scope to a single issue should keep the incremental costs minimal.

In assessing the costs and benefits associated with the procedure one must also consider the manner in which the procedure advances the integrity of the administrative process. Any increase in utility rates in the absence of an opportunity for participation by the public or of scrutiny by the state commission that was established to regulate utility matters offers an appearance of unfairness. This abdication of public control over utility rate increases certainly raises fears that the power to set utility rates will be exercised not in the public interest, but rather in the private interests of the utility. In fact, such criticisms and suspicions have been suggested by actions taken by consumer groups and the Federal Trade Commission. Although the continued adjustment of rates in response to

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72 The adverse effect of regulatory lag is most acute where the cost of production is rising rapidly and it is months or years before a new rate schedule is approved by the utility commission to reflect the changed economic circumstances. Most commissions cushion the rate schedule so that the utility may incur increased costs for a short period before its earnings will fall below the market's minimum permissible rate of return. Hence, while the short delay may erode the commission approved rate of return, the utility's earnings should not fall significantly before rate relief via the fuel adjustment procedure is approved.

73 Although the continued adjustment of rates in response to

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74 Unlike other administrative contexts in which the introduction of the due process model would be novel, state utility commissions have long operated in a framework of procedural due process in ratemaking. Hence, due process in fuel adjustment will not import the costs of unfamiliarity. The administrative cost argument is further undercut by the fact that utility regulatory costs are generally borne by the consumers—the very class that benefits from the process. For example, the costs of utility regulation in Indiana are financed by a special fee assessed against the utilities operating within the state. The fee is an operating expense that is recovered by the utility through higher rates. IND. CODE § 8-1-6-1 (1976).


76 On the responsibility of the state utility commission to pursue the public interest, see J. BONBRIGHT, PRINCIPLES OF PUBLIC UTILITY RATES 26-41 (1961).

77 See 1 F. COOPER, STATE ADMINISTRATIVE LAW 84 (1960).

78 A leading consumer periodical has expressed concern that the fuel adjustment clause is being used by some utilities to buy fuel from themselves at artificially high prices and to pass those prices on to the consumer, thereby making an extra profit through a fuel supplying subsidiary not subject to regulation. The Fuel Adjustment Caper, 39 CONSUMER REP. 837 (1974).

The Federal Trade Commission has begun a "secret" investigation of the use of the fuel adjustment clause. The Commission has subpoenaed considerable information from nine utilities concerning:

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the structure, operations, and effect of a fuel adjustment clause including information on sales, or negotiations for sales of fuel to utilities, purchases or negotiations for purchase of fuel by utilities, ownership of fuel reserves and production facilities by a utility, and all related matters for the purpose of the
fuel cost changes serves the public interest, the benefit will be lost if the public, believing that utilities are misusing the fuel adjustment clause, successfully force legislation which would prevent its use. While there is little evidence to suggest that the fuel adjustment clause has, in fact, been misused by any utility, it is the potential for misuse that generates the concern. The use of pre-rate increase hearings in connection with fuel adjustment should alleviate many of these concerns and thereby serve to enhance the integrity of the administrative process by restoring public confidence in the procedure used to increase utility rates. If the state utility commissions expect, as they must, to allow utility rates to rise in response to continued inflation and capital expansion, it is imperative that the public maintain confidence in that administrative process.

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development of a comprehensive study of the energy industry.

PUB. UTIL. FORT., Feb. 27, 1975, at 14.

See text accompanying notes 53-57 supra.

Senator Lee Metcalf, a long time critic of the fuel adjustment clause, has proposed legislation to prohibit its use by state regulatory commissions. A bill to restrict the use of fuel adjustment clauses was also put before the Indiana legislature. See INDIANA SENATE JOURNAL 125 (1972).

Potential "misuses" include inadvertent miscalculations of fuel costs which generate a surcharge in excess of the incremental fuel costs to the utility, intentional misrepresentations of the cost of fuel and inclusion of extraneous items in the fuel adjustment clause. See Schiffel, Electric Utility Regulation: An Overview of Fuel Adjustment Clauses, PUB. UTIL. FORT., June 19, 1975, at 27.

The decision to implement fuel adjustment is made in an institutional context and consequently is not immune to the observation that decisionmaking is often infected with bias or at least the appearance of bias arising from the particular institutional structure. See McCormack, The Purpose of Due Process: Fair Hearing or Vehicle for Judicial Review?, 52 TEXAS L. REV. 1257 (1974).

The emergence of individuals and groups willing to assist administrative agencies in identifying interests deserving protection, in producing relevant evidence and argument suggesting appropriate action, and in closing the gap between the agencies and their ultimate constituents presents an opportunity to improve the administrative process.

Gelhorn, Public Participation in Administrative Proceedings, 81 YALE L.J. 359, 403 (1972).

That the administrative agency is less effective when it lacks public confidence is the conclusion of more than one student of administrative agencies. See, e.g., Freedman, Crisis and Legitimacy in the Administrative Process, 27 STAN. L. REV. 1041 (1975).