

UNREPORTED
IN THE COURT OF SPECIAL APPEALS
OF MARYLAND

No. 2228

September Term, 2013

WASHINGTON GAS ENERGY SERVICES

v.

MARYLAND PUBLIC SERVICE COMMISSION

Eyler, Deborah S.,
Berger,
Sharer, J. Frederick
(Retired, Specially Assigned),

JJ.

Opinion by Berger, J.

Filed: December 30, 2014

In 2010, the Maryland Public Service Commission (“the Commission”) established the Purchase of Receivables (“POR”) program. Under the POR program, a utility such as Baltimore Gas and Electric (“BGE”) purchases a supplier’s receivables, which are amounts due to the supplier for electric or gas usage by the customers of the supplier. The POR program enables customers to pay a single utility bill, rather than paying separate bills for costs to the utility and supplier. After the utility purchases receivables, the amounts that had been due from the customer to the supplier become amounts due to the utility. The utility collects the amount due directly from the supplier’s costumers. The utility makes payments to a supplier through a mechanism called a “discount rate,” which takes into consideration various factors, such as implementation costs, credit risk, and program development.¹

This appeal involves a dispute regarding certain discount rates which were applied during the 2011-12 (“Year 2”) and 2012-13 (“Year 3”) years. Washington Gas Energy Services (“WGES”), appellant, contends that the Commission failed to follow the rules set forth in the POR program tariff when setting certain discount rates for Year 2 and Year 3 to zero. According to WGES, the Commission’s failure to follow the POR program tariff when calculating the applicable discount rate for Year 2 and Year 3 resulted in the over-collection of over \$2 million of suppliers’ money by BGE. WGES further asserts that the Commission’s actions exceed the Commission’s jurisdiction by regulating supply pricing.

¹ For example, if a utility purchased \$1,000 worth of receivables from a supplier, and a 0.2173% discount rate applied, the utility would pay the supplier \$997.83 after applying the discount rate.

WGES asks that we order the Commission to instruct BGE to return the over-collected funds to suppliers.

WGES presents a single question for our review, which we have rephrased as follows:

Whether the Commission exceeded its statutory authority, employed unlawful procedure, or acted arbitrarily or capriciously when setting certain discount rates to zero for the Year 2 and Year 3.

For the reasons we shall explain, we answer the question in the negative and accordingly, we shall affirm the judgment of the Circuit Court for Baltimore City.

FACTS AND PROCEEDINGS

A. Background

Since deregulation, energy customers in Maryland have been able to purchase electricity and/or gas from either a utility, such as BGE, or a third-party energy supplier. Regardless of whether a customer selects the utility or the third-party supplier, the energy is delivered by the utility to the customer. The supplier can elect to have its commodity charges reflected on the customer's utility bill, resulting in a single bill for both the supplier's commodity charge and the utility's delivery charge. The combination of supplier and utility charges on a single bill is referred to as consolidated billing.

In 2009, the Commission began to require utilities using consolidated billing to purchase the receivables of the energy suppliers whose commodity charges appear on the utility's bills. *See* COMAR 20.53.05.06 (providing, with respect to electric utilities, that "[a] utility providing utility consolidated billing shall either purchase the receivables of a supplier

or prorate customer payments between the utility and a supplier.”); COMAR 20.59.05.03A (providing the same with respect to gas utilities). Regulations provided for the utility to recover costs associated with purchasing supplier receivables.²

In a letter order issued October 7, 2009, the Commission directed BGE to adopt a discount provision to be applied when BGE purchased suppliers’ receivables. The Commission directed BGE to propose an appropriate discount rate in its modified tariff revisions that was comprised of the following components: “(1) commodity-related bad-debt collections; (2) program development and operations costs associated with COMAR provision implementation, including administrative and collection costs; and (3) the risk associated with the continuation of the supplier-customer relationship.” The Commission explained that BGE’s proposal could include a methodology to review the factors annually and propose annual changes in the discount rate “based on [BGE’s] historical data related to the POR.”

² COMAR 20.53.05.06C provides, with respect to electric utilities:

If the utility chooses the option of purchasing supplier receivables, supplier receivables shall be purchased with full and timely cost recovery for the utility under terms and conditions approved by the Commission.

COMAR 20.59.05.03C provides, with respect to gas utilities:

If the utility chooses the option of purchasing supplier receivables, supplier receivables shall be purchased with full and timely cost recovery for the utility under terms and conditions approved by the Commission.

BGE submitted its proposed discount rate calculation formula to the Commission on January 15, 2010. BGE’s proposed formula included a reconciliation component that would calculate the imbalance between actual costs incurred by BGE for POR program and the payments made by BGE to suppliers. The reconciliation component would be included in the calculation for the following year of the program. As a result, BGE’s proposed discount rate formula could result in a refund to suppliers if BGE spent less on the POR program than anticipated, or a charge to suppliers if BGE spent more on the POR program than anticipated. The discount rate formula provided that the refund or charge would be factored into the discount rate for the following year.

On June 10, 2010, the Commission issued a letter order approving electric POR discount rates for the 2010-11 year.³ The Commission accepted BGE’s discount rate calculation with two modifications.⁴ The Commission also approved discount rates for gas

³ The Commission approved the following electric discount rates for 2010-11 year:

Service Type	Discount Rate
Residential	0.6249%
Type I	0.3674%
Type II	0.2173%
Hourly-Priced Service	0.0507%

⁴ The Commission directed that BGE add a cash working capital component and further directed that BGE use late fee revenues to offset the uncollectible expense component.

POR.⁵ The formula for calculating gas POR discount rates was substantially similar to that for calculating electric POR discount rates. The relevant formulas were included in BGE’s electric and gas supplier tariffs, both of which were approved by the Commission.

B. Discount Rate Calculation for Year 2

On April 29, 2011, BGE submitted proposed discount rates for Year 2, applying the formula set forth in the Commission’s June 10, 2010 letter order. The formula resulted in the following electric POR discount rates:

Service Type	Discount Rate
Residential	0.8154%
Type I	1.4331%
Type II	-0.3039%
Hourly-Priced Service	-0.0645%

The formula resulted in negative discount rates for two electric rate classes. The application of a negative discount rate for Type II would have resulted in BGE paying the supplier \$10,030.39 for \$10,000.00 worth of receivables. For Hourly-Priced Services, the application

⁵ The Commission approved the following gas discount rates for the 2010-11 year.

Rate Schedule	Discount Rate
Residential - Schedule D	2.40%
General Service - Schedule C	0.98%

of the negative discount rate would have resulted in BGE paying the supplier \$10,006.45 for \$10,000.00 worth of receivables.

The application of the formula resulted in the following gas POR discount rates:

Rate Schedule	Discount Rate
Residential - Schedule D	2.3942%
General Service - Schedule C	-0.1457%

The formula resulted in a negative discount rate for one gas rate class. The application of the negative discount rate would result in BGE paying \$10,014.57 for \$10,000.00 worth of General Service - Schedule C gas receivables.

BGE argued that the negative discount rates were caused by the inclusion of late payment revenue in the discount rates. BGE further argued that the late payment revenues should not be included in the discount rate calculation. BGE further argued that including late payment revenues in the discount rate calculation benefitted suppliers but resulted in higher distribution rates to customers. BGE proposed modifying the tariff to remove late payment revenues from the discount rate calculation for Year 2.

The Commission considered the matter at its weekly administrative meeting on July 13, 2011, at which counsel for BGE and WGES appeared. WGES argued that the negative rates should be applied for Year 2 to balance out the over-collection during Year 1. The Chairman pointed out that there had been only “one year’s worth of experience” with PORs and that the long term goal was “to try to set this right every year” and “true it up.”

BGE proposed that the negative rates be set to zero “just for this year and then get with the stakeholders, both electric and gas, to see if a structural change is necessary.” After hearing from all parties, the Commission determined that the proposed negative discount rates would be replaced with discount rates of zero. The Commission did not accept BGE’s proposal regarding removing late payment revenues from the discount rate calculation.

The Commission subsequently confirmed its ruling in a letter order issued later the same day, which directed BGE to submit a revised tariff “replacing each negative Discount Rate proposed with a Discount Rate of 0.00%.” The Commission further directed BGE to modify the tariff “to reflect that any amount over or under-collected by the [BGE] shall earn interest at the same rate as is paid on customer deposits and not at [BGE’s] authorized rate of return.”

WGES filed an application for rehearing on August 12, 2011. BGE filed a response to WGES’s application for rehearing, requesting that the application for rehearing be denied and that the Commission affirm its ruling that the negative discount rates be set at zero. The Commission did not rule on WGES’s application for rehearing.

C. Discount Rate Calculation for Year 3

On March 30, 2012, BGE performed the discount rate calculation for Year 3. The formula resulted in negative discount rates for three electric rate classes:

Service Type	Discount Rate
Residential	-0.4063%
Type I	-1.0379%
Type II	0.2669%
Hourly-Priced Service	-0.2512%

The formula resulted in a negative discount rate for one gas rate schedule:

Rate Schedule	Discount Rate
Residential - Schedule D	-0.3339%
General Service - Schedule C	0.3678%

Consistent with the Commission’s direction the previous year, BGE proposed setting the negative rates to zero. BGE further proposed modified tariff language which provided that going forward, in the event the formula resulted in a negative discount rate, the discount rate would be reset to 0.000% and the associated costs would be included in a reconciliation component in a future year.

In a June 21, 2012 letter order, the Commission approved the proposed tariff language stating that, “[i]n the event the calculation results in a negative final Discount Rate, the Discount Rate will be set to 0.000% and the associated costs will be included in the future year’s Reconciliation Component.”⁶ The Commission further approved BGE’s proposed rates for Year 3, including the reset of the negative discount rates to zero. Recognizing that

⁶ WGES does not contest the Commission’s authority to modify the tariff in this respect, nor does WGES contest the Commission’s authority to reset negative rates to zero after the modification of the tariff.

negative discount rates had continued to persist and that the matter required attention, the Commission directed the Supplier Coordination Working Group to convene to consider “the inclusion of late payment charges in the discount rate or other options that will minimize the possibility of negative discount rates occurring in the future.” On July 20, 2012, WGES filed a request for rehearing with the Commission, arguing that the over-collected monies should be returned to suppliers. WGES also filed a petition for review in the Circuit Court for Baltimore City.

D. Discount Rate Calculation for Year 4

On March 14, 2013, BGE submitted proposed discount rates for the fourth year of the POR program. Negative discount rates again appeared, with three negative discount rates for electric and one negative discount rate for gas.

The rates as calculated according to the formula were, for electric:

Service Type	Discount Rate
Residential	0.1342%
Type I	-1.5107%
Type II	-0.5125%
Hourly-Priced Service	-0.7234%

The rates as calculated according to the formula were, for gas:

Rate Schedule	Discount Rate
Residential - Schedule D	1.7988%
General Service - Schedule C	0.7088%

BGE again proposed setting the negative discount rates to zero. The Commission issued a letter order on May 15, 2013, approving the electric and gas discount rates with the negative discount rates reset to 0.000%. The day prior, on May 14, 2013, the Commission issued a letter order denying WGES's July 20, 2012 application for rehearing, explaining that "to allow discount rates to remain negative would effectively require BGE to pay suppliers for the use of its billing system, a result entirely at odds with the purpose of the discount rate associated with the purchase of suppliers' receivables." The Commission noted that "POR regulations are designed to compensate BGE for the use of its billing system, not to provide a windfall for suppliers." The letter order further provided that the Commission had "referred the issue of persistent negative discount rates to the Supplier Coordination Working Group and will duly consider any recommendations they may have."

WGES filed a second petition for judicial review on May 29, 2013, seeking review of the Commission's July 13, 2011 and May 14, 2013 letter orders. The circuit court held a hearing on December 9, 2013, and issued a written order denying WGES's petition for review on December 13, 2013.

This timely appeal followed.

STANDARD OF REVIEW

When reviewing decisions of the Commission, we apply the standard of review as set forth in Section 3-203 of the Public Utilities Article, which provides:

Every final decision, order, or regulation of the Commission is prima facie correct and shall be affirmed unless clearly shown

to be: (1) unconstitutional; (2) outside the statutory authority or jurisdiction of the Commission; (3) made on unlawful procedure; (4) arbitrary or capricious; (5) affected by other error of law; or (6) if the subject of review is an order entered in a contested proceeding after a hearing, unsupported by substantial evidence on the record considered as a whole.

Md. Code (1998, 2010 Repl. Vol.), § 3-203 of the Public Utilities Article (“PU”). We do not review the circuit court’s decision, but rather, we “look[] through the circuit court’s . . . decision[], although applying the same standards of review, and evaluate[] the decision of the agency.” *People’s Counsel v. Surina*, 400 Md. 662, 681 (2007).

DISCUSSION

WGES asserts that the Commission failed to follow its own rules and acted outside the scope of its authority when it reset the negative discount rates to zero for Years 2 and 3. WGES further argues that by resetting the negative discount rates to zero, the Commission impermissibly regulated supply costs and engaged in retroactive ratemaking. The Commission responds that it was not bound to accept the negative discount rates produced by the calculation method in the tariff and that it did not regulate WGES supply costs. The Commission further asserts that it properly exercised discretion in regulating BGE’s POR program and did not exceed its authority. For the reasons explained below, we agree that the Commission acted within the scope of its discretion when setting discount rates for Years 2 and 3 to zero.

WGES asserts that the imbalances that resulted from the first two years of BGE’s POR program were “overcompensation” to BGE. We clarify that the excess monies

collected by BGE are explicitly held separately to be included in later years' reconciliation components. Critically, all parties agree that BGE will not retain the over-collected funds indefinitely. Indeed, the suppliers will eventually receive over-collected amounts through an adjusted discount rate in future years. Furthermore, the over-collected monies earn interest "equivalent to the interest rate set by the Commission annually for customer deposit held by" BGE.

While considering the actions of the Commission within the context of the deferential standard of review applied in such cases, we must consider the factual background under which this dispute arose. The POR program was newly established and future costs were uncertain at the time the discount rate calculation formula was created. The Commission reasonably believed that the discount rate would become positive over time, at which point WGES would receive accumulated over-collections through the discount rate. Other parties agreed with this approach. The National Energy Marketers Association, for example, acknowledged that "the discount rate calculation may take awhile to achieve a stable, steady state," and recommended that the current discount rate calculation methodology be maintained "in the interest of achieving a reasonable, measured result going forward." Furthermore, the Retail Energy Supply Association, while emphasizing that a working group needed to consider proper cost recovery for the future, as of June 18, 2012, "favor[ed] application of the currently-effective tariff methodology with the negative rates zeroed out."

There is no indication that any party anticipated, when initially devising the discount rate calculation methodology, that negative discount rates would result. The Commission was faced with the question of precisely what action to take when faced with a negative discount rate calculation for Year 2 of the POR program. Our “task on review is *not* to substitute [our] judgment for the expertise of those persons who constitute the administrative agency.” *United Parcel Service Inc. v. People’s Counsel for Baltimore County*, 336 Md. 569, 576-77 (1994) (internal quotation and citation omitted) (emphasis in original). We, therefore, hold there was no illegality or unreasonableness in the Commission’s decision to set negative discount rates to zero and refer the matter to a working group for further consideration.

To be sure, “an agency of the government generally must observe rules, regulations or procedures which it has established.” *Pollock v. Patuxent Inst. Bd. of Review*, 374 Md. 463, 503 (2003). Our review of the record indicates that the Commission did not fail to observe its rules, regulations, or procedures in the present case. The tariff explicitly provided that BGE was required to calculate the discount rate based upon the formula. The tariff further provided that BGE file the resulting discount rates with the Commission by May 30 of each year. The proposed discount rates would “be effective with the purchase of receivables beginning in July *pending Commission approval.*” The tariff explicitly provided for the Commission to approve or disapprove the discount rates which resulted from the application of the formula. BGE was required to follow the terms of the formula when

determining the appropriate discount rates to propose to the Commission, but the tariff is silent as to under what circumstances the Commission was free to approve or disapprove of the proposed discount rates. Faced with the novel problem of negative discount rates, the Commission acted within its discretion when determining the appropriate steps to take in the future. Under the circumstances, we cannot say that the Commission's decision to allow the over-collected funds to earn interest and ultimately return the over-collected funds through the reconciliation component in future years was arbitrary, capricious, outside the statutory authority or jurisdiction of the Commission, or made on unlawful procedure.

We are further unpersuaded by WGES's contentions that the Commission engaged in impermissible retroactive rate-making and regulation of supply costs. The discount rates set for each year considered past costs, but the rates applied only prospectively, not retroactively. In support of its argument that the Commission impermissibly regulated supply costs, WGES points to certain statements made by then-Chairman Nazarian, characterizing WGES's requested return of over-collected funds as a windfall to suppliers. First, we note that there is no indication that Chairman Nazarian's comments on this issue formed the basis for the Commission's actions. More importantly, the Commission did not require WGES to charge any particular rate. Simply put, by setting the negative discount rates to zero, the Commission exercised its authority to regulate the POR program and did not set WGES's rates or regulate its supply costs.

WGES has not shown the actions of the Commission to be arbitrary or capricious, outside of the statutory authority of the Commission, contrary to the regulations promulgated by the Commission, or affected by other error of law. Further, this Court will not substitute its judgment for the Commission's determinations under the unique circumstances of this case.

**JUDGMENT OF THE CIRCUIT COURT FOR
BALTIMORE CITY AFFIRMED. COSTS TO BE
PAID BY APPELLANT.**