SUPREME COURT OF NEW JERSEY

NO. 61,685

IN THE MATTER OF ATLANTIC CITY ELECTRIC COMPANY D/B/A CONECTIV POWER DELIVERY FOR APPROVAL OF AMENDMENTS TO ITS TARIFF TO PROVIDE FOR AN INCREASE IN RATES FOR ELECTRIC SERVICE	:	**ON CROSS PETITION FOR CERTIFCATION OF THE FINAL ORDER OF THE SUPERIOR COURT OF NEW JERSEY APPELLATE DIVISION DOCKET NO. A-6947-03T3** **SAT BELOW: HON. A.A. RODRIGUEZ SABATINO AND LYONS**

DEPARTMENT OF THE PUBLIC ADVOCATE,
DIVISION OF RATE COUNSEL
CROSS PETITION FOR CERTIFICATION

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I. STATEMENT OF THE MATTER INVOLVED

The Department of the Public Advocate, Division of Rate Counsel[1] ("Rate Counsel") brings this Cross Petition for Certification from the Appellate Division's August 9, 2007 decision in *In The Matter Of Atlantic City Electric Company d/b/a Conectiv Power Delivery For Approval Of Amendments To Its Tariff To Provide For An Increase In Rates For Electric Service*, App. Div. Dkt. No. A-6947-03T3 (August 9, 2007) in which the court upheld an Order of the Board of Public Utilities ("BPU" or the "Board"), in which the Board allowed Atlantic City Electric Company ("Atlantic," "ACE" or the "Company"), an investor owned electric utility, to charge captive ratepayers more than $30 million in excess costs incurred during the State's transition to a competitive energy market pursuant to the *Electric Discount and Energy Competition Act* ("EDECA" or the "Act"). *N.J.S.A. 48:3-50 et seq.*

In addition, Rate Counsel will not be filing a brief in opposition to Atlantic's Petition but will rely on our briefs and appendices filed in the Appellate Division.

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[1] Pursuant to *N.J.S.A. 52:27EE-1* effective January 1, 2006, the Division of the Ratepayer Advocate became the Division of Rate Counsel, within the Department of the Public Advocate.

II. QUESTIONS PRESENTED

Whether The Appellate Division Erred By Basing Its Affirmance Of The LEAC Interest Calculation on a Finding That The Deferred Balance Proceeding Could Qualify As An Appropriate Rate Proceeding Under the Board's Regulation, a Finding That Was Not Made By The Board.

Whether The Appellate Division Erred in Adopting the Board's Decision Not Supported By the Board to Charge Atlantic's Ratepayers the Cost of Excess Capacity Purchased by Atlantic Due to the Company's Failure to Consummate The Sale of Its Fossil Generation Assets.

III. ERRORS COMPLAINED OF

The Appellate Division, in affirming the decision of the Board, granted to the Board "considerable deference." *Slip op.* at 59. The court found that there was "reasonable support in the evidence" for the Board's finding and that the rulings were "not contrary to the governing law." *Slip op. at 60.* Rate Counsel submits however that "such deference is premised on [the court's] confidence that there has been a careful consideration of the

facts in issue and appropriate findings addressing the critical issues in dispute." *Bailey v. Board of Review*, 339 *N.J. Super.* 29, 32 (App. Div. 2001). The Appellate Division's deference on the issues Rate Counsel has brought before this Court was misplaced.

In the first of these two issues, the Appellate Division upheld the Board's disregard of Board regulation, Board policy and Board precedent in modifying a long standing interest calculation without explanation, thereby increasing the Company's deferred balance and customers' rates by approximately $2.0 million. The Board offered no reason for this deviation from the rules, merely finding:

> [New Jersey Large Energy Users] took no position on this issue. While Staff took no position in its Briefs, it agreed with the Company in the Exceptions to the Initial Decision. The ALJ also agreed with the Company and so do we. Accordingly, we **HEREBY ADOPT** the finding of the ALJ on this issue, and **HEREBY DENY** the RPA's proposed reduction of $1.993 million in ACE's deferred BGS balance.

In the Matter of the Petition of Atlantic City Electric Company, BPU Dkt. No. ER02020510, *Final Order* (July 8, 2004), p. 112. *Aa120*

Such a decision by the Board is deficient in its findings of facts and in its statement of the reasoning process that led to the result. *Stevens v. Board of Trustees of the Public Employees Retirement System*, 294 *N.J. Super.* 643, 684 (App. Div. 1996)

(agency decision simply adopting a party's exception is not supported by adequate factual findings and legal conclusions.) The Appellate Division's affirmance of this finding is contrary to the public interest in avoiding a violation of law and public policy and as such should be reversed by this Court.

The second issue before this Court relates to the Company's premature anticipation of the sale of its fossil generation assets. So sure was the Company that the sale would not fall through that the Company contracted for large amounts of electric capacity based on this assumption. When the sale fell through, the Company was forced to sell this excess capacity at a loss, a $29 million loss. The Appellate Court cites the findings of the ALJ and the Board that ACE "did not act unreasonably in failing to consummate the fossil unit sale." The Appellate Division found "justifiable" ACE's reliance on the Board's approval of the sale of its fossil generation assets in determining future energy and capacity needs. Rate Counsel submits that creating a standard of "did not act unreasonably" was not the intent of the Legislature in enacting EDECA's provisions concerning the sale of electric generation plants, and is an insufficient basis upon which to saddle ratepayers with $29 million in excess costs.

With the passage of EDECA, it was the avowed intent of the Legislature to lower the cost of electricity and improve the quality and choices of service for all the State's ratepayers.

N.J.S.A. 48:3-50a. The legislation authorized the BPU to determine the costs, reasonably incurred in transitioning to a competitive market, that utilities could recover from ratepayers. *N.J.S.A.* 48:3-50b. EDECA provides that "charges assessed to customers for basic generation service shall . . . be based on the reasonable and prudent cost to the utility of providing such service, . . ." *N.J.S.A.* 48:3-57a. The Legislature directed the BPU that recovery would be subject to the achievement of the goals and provisions of the Act and "to the public utility having taken and continuing to take all reasonably available steps to mitigate the magnitude of its above-market electric power generation and supply costs." *Id.*

Thus, the standard set forth by the Legislature in EDECA is not "did not act unreasonably," it is much higher. Recovery of above market costs is premised on a finding that the utility took all reasonably available steps to mitigate its costs, and that the utility's costs were reasonable and were prudently incurred. The Board did not make such a finding and in fact, based on the record evidence in this proceeding, it could not. The Appellate Division's approval of the Board's decision to pass on 100% of these excess capacity costs to Atlantic's ratepayers violates the letter and the spirit of EDECA.

IV. REASONS FOR CERTIFICATION

1. The Appellate Division Erred By Basing Its Affirmance Of The LEAC Interest Calculation on a Finding That The Deferred Balance Proceeding Could Qualify As An Appropriate Rate Proceeding Under the Board's Regulation, a Finding That Was Not Made By The Board.

The Levelized Energy Adjustment Clauses ("LEAC") were created by the BPU in the 1970s to adjust electric utility rates for year to year differences in volatile fuel prices for generating electricity. Recognizing that with the implementation of the LEAC mechanism the Board had bestowed a huge benefit on the utilities, the Board established a policy of one-way interest calculation on the accumulated LEAC balance, that is, ratepayers were entitled to interest on utility over-collections, the utility was not entitled to interest on under-collected amounts.[2]

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[2] The Board's LEAC interest calculation regulation provides that:

> (a) The clause cost adjustment will be effective on a 12-month basis, unless otherwise specified by the Board within the context of an appropriate rate proceeding.
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> . . .
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> (e) A cumulative net positive interest balance at the end of the clause period is owed to customers and shall be returned to customers in the next clause period. A cumulative net negative interest balance shall be zeroed out at the end of the clause period.

N.J.A.C. 14:3-13.4 (emphasis added)

To implement this policy, the Board directed that interest was to be calculated each month, and, at the end of the LEAC year, that interest would be summed. If, at the end of the LEAC year, interest was owed to ratepayers, that interest was credited to the LEAC balance. If, at the end of the LEAC year, interest was owed to the utility, the utility "zeroed out" the interest through appropriate accounting entries. The utility could not charge customers for that interest.

In calculating the LEAC balance to be included in the Company's deferred balance, the Company used a twenty-six month calculation. That is, the Company calculated the interest monthly but, rather than zeroing out the net negative interest after twelve months, the Company carried that negative balance into the next 12 month period and used it to cancel out an equal amount of interest due to ratepayers in those next 12 months, thereby depriving ratepayers of interest earned on subsequent over-collections.

In rejecting the Ratepayer Advocate's correction to the Company's LEAC interest calculation, the ALJ characterized as "persuasive" the Company's position that the "Ratepayer Advocate's adjustment would deny the Company any recognition of interest expense incurred over an arbitrarily selected 12-month period to purchase fuel and power used, but not yet paid for by customers . . . ." *Aa175. Initial Decision*, p. 19. In

wholeheartedly adopting the Company's position, the ALJ ignored the fact that the 12 month period was not arbitrarily selected but was required by BPU regulations and that in those same regulations the Board had determined that the Company is not entitled to collect interest from ratepayers on under-recoveries, a "cumulative net negative interest balance shall be zeroed out at the end of the clause period." *N.J.A.C.* 14:3-13.4

The BPU adopted the ALJ's "reasoning" without fully explaining its reasoning or setting out a specific finding of fact. In denying ratepayers interest on 14 months of LEAC over-collections the Board properly recognized that the interest was to be calculated over a "clause period" and that regulations permitted LEAC charges to be in effect "for a period other than 12 months **if specified by the Board in a rate proceeding**." *Aa119-120. Final Order*, pp. 111-112 (Emphasis added). Then without the protection of the required rate proceeding, the Board allowed the Company to deviate from the 12 month clause period. The Board approved the Company's accounting because:

> [New Jersey Large Energy Users] took no position on this issue. While Staff took no position in its Briefs, it agreed with the Company in the Exceptions to the Initial Decision. The ALJ also agreed with the Company and so do we. Accordingly, we **HEREBY ADOPT** the finding of the ALJ on this issue, and **HEREBY DENY** the RPA's proposed reduction of $1.993 million in ACE's deferred BGS balance. *Final Order* p. 112. *Aa120*

This decision and order of the Board is deficient in its findings of facts and in its statement of the reasoning process that led to the result. *Stevens v. Board of Trustees of the Public Employees Retirement System*, 294 *N.J. Super.* 643, 684 (App. Div. 1996)(agency decision simply adopting a party's exception is not supported by adequate factual findings and legal conclusions.) There is no reason given to explain the Board's failure to apply its own regulations. The Board merely states that the Large Energy Users did not take a position and that the Staff agreed with the Company in its Exceptions to the Initial Decision. In fact, in the Exceptions to the Initial Decision, Staff said "Staff took no position on the adjustment to the LEAC beginning balance proposed by the Ratepayer Advocate." Then, without a reason or an explanation, a footnote to that comment reads, "Staff now agrees with the Company on this issue." *RPAa128.* So, Staff agrees with the Company, the ALJ agrees with the Company, and the Board agrees with the Company. Upon this foundation, without explanation and without reason, and without the basic protections promised to ratepayers in its own regulations, the Board denied ratepayers $2.0 million in interest owed on money the Company over-collected from ratepayers through the LEAC mechanism.

The Appellate Division compounded this error. First, the Appellate Division cited the ALJ's statement and the Board's

agreement that to use other than a twenty-six month calculation was to deny the Company recognition of interest expense incurred over an "arbitrarily selected 12- month period." *Slip op*. at 58. Such expressions of sympathy for the Company's loss of interest expense discounts entirely the rights of Atlantic's customers to the interest owed customers on sums they were over-charged by the utility. The Company is not entitled to recover interest expense on under-recoveries. Moreover, the 12 month period used by Rate Counsel to calculate the LEAC interest was not "arbitrarily selected" but was based on the Company's previous LEAC period. *RPAa24.*

Next, the Appellate Division speculated that the deferred balance proceeding before the Board could qualify as an "appropriate rate proceeding for the purposes of *N.J.A.C.* 14:3-13.4(a)." *Slip op. at 59.* Rate Counsel respectfully suggests that while it may have been within the Board's purview to make such a claim, it is certainly beyond the scope of appellate review for the reviewing court to make this claim on behalf of the Board. In fact, as discussed in Rate Counsel's brief to the Appellate Division, prior Board practice indicates that a utility would request a change to the LEAC clause period within the context of a LEAC rate proceeding before implementing such change. There was no evidence in this proceeding that the Company previously requested or that the Board previously granted

an extended time frame for the calculation of interest on the LEAC balance. Indeed, if the Board had felt that this was an appropriate rate proceeding to adjust the LEAC clause period, the Board certainly could have so indicated. The fact that the Board did not do so speaks volumes. That the Appellate Division imputed this finding to the Board is improper and should be reversed by this Court.

Moreover, the Appellate Division granted to the Board "the authority and flexibility" to modify the clause period, a flexibility and authority not found in the Board's own regulations unless so determined after a fully-developed record in the context of an appropriate rate proceeding. The Board never found that this deferred balance proceeding was "an appropriate rate proceeding" and therefore was without authority to modify the regulatory LEAC calculation.[3]

Finally, the Appellate Division posited that while "the Board's decision would have been enhanced by a more explicit discussion about why it was deviating from the usual twelve-month

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[3] It is well settled in New Jersey that an administrative agency must enforce its regulations that apply to the regulated public. *Hudson County v. Department of Corrections*, 152 *N.J.* 60, 70 (1997)(citations omitted); *In re Hackensack Water Company*, 249 *N.J. Super.* 164 (App. Div. 1991). Such regulations have the force and effect of statutory law. *Hudson County,* at 70. And while an administrative agency is certainly authorized to change its regulations, while such regulations are in effect"the agency is bound by them." *Id.* at 71.

period provided in *N.J.A.C.* 14:3-13.4(a), ultimately this decision amounts to a policy choice that the Board made in implementing 'new and innovative legislation'." *Slip op. at 59.* The Appellate Division is mistaken. This was not a "policy choice" made by the Board in implementing new and innovative restructuring legislation. The calculation of interest on the LEAC balance and the policy choice associated with this calculation was made decades ago in implementing the LEAC, when that regulatory tool was itself new. As explained by the Board:

> Because of the benefits derived by the utilities as a result of the change from the tracking clause to the levelized clause, the Board determined, in every instance, that it would be inequitable to permit the utilities to recover interest on underrecoveries and therefor permitted the payment of interest only on overrecoveries by the utilities. The Board's decision as to these two issues was additionally influenced by the fact that the fuel cost data filed is the sole work product of the utility and that, because of the time constraints for rendering a decision, the time available for the Board, Staff and the Public Advocate to review the filing is indeed limited. . . . To inject issues such as the payment of interest on underrecoveries only serves to delay the Board's decision to the detriment of both the utility and its customers.
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> . . .
>
> It must be stressed that the utility develops the cost projections that, in the first instance, form the basis of the levelized factor. To ask for interest on any shortfall on its own projection is not in the public interest. The request does not fully appreciate the great strides taken by the Board to protect the viability of the utilities from rising fuel costs. By limiting interest to overrecovery situations, it serves as a reasonable check on a utility's cost projections. In addition to meeting the severe problem of regulatory lag in recovering the cost of fuel incurred, the levelized clauses provided stability and consistency in

rates insofar as possible. . .

RPAa159. In the Matter of the Petition of Rockland Electric Company, BPU Docket No. 8810-883, *Decision and Order on Reconsideration*, (October 28, 1982).

Thus, as discussed in Rate Counsel's brief to the Appellate Division, the policies expressed by the Board in implementing the LEAC fully support Rate Counsel's interest calculation correction. That is, that the interest on the LEAC balance should be calculated on an annual basis, with no interest offset for under-recoveries.

In sum, the Appellate Division affirmance of the Board's deviation from long standing regulation and policy only perpetuates a violation of the law and public policy and should be reversed by this Court. The Board failed to make the requisite findings of fact to support its decision to deviate from the 12 month LEAC period. The function of the Appellate Court is to base its review on the agency's finding, not to make such findings when the agency fails to. Accordingly, Rate Counsel respectfully requests that this Court reverse the Appellate Division's decision on this issue and direct the Board to return to Atlantic's customers the interest improperly given to the Company on LEAC under-recoveries.

2. The Appellate Division Erred in Adopting the Board's Decision Not Supported By the Record to Charge Atlantic's Customers Excess Capacity Costs Resulting From The Company's Failure to Consummate The Sale of Its Fossil Generation Assets.

In the fall of 2001, Atlantic made a determination regarding the amount of energy it would procure through the upcoming 2002 BGS auction for the period beginning August 1, 2002 through July 31, 2003. The Company determined its energy and capacity needs based on the assumption that ACE's ownership interest in three fossil generation units: 100% ownership of the B.L. England plant, 3.83% ownership interest in the Conemaugh facility and 2.47% ownership interest in the Keystone facility (collectively the "fossil units") would be successfully sold to NRG Inc. ("NRG"). When the sale of the fossil units fell through on April 1, 2002, the Company had an overabundance of available capacity and was forced to sell excess capacity at below cost rates.

Rate Counsel witness Andrea Crane testified that shareholders, not ratepayers, should bear the burden of the Company's failure to complete the sale of the fossil units. *3T828:5* Based on that determination, Rate Counsel recommended that the Company's Deferred Balance be reduced by the above market revenue requirement associated with the to-be-divested generation costs that exceed the amount associated with the

stranded costs of the facilities.[4]

The Board agreed with the ALJ that it was reasonable for the Company to have assumed that the fossil units would be successfully divested. Nowhere did the Board explain why it was reasonable for the Company to assume that the fossil units would be sold. Nor did the Board explain why it was reasonable for the Company to make purchasing decisions based on its assumption that the sale would successfully conclude and then fail to take the necessary steps to ensure that the sale would indeed go through or to protect ratepayers if the sale did in fact fall through.

Indeed, throughout the sale process there were certain steps the Company should have taken to more fully protect its customers. At some critical point in the fall of 2001, the Company must have realized that it was making decisions worth millions of dollars based on the pending sale of the fossil units. Without question, a reasonably prudent company would have looked at the risk that the sale might fall through and would

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[4] For instance, if the revenue requirement or the cost to run a fossil facility is $0.08 per kwh and the revenue associated with the sale of the power from the facility is $0.05 per kwh, then the Company would include $0.03 per kwh in the deferred balance as stranded costs. The Ratepayer Advocate recommended that the amount included in the MTC as stranded costs should not be the entire amount of stranded costs but only the amount ratepayers would be responsible for if the Company had successfully sold the fossil units. So, for example, if Atlantic's ratepayers would have had to pay only $0.01 per kwh in stranded costs if the plants had been sold in a timely manner, then the Ratepayer Advocate recommended disallowance would have been $0.02 per kwh out of the $0.03 per kwh above market costs.

have taken all necessary steps to protect itself, and thereby its customers, from that risk. As part of its fiduciary duty to protect the interests of its customers, the Company had an obligation to inform the Board that it was making decisions regarding energy purchases based on the "assumption" that the fossil units would be sold. At a minimum, Atlantic should have informed the Board in a timely manner that if a Board Order approving the sale was not issued by a certain date, Atlantic's ratepayers would be exposed to the risk of costly excess capacity costs. Atlantic has claimed no such action. Rather the Company, with its claim of "no control over the Board's actions," has only verified its own failure to act.

The Appellate Division's review of this determination should be more than a "pro forma exercise" in which the court adopts an agency finding not reasonably supported by the record. *In the Matter of Eva Taylor*, 188 *N.J.* 644, 657 (1999). Such a review requires the attention of this Court.

In a few short paragraphs, the Appellate Division summarily adopts the Board's position that the entire cost of the Company's gross mis-calculation of its capacity needs in the fall of 2001 should be borne by Atlantic's customers. The Appellate Division cites the findings of the ALJ and the Board that ACE "did not act unreasonably in failing to consummate the fossil unit sale." The Appellate Division found "justifiable" ACE's reliance on the

Board's approval of the sale of its fossil generation assets in determining future energy and capacity needs.

The Appellate Division erred in this finding because the purchasing decisions made by the Company were made in the fall of 2001, prior to the Board's approval of the sale at a January 2002 agenda meeting. Further, given that the Petition was first filed in early February 2000, and given that various terms of the sale agreement had been hotly contested at the Board, with evidentiary hearings scheduled to be held in December of 2001, the Company's assumption in the fall of 2001 that the sale would be approved without further delay seems more optimistic than justifiable. Indeed, it was entirely foreseeable that a purchaser would want to terminate the contract. And, under the circumstances, the Company's failure to ask the Board for expedited treatment of the case is remarkable.

The Appellate Division also erred in its finding that the ALJ found "and the Board agreed," that retention of the fossil units "arguably benefited" ratepayers. *Slip op. 54.* This alleged ratepayer benefit was purely speculative on the part of the ALJ. As a practical matter, the cost to ratepayers to run the facilities overwhelmed the associated revenues.[5] The Board did

[5] Certainly the record evidence on B.L.England belies any claim to a benefit to ratepayers. Since the start of the Transition Period, operation and maintenance costs at the BL England facility have increased while the costs for comparable plants have remained stable. *Aa439.* Indeed, B.L. England costs are generally higher

not adopt that finding by the ALJ and in fact noted that Board Staff did not agree with this contention. *Aa121* The Appellate Division's finding that the Board agreed with the ALJ is in error and undermines the court's approval of the Board's decision.

In affirming the decision of the Board, the Appellate Division has denied Atlantic's ratepayers the promise of EDECA that only reasonable, prudent costs would be passed through to New Jersey ratepayers. Ratepayers should not be forced to pay "for the consequences of lazy or inefficient management". *I/M/O New Jersey Bell*, 66 *N.J.* 476,495 (1975).(citing *N.J. Central Traction Co. v. Bd of Pub Utility Com'rs.*, 96 *N.J.L.* 90 (Sup. Ct. 1921)). Ratepayers are entitled to more, more than a finding that the Company's actions were not unreasonable. "Good company management is required; honest stewardship is demanded; diligence is expected; careful, even hard, bargaining in the marketplace and at the negotiation table is prerequisite." *Id.*

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than the other plants and B.L. England is the only plant whose costs have consistently increased throughout the seven year period from 1994 to 2001. *Id.*

V. CONCLUSION

Rate Counsel respectfully submits that the decision of the Appellate Division affirming the Board's use of an interest calculation that violated Board regulation, Board precedent and Board policy is contrary to the public interest in avoiding a violation of law and public policy and as such should be reversed by this Court. Similarly, the Appellate Division's approval of the Board's decision to pass on 100% of excess capacity costs to Atlantic's ratepayers violates the letter and the spirit of EDECA and therefore is contrary to the public interest. Finally, Rate Counsel opposes Atlantic's Petition for Certification and relies on our briefs and appendices filed in the Appellate Division to support this opposition.

CERTIFICATION OF COUNSEL

This Cross Petition for Certification presents substantial questions for resolution by this Court, and is being filed in good faith and not for purposes of delay.

Respectfully Submitted,

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Dated: September 25, 2007