FSC'S LAW & ECONOMICS INSIGHTS

Issue 16-3 | Fisher, Sheehan & Colton, Public Finance and General Economics | May/Jun 2016

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Utilities may not re-sequence bill payments to maximize the imposition of late payment charges.

NOTE TO READERS

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Re-sequencing Posting Utility Bill Payments: A Case Study of Abuse Involving Philadelphia Gas Works.

A practice that has long been considered deceptive and abusive in the mortgage, credit card and banking industries has recently reared its head in the public utility industry as well. The practice involves re-sequencing the "posting order" of consumer payments.

In short, the practice re-orders consumer transactions, and posts payments against those transactions out of the sequence in which they were incurred, in order to maximize the fee revenue that can be charged to consumers.

The re-sequencing of payments arises in the context of limits on late payment charges. In Pennsylvania, Public Utility Commission ("PUC") regulations state that a utility may not charge a late fee exceeding 18% annual simple interest. In saying "simple interest," what the PUC has said is that a utility may not charge a late fee on unpaid late fees (that would be "compound interest"). Being limited in the interest rate allowed, a utility's re-sequencing of the posting of payments maximizes the size of the unpaid bill against which that interest rate would be charged.

The process of re-ordering customer payments so as to apply those payments to retire more recent non-interest-bearing late charges before applying them to retire older interest-bearing principal was identified as a practice of the Philadelphia Gas Works ("PGW"), a Pennsylvania-based municipal gas company.[1] PGW has a customer who missed multiple months of pay-

[1] Despite being a municipal utility, PGW is rate-regulated by the Pennsylvania PUC.

ments. Each new missed payment meant that the cumulative unpaid bill, as well as the cumulative unpaid late fee, got bigger. The cumulative unpaid balance for utility service was charged a late fee, while the cumulative unpaid late fee balance was not.

The customer eventually made a large payment, albeit a payment that was still not sufficient to pay all outstanding balances. Rather than applying the payment against the oldest bill first, the utility applied the payment against the non-interest-bearing late fees, leaving the interest-bearing bills outstanding. Under this posting order, in other words, the utility paid the May, June, July (etc.) late fees before paying the unpaid January, February, March (etc.) bills. Only when *all* of the non-interest-bearing late fees had been retired was the balance of the payment (if any) applied to reduce the oldest interest-bearing unpaid bill.

This re-sequencing of customer payments in order to maximize late charge revenues charged to consumers can be expected to result in substantial harm to PGW's residential customers. In 2013, PGW had an average monthly residential arrearage of $46,967,171. Of PGW's 468,943 residential customers (excluding any non-residential customers), 77,839 were in arrears in any given month.[2] It is not difficult to conclude that PGW's practice of re-ordering customer payments to pay more recent non-interest-bearing late charges before retiring older interest-bearing principal results in substantial consumer injury.

[2] Pennsylvania PUC, Bureau of Consumer Services, 2013 Report on Universal Service Programs and Collections Performance, at 6, 25, 26 (November 2014).

Documenting the Fact of Payment Re-sequencing

To understand the manipulation of payments to maximize fees, it is necessary to follow the flow of dollars through an account.

The Make-up of the Bill

In an illustrative situation, the customer begins with an unpaid total amount due of $42,168.19 on June 2, 2004.[3] In turn, that amount due is comprised of two parts: (1) an "unpaid balance" (principal) of $40,023.10; and (2) an unpaid late payment charge of $2,145.09 ($40,023.10 + $2,145.09 = $42,168.19). On June 2, 2004, PGW imposed an additional late payment charge of $600.34, increasing the total balance due to $42,768.53 ($42,168.19 + $600.34 = $42,768.53).

The customer made a payment of $1,434.79 to the customer's account. The entirety of this payment was applied to the unpaid late payment charges irrespective of the age of those late payment charges.

The beginning balance of the unpaid late payment charge was $2,145.09 on June 2, 2004. That balance is reduced by the June 14, 2004 payment of $1,434.79, yielding a balance of unpaid late payment charges of $710.30. The balance of unpaid late payment charges is then increased by the June 2, 2004 late payment charge of $600.34, thus increasing the unpaid late payment charge to $1,310.64 as reported on July 2, 2004.

In the meantime, despite the June 14, 2004 payment of $1,434.79, no reduction is made in the principal irrespective of the age of that principal. The principal of $40,023.10 on June 7, 2004 in-

[3] The customer was a property manager of a multi-family housing complex. The customer was engaged in a significant billing dispute with the utility. Whether PGW should have been imposing late payment charges on a disputed bill at all is not relevant to the issues discussed in this paper.

creases to $40,466.78 on July 8, 2004 despite the intervening payment of $1,434.79 on June 13, 2004. The increase in this calculated unpaid balance can be attributed to the June 7, 2004 bill of $443.68 ($40,023.10 + $443.68 = $40,466.78).

Application of Customer Payments

The results identified above arise because PGW takes the $1,434.79 payment made by the customer and allocates that payment to account charges irrespective of the age of those charges.

Each month, a new late payment charge is rendered and the balance of unpaid late payment charges is increased by the late payment charge from the immediately preceding month. As a result, from March 1, 2004 through June 2, 2004, the cumulative unpaid late payment charge grew by the amount of the late payment charge from the preceding month.

The result of PGW's re-ordering of the customer's payment was that more recent non-interest-bearing late payment charges were paid before older interest-bearing unpaid principal was paid.

- At the time of the June 14, 2004 payment, the late payment charges for March 2004 were paid before the unpaid principal from pre-March 2004 was.

- At the time of the January 20, 2005 payment, the late payment charges for April, May, June, July, August, September, October, November, December, January and February were paid before *any* unpaid principal from pre-March 2004 was.

Since PGW is barred by law from imposing late charges on late charges, PGW's re-ordering of the customer's payment, posting that payment against more recent non-interest-bearing late charges before retiring older interest-bearing charges for principal, artificially inflated total costs to the customer. It left older interest-bearing charges outstanding while retiring newer non-interest-bearing charges.

Sequencing of Payment Posting as a "Pricing" Decision

A utility's decision to post payments in a particular order, particularly when that posting order affects the amount of late payment fee charged to customers, should be considered a pricing decision (i.e., a "rate") of the utility.[4] As such, the posting order should be set forth in a tariff and subject to Commission review. Pricing decisions by Pennsylvania's public utilities are subject to both procedural and substantive mandates imposed by state statute.

Procedural Requirements

Procedurally, any pricing decision by a public utility should be disclosed to a utility's customers as set forth in a filed tariff. Pennsylvania statutes specifically provide that "under such regulations as the commission may prescribe, every public utility shall file with the commission, within such time and in such form as the commission may designate, tariffs showing *all* rates established by it and collected or enforced.

[4] Consider other circumstances in which a Commission regulates decisions regarding the sequencing of posting customer payments. One recent instance, for example, involves discussions regarding "on-bill financing" of utility energy efficiency measures. One common issue with on-bill financing programs is whether a customer payment is posted to the energy efficiency repayment first, or whether the customer's payment is posted to the bill for utility service first.

The question presented to Commission's in this situation is whether a partial payment made by a customer is posted against the utility service first, with payments used to make the energy efficiency measure repayments second, or whether some other posting order is appropriate. The importance of that discussion here, however, is not its resolution so much as it is the fact that regulators found the posting order to be an appropriate matter for Commission oversight.

. ."[5] Those rates, as published in the utility tariff, must be available for public inspection.[6]

Placing pricing in a tariff and making it publicly available is important in the utility context. Setting aside, for the moment, the fact that placing pricing decisions in a tariff makes them subject to Commission review and approval, the requirement that the payment posting sequencing be placed in a tariff (as a pricing decision) has several salutary effects.

The most important effect of placing pricing decisions in a tariff means that customers would have been placed on notice of what the pricing decision was and, as importantly, how a bill would be calculated based on those prices. In PGW's case, even a sophisticated business customer cannot determine the pricing decisions that go into how their monthly bill is calculated. The pricing decision cannot be derived from a review of the bill itself, or from any publicly available documents. Requiring the placement of pricing in utility tariffs which are, in turn, made publicly available, is designed to ensure transparency in the calculation of bills, whether to residential customers or to business/commercial customers.

Substantive Requirements

Substantively, as a pricing decision, PGW's payment posting order is subject to the statutory dictate that rates and services be "just and reasonable." The Commission is under an explicit mandate to ensure that public utility rates are just and reasonable.[7] Under Pennsylvania law, "*every* rate made, demanded, or received by any public utility, or by any two or more public utilities jointly, *shall* be just and reasonable. . ." (emphasis added).

Payment Posting Order as a "Pricing Decision"

After requiring that every rate "made, demanded or received" by a public utility must be "just and reasonable," Pennsylvania law then broadly defines precisely what constitutes a "rate." Pennsylvania law provides that a rate includes not merely "every individual, or joint fare, toll, charge, rental, or other compensation whatsoever of any public utility. . .," but *also* to include "any rules, regulations, practices, classifications or contracts affecting any such compensation, charge, fare, toll, or rental."[8]

Even if the payment posting practice was not a "compensation" unto itself, in other words, it would certainly be a "rate" under the statute as a "rule, regulation [or] practice. . .affecting any such compensation." This conclusion flows precisely from the issue involving the posting order of a customer's payment. PGW's decision to re-sequence customer payments to apply such those payments to more recent non-interest-bearing late payment charges before applying the payments to older interest-bearing principal "affects such compensation" paid by the customer by increasing the total late payment charge fee imposed by PGW. Whether viewed as a "rule" or a "practice," PGW's re-sequencing of customer payments has the effect of increasing the customers' bills in an un-tariffed, un-reviewed, unapproved fashion.

The conclusion that the posting order of payments is a "pricing decision" is not unique to public utilities. One can turn to the banking industry as an analogy. In the banking industry, the posting order of payments has been explicitly recognized as a pricing decision.[9] In the seminal case to date regarding bank re-ordering of check posting, the Ninth Circuit overturned a federal district court decision finding a bank's

[5] 66 Pa. C.S. § 1302 (2014) (emphasis added).
[6] Id. ("Every public utility shall keep copies of such tariffs open to public inspection under such rules and regulations as the commission may prescribe.")
[7] 66 Pa. C.S. § 1301 (2014).

[8] 66 Pa. C.S. § 102 (2014).
[9] *Gutierrez v. Wells Fargo Bank*, 704 F.3d 712 (9th Cir. 2012) (Case Nos. Nos. 10–16959, 10–17468, 10–17689 (decided December 26, 2012).

high-to-low posting process[10] to be both an "unfair" and a "deceptive" business practice under California law.

The Ninth Circuit reversed the lower court decision that the high-to-low posting was an "unfair" practice, holding that federal banking law preempted the California statute as applied to the bank's posting practices. Referring to the Office of the Comptroller of the Currency ("OCC"), the Ninth Circuit court observed:

> OCC letters interpreting § 7.4002 specifically consider high-to-low posting and associated overdraft fees to be a 'pricing decision authorized by Federal law' within the power of a national bank. The OCC has opined that 'a bank's authorization to establish fees pursued to 12 C.F.R. 7.4002(a) necessarily includes the authorization to decide how they are computed.' Accordingly, the OCC has determined that a national bank '*may establish a given order of posting as a pricing decision* pursuant to section 24 (seventh) and section 7.4002.'[11]

"In sum," the Ninth Circuit said, "federal law authorizes national banks to establish a posting order as part and parcel of setting fees, which is a pricing decision. . .Wells Fargo's decision to re-sequence the posting order falls within the OCC's definition of a pricing decision authorized by federal law."[12] The Court could not have been more clear: ". . .we hold that a national bank's decision to post payments to checking accounts in a particular order is a federally authorized pricing decision."[13]

The decision that the posting order of debits is a "pricing decision" has direct applicability to the practice of PGW which involves re-ordering of payments (or "re-sequencing" payments in the Ninth Circuit's language) to post those payments against newer non-interest-bearing late fees before posting them against older interest-bearing principal. The significance, however, does not lie with any federal pre-emption claim. Rather, the significance flows from the fact that the posting order is a "pricing decision." As a pricing decision, the payment posting process is a "rate." As a rate, the posting order is (or should be) subject to the limitation of being "just and reasonable" Under Pennsylvania's statutes.

Mixed Procedural and Substantive Requirements

Once a standard of "just and reasonable" has been determined, PGW, as a public utility, must abide by both the letter and the spirit of that standard. In statutory language, Pennsylvania has declared that:

> no public utility shall, directly *or indirectly, by any device whatsoever*, or in anywise, demand or receive from any person, corporation, or municipal corporation a greater or less rate for any service rendered or to be rendered by such public utility than that specified in the tariffs

[10] Under "high-to-low" posting, when a customer writes multiple checks, the bank posts the largest check to the bank account first, irrespective of the order in which the checks were written. The effect of this process is to drain the account of available funds more quickly, thus making it more likely the bank would charge Overdraft ("OD") or Non-Sufficient Fund ("NSF") fees. Consider the following: a customer has a bank balance of $100 and writes four checks in the following order: $5, $10, $20, $90. Under a high-to-low posting process, the bank would post the $90 check first, even though it was the last check written. In that fashion, it would "bounce" all three of the smaller checks, collecting an OD or NSF fee on each check. If the bank used low-to-high posting, or if the bank had posted the checks in the order in which they were written, the account holder would have had insufficient funds for only the $90 check.

[11] Id. (internal citations omitted) (emphasis added).

[12] Id.

[13] Id.

of such public utility applicable thereto.[14]

This statute articulates the well-accepted regulatory principle that one may not do indirectly what one is barred from doing directly. The Pennsylvania statute could hardly have imposed a clearer, more stringent, requirement. PGW is barred, by statute, from imposing a greater rate than that provided by its tariff "by any device whatsoever."

This bar on seeking to do indirectly what a utility is banned from doing directly applies to the decision to post customer payments out-of-time. In Pennsylvania, a utility is authorized to impose a late payment charge on bills not paid by the due date. By regulation, however, late payment charges are limited to 18% annual simple interest.[15] The Commission, in other words, has determined the limit of a late payment charge to be not merely 1.5% per month, but 18% per year simple interest.[16]

PGW has incorporated that limitation into its tariff as well. According to Section 4.2 of PGW's tariff, "PGW will assess a late penalty for any overdue bill, in an amount which does not exceed 1.5% interest per month on the full unpaid and overdue balance of the bill. . .The interest rate, when annualized, may not exceed 18% simple interest per annum." As can be seen, this tariff language reflects and reiterates the limitations otherwise imposed by Commission regulation in any event.

Having set the limitation, PGW is further bound by the statutory directive which prohibits it from "directly or indirectly, by any device whatsoever" charging a late payment charge that compounds the 1.5% monthly interest rather than applying 18% simple interest per annum. Looked at another way, the statutory language would bar PGW from charging, "directly or indirectly, by any device whatsoever," a rate higher than 18% simple interest.

That is, however, precisely what PGW is seeking to do. The re-ordering of customer payments to apply those payments against more recent non-interest-bearing late charges before reducing older interest-bearing principal is precisely the type of action prohibited by the statute. Being barred from directly imposing a late fee on unpaid late fees, PGW may not accomplish the same objective simply by re-ordering customer payments through a process that retires unpaid non-interest-bearing late fees, irrespective of their age, before retiring unpaid interest-bearing principal.

Fundamental Utility Principles Applied to Re-ordering of Payment Posting.

The manipulation of the posting order of customer payments in order to maximize the late fee revenue charged to customers is objectionable on a number of utility-based regulatory grounds. These fundamental utility regulatory principles lead to the conclusion that re-ordering customer payments in order to maximize the late fee revenue charged to customers is unlawful. Each of these principles is described separately below.

Payment Priority

PGW's practice of re-sequencing customer payments to apply them against non-interest-bearing late charges prior to applying them against interest-bearing principal should be found to violate the principle of "just and reasonable" by referencing the regulation of the priority of payment posting.

Pennsylvania PUC regulations specifically state that in the absence of specific instructions to the contrary from the customer, "payments received by a public utility. . .which are insufficient to pay the balance due for the items plus amounts billed for basic utility service shall first be applied to the basic charges ***for residential public***

[14] 66 Pa. C.S. § 1303 (2014) (emphasis added).
[15] 52 PA Code § 56.22 (2014).
[16] Id.

utility service."[17] The definitional question presented in this regulation is not so much what constitutes a "basic charge" as it is what constitutes the "public utility service" for which the basic charge is imposed.

While "public utility service" is not a defined term in the PUC's regulations, those regulations provide ample guidance on what constitutes a "public utility service" within the contemplation of the regulatory language.

- "Basic services" are defined to include those "services necessary for the physical delivery of residential public utility service. "[18]

- "Default service" is defined to be "electric generation supply service provided under a default service program to a retail electric customer not receiving service from an electric generation supplier."

- The "discontinuance of service" is defined to mean "the cessation of service with the consent of the customer. . ."

- A "dwelling" is defined to include "a house, apartment, mobile home or single meter multiunit structure being supplied with residential service."

- An "emergency" is defined to mean "an unforeseen combination of circumstances requiring temporary discontinuance of service to effect repairs or maintenance or to eliminate an imminent threat to life, health, safety or property."

- "Residential service" is defined to mean "public utility service supplied to a dwelling, including service provided to a commercial establishment if concurrent service is provided to a residential dwelling attached thereto."

[17] 52 PA Code §56.23 (2014) (emphasis added).
[18] 52 PA. Code §56.2 (2014).

- The "termination of service" is defined to mean "cessation of service, whether temporary or permanent, without the consent of the customer. "

- The "unauthorized use of utility service" is defined to mean "unreasonable interference or diversion of service, including meter tampering (any act which affects the proper registration of service through a meter), by-passing unmetered service that flows through a device connected between a service line and customer-owned facilities and unauthorized service restoral."

The closest that the regulations come to explicitly defining what constitutes "public utility service" is when the regulations define "natural gas distribution service" as "the delivery of natural gas to retail gas customers utilizing the jurisdictional facilities of a natural gas distribution utility. . ."

It seems clear that under the PUC's regulations, the "public utility service" is the actual delivery of natural gas (or electricity in the case of an electric utility).[19] If a fee is not a charge "for public utility service," that fee may not claim first priority in a utility's payment posting sequencing. Since late payment charges are not a charge for the utility service, itself, unless the customer specifically instructs the utility to post his or her payments to late charges first, that payment sequencing may not occur under the regulation.

Minimizing Late Payments

In Pennsylvania, the state PUC seeks to administer the utility bill payment process to minimize late payments by customers. One explicitly stated intent of the PUC's regulations is that

[19] See also, the discussion of the quality of residential electric service and billing in a retail environment, *Re Guidelines for Maintaining Customer Services*, 178 P.U.R. 4th 469 (July 11, 1997).

"[p]ublic utilities shall utilize the procedures in this chapter to effectively manage customer accounts to prevent the accumulation of large, unmanageable arrearages."[20]

When given alternative choices on how to treat customer payments, the PUC has consistently chosen the alternative that would minimize the need to impose late charges. The PUC's regulations, for example, provide that for remittances by mail, "payment shall be deemed to have been made on the date of the postmark."[21] The PUC, in other words, does not allow the utility to maximize fees by assigning the payment date to the date a payment was received (let alone to the date when a customer payment was both received and processed).

Similarly, the PUC regulations provide that, in the absence of payment by mail, "the effective date of payment to a branch office or authorized payment agent. . .is the date of actual receipt of payment at that location."[22] Again, the regulations are designed to apply money against an account in as expeditious manner as possible to meet the objective, quoted above, of "prevent[ing] the accumulation of large, unmanageable arrearages." The regulations do not allow a holding period by the branch office (or payment agent) before payments are applied against a customer's balance. Nor does the PUC allow for a delay between when payments are "actually received" and when those payments are applied against customer accounts.

These principles are applied across-the-board. If a utility payment is made by check, the payments must be credited on the day the check is delivered, not when it is cashed. If a check is delivered "after hours" to the utility, the payment is as of the date of delivery. Checks received on one day may not be dated on the following day for purposes of administrative convenience. For purposes of payment processing, in other words, the "day" may not end at noon (or mid-afternoon).

It would be inconsistent, at best, for the PUC to address the <u>*day*</u> of payment receipt by a public utility, but then to allow that utility to re-order the payment by <u>*months*</u> to apply that payment out-of-time in order to maximize fee revenue. It would be inconsistent to require a utility to post a mailed payment upon mailing rather than upon receipt and then to allow that utility to re-order payments to maximize late fees by applying the payment to bills out-of-time. It would be just as inconsistent to require a utility to deem a payment received upon receipt by a third-party payment agent, but then to allow that utility to maximize late fees by applying the payment to more recent non-interest-bearing late fees before posting those payments against older interest-bearing principal. It would be inconsistent for the PUC to require that payments be deemed received "today" rather than "tomorrow" when received late in the day, but then to allow the utility to re-order the payment posting to pay bills months out-of-time.

The Principle of "Good Faith and Fair Dealing" as Applied to Re-sequencing Payments Made for Natural Gas Service.

In Pennsylvania, public utilities are explicitly required to abide by the doctrines of "good faith and fair dealing." According to the PUC, "[e]very privilege conferred or duty required under this chapter imposes an obligation of good faith, honesty and fair dealing in its performance and enforcement."[23] When considered in the context of the current inquiry, it matters not whether the authorization to collect a late payment is considered to be a "privilege conferred" or whether the limitation of late charges to 18% simple interest per annum is a "duty required." In either case, the performance and/or enforcement is to be undertaken constrained by the obligation of "good faith and fair dealing."

[20] 52 PA Code §56.1 (2014).
[21] 52 PA Code § 56.21(2)(i) (2014).
[22] 52 PA Code § 56.21(3) (2014).

[23] 52 PA. Code §56.1 (2014).

The obligation of "good faith, honesty and fair dealing" imposed on Pennsylvania utilities reflects the "good faith and fair dealing" obligation imposed on all merchants by the Uniform Commercial Code ("UCC"). The majority view is that Article 2 of the UCC applies to consumer purchases of utilities.[24] Indeed, in a case specifically involving PGW, the court held that the UCC was applicable to the sale of natural gas.[25]

The application of a "good faith and fair dealing" requirement to PGW is important because "good faith" is defined by the U.C.C. as "the observance of reasonable commercial standards of fair dealing in the trade."[26] One critical question thus becomes whether re-ordering payments to post those payments against more recent non-interest-bearing late charges before posting the payment against older interest-bearing principal represents such "reasonable commercial standards of fair dealing."

A utility practice of re-ordering payments is conceptually analogous to a bank's process of re-ordering the posting of transactions to maximize overdraft ("OD") and non-sufficient funds ("NSF") charges as described above. The unfair and deceptive nature of bank practices re-ordering payments has been challenged in pending litigation involving dozens of the largest banks in America.[27] As of June 2013, at least 14 banks (including several large ones) had settled such challenges to their posting practices, some for hundreds of millions of dollars.[28]

Banking regulators have taken increasingly strict action to prevent the manipulation of posting order resulting in an increase in bank fees paid by consumers. In November 2010, the Federal Deposit Insurance Corporation ("FDIC") issued its "Overdraft Payment Supervisory Guidance." FDIC, which has broad jurisdiction because nearly all banks and thrifts, whether federally-chartered or state-chartered, carry FDIC insurance,[29] noted that:

> With changes in technology, the range of services and number of transactions potentially causing an overdraft has broadened to include not only paper checks, but also automated teller machine (ATM) withdrawals, point-of-sale (POS) debit card use, preauthorized debits, telephonic fund transfers, and online banking transactions.[30]

FDIC continued, stating:

> Overdraft fees can exceed the amount of the overdraft and can occur multiple times in a

[24] See generally, Annotation, Electricity, gas or water furnished by public utility as 'goods' within provisions of Uniform Commercial Code, Article 2 on sales, 48 A.L.R.3d 1060 (1973); see also Mallor, "Utility 'Service' Under the Uniform Commercial Code: Are Utilities In for a Shock?", 56 The Notre Dame Lawyer 89 (1980) Gardiner v. Philadelphia Gas Works, 413 Pa. 415, 197 A.2d 612 (Pa. 1964) (natural gas a "good" per U.C.C.).

[25] Gardiner v. Philadelphia Gas Works, 413 Pa. 415, 197 A.2d 612 (Pa. 1964) (natural gas a "good" per U.C.C.).

[26] UCC, Section 2-103.

[27] In Re. Checking Account Overdraft Litigation, MDL, 2011 U.S. District LEXIS 6669 (S.D.Fla. June 3, 2011).

[28] Settlements have included, but are not necessarily limited to: Bank of America ($410 million); Citizens Bank ($137.5 million); JP Morgan Chase Bank ($110 million); TD Bank ($62 million); Union Bank N.A. ($35 million); Bank of Oklahoma ($19 million); Commerce Bank ($18.3 million); Associated Bank ($13 million); Harris Bank ($9.4 million); Intrust Bank ($2.7 million); Iberia Bank ($2.5 million); and Great Western Bank ($2.2million). Other settlements of cases related to transaction posting order that were not consolidated into the Multi-District Litigation in South Florida include Bank of Hawaii ($9 million) and Fifth Third Bank ($9.5 million).

[29] Mark Jickling and Edward Murphy (December 8, 2010). Who Regulates Whom? An Overview of U.S. Financial Regulation, Congressional Research Service, CRS Report R20429, at 4, 15, Congressional Research Service: Washington D.C.

[30] FDIC Consumer Protection, Supervisory Guidance for Overdraft Protection Programs, FIL-81-2010, , at 1 (November 24, 2010). (hereafter, Overdraft Payment Supervisory Guidance).

single banking day, depending on the type and amount of transactions and the transaction-clearing practices of the institution. For example, batch processing checks and clearing them from largest to smallest likely increases the number of items triggering an overdraft.[31]

The FDIC then laid out a series of actions that "the FDIC expects its supervised institutions to take. . .regarding automated overdraft payment programs." Among those "expected actions" was for institutions to:

> Review check-clearing procedures of the institution and any third-party vendor to ensure they operate in a manner that avoids maximizing customer overdrafts and related fees through the clearing order. Examples of appropriate procedures include clearing items in the order received or by check number.[32]

The FDIC supervisory policy followed earlier expressions of concern by federal banking regulators. In 2005, for example, the Office of Thrift Supervision ("OTS")[33] specifically stated that, as a best practice, transaction-clearing processes should not be manipulated to inflate fees.[34]

Even more recently, the FDIC went further, instructing banks that they should "avoid[...] maximizing customer overdrafts and related fees through the clearing order." FDIC directed that transactions should be processed "in a neutral order that avoids manipulating or structuring processing order to maximize customer overdraft and related fees." FDIC added that "[r]eordering transactions to clear the highest item first is not considered neutral."[35]

Outlawing the practice of manipulating payment posting to maximize customer fees can find analogies in the credit card industry as well. The Credit CARD Act's amendment to the Truth in Lending Act ("TILA") requires that any payments above the minimum payment be applied to the balance carrying the highest interest first (as opposed to the lower interest rate first, or pro rata based on the amount of each balance carrying a different interest rate).[36] Not only is this outlawed practice analogous to the manipulation of the posting of checks (high to low),[37] it is also analogous to a utility posting payments against more recent non-interest-bearing late fees before posting those payments against older interest-bearing principal.

As can be seen, re-ordering customer payments in order to maximize fees does not represent the application of "reasonable commercial standards of fair dealing." Manipulating the posting of payments to maximize fees to customers has been outlawed in the banking industry; has been outlawed in the credit card industry; and, as has been described above, should be outlawed in the utility industry.

Summary and Conclusions

PGW engages in the practice of re-sequencing customer payments. This re-sequencing re-orders customer payments to retire customer bills out-of-time in order to maximize late fee

[31] Id.
[32] Id., at 4.
[33] This was prior to the time OTS was merged with the Office of the Comptroller of the Currency ("OCC").
[34] Office of Thrift Supervision. Guidance on Overdraft Programs, 70 Fed. Reg. 8428, 8431 (Feb. 18, 2005).

[35] FDIC, Overdraft Payment Program Supervisory Guidance, Frequently Asked Questions.
[36] "Upon receipt of a payment from a cardholder, the card issuer shall apply amounts in excess of the minimum payment amount first to the card balance bearing the highest rate of interest, and then to each successive balance bearing the next highest rate of interest, until the payment is exhausted." 15 USCA § 1666c(b)(1) (2014).
[37] It is also analogous to the bank practice of posting debits to an account prior to posting credits to the account, thus maximizing overdrafts and thus overdraft fees paid by consumers.

revenue charged to customers. The re-sequencing occurs because, in Pennsylvania, while public utilities are allowed to impose late charges on unpaid bills, they are banned from imposing late charges on late charges (i.e., compounding interest).

PGW's practice of re-sequencing payments is designed to accomplish indirectly what it is not allowed to do directly. The utility practice involves posting customer payments against more recent non-interest-bearing late charges before posting payments against older interest-bearing principal. Through this practice, for example, an unpaid July late payment charge will be retired before unpaid principal from March.

The PGW practice of re-sequencing customer payments is akin to payment re-ordering practices in the banking and credit card industry that have been held to be unlawful. Banks, for example, may not re-order the posting of checks to post high-to-low. Credit card issuers must post customer payments to retire balances with the highest interest rate first, rather than re-ordering payments to retire the lowest interest rate balances first.

Aside from violating the utility's obligation to operate with "good faith and fair dealing," the PGW practice of re-sequencing customer payments to retire more recent non-interest-bearing late payment charges before retiring older interest-bearing principal, the PGW practice violates any number of additional regulatory requirements. The practice of manipulating the posting of customer payments, however, should be unequivocally found to be an "unjust and unreasonable" utility practice in addition to being contrary to specific regulatory principles.

For more information regarding utility re-ordering of payments, or for a copy of FSC's complete report on utility reordering of payments (including all data tables), please write:

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Fisher, Sheehan and Colton, Public Finance and General Economics (FSC) provides economic, financial and regulatory consulting. The areas in which *FSC* has worked include energy law and economics, fair housing, affordable housing development, local planning and zoning, energy efficiency planning, community economic development, poverty and telecommunications policy, regulatory economics, and public welfare policy.