RATE CASE EXPENSE: A UNIQUELY ANTI-CONSUMER FORM OF LITIGATION FEE SHIFTING

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Synopsis: In nearly every jurisdiction in America, including at the federal level, energy consumers are responsible for paying—as part of their service rates—the legal bills associated with utilities litigating in front of various public commissions and courts against consumers. This is called "rate case expense," and, although there has been a recent uptick in interest in it in several states, this is the first academic article to focus on the topic. This article puts forward several insights to advance these discussions. First, rate case expense should be understood as a form of fee shifting. Second, understanding rate case expense recovery this way reveals it to be unique. Reasons for this uniqueness include that rate case expense recovery (i) is not explicitly authorized by statute, (ii) can typically be recovered regardless of whether the utility prevails in the litigation, (iii) is rarely scrutinized or reduced by adjudicators. Third, rate case expense recovery is difficult to justify as a form of fee shifting and in fact operates against fee shifting's traditional justifications. For instance, rate case expense recovery shifts costs from the party with more resources to parties with fewer, and it subsidizes resistance to a regulatory regime, whereas fee shifting is traditionally seen as a way to overcome economic imbalances and subsidize enforcement of regulatory regimes. Fourth, because rate case expense is a form of fee shifting, it should have guardrails and limits comparable to those for conventional fee shifting. Fifth, many of the approaches that state regulators have applied to limit rate case expense recovery are consistent with both (1) established policy and scholarship on fee shifting and (2) the ratemaking principles that justify recovery of these expenses by utilities. This article puts forward several such approaches.

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I. INTRODUCTION

In cost-of-service ratemaking litigation, adversaries operate under a fee shifting regime that makes a utility's ratepayers responsible for the costs the utilities just incurred litigating against their interests. This appears to be the first article that focuses on this practice or that categorizes it as a form of fee shifting. For at least a century, regulators adjudicating cost-of-service disputes have allowed utilities to recover from their ratepayers the costs of litigating (against those same ratepayers) in the instant disputes.[1] This essentially forces utility

1. *See, e.g.*, Columbus Gas & Fuel Co. v. City of Columbus, 17 F.2d 630, 640 (S.D. Ohio 1927) ("Legal expenses in connection with rate cases have been given the stamp of approval by courts, when these expenses have been incurred in rate litigation before commissions and before courts.") (citing Monroe Gaslight & Fuel Co. v. Michigan Pub. Utils. Comm'n, 11 F.2d 319, 325 (E.D. Mich. 1926); Winona v. Wisconsin-Minnesota Light & Power Co., 276 F. 996, 998 (D. Minn. 1921)).

ratepayers to indemnify regulated utilities for (typically) all costs incurred *against* the interest of those same ratepayers. The obvious moral hazard this creates has long been known. Writing in 1928, one commenter explained the dynamic thus:

> The common course in a rate case is for the company to spare no efforts as to lawyers, engineers, accountants and other experts to present the facts fully from its own standpoint. The cost is then included in operating expense and charged to the consumers. On the public side, however, there is usually parsimonious regard for its several expenses; only the minimum effort is made in preparing the facts and analysis. The commission usually does little or nothing except to hear both sides. Consumers therefore pay for the elaborate and costly preparation of the company, also the skimpy preparation of their own side, and finally pay the high rates sought by the company.[2]

While that commenter was optimistic that regulators were "taking a turn toward the better representation of the public interest,"[3] precious little was achieved on this front in the intervening years, especially at the federal level.[4] Several states, however, have adopted a more complete and nuanced understanding of this issue and have meaningful scrutiny, limits, and other measures to counteract this imbalance.[5] More recently, there has been renewed interest in this topic at the state level.[6]

This article seeks to build on that commonsense impulse expressed nearly a century ago and pursued by generations of administrative litigators since, that consumers should not always be financially responsible for the legal arguments a utility makes against their statutorily protected interests. The article first comprehensively addresses the origins of the practice of rate case fee recovery and assesses its theoretical justification against established ratemaking principles. State regulators provide helpful "laboratories of democracy" with their diverse, and significantly more thoughtful, approaches to this topic. The article therefore includes a survey of fifty-two jurisdictions (all states plus the District of Columbia and Puerto Rico) as the Appendix hereto.

This article proposes that recovery of rate case expenses fundamentally operates as a form of fee shifting because one party to the dispute is made responsible for the legal fees of its adversary in that dispute. It next assesses rate case expense recovery against established scholarship on fee shifting. This provides guidance as to how the practice of rate case expense recovery can (and cannot) be justified, as well as cautions about the pitfalls of unconstrained application. It concludes that because one of the key differences between rate case expense recovery and other forms of fee shifting is that rate case expense is generally awarded to a utility regardless of the merits of its case, it likely operates

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2. *Public Utilities*, 17 NAT'L MUN. L. REV. 348, 351 (1928) (describing recent efforts of Indiana regulators to rein in such costs). *See* the Appendix to this article at 17-18 for a description of how Indiana regulators currently handle rate case expenses.

3. *Public Utilities*, 17 NAT'L MUN. L. REV. 348, 351 (1928).

4. *See infra* Part II.B.1

5. *Id.*

6. *See, e.g.*, Jason Plautz, *States Challenge Utility Costs Backed by 'Fleet of Lawyers'*, ENERGY WIRE (Apr. 6, 2023), https://www.eenews.net/articles/states-challenge-utility-costs-backed-by-fleet-of-lawyers/; Appendix at 6-8 (Colorado), 8-10 (Connecticut), 16 n.127 (noting proposed legislation in Illinois) 35-36 (New Hampshire).

to encourage utilities' lawyers to pursue low merit substantive and procedural arguments. This imposes costs on consumers, regulators, and other participants in the proceeding. Many state regulators have recognized this problem. As Chairman Sievers of the Kansas Corporation Commission articulated, utilities are essentially "spending someone else's money" when conducting their rate cases and therefore have "no incentive to minimize that spending or direct insight into the benefits of such spending."[7]

Guided by the scholarship on fee shifting, this article identifies policy proposals to limit or scrutinize rate case expense recovery that are consistent with, and further, the ratemaking principles underlying its recovery while, at least partially, correcting for the perverse incentives created when recovery of legal fees is not tied to the legal merits. These proposals track with those employed by those few state regulators who have seriously confronted these issues.

II. RECOVERY OF RATE CASE LITIGATION EXPENSES IN COST-OF-SERVICE RATES

Rate case expense recovery represents a unique intersection of procedure and substance. Because utilities[8] are substantively permitted a reasonable opportunity to recover their prudently-incurred costs of providing service, regulators also permit them to recover the costs of presenting their case to that agency, i.e., their rate case expenses. State regulators exercise varying degrees of scrutiny as to what level of rate case expenses is appropriate for utilities to recover, with the Federal Energy Regulatory Commission (FERC) exercising perhaps the least.[9] Importantly, FERC and most state regulators do not consider the merits of a utility's case when evaluating requests to recover rate case expenses.[10] Utilities are typically allowed to recover most, or all, expenses incurred employing one of three methods: a normalized level of historic experience, an amortization of present costs over several years, or a guaranteed dollar-for-dollar surcharge.[11]

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7. Kansas City Power & Light Co., Docket No. 10-KCPE-415-RTS, 2012 Kan. PUC LEXIS 89, at *166 (Jan. 18, 2012) (discussing the framework established by Milton Friedman in MILTON FRIEDMAN & ROSE FRIEDMAN, FREE TO CHOOSE: A PERSONAL STATEMENT 115-119 (1990)).

8. This article uses "utilities" as shorthand to refer generally to businesses regulated on a cost-of-service basis, which may also include "carriers." To use examples from the federal level, entities regulated under the Federal Power Act are "utilities," (16 U.S.C. § 796 (22), (23)); entities regulated under the Interstate Commerce Act are "common carriers" (49 App. U.S.C. § 3(a) (1988)); and entities regulated under the Natural Gas Act are "companies" (15 U.S.C. § 717(a)). However, despite the differences in term and scope of regulations, the substantive cost of service regulation is the same and precedent presumably applies across statutes. *See* Flint Hills Res. Alaska, LLC v. FERC, 627 F.3d 881, 887 (D.C. Cir. 2010); Tennessee Gas Pipeline Co. v. FERC, 860 F.2d 446, 454 (D.C. Cir. 1988). Utility is also the preferred term as it is more prevalent at the state level where more of the cited discussions have taken place.

9. *See infra* Part II.B.1.

10. *See infra* Part II.B.1.c; Pennsylvania Pub. Util. Comm'n v. West Pa. Water Co., No. C-871582, 1988 Pa. PUC LEXIS 422, at *30 (July 1, 1998) ("The fact that the claim in support of which this study was offered was not a successful claim does not mean that the cost of this study is not a proper ratemaking expense. As stated by the ALJ, the test is not the success or failure of the issue, but one of the reasonableness and good faith with which the study was undertaken.").

11. *See infra* Part II.B.1.

A. Foundation and Purpose of Rate Case Expense Recoverability

The issue of rate case expense arises when utility rates are set on a cost-of-service basis under the "just and reasonable" standard.[12] The ultimate purpose of this form of regulation is to protect ratepayers from excessively high prices.[13] At the same time, rates set must afford the utility an opportunity to recover their operating costs plus a reasonable return on their investment.[14] At the extreme end, when a regulator sets rates too low, this may constitute a "taking" of property under the Fifth and Fourteenth Amendments.[15] Rates falling between these two extremes are understood to fall within a statutorily permissible "zone of reasonableness," which reviewing courts are loathe to upset.[16] This principle is typically implemented using some version of the following formula, which should already be familiar to many energy professionals:

$$R = O + D + T + (RB)r$$

Where R is the revenue requirement, O is operating expenses, D is depreciation expense, T is taxes, RB is rate base (i.e., the gross value of investments less accrued depreciation), and r is the authorized rate of return.[17]

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12. Using the example of FERC's three ratemaking regimes. Interstate Commerce Act, 49 App. U.S.C § 1(5) (1988) (ICA) (oil); Natural Gas Act, 15 U.S.C. § 717(c)(a) (NGA) (natural gas); Federal Power Act, 16 U.S.C. § 824d (FPA) (electric transmission).

13. Chicago v. FPC, 458 F.2d 731, 751 (D.C. Cir. 1971) (". . . the primary purpose of the Natural Gas Act is to protect consumers. Thus, when the inquiry is whether a given rate is just and reasonable to the consumer, the underlying concern is whether it is low enough so that exploitation by the producer is prevented."); Municipal Light Bs. v. FPC, 450 F.2d 1341, 1348 (D.C. Cir. 1971) (the "primary aim [of the FPA] is the protection of consumers from excessive rates and charges.") (citing Atlantic Refin. Co. v. Public Serv. Comm'n, 360 U.S. 378, 388-89 (1959); FPC v. Hope Nat. Gas Co*.,* 320 U.S. 591, 610-12 (1944))); Farmers Union Cent. Exch., Inc. v. FERC, 734 F.2d 1486, 1507 (D.C. Cir. 1984) ("Whether the purpose of oil pipeline rate regulation is 'consumer protection' or 'producer protection,' the statute requires meaningful rate regulation.") (internal footnotes omitted). *See also* RICHARD A. POSNER, NATURAL MONOPOLY AND ITS REGULATION 5-33 (Cato Inst. 1999) (questioning rationales); CHARLES F. PHILLIPS, JR., THE REGULATION OF PUBLIC UTILITIES: THEORY AND PRACTICE 152-60, (Pub. Utils. Reps. 1984).

14. *See* FPC v. Hope Nat. Gas Co., 320 U.S. 591, 603 (1944); Bluefield Water Works & Improvement Co. v. Public Serv. Comm'n of W. Va., 262 U.S. 679, 692 (1923).

15. Duquesne Light Co. v. Barasch, 488 U.S. 299, 307-08 (1989) ("[T]he Constitution protects utilities from being limited to a charge for their property serving the public which is so 'unjust' as to be confiscatory." (citing Covington & Lexington Tpk. Road Co. v. Sandford, 164 U.S. 578, 597 (1896); FPC v. Natural Gas Pipeline Co., 315 U.S. 575, 585 (1942); FPC v. Texaco Inc., 417 U.S. 380, 391-92 (1974)).

16. *See* Maine v. FERC, 854 F.3d 9, 24 (D.C. Cir. 2017) (describing that falling within the zone of reasonableness is a necessary but not sufficient condition for a regulator to approve a rate); Permian Basin Area Rate Cases, 390 U.S. 747, 767 (1968); *see also, e.g.*, Coalition for Clean Affordable Energy v. New Mexico Pub. Regul. Comm'n, 2024-NMSC-016, ¶ 6,549 P.3d 500, 505 (2024); Columbus Tel. Co. v. Kansas Corp. Comm'n, 31 Kan. App. 2d 828, 835 (2003); Equal Access Corp. v. Utilities Bd., Utils. Div., Iowa Dep't of Com., 510 N.W.2d 147, 151 (1993).

17. *See, e.g.*, Alabama Power Co. v. FERC, 160 F.3d 7, 8 n.1 (D.C. Cir. 1998) (citing CHARLES F. PHILLIPS, JR., THE REGULATION OF PUBLIC UTILITIES 177 (3d ed. 1993)).

Rates are then set by dividing the revenue requirement by the anticipated rate of assessed transactions or units, allocated among ratepayers.[18]

This article focuses on the operating expenses part of the equation, where rate case expenses are claimed.[19] In determining a reasonable level of operating expenses, FERC and many state regulators employ a "test period" or "test year" approach wherein costs are set based on a historic period adjusted for known and measurable changes and to remove the impact of extraordinary and non-recurring events.[20]

Importantly, such rates are never meant to *guarantee* recovery of costs. As articulated by FERC, "while regulated companies must have a reasonable opportunity to recover their costs, they enjoy no guarantee that they will necessarily do so."[21] In fact, rate regulation does not even guarantee continued viability. As the Supreme Court has articulated, "regulation does not insure that the business shall produce net revenues,"[22] and the due process clause "cannot be applied to insure values or to restore values that have been lost by the operation of economic forces."[23] There are limits on what types of expenses may be recovered. Notably, because utilities are only permitted to recover their *operating* expenses in rates, they cannot recover "nonoperating" expenses,[24] such as transaction costs[25] or lobbying.[26] Imprudent expenses are also not recoverable from ratepayers.[27] In addition, the "rule against retroactive ratemaking" prohibits

18. There are different methods for allocating costs among rate payers. For instance, the "postage stamp" formula is one where all transactions are assessed the same rate regardless of distance. *See, e.g.*, *Northwest Pipeline Corp*., 82 FERC ¶ 61,158, 61,576 (1998).

19. Although utilities occasionally seek to have their rate case expenses treated as an investment that should earn return, these requests are rarely granted. *See* Appendix.

20. Opinion No. 586, *Epsilon Trading, LLC v. Colonial Pipeline Co*., 185 FERC ¶ 61,126 at P 306 (2023) ("The Commission uses a test-period methodology to determine representative costs."); *id.* at P 258; Opinion No. 885, *Panhandle E. Pipe Line Co., LP*, 181 FERC ¶ 61,211 at P 246 (2022), *order on reh'g*, 184 FERC ¶ 61,181 (2023), *order on reh'g*, 186 FERC ¶ 61,015 (2024) ("test period ratemaking methodology recognizes that, as time passes, costs, revenues, contract demand, and other factors change so that it is best to take a 'picture' of the company's operations at a single, consistent point in time . . . to avoid a moving target record.") (quoting *Iroquois Gas Transmission Sys., L.P*., 86 FERC ¶ 61,261, 61,956-57 (1999)); *Nebraska Pub. Power Dist. v. Tri-State Generation and Transmission Ass'n, Inc*., 177 FERC ¶ 61,194 at P 49 (2021). *See also, e.g.*, Los Angeles v. Public Utils. Comm'n, 7 Cal. 3d 331, 347 (1972) (unless "extraordinary or that the anticipated increase in revenue will not be sufficient to offset all anticipated increases in expenses and investment, there is no basis for adjusting the test year figures."); Central Power & Light Co. v. Public Util. Comm'n of Tex., 36 S.W.3d 547 (Tex. Ct. App. 2000).

21. *ISO New England Inc*., 172 FERC ¶ 61,251 at P 23 (2020).

22. FPC v. Natural Gas Pipeline Co. of Am., 315 U.S. 575, 590 (1942).

23. Market St. Ry. Co. v. Railroad Comm'n of Cal., 324 U.S. 548, 567 (1945).

24. Notice of Inquiry, *Rate Recovery, Reporting, & Accounting Treatment of Industry Association Dues & Certain Civic, Political, & Related Expenses*, 177 FERC ¶ 61,180 at P 6 (2021) ("The Commission presumes that expenses recorded in below the line, nonoperating accounts may not be recovered in rates, without a further showing justifying such recovery for ratemaking purposes.").

25. *See, e.g.*, *Southwest Pub. Serv. Co*., 188 FERC ¶ 61,102 at P 43 (2024).

26. *See, e.g.*, Opinion No. 554, *Potomac-Appalachian Transmission Highline, LLC*, 158 FERC ¶ 61,050 at P 56 (2017).

27. Opinion No. 544, *BP Pipelines (Alaska) Inc*., 153 FERC ¶ 61,233 at P 13 (2015) ("The regulated entity has the burden of proof to establish prudence. However, in order to ensure that rate cases are manageable, a presumption of prudence applies until the challenging party creates a serious doubt as to the prudence of an

FERC and state regulators from adjusting current rates to recover expenses from prior periods.[28]

Setting rates at this "just and reasonable" level typically involves an administrative proceeding with a trial-type hearing called a "rate case." These proceedings are often involved, expensive, and time-consuming for all parties involved.[29] Rate cases are initiated by a utility filing an application to change its rates, or by a rate-paying entity filing a complaint challenging the existing rates.[30] There are essentially two sides to a rate case: the utility seeking higher rates and ratepayer interests seeking lower ones. Sometimes there is also a neutral participant in these adjudications, such as the Office of Administrative Litigation (i.e., Trial Staff) at FERC, that is tasked with "representing the public interest."[31] Such official advocates are particularly important because ratepayers face barriers to participation, including their diffusion of interests relative to the high costs of participating.[32] Some states have also addressed this problem through intervenor compensation regimes.[33] Nevertheless, regulators frequently rely on the participation of intervenors representing the interests of affected ratepayers.[34] While these proceedings are often costly and time-consuming, they do not have to be. Rate cases are often successfully resolved through settlement, which is strongly favored by FERC policy.[35]

Utilities have successfully characterized this expense of litigating against ratepayers as a proper cost of operating their businesses, which means they should recover it from their ratepayers through rates. As seen in the Appendix below, essentially every state regulator and a good number of state courts agree with them. FERC has also agreed that such costs are recoverable in each of its ratemaking

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expenditure . . . Serious doubt must be more than a bare allegation of imprudence, but this threshold may not be so demanding that it effectively reverses the statutory burden of proof. Once such serious doubt has been raised, the pipeline has the burden of dispelling these doubts and proving the questioned expenditure to have been prudent.") (internal citations and quotations omitted).

28. SFPP, L.P. v. FERC, 967 F.3d 788, 801 (D.C. Cir. 2020). *See also, e.g.*, Spire Mo., Inc. v. Public Serv. Comm'n, 618 S.W.3d 225, 232–33 (Mo. 2021); People *ex rel.* Madigan v. Illinois Com. Comm'n, 25 N.E.3d 587, 600 (Ill. 2015).

29. *See* Stephen C. Pearson, *Innovations in FERC Hearing Procedures*, 41 ENERGY L. J. 23, 25-27 (2020).

30. *See, e.g.*, Scott Hempling, *Litigation Adversaries and Public Interest Partners: Practice Principles for New Regulatory Lawyers*, 36 ENERGY L. J. 1, 6 (2015). This article focuses on the former example, although the discussion should apply equally to complaint proceedings.

31. *Statement of Admin. Pol'y on Separations of Functions*, 101 FERC ¶ 61,340 at P 17 (2002); 18 C.F.R. § 385.102(b)(2); *see also High Land Off-Shore Sys., LLC*, 110 FERC ¶ 61,043 at P 30 (2005).

32. *See* Darryl G. Stein, *Perilous Proxies: Issues of Scale for Consumer Representation in Agency Proceedings*, 67 N.Y.U. ANN. SURV. AM. L. 513, 533-46 (2012).

33. *See, e.g.*, CAL. PUB. UTILS. CODE § 1801.3.

34. *See, e.g.*, Order No. 561, *Revisions to Oil Pipeline Regulations Pursuant to the Energy Policy Act of 1992*, [Reg. Preambles 1991-1996] FERC STATS. & REGS. ¶ 39,985, at 30,967, 58 Fed. Reg. 58,753 (1993) (to be codified at 18 C.F.R. pts. 341-47, 360-61, 375, *order on reh'g*, FERC STATS. & REGS. ¶ 31,000 (1994), *aff'd* Association of Oil Pipe Lines v. FERC, 83 F.3d 1424 (D.C. Cir. 1996) (noting the agency "rel[ies] primarily on the affected parties to bring challenges to rates" under the ICA).

35. *See, e.g.*, *Florida Power & Light Co*., 175 FERC ¶ 61,024 at P 6 (2021); *see also* 18 C.F.R. §385.602 (2025).

regimes.[36] FERC has noted that "[t]raditionally, public utilities are permitted to seek recovery of reasonable regulatory expenses from their customers when the expenses are attributable to the service provided to those customers."[37] Therefore FERC's "longstanding precedent is that regulated utilities 'are entitled to recover their reasonably incurred rate litigation costs' incurred in Commission rate making proceedings as ordinary and usual business expenses."[38]

Where there is remarkably little federal judicial precedent on the issue, especially recently, early cases supported utilities' ability to recover rate case expenses. In one Supreme Court decision from 1935, the Court concluded that rate case expenses "must be included among the costs of operation in the computation of a fair return."[39] In that matter, the company prevailed in showing the rates to be confiscatory, with the Supreme Court finding the merits of the utility's argument before the regulator to be important, noting it might be a "different case . . . if the company's complaint had been unfounded, or if the cost of the proceeding had been swollen by untenable objections."[40] In another case from 1939, the Supreme Court was again faced with an order denying the regulated entity the ability to recover its rate case expenses—this time incurred defending unreasonably high rates.[41] There, in upholding the exclusion of these costs by the state commission, the Supreme Court opined in dictum "that the utility should be allowed its fair and proper expenses for presenting its side to the commission," even "where the rates in effect are excessive."[42] Nevertheless, the Court allowed the rates to stand because it was "satisfied the reduction required" by excluding those costs in this case was "not shown to be confiscatory."[43]

The only recent federal judicial decision on the topic upheld FERC's limits on rate case expense recovery. The D.C. Circuit, reviewing a FERC oil pipeline order under the ICA, upheld FERC's policy of requiring that rate case expense in a complaint proceeding (recovered through a surcharge) first be offset by the "unpaid" refunds attributable to noncomplaining shippers that the pipeline retained.[44] The Court concluded that FERC

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36. *See* Opinion No. 534, *Midwest Indep. Transmission Sys. Operator, Inc*., 148 FERC ¶ 61,206 at P 221 (2014) (citing Opinion No. 133, *Public Serv. Co. of N.M*., 17 FERC ¶ 61,123, 61,251 (1981), and *City of Coll. Station, Tex.*, 86 FERC ¶ 61,165, 61,582 (1999) (citing *Alabama-Tennessee Nat. Gas Co.*, 11 F.P.C. 75, 82-83 (1952), and Opinion No. 730, *Sierra Pac. Power Co*., 53 F.P.C. 1795, 1805 (1975)); Opinion No. 528, *El Paso Nat. Gas Co*., 145 FERC ¶ 61,040 at P 73 (2013); Opinion No. 511-A, *SFPP, L.P.*, 137 FERC ¶ 61,220 at P 39 (2011); Opinion No. 435-A, *SFPP, L.P., Mobil Oil Corp. v. SFPP, L.P.*, 91 FERC ¶ 61,135, 61,512 (2000).

37. 86 FERC ¶ 61,165, 61,582 (1999) (cited in 148 FERC ¶ 61,206 at P 221 (2014)).

38. 158 FERC ¶ 61,050 at P 135 (2017) (quoting 137 FERC ¶ 61,220 at P 39); *see also* 91 FERC ¶ 61,135, at 61,512.

39. West Ohio Gas Co. v. Public Utils. Comm'n of Ohio, 294 U.S. 63, 73 (1935).

40. *Id.*

41. Driscoll v. Edison Light & Power Co., 307 U.S. 104, 114 (1939). *See also* Robert W. Harbeson, *The Supreme Court and Temporary Rate Orders*, 15 J. LAND & PUB. UTIL. ECON. 287, 291-92 (August 1939) (providing contemporary analysis of *Driscoll*, 307 U.S. 104 (1939)).

42. *See Driscoll*, 307 U.S. at 120-21.

43. *Id.* at 121-22, 121 n.27 (calculating a hypothetical cost of service that "produces an estimated return very close to the reasonable rate, even with the addition to the operating expenses of the other items").

44. BP W. Coast Prods., LLC v. FERC, 374 F.3d 1263, 1293-94 (D.C. Cir. 2004).

> could reasonably conclude that because [the pipeline] had reaped a windfall by charging rates in excess of those ultimately deemed just and reasonable . . . it should be required to first fund its litigation expenses out of that pool before it could begin charging those costs to its customers anew.[45]

B. How Regulators Allow Utilities to Recover Rate Case Expenses

Under this paradigm where rate case expenses are recoverable, there are two questions to address: first, what specific expenses or level of expenses can be recovered; and second, how should they be recovered. On the first question, many states have seriously considered the issue and taken diverse approaches, while FERC has hardly scratched the surface. On the second question, there are three general approaches for recovering rate case expenses employed by different states, with FERC applying a different method in each of its three ratemaking regimes (the ICA, the FPA, and the NGA). The merits of these different approaches are discussed below in Part IV, regarding recommendations.

1. Which Rate Case Expenses Are Recoverable

FERC and nearly all states articulate the same standard for recoverability of rate case expenses: the costs should be "prudent" and "reasonable."[46] Of course, like the term "just and reasonable," these terms lack precise definition and can be manifested in many ways.[47] They also reflect different policy goals and perspectives. Compare, for example, the approaches of FERC (which does not appear to have recently disallowed recovery of any rate case expenses) and Connecticut (which disallows any recovery).[48] Most states fall somewhere in between by allowing recovery while attempting to keep these costs in check. The different goals of the regulator can influence its determination of which rate case expenses may be recovered.

Without getting bogged down in semantics, "prudent" and "reasonable" may reflect different scrutiny from subjective or objective perspectives. Whether these terms are lumped together or treated separately by a particular regulator, they could be seen to reflect the subjective and objective views of rate case expenses. That is, a regulator might scrutinize whether the regulated business exercised the proper *subjective* care that its rate case expenses were prudently obtained, overseen, and employed. Or a regulator might scrutinize whether the total level of expenses was permissible relative to an *objective* benchmark such as an industry average or another formula. For instance, the Pennsylvania Commonwealth

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45. *Id.* at 1294.

46. 137 FERC ¶ 61,220 at P 39; 86 FERC ¶ 61,165, at 61,582; *see also, e.g.*, Diamond Bar Ests. Water Co., No. DIA-W-07-01, 2007 Ida. PUC LEXIS 198, at *10 (Oct. 19, 2007) (the Idaho PUC has "consistently found that prudent and reasonable costs for a [regulated utility] to file and litigate a rate case before us are an expense properly recoverable in rates.").

47. Morgan Stanley Cap. Grp. Inc. v. Public Util. Dist. No. 1 of Snohomish Cnty., 554 U.S. 527, 532 (2008). *See also* Farmers Union Cent. Exch., Inc. v. FERC, 734 F.2d 1486, 1501 (D.C. Cir. 1984) ("The 'just and reasonable' statutory standard is, of course, not very precise, and does not unduly confine FERC's ratemaking authority. As this court once explained, the necessity for an anchor to hold the terms 'just and reasonable' to some recognizable meaning is plain, for the words themselves have no intrinsic meaning applicable alike to all situations.") (cleaned up) (quoting City of Chicago v. FPC, 458 F.2d 731, 750 (D.C. Cir. 1971)).

48. *See* Appendix at 8-10.

Court, articulated that the Pennsylvania Public Utility Commission can disallow recovery of rate case expense when the record shows the expenses to be "unreasonable, imprudently incurred *or* excessive in amount."[49] The Washington Utilities and Transportation Committee also distinguishes between rate case expenses that are "exorbitant and imprudent" and those that are "extraordinary and excessive, although not imprudent."[50] FERC does not appear to differentiate between the two terms on this issue.[51]

For operating expenses, including rate case expenses, FERC applies a presumption of prudence for all expenses actually incurred, even when the requesting party bears the overall burden of proof, which thus far has been dispositive on this issue.[52] Some states apply this presumption as well,[53] though many do not.[54] Many states apply a heavy, if unstated, deference to utility requests to recovery rate case expenses.[55] While FERC has not recently employed any measure of reasonableness or prudence to find that a utility's incurred rate case expense could not be recovered, state regulators have. These measures are described more fully in the appended survey and are only briefly summarized below. This article groups these measures into two broader categories: (1) *itemized* reasonableness measures and (2) *overall* reasonableness measures. Itemized approaches involve the regulator scrutinizing individual components of the expenses, such as attorney hourly rates, witness fees, and invoices, against different objective or subjective measures of reasonableness or prudence. In contrast, scrutiny of the overall expense level seeks to determine a reasonable level

49. Butler Twp. Water Co. v. Pennsylvania Pub. Util. Comm'n, 473 A.2d 219, 221 (Pa. Commw. Ct. 1984) (emphasis added).

50. Washington Utils. & Transp. Comm'n v. Waste Control, Inc., Order No. 13, 2015 Wash. UTC LEXIS 672, at *49 n. 79 (Aug. 6, 2015).

51. *See, e.g.*, 137 FERC ¶ 61,220 at PP 39-42 (referring to "reasonably incurred," "prudently incurred," and a "reasonable level of" rate case expenses without distinction).

52. *See, e.g.*, 158 FERC ¶ 61,050 at PP 113-14 (outside legal expenses levels are presumed prudent notwithstanding recordkeeping shortfalls), *on reh'g*, 170 FERC ¶ 61,050 (2020), *on reh'g*, 172 FERC ¶ 61,048, *rev'd on other grounds sub nom.*, Newman v. FERC, 27 F.4th 690 (D.C. Cir. 2022); *Louisianna Pub. Serv. Comm'n v. System Energy Res., Inc.*, 183 FERC ¶ 63,020 at P 631 (2023) ("I find that the prudence of SERI's legal and expert witness fees is presumed and that LPSC has failed to demonstrate serious doubt about SERI's prudence to overcome that presumption.") (initial decision), *dispute partially resolved through settlement via* 186 FERC ¶ 61,194 (2024), 188 FERC ¶ 61,124, 189 FERC ¶ 61,143.

53. *See, e.g.*, United Water Del., Inc. v. PSC, 1998 Del. Super. LEXIS 122, at *6 (1998); *In re* Wilmington Suburban Water Corp., 367 A.2d 1338, 1347 (Del. Super. Ct. 1976) (reversing Delaware Public Service Commission on disallowance of rate case expenses).

54. *See, e.g.*, Aqua Utils. Fla., Inc., Order No. PSC-09-0385-FOF-WS, 2009 Fla. PUC LEXIS 415, at *247 (May 29, 2009); Kentucky Power Co., No. 2020-00174, 2021 Ky. PUC LEXIS 21, at *26 (Jan. 13, 2021). *See also* N.M. Stat. Ann. § 62-13-3(A) (2025) (applies a heightened burden to recover rate case expense in New Mexico); El Paso Elec. Co., No. 20-00104-UT, 2021 N.M. PUC LEXIS 39 (Apr. 6, 2021) (quoting PNM Gas Servs. v. New Mexico Pub. Util. Comm'n, 2000-NMSC-012, ¶ 94, 129 N.M. 1); Magnolia Water Util. Operating Co., Order No. U-35822, 2021 La. PUC LEXIS 319, at *15 (Oct. 20, 2021).

55. *See, e.g.*, Chattanooga Gas Co., Docket No. 18-00017, 2019 Tenn. PUC LEXIS 5, at *53-54 (Jan. 15, 2019) (allowing all rate case expenses to be recovered when record was insufficient to determine apportion costs to ratepayers). *See also* Appendix at 11 (District of Columbia), 11-13 (Florida) and n.96 (discussing Florida Pub. Utils. Co., Order No. PSC-2023-0103-FOF-GU, 2023 Fla. PUC LEXIS 53, at *199 (Mar. 15, 2023)), 22 (Louisiana), 26-28 (Massachusetts), 28 (Michigan), 28-30 (Minnesota), 47-48 (Tennessee), 34-35 (Nebraska).

of recoverable costs relative to objective statistical standards or subjective facts of the case.

a. Itemized Scrutiny of Rate Case Expense

Lodestar Method (Kansas Approach)

The lodestar is likely the approach most familiar to attorneys outside the energy area. This method has long been "the guiding light of [the courts'] fee-shifting jurisprudence."[56] The lodestar sets a fee award by multiplying the hours reasonably expended times a reasonable hourly rate in that community.[57] This rate should be "sufficient to induce a capable attorney to undertake the representation of a meritorious" case.[58] The level of reasonable hours spent is reduced to exclude hours that were excessive, redundant, unnecessary, or related to unsuccessful claims.[59] Only one regulator, the Kansas Corporation Commission, has explicitly endorsed the use of the lodestar to calculate recoverable rate case expenses,[60] with the Kansas Court of Appeals finding "no error" in this approach.[61] While not endorsed by name, several state regulators have similarly approached the issue of recoverable rate case expense with an eye toward reasonable hourly rates and time expended.[62] The Colorado Public Utilities Commission has rejected the use of a lodestar during its legislatively mandated re-examination of this issue, saying it involved a "different inquiry."[63] And FERC has affirmed an ALJ's rejection of the use of a lodestar to set recoverable outside legal expenses (in that case originating with a certificate proceeding, not a rate case).[64]

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56. City of Burlington v. Dague, 505 U.S. 557, 562 (1992).

57. ROBERT L. ROSSI, ATTORNEYS' FEES § 10:4 (3d ed. 2025).

58. Perdue v. Kenny A. *ex rel.* Winn, 559 U.S. 542, 552 (2010).

59. ROSSI, *supra* note 57, § 10:4 n. 13-14.

60. Kansas City Power & Light Co., 2012 Kan. PUC LEXIS 89, at *57 ("Because so much of the rate case expense here is attributable to attorney fees, the Commission will consider the lodestar calculation in determining an appropriate amount to award for this proceeding. For guidance, the Commission has reviewed how district courts use the lodestar calculation. Consistently, those courts required each lawyer for whom fees were sought to provide meticulous, contemporaneous time records documenting the time allotted to specific tasks.").

61. Citizens' Util. Ratepayer Bd. v. State Corp. Comm'n, 47 Kan. App. 2d 1112, 1127 (2012) ("After all, it is the method approved by our Supreme Court for use by lower courts when making such a determination.") (citations omitted).

62. *See e.g.*, 83 ILL. ADMIN. CODE 288.110(b) (2023) (discussed in Appendix at 16 & n.130); *see also* Appendix at 49-50 & nn.404-06, as well as the following "use to regulator" discussion.

63. Atmos Energy Corp., Decision No. C23-0293, 2023 Colo. PUC LEXIS 289, at *24-25 (Apr. 21, 2023) ("Determining whether those costs were prudently incurred (which is our charge in a rate case) is a different inquiry than determining whether the winning party in a court case incurred a reasonable amount of attorney fees (that the losing side must pay). Therefore, we decline to apply the 'lodestar test' to determine whether the legal and consulting fees—one of the utility's operating expenses—were prudently incurred so as to be recoverable in utility rates."). *See also* Appendix at 6-8; Potomac Edison Co., No. 9490, 2019 Md. PSC LEXIS 18, at *40 (Mar. 22, 2019) (rejecting a cap on outside counsel hourly fees).

64. *Potomac-Appalachian Transmission Highline, LLC*, 152 FERC ¶ 63,025 at P 80 (2015) ("This model rule is known as the Lodestar method and prohibits excessive legal fees and overhead charges by attorneys. In contrast and as discussed above, the presumption of prudence standard requires a determination as to whether a reasonable utility manager would have paid the bills, in good faith, under the same circumstances, and at the

Scrutinizing Whether Rate Case Expenses Were Useful to the Regulator

There is another line of scrutiny employed by state regulators that focuses on the value of the attorneys' or experts' work to the ratemaking body. Some of the factors considered in this approach, such as necessity and redundancy, overlap with the lodestar method. However, the purpose of this scrutiny is different. Looking to whether legal expenses aided the regulator is aligned with the ratemaking principle that a utility should only recover the cost of providing service at just and reasonable rates. If litigation costs were unnecessary or irrelevant to the regulator, they do not further the provision of that service. Some regulators frame this inquiry in terms of "necessity," looking to whether rate case expenses were needed for the utility's case.[65] One manifestation of this inquiry is disallowing recovery of redundant or duplicative expenses.[66] Texas and Illinois also articulate a "relevance" requirement in their regulations on rate case expenses, which appears closely related to a necessary standard some jurisdictions implicitly apply.[67] Going one step further, some jurisdictions have found the recoverability of rate case expenses to turn on the merits of the specific issue those legal fees were directed toward.[68] Regulators have also found other specific categories of rate case expenses unrecoverable, such as meals and snacks,[69] or the legal

relevant point in time."), *aff'd*, 158 FERC ¶ 61,050, at PP 113-14 (2017), *on reh'g*, 170 FERC ¶ 61,050 (2020), *on reh'g*, 172 FERC ¶ 61,048, *rev'd on other grounds sub nom.*, Newman v. FERC, 27 F.4th 690 (D.C. Cir. 2022).

65. *See, e.g.*, Public Serv. Co. of Okla., Order No. 672864, 2018 Okla. PUC LEXIS 41, at *73 (Jan. 31, 2018) ("the Commission directs that witness fees and expenses of witness Quackenbush, an unnecessary witness that contributed nothing of substance to these proceedings, not be paid by customers but by shareholders."); Washington Utils. Transp. Comm'n v. Puget Sound Pilots, Order No 09, 2020 Wash. UTC LEXIS 627, at *141 (Nov. 25, 2020) (Commission "may limit recovery of excessive legal or expert witness fees when the evidence establishes that certain expenses are unreasonable or unnecessary."); Indiana Mich. Power. Co., No. U-21-461, 2024 MICH. PSC LEXIS 117, at *170 (July 2, 2024) (denying recovery of witness training expenses not shown to be needed).

66. *See, e.g.*, Appendix at 1 (Alabama), 2-3 (Arizona), 16-17 (Illinois), 19-21 (Kansas), 41-42 (Oklahoma), 46-47 (South Carolina), 48-53 (Texas).

67. ILL. ADMIN. CODE tit. 83, §288.110(b)(4) (2023) (requiring assessment of "the relevance of the work products to the justness and reasonableness of the proposed utility rates."); 16 TEX. ADMIN. CODE § 7.5530(b) (2025) (requiring assessment of "whether the work was relevant and reasonably necessary to the proceeding"). *See also* Puerto Rico Elec. Power Auth. Rate Rev., No. CEPR-AP-2015-0001, at ¶ 121 (Jan. 10, 2017) (Final Resolution and Order), *aff'd* Final Resolution (Mar. 8, 2017).

68. Interstate Power & Light Co., Docket No. RPU-2019-0002, 2021 Iowa PUC LEXIS 266, at *14 (Aug. 10, 2021) ("customers should not be required to bear the resulting costs" from novel legal issues created by utility filing); Sunshine Utils. of Cent. Fla., Inc., Docket No.900386-WU, 1994 Fla. PUC LEXIS 613, at *32 (June 15, 1994) ("It is our belief that we are justified in depending upon the court's determination of success in making its determination of reasonableness or prudence. In other words, if a utility succeeds in an appeal, the Commission can fairly conclude it was prudent. On the other hand, if a utility fails in its appeal, the Commission can fairly assume it was not a prudent appeal. Because it is the ratepayers that bear the burden of appellate rate case expense, the Commission is justified in denying appellate rate case expense for appeals in which utilities are unsuccessful. Because we find that this Commission may depend on success at the appellate level as a basis for determining the reasonableness of an appeal, we also conclude that reasonable appellate rate case expense can only mean expense related to issues on which the utility prevails.").

69. Kentucky Power Co., No. 2020-00174, 2021 Ky. PUC LEXIS 21, at *26-27 (Jan. 13, 2021).

expenses of resisting discovery.[70] Somewhat similarly, the Rhode Island PUC found the fact that a utility's initial proposal was not "in line with its final position" showed that the utility "contributed to the excessive costs of the rate case" and could not recover all such costs from ratepayers.[71]

Scrutinizing the Procurement, Management, and Recordkeeping of Rate Case Expenses

Several regulators also scrutinize a utility's procurement and management of attorneys and witnesses in determining what rate case expenses are recoverable. For instance, in Massachusetts and New Hampshire, utilities "must engage in a competitive bidding process"[72] to recover their rate case expenses.[73] Most states do not require or scrutinize the procurement of rate case legal service providers,[74] and at least one FERC ALJ has rejected the idea as well.[75] However, more states will scrutinize the management of rate case expenses once retained, though more often nominally than substantively.[76] Somewhat related to management is the issue of documentation required to meet the burden of proof. One of the more common reasons regulators disallow rate case expenses is failure to substantiate the past expenses or estimated future expenses.[77] Some states have regulations requiring specific documentation to support a request for rate case expenses.[78]

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70. TXU Gas Distrib., Docket Nos. 9145-9148, 2000 Railroad Commn Tex. LEXIS 436, at *46 (Oct. 10, 2000) (disallowing expenses related to resisting discovery) (hearing officer's decision).

71. City of Newport, Utils. Dept., Water Div., Docket No. 2985, 2000 R.I. PUC LEXIS 12, at *37-38 (June 19, 2000) (utility reduced its request from 27% to 11.8% over the course of the proceeding).

72. East Northfield Water Co., Docket No. 19-57, 2020 Mass. PUC LEXIS 99, at *48-49 (Mar. 31, 2020) (citing various decisions) (noting an exception for small water utilities); Massachusetts Elec. Co., Docket No. 18-150, 2019 Mass. PUC LEXIS 264, at *292 (Sep. 30, 2019); NSTAR Elec. Co., Docket No. 17-05, 2017 Mass. PUC LEXIS 371, at *289-90 (Nov. 30, 2017). *See also* Appendix at 26 (noting that the work need not go to lowest bidder when adequate justification is provided).

73. N.H. CODE ADMIN R. ANN. PUC 1905.01-.04 (2013). *See also* N.H. CODE ADMIN. R. ANN. PUC 1905.04(c) (2013) (requiring utilities that choose a service provider other than the lowest bidder to justify that choice by "clear and convincing justification.").

74. *See* Community Nat. Gas Co., 2017 Ind. PUC LEXIS 71, at *66 (Mar. 22, 2017) (declining to adopt such a requirement).

75. 183 FERC ¶ 63,020 at P 643.

76. Public Serv. Co. of Colo., Decision No. C22-0642, 2022 Colo. PUC LEXIS 511, at *70 (Oct. 19, 2022) (encouraging better management); Northern Ill. Gas Co., 2023 Ill. PUC LEXIS 747, at *189 (Nov. 16, 2023) (utilities' "rate case expense of $5,363,900 is uncontested and therefore adopted by the Commission. While the two-time entries amounting to $562.50 are nominal, the Commission strongly encourages Nicor Gas to continue to scrutinize its legal bills for accuracy.").

77. *See, e.g.*, Louisville Gas & Elec. Co., No. 2003-00433, 2004 Ky. PUC LEXIS 525, at *63-64 (June 30, 2004) (disallowing $18,929 in expenses because "when a utility seeks to recover an expenditure in its rates, the Commission is obligated to review the nature of that expenditure to verify that it is just and reasonable. In this instance, we are unable to determine from the evidence of record the nature of certain legal services performed and whether those services were related to this rate case."); Potomac Elec. Power Co., No. 9336, 2014 Md. PSC LEXIS 22, at *78-80 (July 2, 2014).

78. *See, e.g.*, ILL. ADMIN. CODE tit. 83, § 288.100 (2023); 65 ME. CODE R. § 407-850-2(A) (2022); N.H. CODE ADMIN. R. PUC 1905.03 (Documentation of Expenses Required).

b. Scrutiny of the Overall Level of Rate Case Expense

Normalization

One established method of setting recoverable rate case expense levels is by creating a "normalized" average of historic experiences. This is a standard ratemaking method for determining the level of recurring costs that fluctuate over time. It is described in greater detail below, in the section addressing how rate case expenses are recovered.

Caps or Benchmarks

One possible method of setting an overall level of recoverable rate case expense is for the regulator to determine an objective reasonable level that can be recovered regardless of the expenses actually incurred in a particular case. For instance, in the context of water utilities, New York determines a reasonable level of rate case expense by averaging the historic experience of comparable utilities.[79] As described in the Appendix, Colorado recently explored the use of caps for rate case expenses (as well as other measures) in response to a rulemaking spurred by legislation.[80] In a decision by the Kansas Corporation Commission dealing with rate case expense, its chairman penned a concurrence that proposed an alternative approach of presuming rate case expenses to be reasonable where they fell within a "zone of reasonableness" pegged at the relative share of the entire value of the case and to be presumed unreasonable otherwise.[81] The opinion was detailed and grounded in economic discussion of incentives.[82] Both FERC and the California Public Utilities Commission have found that, when utility rates are subject to a cap or index (rather than cost of service) ratemaking, rate case expenses are subsumed within that ratemaking methodology and cannot be separately recovered.[83]

50-50 "Split" (New Jersey Approach)

79. *See* Appendix at 38-39.

80. *See* Appendix at 6-8 (discussing proposed Amendments to The Comm'n's Rules Regulating Elec. Utils., Decision No. C24-0285, 2024 Colo. PUC LEXIS 258, at *49 (Mar. 27, 2024); S.B. 23-291 § 2, 75th Gen. Assemb., Reg. Sess. (Colo. 2023) (codified at COLO. REV. STAT. § 40-3-102.5 (2023)). In fact, Colorado has articulated one recent disallowance as the implementation of a cap. Atmos Energy Corp., Decision No. C23-0293, 2023 Colo. PUC LEXIS 289, at *26 (Apr. 21, 2023).

81. Kansas Power & Light Co., Docket No. 10-KCPE-415-RTS, 2012 Kan. PUC LEXIS 89, at *144-77 (Jan. 18, 2012).

82. Notably the opinion also challenged the distinction between rate case expenses and attorneys' fees as "an historical artifact of regulation." *Id.* at *147-53.

83. Opinion No. 527, *SFPP, L.P.*, 143 FERC ¶ 61,213 at P 105 (2013) (holding that rate litigation surcharge revenue is not excluded when determining oil pipelines entitlement to index-based rate increase); *see also* Appendix at 5-6 (California).

Another approach to limiting rate case expense is to require these costs be "shared" evenly between ratepayers and shareholders. Because shareholders are understood to bear the cost of expenses not recovered from ratepayers, this "sharing" is achieved by reducing the recoverable level of rate case expenses by 50%. The rationale for this approach is not tied to the reasonableness or prudence of the expenses but rather is premised on a belief that rate case expenses are different from other operating expenses because they only partly serve ratepayers and also serve shareholders.[84] Perhaps because of its simplicity, this approach is frequently advocated by parties representing consumer interests. However, it is usually rejected by regulators.[85] Some states, however, articulate that these expenses are "shared" by the utility not earning a return on them, and therefore bearing the "carrying costs" associated with the time-value of money.[86] Currently, the 50-50 split is only employed in New Jersey, which has maintained this policy for a while.[87] Both Tennessee and Pennsylvania also briefly employed the 50-50 split, with both orders struck down.[88] Recently, the Colorado Public Utilities Commission has employed this approach on an itemized basis reducing the allowable expense for two specific witnesses by 50%.[89] Likewise, the Missouri Public Service Commission has evenly split costs between ratepayers and utilities on one occasion based on the specific facts of that case.[90]

Sliding Scale Based on Merit (Missouri-Texas Approach)

The most interesting approach to scrutinizing rate case expense levels, ultimately recommended here, is a statistical sliding scale where the level of rate

84. *See, e.g.*, Suez Water Arlington Hills, Inc., Docket No. WR16060510, 2017 N.J. PUC LEXIS 253, at *95-96 (Nov. 13, 2017) ("some portion of that expense is a cost of maintaining the stockholders investment.") (quoting South Jersey Gas Co., Docket No. 818-754 (Order dated November 24, 1982)); Gordon's Corner Water Co., Docket No. WR00050304, 2001 N.J. PUC LEXIS 125, at *35 (July 13, 2001) ("The Board recognizes that a rate case benefits both ratepayers and shareholders and, absent any special circumstances, sharing of these expenses is appropriate and consistent with prior Board Orders . . . .").

85. See Appendix at 11-13 (Florida), 14 (Hawaii), 15-16 (Idaho), 17-18 (Indiana), 28 (Michigan), 28-30 (Minnesota), 40-41 (Ohio), 54-55 (Washinton).

86. *See e.g.*, Appendix at 45-46 (Rhode Island) ("ratepayers to pay the actual, prudently incurred rate case expenses over a period of time, while stockholders pay the carrying costs on the unamortized balance.") (quoting Providence Gas Co. v. Malachowski, 656 A.2d 949, 953 (R.I. 1995)). Interestingly, Florida articulated this as consistent with a "long-standing policy that the cost of the rate case should be shared." *See* Tampa Elec. Co., Docket No. 080317-EI, 2009 Fla. PUC LEXIS 251, at *79 (Apr. 30, 2009); Aqua Utils. Fla., Inc., Docket No. 100330-WS, 2012 Fla. PUC LEXIS 216, at *335 (Mar. 5, 2012) (rejecting the 50-50 "sharing" of costs.); El Paso Elec. Co., No. 20-00104-UT, 2021 N.M. PUC LEXIS 39 (Apr. 6, 2021) ("excluding the unamortized balance of rate case expenses from rate base accomplishes some sharing of rate case expenses between shareholders and ratepayers.").

87. *See* Appendix at 36-37 (New Jersey).

88. *See* Appendix at 47-48 (Tennessee) and 42-44 (Pennsylvania).

89. Public Serv. Co. of Colo., Decision No. C24-0778, at P 215 (Oct. 25, 2024) ("[H]ence we find it appropriate for shareholders to carry an equal proportion of the cost of those consultants' services for which they too receive a benefit").

90. Laclede Gas Co., Amended Report and Order, Dockets No. GR-2017-0215-0216 (Mo. Pub. Serv. Comm'n Ma. 7, 2018), https://efis.psc.mo.gov/Document/Display/134183, *aff'd sub nom.* Spire Mo., Inc. v. Public Serv. Comm'n, 618 S.W.3d 225, 234 (Mo. 2021)); *id.* slip op. at 53-54; *see also* Appendix at 31-33.

case expenses recoverable corresponds to the merits of the positions taken by the utility. This rule can be expressed as the following formula, where recoverable rate case expenses are equal to:

$$Incurred\ rate\ case\ expense \times \frac{Increase\ Granted}{Increase\ Requested}$$

For instance, if a utility requested a 30% rate increase, but was granted only a 10% rate increase, then they could recover only one-third of the rate case expenses incurred. This practice has been applied by the Missouri Public Service Commission (and affirmed by that state's high court)[91] and is embodied in the regulations of the Texas Public Utilities Commission.[92] When it applied this rule, the Missouri Public Service Commission did not reduce any expense related to a depreciation study that was required to be conducted by the Commission's rules.[93] Texas applies a similar test—among others—but requires a triggering event first. In Texas, this practice—referred to as the "results oriented method"[94]—applies where it is first shown that "rate-case expenses as a whole were disproportionate, excessive, or unwarranted in relation to the nature and scope of the rate case."[95] The Texas PUC intended this method to be applied in limited circumstances when other, more granular disallowances did not apply.[96]

The logic behind this approach is that rate case expenses are unique. As the Missouri PSC cogently explained, this expense item is "different from most other types of utility operational expenses" in several ways, including that it creates an "inequitable financial advantage over other case participants" and provides no incentive to discipline costs.[97] The PSC illustrated this point clearly as follows:

> While [the utility] is able to recoup the costs of its legal counsel and expenses through utility service rates, [the Office of People's Counsel, the entity representing ratepayers] operates within a tight annual budget, and interveners pay their own legal expenses. . . Awarding a utility all of its incurred rate case expenses could provide that utility with a significant financial advantage over other participants in the rate case process, who may be constrained by budgetary and other financial restrictions. Such a practice does not encourage reasonable levels of cost containment in the utility's rate case expense decisions.[98]

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91. *See* Appendix at 31-32 (discussing Kansas City Power & Light Co., 2015 Mo. PSC LEXIS 789 (Sep. 2, 2015), and Kansas City Power & Light Co.'s v. Missouri Pub. Serv. Comm'n, 509 S.W.3d 757, 777 (Mo. Ct. App. 2016)).

92. 16 TEX. ADMIN. CODE § 25.245 (2014). *See also* Appendix at 50-51.

93. Kansas City Power & Light Co., 2015 Mo. PSC LEXIS 789, at *139 (Sep. 2, 2015) (but amortizing this expense level of over 5 years, which how frequently those studies were conducted, while other rate case expenses were amortized over a three-year amortization period).

94. 16 TEX. ADMIN. CODE § 25.245 (2014).

95. 16 TEX. ADMIN. CODE § 25.245(c)(5) (2014).

96. 16 TEX. ADMIN. CODE § 25.245 (2014); *see also* Appendix at 49-50 (describing the other justifications for rate case expense disallowances).

97. Kansas City Power & Light Co., 2015 Mo. PSC LEXIS 789, *133-34.

98. *Id*. at *126-27.

While the Missouri PSC understood the harm caused by unchecked recovery of this unique expense, it also understood that because "customers benefit from having just and reasonable rates, it is appropriate for customers to bear some portion of the utility's cost of prosecuting a rate case."[99] The PSC reasoned that its' chosen approach "directly tie[s] a utility's recovery of rate case expense to both the reasonableness of its issue positions and the dollar value sought from customers in a rate case."[100] In other words, it provides an incentive for the utility not to spend money pursuing unreasonable arguments or to request or defend unreasonable rates. The Texas PUC similarly articulated that scrutiny of this expense incentivizes utilities "to act more like self-funded litigants, while still providing for recovery of reasonable rate-case expenses."[101]

There are other manifestations of this sliding scale approach based on merit. For instance, the Texas PUC previously implemented a "51% Rule," under which a water utility was not permitted to recover any rate-case expenses if the rate increase granted by the commission is less than 51% of the increase proposed by the utility.[102] That is, the utility has to prevail in most of its case. The Rhode Island PUC's precedent, described above, that measured the reasonableness of overall rate case expense levels by comparing the utility's starting position against the increase ultimately supported by the record,[103] is based on a comparable rationale. In that case, however, the Rhode Island PUC did not implement a formulaic reduction based on the merits but rather cut recoverable rate case expenses by one-third.[104] Unlike the even 50-50 split, a sliding-scale approach does not appear to have been broadly raised as an alternative to guaranteed recovery.[105]

Holistic Evaluation of Case

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99. *Id*. at *133.

100. *Id*. at *128.

101. Recovery of Expenses for Ratemaking Procs., 39 Tex. Reg. 6434, 6435 (Aug. 22, 2014) ("the commission concludes that adopting clear evidentiary standards and specific criteria for the review and determination of the reasonableness of rate-case expenses will incentivize utilities and municipalities to act more like self-funded litigants, while still providing for recovery of reasonable rate-case expenses. The commission emphasizes that it retains broad discretion and flexibility when reviewing requests for recovery of or reimbursement for rate-case expenses. The commission further anticipates that in evaluating specific rate-case expense requests, the presiding officer will apply the specific criteria established in the adopted rule in light of the overall 'reasonableness' standard for rate-case expense recovery.").

102. Order Adopting Amendments to 16 TAC 24.44 for Consideration at The October 11, 2019 Open Meeting, Rulemaking to Amend 24.44 Rate-Case Expenses Pursuant to Tex. Water Code §13.187 & §13.1871, Project No. 48526, slip op. at 6 (Tex. Pub. Util. Comm'n Oct. 14, 2019), https://interchange.puc.texas.gov/Documents/48937_25_1037611.PDF.

103. City of Newport, Docket No. 2985, 2000 R.I. PUC LEXIS 12, at *37-38 (June 19, 2000); *see also* Appendix at 45-46.

104. *Id*. at *38.

105. *But see, e.g.*, Southwestern Bell Tel. Co., Docket No. U-2916, ,1979 Ark. PUC LEXIS 7, at *85-86 (Jan. 15, 1979) (rejecting similar proposal noting that some expenses do not impact ultimate revenue level but are "nonetheless very beneficial to the commission."); Potomac Elec. Power Co., No. 1139, 2017 D.C. PUC LEXIS 187, at *177-178 (July 25, 2017).

Many regulators also measure the reasonableness of a utility's requested overall level of rate case expense based on the specific facts of the case. Factors that regulators consider range broadly and include subjective judgments, such as the complexity, scope, or adversarial rigor, as well as the more objective measure of the overall cost levels relative to comparable cases or the monetary value of the case. For example, as mentioned above, the Texas Public Utilities Commission applies its sliding-scale approach only after a finding that "rate-case expenses as a whole were disproportionate, excessive, or unwarranted in relation to the nature and scope of the rate case."[106] The New Hampshire and Illinois regulations likewise require agencies to consider the novelty and complexity presented.[107] Similarly, the Indiana Utility Regulatory Commission has articulated that rate case expenses "must be prudent and reasonable given the complexity of the issues presented."[108] On the other hand, the Iowa Utilities Board has rejected arguments that a more complex case warranted recovery of more rate case expenses when it found that the complexity and novelty originated with the utility.[109] The California PUC has also looked to "the intensity with which [intervenors] chose to pursue their challenges" to a rate increase as "persuasive" justification for rate case expense levels.[110]

One particularly interesting factor is the total rate case expense incurred relative to the value of the case. This is more often considered among the "soft" factors in understanding the case as a whole rather than employing a hard benchmark. The Ohio PUC, for instance, understands that it "must consider the size of the company and a comparison of the rate case expense relative to the required revenue increase."[111] Maine regulations include "the amount of money at issue" among the factors to be considered,[112] and Texas PUC regulations include "the amount of money or value of property or interest at stake" to be a part of the "scope" the Commission must measure the incurred costs against.[113] The Massachusetts Department of Public Utilities has also articulated that it may disallow recovery of rate case expenses "where such expenses are disproportionate

106. 16 TEX. ADMIN. CODE § 25.245(c)(5) (2014).

107. N.H. CODE ADMIN. R. PUC 1904.01(b)(1) (2024) (Agency must consider "[w]hether the issues presented are novel or complex"). Related to the merit-based approach above, the New Hampshire regulations also require its PUC to consider whether the request itself was just and reasonable. N.H. CODE ADMIN. R. Puc 1904.01(b)(7) (2024). ILL. ADMIN. CODE tit. 83, § 288.110(b)(3) (2023) (factors include "[n]ovelty, complexity, or difficulty of the issues.").

108. Switzerland Cnty. Nat. Gas. Co., 2019 Ind. PUC LEXIS 90, at * 56 (Apr. 17, 2019).

109. Interstate Power & Light Co., Docket No. RPU-2019-0002, 2021 Iowa PUC LEXIS 266, at *13-14 (Aug. 10, 2021).

110. Crimson Cal. Pipeline L.P., Decision No. 20-11-026, 2020 Cal. PUC LEXIS 966, at *14 (Nov. 23, 2020); *see also* Global Water – Picacho Cove Water Co., Decision No. 78644, at 148 (Ariz. Corp. Comm'n July 27, 2022), https://docket.images.azcc.gov/0000207261.pdf?i=1759334104604 ("The Applicants' concerns that Staffs pursuit of the Section 1033 tax issue increased the difficulty of its rate case presentation is not entirely without merit.").

111. Water & Sewer LLC, No. 11-4509-ST-AIR, 2012 Ohio PUC LEXIS 749, at *52 (Aug. 15, 2012).

112. 65-407-850 ME. CODE R. § 3.B (2022).

113. 16 TEX. ADMIN. CODE § 25.245(b)(5)(B) (2014).

to the relief being sought."[114] In at least one instance, the Illinois Commerce Commission found that "it [was] unreasonable for rate case expense to represent 18.7%" of a utility's overall revenue request.[115] The New York PSC has also raised concerns as to the quantum of the rate case expense relative to the overall revenue requirement.[116] Finally, as described above, Chairman Sievers of the Kansas Corporation Commission proposed an alternative benchmark comprising ranges of percentages of rate case expense relative to the "awarded revenue requirement from past Commission decisions."[117]

c. Minimal Scrutiny (FERC Approach)

FERC employs a narrower scrutiny than most states, limiting its review to the prudence of a utility's legal expenses in a rate case.[118] It has not recently, if ever, applied this standard to reduce a utility's recoverable rate case expenses.[119] Most recently, a FERC administrative law judge articulated that the Commission "assesses prudence objectively by reference to what a reasonable utility management would pay for outside lawyers in similar regulatory litigation."[120] There the ALJ rejected evidence comparing the fees of other firms or parties in the case and expense levels from prior rate cases, as well evidence as to the lack of competitive solicitation or requests for discounts.[121] As a practical matter, in at least one oil pipeline dispute, FERC has entirely divorced the level of recoverable rate case expense from the merits of the case or the total value. Specifically, in Docket IS09-437, FERC approved a surcharge to recover $6 million in expenses for a rate case where—after nearly a decade of litigation—FERC set the pipelines' rates (exclusive of the surcharge) *below* those in place prior to the pipeline's application.[122]

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114. East Northfield Water Co., Docket No. 19-57, 2020 Mass. PUC LEXIS 99, at *47-48 (Mar. 31, 2020) (citing various decisions); Massachusetts Elec. Co., Docket No. 18-150, 2019 Mass. PUC LEXIS 264, at *290-291 (Sep. 30, 2019); NSTAR Elec. Co., Docket No. 17-05, 2017 Mass. PUC LEXIS 371, at *386-87 (Nov. 30, 2017).

115. North Shore Gas. Co., 2023 Ill. PUC LEXIS 786, at *302 (Nov. 16, 2023).

116. Bristol Water-Works Corp., No. 17-W-0010, 2018 N.Y. PUC LEXIS 353, at *69-74 (July 16, 2018) (noting that the company's rate case expense exceeded its revenues and represented the majority of the requested rate increase).

117. Kansas City Power & Light Co., Docket No. 10-KCPE-415-RTS, 2012 Kan. PUC LEXIS 89, at *169 (Jan. 18, 2012).

118. *See, e.g.*, 137 FERC ¶ 61,220 at P 41.

119. *See, e.g.*, 183 FERC ¶ 63,020 at P 631.

120. *Id*. at P 637.

121. *Id.* at P 638-43.

122. *See* Opinion No. 522-B, *SFPP, L.P.*, 162 FERC ¶ 61,229 (2018); *compare Compliance Filing Implementing Opinion No. 522-B*, FERC Accession No. 20180514-6203, at Schedule 23(A)(1) (May 14, 2018) (calculating lawful rates for the earliest time period exclusive of the surcharge), *with SFPP Tariff No. 177*, FERC Accession No. 20090602-0177 (May 28, 2009) (the pipeline's rates immediately preceding the application). The surcharge awarded also represented approximately 10% of the initial rate increase sought. *Compare Compliance Filing Implementing Opinion No. 522-B*, FERC Accession No. 20180514-6203, at Schedule 23(B), *with SFPP Tariff No. 177*, FERC Accession No. 20090602-0177. *See SFPP Tariff No. 182*, FERC Accession No. 20090803-0061 (July 31, 2009) (tariff containing the requested rates).

2. How Rate Case Expenses Are Recovered

There are three principal methods by which regulators allow utilities to recover rate case expenses: (1) *amortizing* actual or expected expense levels over a period of years, (2) *normalizing* historic expense levels to determine an average yearly level, and (3) applying a temporary *surcharge* to recover all expenses incurred. The regulator's goals in setting a reasonable level of rate case expense can influence its choice among these three. Two competing goals that stand out are whether the regulator should set a rate case expense level to allow the regulated business (1) the *opportunity* to recover a representative level of such reasonable costs the entity is likely to experience when the rates are in effect, or (2) to receive *indemnification* of all actual rate litigation costs incurred. State regulators have different goals that typically align with their chosen method, and FERC—which uses a different method for each of its three ratemaking regimes (gas, power, and oil)—appears to have different goals in each context.

a. Amortization

Amortization rate case expenses is the approach most widely used by state regulators and is used by FERC when regulating electric utilities under the Federal Power Act (FPA)[123] and, in rare circumstances, under the Natural Gas Act (NGA).[124] This approach has been identified as "customary" by the Federal Power Commission as far back as 1942.[125] Under this approach "regulatory expenses should be amortized over the period of time during which the rates at issue are expected to be in effect."[126] FERC and most state regulators set this amortization period to match the expected interval between rate cases.[127] FERC and most regulators do not require rates be reduced after the conclusion of the amortization period, as would be expected with a surcharge.[128] While rate case expenses are

123. *See* Michael E. Small, *A FERC Electric Rate Primer*, 5 ENERGY L. J. 107, 114-15 (1984) ("In determining whether regulatory expenses are reasonable three questions arise: (1) whether the amortization period is appropriate; (2) whether prior rate case expenses can be recovered; and (3) whether the total amount of expense is reasonable."). Since the publication of that article, FERC has resolved the second question in the negative in the context of a gas case, reasoning from "standard Commission policy to amortize gas pipeline and electric utility rate case expense" which FERC reasoned did not include giving "rate base effect to the unamortized balance." *Kuparuk Transp. Co*., 45 FERC ¶ 63,006, 65091 (1988) ("such special treatment is denied.").

124. *Enbridge Pipelines (KPC)*, 100 FERC ¶ 61,260 at PP 359-63 (2002).

125. Colorado v. Public Serv. Comm'n of Colo., 3 F.P.C. 32, 55 (1942).

126. 148 FERC ¶ 61,206 at P 221 (citing 17 FERC ¶ 61,123, 61,251 (1981) (citing *Alabama-Tennessee Nat. Gas Co*., 11 F.P.C. 75, 82-83 (1952), and Opinion No. 730, *Sierra Pac. Power Co*., 53 F.P.C. 1795, 1805 (1975) and 86 FERC ¶ 61,165, at 61,582 (1999)).

127. *Id*. at PP 221-22. *See also, e.g.*, Appendix at 11 (District of Columbia), 13-14 (Georgia), 14 (Hawaii), 16-17 (Illinois).

128. 148 FERC ¶ 61,206 at P 223 ("A one-year amortization period would guarantee [utility] over-collection of its regulatory expenses as the rates have been in effect for longer than one year and will remain in effect indefinitely until such time that a superseding rate case is filed."); *see, e.g.*, Appendix at 11-13 (Florida); *but see id.* at 54-55 (Washington).

being amortized, FERC and most states prohibit utilities from including the unamortized portion in their rate base or otherwise earning a return.[129]

b. Normalization

Rate case expense levels can also be established via normalization. This is the approach used in a minority of states[130] and by FERC when setting rates under the NGA.[131] Under this approach, the regulator takes the average annual cost experience over a sufficiently long historic period in order to establish a future level.[132] This approach is not limited to rate case expenses, but is employed generally in setting reasonable levels for recoverable expenses that fluctuate widely from year to year.[133] The Delaware Public Service Commission has articulated that "normalization [of rate case expense] is more consistent with the essential concept that rates are set to allow the [utility] to recover normal recurring expenses during the period the rates are to be in effect, and not to guarantee a dollar-for-dollar recovery of past expenses."[134] FERC has long employed this approach for rate case expense under the NGA, and by the Federal Power Commission before it.[135] Although its preference under the NGA is to use normalization, FERC has articulated that it may employ another method "[i]n the absence of sufficient historical data, or where the record indicates that the historical data are not reflective of potential future expense levels."[136] FERC does not appear to have seriously considered this approach when addressing electric utility rate case expenses or explained its different treatment across industries.[137]

c. Surcharges

The last approach employed for rate case expense recovery is a surcharge. This method is used by a handful of states, sometimes in exceptional

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129. Appendix at 16-17 (Illinois), 46-47 (South Carolina); 37-38 (New Mexico), 48-52 (Texas). *But see id.* at 38-39 (New York). While FERC does not appear to have recently addressed this issue under the FPA, it has rejected rate base treatment when implementing an amortization approach under the NGA. Opinion No. 486, *Kern River Gas Transmission Co*., 117 FERC ¶ 61,077 at P 278 (2006).

130. Appendix at 10-11 (Delaware), 22-24 (Maine), 54 (Virginia), 55-56 (West Virginia); *see also id.* at 56-57 (Wisconsin).

131. *See, e.g.*, 145 FERC ¶ 61,040 at PP 73-74.

132. *Id*.

133. *See, e.g.*, 185 FERC ¶ 61,126 at PP 262, 266 (ICA); 18 C.F.R. §154.303(a)(4); 181 FERC ¶ 61,211 at PP 22-27 (NGA).

134. Diamond State Tel. Co., Docket No. 92-47, 1993 Del. PSC LEXIS 22, at *6 (Nov. 30, 1993).

135. *Colorado Interstate Gas Co*., 35 FERC ¶ 63,043, 65,132 (1986), *aff'd* 41 FERC ¶ 61,179 (1987); Opinion No. 600-A, *El Paso Nat. Gas Co.*, 47 F.P.C. 1157 (1972).

136. 145 FERC ¶ 61,040 at P 73. *See also* 117 FERC ¶ 61,077 at P 278 ("The Commission's general approach to Regulatory Commission expenses is to look at a historical three or five-year period in order to establish a representative level of a pipeline's future expense level during the period the rates are effective. However, here, Kern River did not provide historical data and both staff and Kern River concur that historical amounts are not reflective of potential future expense levels.").

137. While FERC's disparate treatment of rate case expense recovery has not been challenged on judicial review, disparate ratemaking treatment across statutes has been found to be arbitrary and capricious. See, e.g., Environmental Action, Inc. v. FERC, 939 F.2d 1057, 1063 (D. C Cir. 1991).

circumstances, as well as by FERC under the Interstate Commerce Act (ICA).[138] In that context, FERC has articulated that "[w]here significant litigation costs have been incurred and it is uncertain whether those litigation costs will continue into future years, a surcharge based upon actual litigation costs provides an appropriate means to avoid both over-recovery and under-recovery," whereas "there is little assurance that base period data, test period data, or any other normalization would provide sufficiently representative estimates of future expense levels."[139] Like amortization, a surcharge is designed to allow recovery over a set period of time. Unlike amortization, however, it does not "permanently embed a litigation recovery" in the entity's rates.[140] FERC sets the target recovery period for rate case expense surcharges to align with "the length of the litigation at issue."[141] This differs from amortization, which is usually intended to align with the frequency of rate cases. State regulators that have articulated a policy on surcharge period timing have focused on ratepayer impact rather than rate case intervals or the term of litigation.[142] In the context of rate complaints under the ICA—where reparations are available only to complaining shippers—FERC has a policy of "credit[ing] the amount of unpaid reparations to noncomplaining shippers against the total" rate case expense that can be recovered through a surcharge.[143]

III. ANALYZING RATE CASE EXPENSE RECOVERY AS A FORM OF FEE SHIFTING SHOWS IT TO BE UNJUSTIFIED AND FRAUGHT WITH PERVERSE INCENTIVES

Rate case expense recovery is fundamentally a form of fee shifting because one side (the ratepayers) of the legal dispute (the rate case) is responsible for the other side's (the utility's) litigation expenses stemming from that dispute. In contrast to the dearth of scholarship that addresses rate case expense recovery,[144] there is a breadth and depth of scholarship examining fee shifting from several perspectives. A full survey of this fee shifting scholarship is beyond the scope of this article, which focuses on the generally established legal foundations, purposes, and likely effects of fee shifting to inform policy on rate case expense recovery. Comparing rate case expense recovery to other forms of fee shifting shows that awarding recovery without meaningful limits is unsound policy and anathema to legal norms.

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138. *See, e.g.*, Opinion No. 511, *SFPP, L.P.*, 134 FERC ¶ 61,121 at P 35 (2011).

139. *Id*.

140. *Id*. at P 37.

141. 153 FERC ¶ 61,233 at P 136 (citing 134 FERC ¶ 61,121 at PP 35-37).

142. *See* Appendix at 48-52 (Texas), 18-19 (Iowa); *see also* Global Water-Palo Verde Utils. Co., Decision No. 78644, at 148-49 (Ariz. Corp. Comm'n July 27, 2022), https://docket.images.azcc.gov/0000207261.pdf?i=1759334104604 (setting recovery period "to moderate the impact" of the last phase of the rate increase).

143. 185 FERC ¶ 61,126 at PP 273-76 (*see* Opinion No. 571, *Chevron Prods. Co. v. SFPP, L.P.*, 172 FERC ¶ 61,207 at PP 59, 65-66, 70-71 (2020); *Mobil Oil Corp. v. SFPP, L.P.*, 100 FERC ¶ 61,353 at P 12 (2002); BP W. Coast Prods., LLC v. FERC, 374 F.3d 1293, 1294 (D.C. Cir. 2004)).

144. *See* PHILLIPS, *supra* note 13, at 237-38; Michael E. Small, *A FERC Electric Rate Primer*, 5 ENERGY L. J. 107, 114-15 (1984); 78 Ohio Jur. 3d Public Utilities § 155 (2025); 73B C.J.S. Public Utilities § 93 (2025); 64 Am. Jur. 2d Public Utilities § 114 (2025).

The legal foundation of rate case expense recovery is academically unique compared to other forms of fee shifting because it is implied rather than expressly authorized. This lack of legislative oversight may explain in part its policy failures. The established justifications for fee shifting also provide a stark contrast to rate case expense recovery. In fact, besides the premise that fee shifting can help fully compensate a party vindicating their legal rights, nearly every basis used to justify fee shifting is inapplicable or cautions against the practice of rate case expense recovery. Specifically, such recovery (1) makes the intended beneficiaries of regulation (ratepayers) pay for the targets of regulation (utilities) to resist its enforcement; (2) disincentivizes the public good of participating in regulatory proceedings; and (3) exacerbates barriers to participating in proceedings for those with fewer resources and small-value claims (individual ratepayers) while subsidizing the better-resourced parties with higher-value claims (utilities). The litigation incentives created by allowing rate case expense recovery regardless of their level or the merits of a case, as discussed in the following section, also strongly validate the need for their reform.

A. Rate Case Expense Recovery Is a Form of Fee Shifting

Rate case expense recovery operates as a form of fee shifting because it makes one side to a dispute (i.e., ratepayers) responsible for paying the attorneys' fees and related costs of their adversary to that dispute (the utility). Definitions of fee shifting tend to assume that fees are only ever shifted to (i.e., ultimately paid by) the losing party. For instance, Black's Law Dictionary defines "fee-shifting" as "[t]he transfer of responsibility for paying fees, esp. attorney's fees, from the prevailing party to the losing party."[145] The limit in Black's definition, however, is understandable, given that virtually every other fee shifting regime—for glaringly obvious policy reasons—makes recovery of legal fees contingent on success.[146] This article uses a broader definition of fee shifting that includes awarding fees to non-prevailing parties. This definition is consistent with recent Supreme Court precedent on the topic.[147] Fee shifting can thus be defined as:

> The transfer of responsibility from one party to a dispute to another party to that dispute, of paying the latter's attorney's fees and related fees incurred in said dispute.

Rate case expense recovery fits this definition perfectly in intent and effect because one set of parties (the ratepayers) of the legal dispute (the rate case) are responsible for the other side's (the utility's) attorney and related expenses. As described above, rate case litigation pits utilities against ratepayers. When a utility can recover its attorney's fees from that dispute as rate case expense, it is ratepayers who ultimately bear that financial burden. FERC's stated goal is to allow the regulated entity to recover all expenses associated with a dispute,

145. *Fee-shifting*, Black's LAW DICTIONARY (12th Ed. 2024).

146. Ruckelshaus v. Sierra Club, 463 U.S. 680, 684 (1983).

147. *See* Peter v. Nantkwest, Inc., 589 U.S. 23, 29 (2019) ("contrary to the Government's suggestion, Congress has indeed enacted fee-shifting statutes that apply to nonprevailing parties.").

whether in the form of a tracking and surcharge mechanism[148] or an estimate.[149] When FERC employs a normalized level of recoverable expense, that level is still meant to set "a representative level of a [business's] future [rate case expenses] level during the period the rates are effective" that ratepayers must bear.[150] As described above and in the Appendix hereto, state regulators share a similar understanding, especially those who exercise oversight of this cost item comparable to FERC's.

While fee shifting is unique in many ways, these differences do not change the reality for participants litigating before regulators and courts. Rate case expense recovery undeniably introduces fee shifting to the arena of regulatory litigation. Many state regulators understand this.[151] It is therefore reasonable to lean on the established scholarship and precedent on fee shifting to assess the merits and consequences of rate case expense recovery. This body of analysis can inform whether rate case expense recovery can be justified, what its pitfalls are, and what reforms can or should be adopted.

B. Legal Foundation of American Fee Shifting in Conventional Disputes Is Antithetical to Rate Case Expense Recovery

In the American legal system parties to disputes normally must bear their own costs "unless a statute or contract provides otherwise."[152] This is known as the "American Rule," to contrast it to the "English Rule," where the loser is normally required to pay the winner's reasonable legal fees.[153] Limited exceptions

148. 134 FERC ¶ 61,121 at P 37.

149. 148 FERC ¶ 61,206 at PP 221-24 (describing a reasonable estimate and noting it reflects "the full amount of [the entity'] regulatory expenses").

150. 145 FERC ¶ 61,040 at P 73.

151. Community Utils. Of Ind., Inc. 2023 Ind. PUC LEXIS 102, at *5 (May 3, 2023) (endorsing statement that "rate cases are considered the exception to the general American Rule"); Appendix at 19-21 (Kansas) (quoting Kansas City Power & Light Co., Docket No. 10-KCPE-415-RTS, 2012 Kan. PUC LEXIS 89, at *40 (Jan. 18, 2012) ("If the American Rule were applied here, [the utility] would be responsible for paying its own expenses and costs, [and] would not recover any rate case expense from ratepayers . . . But historically Kansas utilities have been allowed recovery of prudently incurred rate case expense that is just and reasonable as one of the many components making up revenue requirement."); Sunshine Utils. Of Cent. Fla. Inc., Docket No. 900386-WU, 1994 Fla. PUC LEXIS 613, at *17 (June 15, 1994) (borrowing insight from fee shifting cases for rate case expense recovery); North Shore Gas Co., 2014 Ill. PUC LEXIS 827, at *106 (Nov. 7, 2014) (same); Mid-Kansas Am. Pipeline Co., Docket No. 12-MDAP-068-RTS, 2012 Kan. PUC LEXIS 40, at *8 (Jan. 11, 2012) (setting for briefing whether rate case expenses should be recovered "or the American rule" should apply); *see also* Appendix at 31-33 (Missouri) (quoting Kansas City Power & Light Co., 2015 Mo. PSC LEXIS 789, at *133-34 (Sep. 2, 2015) (recognizing that rate case expenses were unique in part because rate cases were adversarial and "requiring all rate case expense to be paid by ratepayers provides the utility with an inequitable financial advantage over other case participants."). *But see* Atmos Energy Co., Decision No. C23-0293, 2023 COLO. PUC LEXIS 289, at *24-25 (Apr. 21, 2023) (differentiating rate case expense inquiry from lodestar inquiry in attorneys' fee disputes).

152. Baker Botts L.L.P. v. ASARCO LLC, 576 U.S. 121, 121 (2015) (quoting Hardt v. Reliance Standard Life Ins. Co., 560 U.S. 242, 252–53); Lackey v. Stinnie, 604 U.S. 192, 199 (2025) ("Federal courts may depart from [the American] rule only when 'there is express statutory authorization' to do so.") (quoting Hensley v. Eckerhart, 461 U.S. 424, 429 (1983).

153. Susan M. Olson, *How Much Access to Justice from State Equal Access to Justice Acts*, 71 CHI.-KENT L. REV. 547, 549-50 (1995). While referred to in the Unites States as the English Rule, it is followed in some form by nearly every jurisdiction outside of the United States. *See* David P. Riesenberg, *Fee Shifting in Investor-*

to the American Rule arise in class action cases, where attorneys may be paid through the common fund,[154] or in cases of misconduct.[155] Other exceptions, such as the "private attorney general" theory, have been put forward but rejected at the federal level.[156] Even when provided for by statute, such authorization is construed narrowly against the presumption against fee shifting, with courts demanding "express statutory authorization."[157]

Ironically, FERC appears to believe that it also adheres strictly to the American Rule, claiming it is "well-established" that the agency cannot award attorneys' fees without statutory authorization.[158] State energy regulators typically, but not universally, reach similar conclusions.[159] This paradigm is reversed, however, when the utility seeks to recover its litigation expenses. As described above, recovery of rate case expense is not authorized by any statute, but rather by an implicit authority in setting cost-of-service rates. In fact, as shown in the Appendix, where states have specific statutes governing the practice, they

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State Arbitration: Doctrine and Policy Justifying Application of the English Rule, 60 DUKE L.J. 977, 1000 (2011). Within the United States, the state of Alaska is unique in generally following the English Rule of awarding prevailing party fees as a matter of course. *See generally* Virginia Cella Antipolo, *The Impact of Economic Incentives on the Award of Attorney's Fees in Public Interest Litigation*, 1 ALASKA L. REV. 189 (1984).

154. *See* Boeing Co. v. Van Gemert, 444 U.S. 472, 478 (1980) ("The common-fund doctrine reflects the traditional practice in courts of equity, . . . and it stands as a well-recognized exception to the general principle that requires every litigant to bear his own attorney's fees,") (citing Alyeska Pipeline Service Co. v. Wilderness Society, 421 U.S. 240, at 257–258 (1975)).; Maureen Carroll, *Fee-Shifting Statutes and Compensation for Risk*, 95 IND. L.J. 1021 (2020).

155. *See, e.g.*, Alyeska Pipeline Serv. Co. v. Wilderness Soc'y, 421 U.S. 240, 258-59 (1975).

156. *Id*. at 270 (the American Rule "is deeply rooted in our history and in congressional policy; and it is not for us to invade the legislature's province by redistributing litigation costs in the manner suggested by respondents and followed by the Court of Appeals.").

157. *Lackey*, 604 U.S. 192, 199 (2025) (quoting Hensley v. Eckerhart, 461 U.S. 424, 429 (1983)); *see also* Peter v. Nantkwest, Inc., 589 U.S. 23, 28 (2019) (citing Sebelius v. Cloer, 569 U.S. 369 (2013)); *id.* 31-32 ("the term "expenses" alone does not authorize recovery of attorney's fees"); *see also* Baker Botts L.L.P., 576 U.S. 121, 133-34 (2015).

158. *Newmont Nevada Energy Inv. LLC v. Sierra Specific Power Co*., 147 FERC ¶ 61,030 at P 42 (2014) ("The Commission has stated that '[a]lthough the federal courts are empowered to award attorneys' fees where a party has litigated in bad faith, as a limited exception to the general 'American Rule' that parties to litigation pay their own attorneys' fees regardless of a lawsuit's outcome, no statute confers such authority on the Commission, and the Commission has never claimed such authority.'") (quoting *State of Cal.,* ex rel. *Lockyer v. British Columbia Power Exch. Corp*., 139 FERC ¶ 61,213 at P 24 (2012)).

159. *Compare* Southwestern Elec. Power Co., Order No. 38, 2015 Ark. PUC LEXIS 203, at *16 (May 20, 2015) ("Without specific statutory authority, the Commission cannot make an award of attorneys' fees."); Pastrick v. Southwestern Bell Tel. Co., No. TC-2002-301, 2003 Mo. PSC LEXIS 1055, at *7 (Aug. 21, 2003); Oak Hill Garbage Disposal, Inc. v. Lusk Disposal Serv., Inc., No. 03-0950-SWF-C, 2003 W. Va. PUC LEXIS 3398, at *10 (July 25, 2004); Tampa Elec. Co., Docket No. 120192-EI, 2013 Fla. PUC LEXIS 43, at *8 (Feb. 7, 2013), *with* Stewart v. Utah Pub. Serv. Comm'n, 885 P.2d 759, 783 (1994); Barenberg v. Louviers Mut. Serv. Co., Docket No. 07F-036W, 2008 Colo. PUC LEXIS 942, at *5 (Sep. 23, 2008) ("The Commission has considerable discretion and broadly based authority in awarding attorneys fees and costs to complainants in utility disputes.") (citing Mountain States Tel. & Tel. Co. v. Public Utils. Comm'n of Colo., 576 P.2d 544, 547 (1978)). *See also* Consumers Lobby Against Monopolies v. Public Utils. Com., 25 Cal. 3d 891 (1979), disapproved of on other grounds by *Kowis v. Howard*, 3 Cal. 4th 888, 838 P.2d 250 (1992) (California PUC has authority to award attorney's fees in reparations complaints but not in rate cases); Linda M. Ross, *Consumers Lobby Against Monopolies v. Public Utilities Commission: The PUC's Power to Award Attorney Fees*, 69 CALIF. L. REV. 969 (1981).

serve primarily to limit recovery, not to authorize it. A default rule in favor of fee shifting implied rather than expressly authorized would be inconceivable in every other American legal setting.

C. The Policy Justifications for Fee Shifting Are Mostly Incompatible with Rate Case Expense Recovery

It is difficult to justify rate case expense using the rationales that lawyers and economists have put forward to justify other forms of fee shifting. Many federal and state statutes provide for fee shifting.[160] In each case, the legislature has affirmatively selected fee shifting as a means of achieving one or more policy goals. This article measures rate case expense recovery against these policy justifications for fee shifting. In doing so, it borrows the influential list of six rationales identified by Prof. Thomas Rowe, Jr.[161] These are fairness considerations, full compensation, punishment and deterrence, public benefits, imbalanced resources of the parties, and creating efficient litigation incentives generally.[162] Though composed several decades ago, the list put forward by Rowe still appears to encompass the full debate,[163] and the broader umbrella categories provide a ready point against which to measure rate case expense recovery.

This comparison shows another way that rate case expense recovery is unique: not only does it not serve to advance any of the traditional rationales, in most cases it operates against them. Indeed, the only policy goal (sometimes) furthered by rate case expense recovery is that of full compensation for legal vindication. The punitive rationale is not applicable. The goals of public benefit, overcoming imbalanced resources of the parties, and litigation incentives are all actively undermined by it, as is the fuzzier goal of "fairness," at least according to American legal norms.

1. Fairness

The first rationale identified by Professor Rowe is that of "fairness."[164] While abstract ideas of fairness are mostly beyond the scope of this article, the recovery of rate case expenses can certainly be said to cut against American legal norms, which disfavor fee shifting. Most assessments of the normative fairness of fee shifting focus on the concrete outcomes, i.e., rationales two through six below.[165] As Professor Rowe discusses, views of the "fairness" of fee shifting in the abstract are very dependent on culture. While the English Rule is the majority practice

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160. *See* Ruckelshaus v. Sierra Club, 463 U.S. 680, 684 (1983) (stating there were more than 150 federal statutory fee-shifting provisions); *State Attorney Fee Shifting Statutes: Are We Quietly Repealing the American Rule*, 47 LAW & CONTEMP. PROBS. 321 (1984) (survey identifying 1,974 state fee-shifting statutes); Olson, *supra* note 153, at 552 (describing state fee shifting statutes); HENRY COHEN, CONG. RSCH. SERV., R94-970, AWARDS OF ATTORNEYS' FEES BY FEDERAL COURTS AND FEDERAL AGENCIES 64-114 (2009) (listing federal statutes).

161. Thomas D. Rowe Jr., *The Legal Theory of Attorney Fee Shifting: A Critical Overview*, 1982 DUKE L.J. 651 (1982).

162. *Id.* at 653-66.

163. *See, e.g.*, Harold J. Krent, *Explaining One-Way Fee Shifting*, 79 VA. L. REV. 2039, 2045-75 (1993) (identifying rationales for one-way fee shifting that fit within these larger umbrellas).

164. Rowe, *supra* note 161, at 653-57.

165. *See, e.g.*, Issachar Rosen-Zui, *Just Fee Shifting*, 37 FLA. ST. U. L. REV. 717 (2010).

globally (perhaps because it is perceived as discouraging litigation), "American attitudes, however," are more opposed to fee shifting because we "tend to regard litigation as everyone's right and to emphasize the importance of not excessively hindering access to justice."[166]

Though fairness is not the focus of this article, we should not completely ignore important societal norms. State regulators and legislatures that restrict, or prohibit, rate case expense recovery certainly appear concerned with its perceived unfairness.[167] Without the benefit of a survey, the author still submits it is likely that the typical American ratepayer (who would normally have to pay their own legal bills) would not find it "fair" that the rates they pay for water, electric, gas, and other regulated services must all be increased to pay for lawyers in regulatory proceedings to argue against the lawyers that represent the ratepayers' interests. Common notions of fairness also cut against the idea that rate case expenses can be recovered regardless of the merits of the utility's case. As the Supreme Court has articulated, acceptance of the "established rule [that] a successful party need not pay its unsuccessful adversary's fees. . . reflects, at least in part, intuitive notions of fairness to litigants."[168]

2. Full Compensation

The full compensation (or "make whole") rationale is the one justification of fee shifting that *does* (partially) apply to the logic of rate case expense recovery. This argument is that, because attorneys must be paid to vindicate legal rights, fee shifting is required for a legally harmed party to truly be made whole.[169] This rationale has, however, been consistently rejected by federal courts as a basis to infer fee shifting.[170] As described above, the rationale for rate case expense recovery is that utilities should be compensated for their operating costs, which include the costs of prosecuting rate cases. To the extent the full compensation rationale is invoked to justify rate case expense recovery, an important distinction is that recovery of rate case expenses is typically divorced from the merits of the underlying case.

Rate case expenses are typically recovered by utilities in their rates regardless of how successful they are in their rate case.[171] As the Supreme Court opined in dictum, a "utility should be allowed its fair and proper expenses for presenting its

166. Rowe, *supra* note 161, at 656 (citing Philip Corboy, *Contingency Fees: The Individual's Key to the Courthouse Door*, 2 Litig. 27 (1976)).

167. *See* Appendix at 30-31 (Mississippi); Suez Water Arlington Hills Inc., Docket No. WR16060510, 2017 N.J. PUC LEXIS 253, at *30 (Nov. 13, 2017) ("Rate Counsel noted that the Board's long standing 50/50 rate case sharing policy is rooted in fundamental fairness, as both shareholders and ratepayers benefit from a rate case proceeding.") (discussed in Appendix at 36-37); Plautz, *supra* note 6.

168. Ruckelshaus v. Sierra Club, 463 U.S. 680, 685 (1983). Note however that there are rare exceptions where the government pays an unsuccessful parties' legal fees, such as the National Childhood Vaccine Injury Act of 1986. *See* Sebelius v. Cloer, 569 U.S. 369 (2013).

169. Rowe, *supra* note 161, at 657.

170. *See, e.g.*, Summit Valley Indus. Inc. v. Local 112, United Bhd. of Carpenters & Joiners of Am., 456 U.S. 717, 725 (1982).

171. *See* discussion *supra* Part II.B.1.c.

side to the commission" even "where the rates in effect are excessive."[172] The full compensation rationale, to the extent it applies to rate case expense recovery, does so only to the extent the utility prevails. In fact, Rowe and other scholars of fee shifting have expressed that this rationale does not apply unless the liable party has affirmatively committed some wrongful act.[173] Any concern with ratepayer culpability is obviously inapplicable to a cost-of-service ratemaking. The bare minimum that a case be meritorious does, however, apply. Legal fees spent pursuing unsuccessful (even if viable) arguments cannot have been required to secure the relief ultimately awarded.[174]

While an imperfect fit, the full compensation rationale does provide some justification for rate case expense recovery as a form of fee shifting, insofar as it overlaps with the traditional ratemaking justification. The comparison is somewhat limited, and indeed raises more points of scrutiny than assurances. However, the concern that utility rates compensate for their costs should be considered in recommending reforms to the general practices around rate case expenses.

3. Punishment and Deterrence

Another justification for fee shifting is that it can punish and deter misconduct that occurs both outside and within litigation.[175] This rationale does not apply to rate case expense recovery. Rate case expenses are recovered by utilities from their ratepayers. There is no reason to believe that the recoverability of rate case expenses influences the conduct of either utilities or ratepayers outside of the litigation. Automatic indemnification would of course influence behavior within litigation, as described below. For instance, ratepayer advocates might be discouraged from challenging even very unsound legal positions of a utility, if they believe any positive results might be offset by an increase in the utility's recoverable litigation costs.[176] It is also possible, as FERC and other regulators have found, that ratepayer conduct in a proceeding can influence the level of litigation costs.[177] However, participating in a rate case is not considered to be a wrong to be deterred. To the contrary, it is the public policy of FERC to encourage public participation in its rate cases.[178] Therefore, rate case expense recovery

172. Driscoll v. Edison Light & Power Co., 307 U.S. 104, 120-21 (1939).

173. Rowe, *supra* note 161, at 658 ("The make-whole rationale as defined here, by contrast, requires fee shifting only if the loser was somehow at fault--either in his primary conduct or in the course of litigation-in forcing the winner to spend money on legal services."); Krent, *supra* note 163, at 2070-71.

174. And as described in the recommendation section, legal fees spent on unavailing arguments are not truly related to or required for the provision of regulated services.

175. Rowe, *supra* note 161, at 660-61.

176. For instance, even if ratepayers believe they have a strong chance (60 to 80%) of prevailing on a specific issue worth $500,000 net present value, but they would need to expend $50,000 additional legal fees to pursue that claim and the utility would be expected to spend $350,000 in responding to their arguments, then raising that issue has a net negative value (minus $100,000 to $0).

177. *See, e.g.*, 137 FERC ¶ 61,220 at P 41 ("Although SFPP made the decision to file the rate increase, it does not control the degree to which shippers have litigated the issues raised in this proceeding."); *see also* Crimson Cal. Pipeline L.P., Decision No. 20-11-026, 2020 Cal. PUC LEXIS 966, at *14 (Nov. 23, 2020).

178. *See Office of Public Participation*, FERC, https://www.ferc.gov/OPP, (last visited Oct. 2, 2025).

cannot be justified as a means of punishment or deterrence. If anything, it has the potential to deter public participation that is generally considered positive.

4. Public Benefits and Regulatory Enforcement

Fee shifting is also sometimes justified because it can support litigation in the public interest or enforce a regulatory regime.[179] This consideration does not justify the recoverability of rate case expenses; in fact, it cuts strongly against it. This is one of the most common rationales invoked to justify fee shifting in America. As the Supreme Court articulated, "under some, if not most, of the statutes providing for the allowance of reasonable fees, Congress has opted to rely heavily on private enforcement to implement public policy and to allow counsel fees so as to encourage private litigation."[180] The theory goes that in many cases "potential plaintiffs may well refrain from bringing socially beneficial suits because the gains would not sufficiently further their private interests."[181] Robert Percival and Geoffrey Miller explain that this arises when "the benefits of such litigation are widely scattered."[182] These disincentives are difficult to overcome with voluntary contributions because of transaction costs and "free riders."[183] Relatedly, Professor Krent has similarly articulated that "fee shifting serves as a means of encouraging private parties to help enforce federal regulatory requirements, particularly where government enforcement might prove inefficient."[184]

The goal of funding public interest litigation is uniquely disserved by shifting rate case expenses to ratepayers. Rate cases are tried under regulatory regimes whose primary purpose is to protect consumers from unreasonably high rates charged by utilities.[185] Lower rates (so long as they are not confiscatory) are themselves a public benefit.[186] In these disputes, the utilities' lawyers are arguing for *higher* rates. Rate case expense recovery therefore uniquely shifts fees *against* public benefits and regulatory enforcement. Furthermore, it is the ratepayers that constitute the (often extremely) dispersed set of interests. It is their attorneys (often funded with donations, government expenditures, or through an established "intervenor compensation" mechanism) that are enforcing the regulatory regime by seeking lower rates for the broader public. Rate case expense recovery therefore cannot be justified as supporting regulatory enforcement; in fact, it subsidizes *resistance* to enforcement of laws primarily aimed at protecting ratepayers from unjustified rate increases.

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179. Rowe, *supra* note 161, at 662-63. Professor Rowe calls this the "'private attorney general' theory." However, this article will not use that term to keep it distinct from the now largely rejected common law exception to the American rule.

180. Alyeska Pipeline Serv. Co. v. Wilderness Soc'y, 421 U.S. 240, 263 (1975).

181. Rowe, *supra* note 161, at 662.

182. Robert V. Percival & Geoffrey P. Miller, *The Role of Attorney Fee Shifting in Public Interest Litigation*, 47 LAW & CONTEMP. PROBS. 233, 237-38 (1984).

183. *Id.* at 238-39.

184. Krent, *supra* note 163, at 2057.

185. *See* discussion *supra* p. 5; *see also supra* note 13.

186. *See, e.g.*, *Northern Border Pipeline Co*., 53 FERC ¶ 61,051 (1990); *Colorado Interstate Gas Co*., 97 FERC ¶ 61,385 (2001); *Great Basin Gas Transmission Co*., 189 FERC ¶63,010 (2024).

5. Overcoming Economic Barriers

Another frequently invoked justification for fee shifting is that it can place litigants on a more even footing when they face imbalanced resources that prevent access to the legal process.[187] As with the "full compensation" rationale, the costs of litigating relative to the value of the claim can be prohibitive for many individuals absent fee shifting.[188] One such example would be the federal and state "Equal Access to Justice" Acts, which award fees against government defendants in suits by individuals.[189] This rationale applies only to one-way fee shifting.[190] Two-way "English Rule" fee shifting tends to deter litigation against wealthier defendants by poorer or more risk-averse plaintiffs, who must risk paying the wealthier party's defense bills in order to bring a legal action.[191]

As with other considerations, this rationale for fee shifting does not support recovery and rate case expense, but rather cautions strongly against it. In a typical rate case, no serious argument can be made that the regulated utility faces an imbalance of resources relative to the ratepayers. Utilities tend to be large, well-resourced businesses, and their rate cases are very high value propositions for them. To the contrary, as state regulators have identified, it is intervenors representing ratepayer interests that face financial barriers to participate in rate cases.[192] Even if a ratepaying entity has relatively greater resources, they still have a much lower stake in the proceeding relative to the utility (unless they are the only ratepayer). Notably, many states have established "intervenor compensation" regimes designed to encourage participation in rate cases by interested parties that cannot otherwise afford to.[193] Even FERC has the theoretical authority to award fees to intervenors whose participation presents financial hardship.[194] There are

187. Rowe, *supra* note 161, at 663-65.

188. Carroll, *supra* note 154, at 1034-36 (describing such situations as "gaps in the market for legal services").

189. Rowe, *supra* note 161, at 664-65 (discussing 28 U.S.C. § 2412 (d)(1)(A)); Olson, *supra* note 153, at 547.

190. Krent, *supra* note 163, at 2050 n.48. One-way shifting, which is the form typical in America, limits recovery to one party, e.g. the plaintiff in a particular case. By contrast "two-way" fee shifting allows recovery to either party as captured in the "English" Rule that is dominant globally.

191. *See, e.g.*, Rosen-Zui, *supra* note 165, at 740; Keith N. Hylton, *Fee Shifting and Predictability of Law*, 71 CHI.-KENT L. REV. 427, 445-46 (1995).

192. Kansas City Power & Light Co., 2015 Mo. PSC LEXIS 789, at *126-128 (Sep. 2, 2015) ("While [the utility] is able to recoup the costs of its legal counsel and expenses through utility service rates, [the Office of People's Counsel], the entity representing ratepayers, operates within a tight annual budget, and interveners pay their own legal expenses.").

193. *See, e.g.*, CAL. PUB. UTIL. CODE § 1801.3 ("The provisions of this article shall be administered in a manner that encourages the effective and efficient participation of all groups that have a stake in the public utility regulation process."), Southern Cal. Edison Co. v. Public Utilities Com., 117 Cal. App. 4th 1039, 1049-51 (2004); 220 ILL. COMP. STAT. ANN. 5/9-229(b) (2025); Second Notice Order, Docket No. 22-0238, at 14 (Ill. Corp. Comm'n Jan. 19, 2023), https://icc.illinois.gov/docket/P2022-0238/documents/332886/files/579610.pdf ("the purpose of the legislation is to assist eligible entities that may not otherwise be able to participate in Commission proceedings due to financial constraints. One of the main goals of the legislation is to encourage participation for new stakeholders and remove economic barriers associated with undue financial risk.").

194. 16 U.S.C. § 825q-1(b)(2). This authority has been cut short by Congress's later limitation in appropriation bills. *See* HENRY COHEN, CONG. RSCH. SERV., R94-970, AWARDS OF ATTORNEYS' FEES BY FEDERAL COURTS AND FEDERAL AGENCIES 60 (2009) (discussing P.L. 102-377 (1992), § 502).

no similar financial barriers to participation on the part of utilities. Rate case recovery cannot therefore be justified as necessary to overcome cost barriers faced by utilities.

Interestingly under this rationale, fee shifting is most justified when the costs are high relative to the value of the case.[195] As described above and in the Appendix, however, utility regulators that consider high legal costs relative to a utility's claims have found this indicates that rate case expense in a specific case might be unreasonably high.

6. Economic Incentives Generally

Finally, fee shifting is justified as creating better overall economic incentives, primarily by discouraging low merit claims (and encouraging meritorious but small claims described above).[196] This rationale, however, is premised on two elements that are absent regarding rate case expenses: two-way shifting and connection to the merits.[197] Therefore, this rationale for fee shifting does not support rate case expense recovery. In fact, because rate case expenses are virtually guaranteed to be recovered, their recovery creates uniquely problematic litigation incentives, which are discussed in the following section.

D. Experience with Fee Shifting Shows That Rate Case Expense Recovery Requires Limits and Scrutiny

The availability of fee shifting changes the dynamics of litigation; indeed, it is usually why jurisdictions implement it. An established body of empirical and theoretical scholarship analyzes the effects and effectiveness of fee shifting. Because rate case expense recovery is a form of fee shifting, this scholarship can provide important insight into the benefits and drawbacks of its current policy.[198] Generally, one-way fee shifting is understood to increase the number of claims and the level of legal expenditures, and to skew settlement positions. Because rate case expense is generally guaranteed regardless of the merits of a case, these impacts extend beyond those previously examined in other fee shifting contexts. Other fee shifting regimes also have important limitations tied to the level of costs

195. Carroll, *supra* note 154, at 1034-36 (illustrating with hypotheticals); Krent, *supra* note 163, at 2051-52.

196. Rowe, *supra* note 161, at 665-66; Rosen-Zui, *supra* note 165, at 753 ("The English 'loser pays' rule, it is maintained. . . improves claim quality by reducing the likelihood of frivolous lawsuits while increasing the likelihood of strong low-value lawsuits.").

197. Rowe, *supra* note 161, at 665; Krent, *supra* note 163, at 2040 ("Less litigation should ensue under two-way fee shifting than under one-way fee shifting because potential litigants may be deterred from litigating by the prospect of paying their adversaries' fees."); Brandon Chad Bungard, *Fee - Fie - Foe - Fum: I Smell the Efficiency of the English Rule Finding the Right Approach to Tort Reform*, 31 SETON HALL LEGIS. J. 1, 44-45 (2006).

198. The converse is also true: utility experience with rate case expense can inform the study of fee shifting. The generally public nature of utility operating expenses and rate case proceedings especially could provide a broad and deep dataset to test established theories. Furthermore, while utility rate disputes can be resolved through settlement, they usually cannot be resolved through private ordering in the absence of a formal filing. This means the public data should reflect the outcome of all potential as well as litigated disputes. Valuable comparisons could include reported rate case expenses of comparable utilities across jurisdictions with different treatment, or in the same jurisdiction before and after policy changes.

and the merits of the case, which help to blunt the most perverse incentives. In most jurisdictions, comparable limits for rate case expense recovery are lacking and needed.

1. One-Way Fee Shifting Increases the Number of Disputes and Litigation Expenditures

The precise effect fee shifting has on disputes is a matter of debate, with ongoing theoretical and empirical efforts to quantify its impact.[199] This article does not aim to resolve this theoretical debate or conduct a new empirical evaluation. However, three facts are generally agreed upon, described below. First, the availability to a party of fee shifting increases the likelihood that a party will initiate a proceeding or bring a particular claim. Second, after a proceeding has commenced, the availability of fee shifting tends to increase overall legal expenditures. And third, the availability of fee shifting impacts settlement bargaining strength and can discourage settlement overall.

Because rate case expense recovery operates only one way (from ratepayers to utilities), literature that focuses on comparing the incentives under the English Rule of two-way fee shifting and the American Rule of no fee shifting has limited value.[200] As professors Rowe and Shavell explain, it is important to distinguish between specific fee shifting regimes, particularly one-way versus two-way shifting.[201] As Rowe explains, "a one-way pro-prevailing-plaintiff rule. . . should uniformly encourage the pursuit of claims of all sorts in all situations" because that regime creates an "expect[ation of] greater net recoveries, without adding a counterbalancing threat of loss" that would exist under a two-way fee shifting regime.[202] However, some scholars have pushed back on this intuitive conclusion, arguing that it is not borne out by empirical evidence.[203]

The exact effect that one-way fee shifting has on settlement is more uncertain; however, it is generally understood to impact the bargaining strengths. Theoretically, a rational and risk-neutral party should only be expected to settle a dispute for an amount equal to or greater than their expected gain less the costs of

199. *See, e.g.*, John Yukio Gotanda, *Awarding Costs and Attorneys' Fees in International Commercial Arbitrations*, 21 MICH. J. INT'L L. 1, 27 n.172 (Fall 1999) (and articles cited therein).

200. *See, e.g.*, John C. Hause, *Indemnity, Settlement, and Litigation, or I'll be Suing You*, 18 J. LEGAL STUD. 157 (1989); James W. Hughes & Edward A. Snyder, *Litigation and Settlement Under the English and American Rules: Theory and Evidence*, 38 J.L. & ECON. 225 (1995); John J. Donohue, *The Effects of Fee Shifting on the Settlement Rate: Theoretical Observations on Costs, Conflicts, and Contingency Fees*, 54 L. & CONTEMP. PROBS. 195 (1991).

201. Thomas D. Rowe, *Predicting the Effects of Attorney Fee Shifting*, 47 L. & CONTEMP. PROBS. 139, 143-44 (1984); Steven Shavell, *Suit, Settlement, and Trial: A Theoretical Analysis Under Alternative Methods for the Allocation of Legal Costs*, 11 J. LEGAL STUDS. 55 (1982).

202. Rowe, *supra* note 201, at 147. *See also id.* at 150 (opining that while one-way fee shifting "should not encourage nuisance suits much more than the American rule" any effect of a one-way rule "could only be in the direction of more encouragement for nuisance litigation.").

203. *See, e.g.*, Margaret H. Lemos, *Special Incentives to Sue*, 95 MINN. L. REV. 782, 805-10 (2011) ("Although one-way fee shifts theoretically should increase the rate of litigation by reducing its cost, the data available on the consequences of fee shifting call into question its efficacy in that respect.").

litigating a matter.[204] Fee shifting generally lessens the likelihood of settlement on the theory that it "magnifies the effects of differences of opinion about the trial outcome" that prevented parties from settling in the first place.[205] Counterbalancing this concern is the principle that fee shifting also increases legal expenses, and that (merit-based) fee shifting increases the risks of losing, both of which make settlement more attractive for risk-averse parties.[206] Some authors have even argued that one-way fee shifting encourages settlement better than other arrangements.[207] However, most commenters hypothesize that fee shifting tends to discourage settlement, even if the effect is more pronounced in two-way than in one-way regimes.[208] In addition to the likelihood of settlements, fee-shifting can influence their substance as well.[209] As one commenter noted, when costs can "be forced on an adversary with little or no chance of recovery, [that] can distort the bargaining process and lead to settlements (or abandonment of claims) with little seeming basis in the substantive merits of a dispute."[210]

Most relevant for this article is the effect one-way fee shifting has on litigation spending once a proceeding commences.[211] In analyzing the impact of fee shifting on legal spending, scholarship in the field of law and economics seeks to model rational conduct, with the simplest modeling for risk-neutral parties. Under this basic framework a (risk-neutral) litigant can be expected to "spend[] up to the point where a dollar spent increases the expected value of the litigation" by a like amount.[212] For the same reason articulated above, fee shifting (especially when one-way) is generally understood to increase costs.[213] Where there is a chance that the party will not ultimately bear the associated costs, each decision to increase legal expenditures is more likely to be justified.

Importantly and regrettably, this increase cannot be attributed only to the more zealous pursuit of meritorious and substantive claims. Rather, unrelated procedural costs, including discovery and motions practice can play a large part. Parties have the incentive—and ability—to increase legal costs their opponent will

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204. STEVEN SHAVELL, FOUNDATIONS OF ECONOMIC ANALYSIS OF LAW 401 (Harv. Univ. Press 2004); RICHARD A. POSNER, ECONOMIC ANALYSIS OF LAW 555-56 (Little Brown Co., 4th ed. 1992).

205. SHAVELL, *supra* note 204, at 430.

206. *Id*. at 431. *See also* POSNER, *supra* note 204, at 572-73.

207. See, e.g., Keith N. Hylton, *Fee Shifting and Incentives to Comply with the Law*, 46 VAND. L. REV. 1069 (1993). *See also* Eric Talley, *Liability-Based Fee-Shifting Rules and Settlement Mechanisms Under Incomplete Information*, 71 CHI.-KENT L. REV. 461 (1995) (concluding that hypothetical "winner pays" fee shifting is most likely to encourage settlement).

208. Rowe, *supra* note 201, at 157, 157 n. 75.

209. Thomas D. Rowe, Jr. & David A. Anderson, *One-Way Fee Shifting Statutes and Offer of Judgment Rules: An Experiment*, 36 JURIMETRICS J. 255 (Spring 1996).

210. Thomas D. Rowe, Jr., *Study on Paths to a "Better Way": Litigation, Alternatives, and Accommodation*, 38 DUKE L. J. 824, 877-78 (citing Richard Marcus, *The Revival of Fact Pleading Under the Federal Rules of Civil Procedure*, 86 COLUM. L REV. 433, 456 (1986)).

211. This article does not assert that the ability to recover rate case expenses would be the deciding factor in a utility's filing of a rate case at all absent extraordinary circumstances.

212. POSNER, *supra* note 204, at 564.

213. Krent, *supra* note 163, at 2082; Braeutigam et. al., *An Economic Analysis of Alternative Fee Shifting Systems*, 47 L. & CONTEMP. PROBS. 173, 180 (Winter 1984).

have to bear.[214] One area ripe for strategic manipulation is discovery. When operating under one-way fee shifting, the indemnified party has an incentive to issue burdensome discovery requests to drive up their opponent's costs, while the party without the ability to recover those costs (typically the defendant) "has no incentive to reciprocate."[215] Even worse, when a party views fee recovery as likely, they actually "face an incentive to maximize [their] own costs" in order to drive up the costs their opponent will eventually bear.[216]

2. Fee Shifting in Conventional Litigation Has Many Limits

Fee shifting in every other context has many limits. As described above in Part III.B, explicit legislative authorization or exceptional circumstances are required for fee shifting to be available at all. When it is available, there are further limits, two of which are key. First, recovery of fees is nearly always limited to parties prevailing on the merits in some form. Second, the amount of fees recovered is seriously scrutinized in terms of both hours and rates in a manner meant to mirror the competitive market for legal services. In addition, Rule 68 of the Federal Rules of Civil Procedure creates a procedural limitation if a claimant to fees is awarded less in damages than offered in settlement.

Limiting fee recovery to winning parties is a near universal rule.[217] Indeed, this requirement is strictly construed.[218] As the Supreme Court has explained,

> virtually every one of the more than 150 existing federal fee-shifting provisions predicates fee awards on some success by the claimant; while these statutes contain varying standards as to the precise degree of success necessary for an award of fees—such as whether the fee claimant was the 'prevailing party,' the 'substantially prevailing' party, or 'successful'—the consistent rule is that complete failure will not justify shifting fees from the losing party to the winning party.[219]

According to the Supreme Court this "reflects, at least in part, intuitive notions of fairness to litigants."[220]

The amount of fees that can be recovered is also carefully scrutinized with "the degree of success obtained" identified as "the most critical factor" by the

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214. Paul Stancil, *Balancing the Pleading Equation*, 61 BAYLOR L. REV. 90, 107 (2009).

215. William H. Wagener, *Modeling the Effect of One-Way Fee Shifting on Discovery Abuse in Private Antitrust Litigation*, 78 N.Y.U. L. REV. 1887, 1998-99 (2003). *Id.* at 1906-08, 1910-12.

216. Stancil, *supra* note 214, at 106-07 ("especially if there are significant differences in the marginal value of money to the two parties").

217. For academic interest, one commenter has hypothesized that hypothetical "winner pays" system would create the strongest incentives to settle disputes but does not advocate for that rule. *See* Talley, *supra* note 207.

218. *See, e.g.*, Lackey v. Stinnie, 604 U.S. 192, 203-04 (2025) (obtaining a preliminary injunction did make one a "prevailing party" for purposes of a fee shifting statute, even if voluntary compliance then resolved the dispute); Buckhannon Bd. & Care Home, Inc. v. West Virginia Dep't of Health & Hum. Res., 532 U.S. 598, 600 (2001).

219. Ruckelshaus v. Sierra Club, 463 U.S. 680, 684 (1983). There are exceptions to this rule. *See* Peter v. Nantkwest, Inc., 589 U.S. 23, 29 (2019) (noting nonprevailing party can recover fees under specific statutes).

220. *Ruckelshaus*, 463 U.S. at 685. Note however that there are rare exceptions where the government pays an unsuccessful parties' legal fees, such as the National Childhood Vaccine Injury Act of 1986. *See* Sebelius v. Cloer, 569 U.S. 369 (2013)

Supreme Court.[221] The starting point for a recoverable fee level is the "lodestar," described above, which sets the fee award by multiplying the hours reasonably expended times a reasonable hourly rate in that community.[222] This amount can (rarely) be increased, but more often is reduced, including when "the relief, however significant, is limited in comparison to the scope of the litigation as a whole."[223] However, the Supreme Court has disapproved of a strict formulaic approach reducing fee awards by the ratio of successful to unsuccessful issues.[224] Lower courts have rejected similar reductions based on the ratio of the relief obtained and the relief requested.[225]

Another limitation to fee awards operates through Rule 68 of the Federal Rules of Civil Procedure.[226] Many states have their own cognate provisions.[227] This rule creates a mechanism for an offer of judgment and imposes the post-offer "costs" on the offeree if they rejected the offer and are ultimately awarded less after trial. "Costs" under Rule 68 does not include attorneys' fees, unless the relevant statute specifically provides for them.[228] This means an offeree may lose their right to recover their own attorneys' fees if they reject such an offer of settlement, even if they would not risk incurring their opponent's fees.[229] While the purpose of Rule 68 is to promote settlement,[230] its effectiveness has been heavily debated, with its critics hypothesizing that its main effect is wealth transfer.[231]

3. Current Scrutiny and Limits of Rate Case Expense Recovery Are Inadequate to Check Its Perverse Incentives

Because recovery of rate case expenses is a form of one-way fee shifting, it creates the same incentives described above to increase legal expenditures and claims and resist otherwise fair settlement offers.[232] In fact, because the rate case expense is usually awarded without regard to the merits of the case or the level of the expenses, utilities have only remote incentives to limit their litigation expenses, creating pronounced incentives to increase their spending on discovery, motions, and legal theories regardless of their merit. The typical outside restriction

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221. Farrar v. Hobby, 506 U.S. 103, 114 (1992) (quoting Hensley v. Eckerhart, 461 U.S. 424, 436 (1983)).

222. ROBERT L. ROSSI, ATTORNEYS' FEES § 10:4 (3d ed. 2025).

223. *Hensley*, 461 U.S. at 430.

224. *See id*. at 435 n.11 (1983). The court has also rejected arguments that the level of fees themselves must be in proportion to the level of relief obtained. *See* City of Riverside v. Rivera, 477 U.S. 561, 574 (1986).

225. *See, e.g.*, Yellow Pages Photos, Inc. v. Ziplocal, LP, 846 F.3d 1159, 1164 (11th Cir. 2017).

226. FED. R. CIV. P. 68.

227. *See* Philip Michael Thompson, *Sanctioning Hard Bargaining: A Critique of State Offer-of-Settlement Rules*, 44 GA. L. REV. 1133 (2010).

228. *See* Marek v. Chesny, 473 U.S. 1, 9 (1985).

229. *Id*. at 1.

230. *Id*. at 5.

231. *See, e.g.* Robert G. Bone, *"To Encourage Settlement": Rule 68, Offers of Judgement, and the History of the Federal Rules of Civil Procedure*, 102 NW. U. L. REV. 1561, 1571-72 (2008); David A. Anderson, *Improving Settlement Devices: Rule 68 and Beyond*, 23 J. LEGAL STUDS. 225 (1994); Geoffrey P. Miller, *An Economic Analysis of Rule 68*, 15 J. LEGAL STUDS. 93, 118-21 (1986) (hypothesizing that Rule 68 only marginally promotes settlement in one-way fee shifting regimes); POSNER, *supra* note 204, at 575-76.

232. *See* discussion *supra* Part III.D.1.

on recovering utility expenses—the prudency standard—is inadequate to restrict these incentives. Several state regulators appreciate this dynamic, but FERC has yet to.

In the existing fee shifting scholarship it does not appear that anyone has attempted to model the incentives created by *guaranteed* one-way fee shifting disconnected from the merits. While formal mathematical modeling is beyond the scope of this paper, any incentive to litigate more issues created by the *possible* recovery of legal expenses should apply more strongly when the recovery of legal expenses was a near certainty. To provide context for the unfamiliar: a typical rate case is not built on one or even a handful of claims. Rather, a typical rate case is built on numerous items comprising alleged costs and revenue. Each item is separately supported factually and legally, with many items not disputed by other participants. Disposition of each item increases or decreases the overall rate, and it is rare for one item to constitute the bulk of the value of the case.[233]

With that context, take the hypothetical of a utility that will certainly file a rate case but is deciding whether to raise *Theory X* as part of this case. Theory X is not technically frivolous but is incompatible with current policy. The utility accurately estimates it has a 5% chance of prevailing, and prevailing would represent a net present value of $2,000,000 in associated increased rates. If the theory will cost an incremental $500,000 to support, the utility could not justify this expense because the discounted value of $100,000 is far exceeded by the costs. But with rate case expense recovery, the "costs" side of its decision is essentially wiped clean. The utility would be constrained only by remote or unquantifiable factors, such as the time value of money,[234] its credibility with decisionmakers, or the availability of preferred vendors. As Chairman Sievers of the Kansas Corporation Commission articulated, utilities are essentially "spending someone else's money" and therefore have "no incentive to minimize that spending or direct insight into the benefits of such spending."[235]

The incentive to increase costs during litigation is just as strong. After all, one-way shifting is understood to raise expenditures because of the *possibility* they will be paid by the other party[236] and in most jurisdictions, recovering the lion's

233. An exception to this might be an allegation that the rates at issue are not subject to regulation, such as through lack of authority by the regulator or lack of market power by the utility. Or perhaps a utility's cost of service has been set by an existing formula that eliminates the need to dispute most items.

234. This would only apply if rates reflecting the rate case expense were not allowed to go into effect on an interim basis.

235. Kansas City Power & Light Co., Docket No. 10-KCPE-415-RTS, 2012 Kan. PUC LEXIS 89, at *166 (Jan.18, 2012) (Sievers, Comm'r, concurring) (discussing the framework established by Milton Friedman in MILTON FRIEDMAN & ROSE FRIEDMAN, FREE TO CHOOSE: A PERSONAL STATEMENT 115-19 (1990)). *Id*. at *167 ("In the regulatory environment, excessive legal or rate case expenses are not naturally controlled by the discipline of the market. Investors don't punish utility managers for spending too much on legal fees and rate cases so long as those expenses are automatically flowed through to rates -- they are gambling with someone else's money. Inflating prices with excessive legal and rate case expenses will not be punished in the market by more cost efficient new entrants offering lower-priced alternatives because government flatly prohibits competitive entry. The regulatory theory is that a single, regulated provider can and will provide service at lower costs than multiple, competing providers and that regulators can and will prevent imprudent expenditures.").

236. SHAVELL, *supra* note 204, at 431-32.

share of rate case expenses is nearly certain for utilities.[237] In the hypothetical above, replace *Theory X* with *Motion X* or *Discovery X* and the dilemma remains. Because the subsidy is disconnected from the merits of the case, rate case expense recovery fuels low-merit litigation practice just as strongly as it does valuable advocacy. Because a risk-neutral litigant can be expected to spend up to the point where the costs exceed the value, utilities can justify nearly any litigation expenditure if there is even a small chance of improving the utility's position. The motion or discovery need not have *any* chance of success if it still presents litigation value by raising the utility opponent's costs. As one commenter put it, "a procedure that makes it tactically advantageous to increase the costs that one's opponent must incur in the effort to obtain justice seems unsound."[238] This incentive also usually applies to judicial appeals, representing an unjustified drain on judicial resources as well.[239]

Without empirical evidence, it is unclear if rate case expense recovery discourages settlement occurring or whether it simply gives greater bargaining strength to utilities in settlement discussions. The choice to settle is primarily a factor of a party's expectations of the outcome of the proceeding and their costs of litigating it.[240] If a utility expects that all its litigation costs will be borne by ratepayers, excluding other factors,[241] it has no incentive to settle for less than the full value it expects to achieve at hearing. On the other hand, ratepayers could be expected to settle the case for as little as their expected value of the case less *both* their litigation expenses and the utility's. That is because ratepayers and their advocates can justify contesting an application (or issue within an application) only if the expected value exceeds both sides' litigation costs (or incremental litigation costs) as well.[242] This could cause ratepayers and their advocates to abandon meritorious claims. It also can create the distorted bargaining commenters have identified, where parties settle or abandon claims on terms unrelated to the merits of the case.[243] As the Missouri PSC articulated, "[a]warding

237. *See generally* Appendix.

238. Albert W. Alschuler, *Mediation with a Mugger: The Shortage of Adjudicative Services and the Need for a Two-Tier Trial System in Civil Cases*, 99 HARV. L. REV. 1808, 1831 (1986).

239. *See, e.g.*, Don Charles Uthus & Diane McIntire, *Public Utility Rate Regulation and the Iowa Administrative Procedure Act - Extending Maximum Procedural Protection to Public Utilities at Public Expense*, 26 DRAKE L. REV. 483, 490 (1977) (arguing Iowa utilities were overly zealous in appeals in part because most litigation costs were "eventually paid by the customer").

240. SHAVELL, *supra* note 204, at 401-03.

241. One such factor, which could cut both ways, might be timing. For instance, a utility may have a separate incentive to settle if the requested rate increases are not implemented on an interim basis. In that position a settlement could be an avenue to implement rates sooner. On the other hand, if the rates requested are implemented on an interim basis, then the utility has an incentive not to resolve the proceeding quickly, because in such a situation the conclusion could not be more advantageous than the status quo. In complaint proceedings, this incentive could be delayed if, as in the Natural Gas Act, the regulator is only authorized to change rates prospectively of its final order without other refunds for complaining ratepayers as are available under the Federal Power and Interstate Commerce Acts.

242. For individual ratepayers, their share of rate case expenses, while not complete, still tracks their relative stake in the case as a whole, which is determined by their share of the regulated transactions and by extension, the utility's overall cost of service.

243. Rowe, *supra* note 210, at 877-78 (citing Richard Marcus, *The Revival of Fact Pleading Under the Federal Rules of Civil Procedure*, 86 COLUM. L REV. 433, 456 (1986)).

a utility all of its incurred rate case expenses could provide that utility with a significant financial advantage over other participants in the rate case process, who may be constrained by budgetary and other financial restrictions."[244]

At FERC and many state regulators, the only limit on rate case expense is the standard of imprudence. This standard varies across jurisdictions,[245] but generally follows FERC's articulation that a prudent decision is one that "reasonable utility management [] would have made, in good faith, under the same circumstances, and at the relevant point in time. . . based upon what the company knew or should have known at the time a decision was made."[246] FERC and many (but not all) jurisdictions employ a strong presumption of prudence for all expenditures made.[247] FERC has even articulated that this subjective standard is comparable to the reasonable person standard used to determine ordinary negligence.[248]

This prudence test, however, is inapposite to the problems presented by unrestrained rate case expense recovery. Shifted fees are limited to prevailing parties and restrained by the lodestar to reach a level that "is sufficient to induce a capable attorney to undertake the representation of a meritorious" case.[249] On the other hand, the prudence standard (especially as FERC applies it) requires the utility be affirmatively shown to be "imprudent" before ratepayers can be protected from paying any litigation costs. Prudent management, however, will not prevent a utility from initiating low-merit claims and procedural actions when they reasonably expect those costs to be recovered from ratepayers.[250] The prudency standard of review is therefore insufficient to protect regulatory and judicial resources—or ratepayers—from over-litigation on the part of utilities.

State regulators recognize that normal prudency reviews are inadequate to control these incentives to over-litigate. For instance, Missouri's PSC articulated that allowing complete recovery of rate case expense "does not encourage reasonable levels of cost containment in the utility's rate case expense decisions."[251] In promulgating its rules governing the issue, Maine's PSC articulated that "actual expenses" would "potentially reward[] overspending and

244. Kansas City Power & Light Co., 2015 Mo. PSC LEXIS 789, at *127 (Sep. 2, 2015).

245. SCOTT HEMPLING, JUST-AND-REASONABLE PRICES IN NONCOMPETITIVE MARKETS: COST-BASED RATES SET BY THE REGULATOR 273-89 (Am. Bar Ass'n 2019).

246. 158 FERC ¶ 61,050 at P 99.

247. *Id*. at P 100 (noting that although the "regulated entity has the burden of proof to establish prudence. . . the Commission presumes that all expenditures are prudent."). *But see* Opinion No. 505, *Entergy Servs., Inc*., 130 FERC ¶ 61,023 at P 52 (2010) ("The utility does not have the burden of demonstrating that expenditures are prudent.").

248. Opinion No. 231, *New England Power Co*., 31 FERC ¶ 61,047, 61,084 (1985) ("What we glean from the cases which is most helpful is the so-called "reasonable man" test, and, as discussed below, we find it appropriate to follow a similar test here.").

249. Perdue v. Kenny A. *ex rel*. Winn, 559 U.S. 542, 552 (2010).

250. *See, e.g.*, 183 FERC ¶ 63,020 at P 631 ("For the reasons discussed below, I find that the prudence of SERI's legal and expert witness fees is presumed and that LPSC has failed to demonstrate serious doubt about SERI's prudence to overcome that presumption"); *see also supra* note 122 and accompanying text.

251. Kansas City Power & Light Co., 2015 Mo. PSC LEXIS 789, at *127-28 (Sep. 2, 2015) ("Prudency reviews, by their nature, are not a strong incentive to control costs.").

inefficient use of outside counsel and consultants."[252] Similarly, Connecticut's Public Utilities Regulatory Authority identified that "there is no intrinsic motivation for the Company to curtail such expenses if the Company and its outside lawyers and consultants assume such costs will be fully recovered from ratepayers."[253] The Arizona Corporation Commission has also expressed a concern that "the expenditure of resources toward rate case presentation is largely within an applicant's control and uncritical acceptance of all expenditure levels can promote a cycle of escalating rate case expenses."[254] The Texas PUC articulated a goal that scrutiny of rate case expenses in general incentivizes utilities "to act more like self-funded litigants, while still providing for recovery of reasonable rate-case expenses."[255] FERC, however, has elected not to see this problem. According to FERC, concerns that recovery of rate case expense "will create perverse incentives" are fully addressed by the fact that recoverability is "limited to [] prudently incurred litigation costs."[256]

IV. RECOMMENDATIONS

Meaningful limits and scrutiny of recoverable rate case expenses are highly justified and can be fully consistent with ratemaking principles. As shown above, guaranteed recovery of all litigation expenses—regardless of amount or merit—creates unsound incentives to over-litigate that inflate ratepayer costs and strain government resources. Meaningful limits should be imposed, and these limits should be informed by fee shifting analyses to account for the perverse incentives, while remaining fundamentally consistent with ratemaking principles. The specific approach most strongly recommended here is the *Missouri-Texas Approach* of sliding scale recovery based on merit. Regulators should also consider a procedural offer of settlement limitation. Different approaches may, of course, be more compatible with the different, policies, procedures, industries, and settings. The most important feature of any reform is a realistic limit such that a utility must plan to internalize some or all of their unsuccessful litigation costs.

252. Amendments to Regul. Proc. Expenses (Chapter 850), Docket No. 2022-00072, 2022 Me. PUC LEXIS 121, at *5-6 (Aug. 3, 2022).

253. Aquarion Water Co., Docket No. 22-07-01RE01, 2024 WL 3723916, at *9 (July 31, 2024) ("In a typical attorney-client or consultant arrangement, the client is incentivized to monitor the attorney's or consultant's fees and work product to avoid inefficient or unnecessary costs. At the same time, the attorney or consultant is similarly incentivized to provide efficient services to avoid the risk that billed work will be rejected by the client. However, if full cost recovery is assumed, the incentive structure has no inherent cost containment measure. As such, the requirement that the Company produce evidence in support of the prudency of the requested rate case costs is essential to ensure just and reasonable rates.").

254. Global Water-Palo Verde Utils. Co., Decision No. 78644, at 147 (Ariz. Corp. Comm'n, Jul. 27, 2022), https://docket.images.azcc.gov/0000207261.pdf?i=1759431571361.

255. Recovery of Expenses for Ratemaking Procs., 39 Tex. Reg. 6434, 6435 (Aug. 22, 2014).

256. 137 FERC ¶ 61,220 at P 41.

A. The Missouri-Texas Approach Is the Simplest Approach to Deriving a Reasonable Level of Rate Case Expense That Corresponds to the Merits of the Utility's Case

Jurisdictions that allow rate case expenses to be recovered should consider some version of the *Missouri-Texas Approach* to limiting that recovery. This approach employs a sliding scale of recovery based on the result achieved relative to the result sought. This approach is (1) simple to administer, (2) most consistent with ratemaking principles, and (3) most likely to create proper litigation incentives and correct for otherwise distorting effects. While other approaches have their merits, none has all these strengths to the same degree.

As described above, Missouri has employed a method where utilities can recover a fraction of their incurred rate case expenses where the numerator is the change in rates requested and the denominator is the change in rates granted.[257] Under this framework a utility that is granted their full requested increase will recover all their rate case expenses, a utility whose request is denied entirely would recover no costs, and a utility whose request is partially granted would recover costs in proportion to its victory. One major advantage of this approach is its simplicity; it does not require individual examination of legal invoices to determine which were too high or related to unreasonable claims.

This allocation is consistent with ratemaking principles traditionally used to justify rate case expense recovery. One such rationale is that a utility is entitled to recover its *reasonable* expenses.[258] As the Missouri PSC articulated, this approach "directly tie[s] a utility's recovery of rate case expense to both the *reasonableness* of its issue positions and the dollar value sought from customers in a rate case."[259] The approach is also grounded in a realistic understanding of the incentives at issue,[260] as well as the difficulty in scrutinizing individual legal invoices for reasonableness.[261] Rate case expense recovery is also justified on the grounds that ratepayers benefit from financially healthy utilities and rate cases are "necessary to establish reasonable rates."[262] Under a sliding scale approach to rate case expense recovery, the level of recoverable expenses tracks the proportion actually spent "to establish reasonable" (rather than excessive) rates. Expenses spent pursuing unreasonably high rates do not advance these goals.

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257. *See* discussion *supra* Part II.B.1.b. The Texas PUC employs a similar method (among other approaches) but may only do so after a separate finding that litigation costs were excessive.

258. *See, e.g.*, PHILLIPS, *supra* note 13, at 237-38.

259. Kansas City Power & Light Co., 2015 Mo. PSC LEXIS 789, at *128 (Sep. 2, 2015) (emphasis added).

260. *Id.* at *126-28.

261. *In re* Kansas City Power & Light Co. v. Missouri Pub. Serv. Comm'n, 509 S.W.3d 757, 778 (Mo. Ct. App. 2016) ("The majority of costs, for example, those related to infrastructure and transmission costs, are transparent and verifiable by the PSC. Rate case expenses are opaque, shielded from effective oversight by privilege and confidentiality. It would be an abdication of the PSC's responsibility to set just and reasonable rates to allow a utility to benefit from imprudently incurred litigation expenses.").

262. *See, e.g.*, Crimson Cal. Pipeline L.P., Decision No 24-05-007, 2024 Cal. PUC LEXIS 268, at *16 (May 9, 2024); *see also In re Kansas City Power & Light Co*., 509 S.W.3d at 778 ("[T]he PSC recognized that rate cases are both beneficial to shareholders of a utility and also utility customers, but in different ways. Shareholders benefit from the rate case expenses as the costs are incurred to increase the utility's revenues and profitability. Customers benefit by having a healthy utility."); Pennsylvania Pub. Util. Comm'n v. National Fuel Gas Distrib. Corp., 1982 Pa. PUC LEXIS 132, at *42 (Mar. 26, 1982).

There are some weaknesses to this approach. With its simplicity, it is less precise than other approaches aim to be. It also does not account for litigation of issues unrelated to the total revenue requirement, such as rate design.[263] However, as implemented by Missouri, the approach separately allows full recovery of rate case expenditures that are legally required, such as mandated studies.[264] The distinction between required and discretionary litigation expenses could allow a utility to recover the full costs of litigating its meritorious positions while forgoing (or internalizing the cost of) low-value claims aimed at increasing their rate levels. The Texas variation of this rule also has a triggering mechanism such that it applies only after rate case expenses are shown to be unreasonably high.[265]

Importantly, this approach also cabins the otherwise unchecked incentive created by the majority approach to rate case expense recovery. As described above, the recovery of legal expenses regardless of the merits creates uniquely perverse incentives to drive up costs, including the imposition of costs on a utility's opponent. The *Missouri-Texas Approach* would also likely promote settlement and narrow disputes by promoting more realistic litigation positions. In fact, the approach bears a striking resemblance to the fee shifting rule known as the "Welamson doctrine" applied in several European countries.[266] This rule shifts fees between parties in proportion to their relative success, measured as a percentage of their monetary reward received relative to the award sought.[267] While not widely adopted, some scholars assert that the rule "compensate[s] parties for legal costs expended to the extent that their claims were found to be justified by the tribunal" and "deter[s] parties from asserting unrealistic claims, facilitate[s] settlements, and ultimately lead[s] to a more efficient dispute resolution system."[268] Others have studied the concept of awarding fees based on the margin of victory and hypothesize that such rules could create better incentives than the American or English Rules.[269]

The main criticism of the Welamson doctrine is that it works "well in simple cases containing a single claim for damages" but not as well in "cases dealing with multiple claims and counterclaims, as well as cases involving both claims for damages and equitable relief."[270] Rate cases essentially are disputes "where the main issue is quantum,"[271] i.e., the rate increase to be authorized. Another criticism is that creating proper litigation incentives through fee shifting requires

263. Southwestern Bell Tel. Co., Docket No. U-2916, 1979 Ark. PUC LEXIS 7, at *85-86 (Jan. 15, 1979).

264. Kansas City Power & Light Co., 2015 Mo. PSC LEXIS 789, at *139 (Sep. 2, 2015).

265. 16 TEX. ADMIN. CODE § 25.245(c)(5) (2014).

266. Gotanda, *supra* note 199, at 39-42 (1999); Mika Savola, *Awarding Costs in International Commercial Arbitration*, 63 SCANDINAVIAN STUDS. L. 275, 310-12 (2017); J. Gillis Wetter & Chart Priem, *Costs and Their Allocation in International Commercial Arbitrations*, 2 AM. REV. INT'L ARB. 249 (1991).

267. Gotanda, *supra* note 199, at 39-40 *nn.181-82.

268. *Id*. at 42.

269. Lucian Arye Bebchuk & Howard F. Chang, *An Analysis of Fee Shifting Based on the Margin of Victory: On Frivolous Suits, Meritorious Suits, and the Role of Rule 11*, 25 J. LEGAL STUDS. 371 (1996).

270. Gotanda, *supra* note 199, at 41; Savola, *supra* note 267, at 312-13.

271. Savola, *supra* note 267, at 312.

a party to have sufficient *ex ante* knowledge of the case.[272] Utilities initiating rate cases, which concern their own costs and revenues, should have more than sufficient *ex ante* information. Thus, the Welamson doctrine and similar margin of victory concepts provide theoretical support to the *Missouri-Texas Approach*.

Part II.B., above, and the Appendix describe a variety of approaches to limiting and scrutinizing rate case expense that each have their own advantages. They all have other limitations that make the *Missouri-Texas Approach* stronger. The New Jersey approach of "sharing" rate case expense with half borne by utility shareholders and half by ratepayers is sound from a ratemaking principle, since these costs are understood to benefit both parties.[273] It is somewhat limited in terms of the incentives it creates. While it does blunt the incentives created by guaranteed full recovery, there is no connection to the merits of the case. A utility would recover the same expenses spent on a rejected case as one fully granted. A "lodestar"-type approach has the advantage of being potentially more precise, and lawyers are already familiar with it. This would require more effort, however, and raise satellite issues to the dispute without more assurance that it accurately quantifies the expenses required for a reasonable rate case presentation. Other subjective approaches may also be beneficial if employed meaningfully. If not, they would provide less benefit than the rarely used prudence standard.

B. Settlement Offer Rule

Regulators should also seriously consider an offer of settlement rule like Federal Rule 68 that would limit a utility's recovery of rate case expense if it rejects a settlement offer but then does not obtain a higher rate after a hearing. Notably, the Texas PUC previously had just such a rule for water utilities, although it was withdrawn in 2019 with little explanation.[274] While some have doubted the rule's efficacy, such a rule would create real incentives for utilities to accept reasonable settlements, and for ratepayer interests to put forward reasonable offers.[275] It would also align with ratemaking principles because in such a situation the excluded expenses could have been easily avoided and were thus not reasonably incurred and unnecessary to providing regulated service at reasonable rates.

V. CONCLUSION

Utility recovery of case expenses recovery presents an anomalous proposition in the American legal landscape that has not received enough attention. It is a unique form of guaranteed fee shifting that operates against consumers and in favor of efforts to resist regulation. It has also received insufficient scrutiny from

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272. Avery W. Katz, *Fee Shifting in Litigation: Survey and Assessment* 24 (Univ. Pa. L. Sch. Inst. L. & Econ. Rsch., Working Paper No. 10-30, 2010).

273. *See* discussion *supra* pp. 14-15.

274. Order Adopting Amendments to 16 TAC 24.44 for Consideration at The October 11, 2019 Open Meeting, Rulemaking to Amend 24.44 Rate-Case Expenses Pursuant to Tex. Water Code §13.187 & §13.1871, Project No. 48526, slip op. at 6 (Tex. Pub. Util. Comm'n Oct. 14, 2019), https://interchange.puc.texas.gov/Documents/48937_25_1037611.PDF.

275. *See* discussion *supra* pp. 35.

regulators. The appended survey and analysis are intended to aid advocates and regulators interested in seriously examining current practice and its consequences. Even if no policy changes are adapted, it is hoped that ALJs, regulators, their staff, and other decision-makers can benefit from understanding the incentives at play when a utility expects full indemnification of its legal expenses. ALJs and hearing-level decisionmakers especially may find this framework helpful to understanding utilities' practice before them. The simple explanation might be that the utility's actions do not seem cost-justified because they are not cost-justified. Identifying this dynamic could be the first step in curbing the drain of unnecessary litigation.