

RATE CASE EXPENSE: A COMMISSION INQUIRY

PRESENTATION TO NARUC
SUBCOMMITTEE ON ACCOUNTING
AND FINANCE
SEPTEMBER 21, 2011

Answers Exhibit No. 52
Date 10-1-12 Reporter KF
File No. EC-0012-CN66

Hanneken
Depo. 6
9/5/2012



STANDARD DISCLAIMER

- ANY VIEWS OR OPINIONS EXPRESSED TODAY AS PART OF THIS PRESENTATION ARE SOLELY MY OWN PERSONAL BELIEFS, AND DO NOT PURPORT TO REPRESENT THE VIEWS, OPINIONS OR POSITIONS OF EITHER THE MISSOURI COMMISSION STAFF, OR THE MISSOURI COMMISSION ITSELF



DEFINITION

- RATE CASE EXPENSE:

ALL INCREMENTAL EXPENSES INCURRED BY A UTILITY DIRECTLY RELATED TO A REGULATORY PROCEEDING IN WHICH THE UTILITY'S RATE LEVELS ARE BEING EXAMINED



DEFINITION

- Types of Rate Case Expense:
 - Outside Counsel
 - Outside Consultants
 - Overtime Incurred by Salaried Employees
 - Travel Costs (Hotel, Meals, Transportation, etc.)
 - Miscellaneous



DEFINITION

- Common Uses of Outside Consultants in Missouri
 - Return on Equity Analyses (almost always)
 - Depreciation Studies (almost always)
 - Rate Design/Class Cost-of-Service Studies
 - Pensions/OPEBs
 - Incentive Compensation
 - Weather Normalization



COMMISSION POLICY

- Missouri Practice Has Been:
 - Recovery of All Prudent and Necessary Costs
 - No Sharing or Cap Mechanisms
 - Amortization/Normalization Over Reasonable Period
 - Recognition Can Be Given to Unrecovered Prior Costs
 - No Governing Rule/Statute
 - No Defined Policy (Reviewed Case-by-Case)



COMMISSION POLICY

- Missouri-American Water Company, Case No. WR-93-212, 1993:
 - “The Commission does not want to put itself in the position of discouraging necessary rate cases by discouraging rate case expense. The operative words, here, however, are necessary and prudently incurred. The record does not reflect efforts at cost containment and consequently it does not support that these expenses have been prudently incurred.”



COMMISSION POLICY

- Missouri Gas Energy, Case No. GR-2004-0209, 2004:
 - Company used outside attorneys who charged high hourly rates - in one instance, \$690 per hour
 - Missouri Commission ordered that such services be repriced for rate purposes at prevailing “local” legal rates; i.e., \$200 per hour



COMMISSION POLICY

- Missouri Gas Energy, Case No. GR-2004-0209, 2004:
 - “... The company is entitled to present its case and the Commission will not lightly intrude into the company’s decisions about how best to present its case. However, the Commission has a responsibility to ensure that the expenses that the company submits to its ratepayers are reasonably and prudently incurred. Otherwise, the company could take a cost-is-no-object approach to its rate case presentation, secure in the knowledge that the ratepayers would be required to pay for any cost that the company might incur.”



COMMISSION POLICY

- Current Office of the Public Counsel Position:
 - No Recovery of Outside Counsel or Outside Consultant Costs When Utility Has the Capability of Providing Service for Itself In-House
 - One-Half of Remaining Costs Should be Allocated to Shareholders



2010 KCPL RATE CASE

- Actually, two separate rate cases for affiliated electric utilities : Kansas City Power & Light Company (ER-2010-0355) and KCPL – Greater Missouri Operations Company (ER-2010-0356), both filed in June 2010
- KCPL sought a \$92.1 million increase, while GMO requested a \$75.8 million rate increase
- Primary reason for increase: capital additions



2010 KCPL RATE CASE

- IATAN 2 Coal Plant
- IATAN 1 Coal Plant Environmental Additions
- KCPL Sought Recovery of Approximately \$1.275 million in Capital Costs for Both Projects in Combination
- Missouri Staff Conducted Construction Audit
 - Recommended approximately \$140 million in Iatan disallowances



2010 KCPL RATE CASE

- \$7.8 Million Total in Missouri Rate Case Expenses
 - Includes \$1.6 million deferred from prior rate case
 - Some 2010 rate case expenses deferred to next rate case
 - Next highest rate case expense total in Missouri in last five years: \$2.1 million



2010 KCPL RATE CASE

- Claimed Costs include:
 - Six outside attorneys from four separate law firms
 - Twelve outside consultants
- Cost per Customer was \$13.33
 - Normal cost per customer: \$2.22



2010 KCPL RATE CASE

- Staff Proposed \$1.2 Million Disallowance of KCPL's Missouri Rate Case Expenses
- Commission Ordered \$400,000 in Rate Case Expense Disallowed
 - Ordered "duplicative" costs eliminated
 - Ordered attorney costs for functions that could have been performed by in-house counsel eliminated



2010 KCPL RATE CASE

- In Its Order Regarding Rate Case Expense, the Commission noted:
 - No evidence of “cost containment”
 - Did not find it reasonable to apply local law firm rates to outside counsel who may practice “in other, possibly more expensive, locations...”
 - Evidence not sufficiently competent to prove [legal] fees were excessive
 - A three-year amortization period was reasonable in lieu of KCPL’s requested two-year period



CASE NO. AW-2011-0330

- Order Directing Staff to Investigate Rate Case Expense Policies
- Issued April 27, 2011, Two Weeks After the Rate Order Was Issued in the KCPL Rate Case
- Not a “Contested Case” – Any Party May File Comments Without Representation of Counsel; No *Ex Parte* Constraints; No Deadline for Decision



CASE NO. AW-2011-0330

- In the Order, the Commission stated:
 - Inquiry was prompted by testimony in recent rate cases and escalating rate case expense requests
 - Will consider whether to change its current rules and practices whereby regulated utilities generally recover all costs they incur in presenting a rate case
 - Will consider whether it is appropriate for shareholders to bear responsibility for a portion of rate case expense



CASE NO. AW-2011-0330

- Will consider whether it is appropriate to establish a dollar or revenue percentage cap on amount of rate case expense to pass on to ratepayers
- Staff shall file a report on its findings
- Staff shall study how “other states handle this issue”



PUC SURVEY

- Survey sent to all 50 other state public utility commissions
- Survey sent out in mid-May; Requested responses by mid-June
- To date, 21 PUCs have responded
- Of those 21 responses, four did not provide detailed responses due to use of formula ratemaking, incentive regulation, etc.
(DE, IN, IO and NJ)



PUC SURVEY

- Question: What overall approach to rate recovery of rate case expense?
 - Allow all prudent costs to be recovered
 - Share or allocate costs between customers and shareholders
 - Set a pre-set cap on total amount to be charged customers
 - Some other approach



PUC SURVEY

- 14 commissions allow recovery of all prudently incurred rate case expenses
- No commission explicitly “shares” this cost
- One commission arguably uses a cap mechanism to limit rate recovery of this cost (NY)
- No commission uses a “tracker” for this cost
- Two commissions use or consider using rate “riders”/surcharges for recovery of rate case expense (TX – established policy; CO – developing policy)



PUC SURVEY

- Question: Are Rate Case Expenses Allowed Recovery Over a Single-Year or Over Multiple Years?
 - Almost all respondents spread recovery of rate case expense over multiple years, usually tied to an expected duration until the next rate case filing
 - Several commissions indicate they provide recovery over both single-year periods and multiple years, depending upon the circumstances



PUC SURVEY

- For those commissions allowing the costs to be spread over multiple years, most respondents said the period used can vary from case to case, as opposed to a set period of time for all utilities



PUC SURVEY

- Question: Does the Commission Allow Recovery of Rate Case Expense as a Normalized Cost, or as an Amortization to Expense?
 - The concept of amortization usually assumes deferral of the costs on the utility's books
 - Most respondents allow recovery as an amortization, either some or all of the time



PUC SURVEY

- Question: Does the Commission Allow Recovery of Unrecovered Rate Case Expenses From a Previous Rate Docket in a Subsequent Rate Filing?
 - The responses split approximately 50/50 on this issue



PUC SURVEY

- Question: Are the Commission's Policies Concerning Recovery of Rate Case Expense Tied to a Statute, Rulemaking, Commission Precedent, or Something Else?
 - Almost all respondents indicated "commission precedent," with many noting that all rate case expense issues are examined on a case-by-case basis (i.e., no "hard" policy)
 - Three PUCs indicated that their treatment is based upon a statute (AL, NM, TX)



PUC SURVEY

- Other Comments:
 - Distinctions noted between treatment large and small companies
 - Distinctions noted between treatment of water/sewer utilities and other industries

PUC SURVEY

- Colorado:
 - In a recent case, Staff proposed to allow recovery of rate case expenses through a separate rate element – the “GRSA.” 10% recovery in Year 1, 20% in Yr. 2, 30% in Yr. 3, 40% in Yr. 4. Rate element will terminate when full recovery achieved. If the utility files a new rate case during the term of the GRSA, then no recovery of any unrecovered prior rate case expenses will be allowed in the next case.
 - Not clear whether the Colorado PUC has adopted this approach.

PUC SURVEY

- Kansas:
 - Recently instituted a proceeding to examine its rate case policies.
 - Like the Missouri case, this appears to be at least in part a reaction to the high levels of expense claimed in the recent IATAN 2 KCPL rate case.



PUC SURVEY

- New York:
 - Uses a fully forecasted test year for major utilities, including a reasonable level of projected rate case expenses. This amount effectively serves as a “cap” on total recovery, as the projected amount is never reconciled to actual rate case expenditures. NY’s approach assumes annual rate proceedings; therefore, costs are not normally spread over multiple years.



PUC SURVEY

- Texas:
 - Rate case expenses are recovered through a rider/surcharge mechanism. Period of recovery is usually from one to three years. Once full recovery achieved, then the surcharge is eliminated from customer bills.



PUC SURVEY

- Arizona:
 - Note: AZ did not respond directly to survey!
 - Based upon materials provided to me from AZ, the AZ PUC apparently applies fairly strict standards of prudence to rate case expenses, with any increase in expense over that incurred in similar recent proceedings of other utilities disallowed unless the company can justify the increased costs.
 - Not an explicit “sharing” arrangement.

CONCLUSION

- Final Comments/Questions
 - Are rate case costs a “normal” expense or a “special” type of expense?
 - Is it a valid goal of regulation to allow utilities to attain dollar-for-dollar recovery of this cost?
 - Who is the primary beneficiary of rate case expense? Should the answer to this question affect what party is ultimately responsible for this expense?
 - How should rate case expense “caps” be structured – does “one size fit all?”
 - Is a “Safe Harbor” approach feasible? (i.e., designation of a pre-set level of expense as presumptively prudent)

CONCLUSION

- Primary Question:
 - How can a regulatory agency best provide adequate incentives for a utility to reasonably limit its rate case expenditures, while not discouraging necessary rate filings or impeding the utility's ability to put forward a well-argued and supported case?

CONCLUSION

- Thanks for all who have responded
- Copies of all responses are available to anyone who asks for them
- There is still time for other PUCs to respond to the survey – **Please Do!**
- Send your survey responses to, or otherwise contact me at:
 - Mark.oligschlaeger@psc.mo.gov
 - (573) 751-7443