

**BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI**

In the Matter of the Tariffs of Aquila, Inc, d/b/a)
Aquila Networks–MPS and Aquila Networks–)
L& P Increasing Electric Rates for the Service)
Provided to Customers in the Aquila Networks)
MPS and Aquila Networks–L&P Service Areas.)

Case No. ER-2007-0004
Tariff No. YE-2007-0001

AARP's Application for Rehearing

COMES NOW AARP, by and through counsel, and pursuant to Section 386.500 RSMo. 2000 and 4 CSR 240-2.160, respectfully applies for a rehearing of the Missouri Public Service Commission's ("Commission's") Report and Order issued in the above-styled matter on May 17, 2007 and bearing an effective date of May 27, 2007 ("Report and Order"). This Report and Order purports to increase Aquila's electric rates and approve a Fuel Adjustment Clause surcharge (FAC).

. This Report and Order is unlawful, unjust, unreasonable, arbitrary, capricious, and unsupported by competent and substantial evidence on the whole record, in the following respects:

1. The FAC approved for Aquila is inconsistent with Section 386.266 and unreasonably slanted against consumers.

Section 386.266.1 only grants the Commission the authority to implement rate adjustments outside of general rate proceedings "to reflect increases and decreases in

its prudently incurred fuel and purchased power costs, including transportation”. By providing for no mechanism to exclude imprudent costs prior to recovery, the FAC approved in the Report and Order violates Section 386.266.1. Reliance on after-the-fact prudence reviews is insufficient to comply with this section.

Subsection 386.266.4(1) RSMo. Supp. 2006. requires that any fuel adjustment mechanism approved by the Commission must be designed to provide the opportunity for a “fair rate of return”. Because the Commission is legally tasked with balancing the interests of shareholders and consumers, such a return must be fair to both sides. As such, placing 95% of the risk of fuel cost risk onto consumers (100% of which is currently borne by Aquila) without making any corresponding adjustment to the return on equity of the electric company is contrary to the authorizing statute, unfairly slanted against consumers, and patently unreasonable. While AARP’s 50/50 sharing proposal would be reasonable, a 95/5 sharing is patently unbalanced and unreasonable, and is unsupported by any competent and substantial evidence.

The 95% FAC approved for Aquila would remove almost all essential incentives for efficiency now in place, even though Section 386.266 as a whole, and subsection 1 in particular belies an intent of any FAC to retain “incentives to improve the efficiency and cost-effectiveness of its fuel and purchased-power procurement activities”. As such, the decision is contrary to the new law’s intent and is bad public policy likely to increase fuel cost in the future.

Although the Commission used a reasonable standard in analyzing whether to grant a FAC in this case, it did not correctly apply that standard. Specifically, the Commission refused to acknowledge the significant ways in which Aquila currently

controls its fuel and purchased power options. The Commission ignored competent and substantial testimony explaining how the Commission's adopted standard should actually be applied to the question of whether Aquila controls its fuel and purchased power expenses. See Exhibit 600, pp. 10-15; Exhibit 601, pp. 9-12; Tr. 844-845, 858-859.

Moreover, the Report and Order includes statements that clearly reveal a clear intention to bias rate recovery in favor of the electric utility. Ibid., pp. 11, 24, 30-42. A ratemaking decision should reasonably balance the interests of ratepayers and shareholders, not "help the utility earn its allowed rate of return." A utility should merely be given a reasonable opportunity to earn a fair return; not be given a virtual guarantee of a certain level of earnings. The Report and Order is also arbitrary and capricious and not based on competent and substantial evidence in that it assumes that Aquila's fuel and purchased power costs will only increase in future years. Id., pp. 24-25.

2. The Report and Order is unlawful and unreasonable because it authorizes an FAC, but does not make any corresponding adjustment to the approved rate of return to reflect the sharp reduction in business risk that such a surcharge will cause.

The Commission's Report and Order would dump 95% of fuel cost variability onto ratepayers through a FAC, essentially removing the utility's major source of business risk. Aquila itself claimed that this was a major concern for "Wall Street".

Subsection 7 of Section 386.266 invites the Commission to recognize changes in business risk resulting from being granted such an extraordinary surcharge mechanism:

“The commission may take into account any change in business risk to the corporation resulting from implementation of the adjustment mechanism in setting the corporation's allowed return in any rate proceeding, in addition to any other changes in business risk experienced by the corporation.”

However, in adopting a version of the return on equity recommendation proposed by witness Michael Gorman, the Commission stated that “the decreased risk associated with having a cost recovery mechanism is already accounted for in Mr. Gorman’s return on equity calculation and no additional adjustment is necessary.” Report and Order, pp 62-63. But that statement is not an accurate reflection of Mr. Gorman’s calculations. There is no support in his testimony for this statement. See Exhibits 507, 508, and 509.

In fact, the Commission found Mr. Gorman’s recommended return was actually *increased* by 10-15 basis points without any adequate finding of fact and without support based upon competent and substantial evidence, stating that it is justified because “the Company is not recovering 100% of its prudently incurred fuel and purchased power costs”. Report and Order, p. 62. Such a statement does not reflect the legal standard for setting rates nor is it necessarily an accurate statement regarding future costs. It is also contrary to the weight of the entire record in this case to grant Aquila an FAC and then bump *up* its ROE based on the rationale that it may not be guaranteed 100% recovery of certain costs.

WHEREFORE, AARP respectfully requests that the Commission grant a rehearing of the Report and Order in this case, and to reconsider its determination of the Fuel Adjustment Clause and the Rate of Return issues.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that copies of the foregoing have been emailed to counsel for each of the parties on the service list for this matter on this 25th day of May 2007.

/s/ John B. Coffman
