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ER-2016-0179

DIRECT TESTIMONY

OF

LENA M. MANTLE

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**Missouri Public
Service Commission**

Submitted on Behalf of the Office of the Public Counsel

UNION ELECTRIC COMPANY

D/B/A AMEREN MISSOURI

FILE NO. ER-2016-0179

December 9, 2016

OPC Exhibit No. 4
Date 8/13/18 Reporter Bjb
File No. EX-2016-0294

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

In the Matter of Union Electric)
Company d/b/a Ameren Missouri's)
Tariffs to Increase Its Revenues)
for Electric Service)

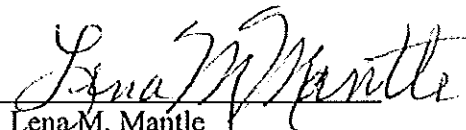
File No. ER-2016-0179

AFFIDAVIT OF LENA M. MANTLE

STATE OF MISSOURI)
) ss
COUNTY OF COLE)

Lena M. Mantle, of lawful age and being first duly sworn, deposes and states:


1. My name is Lena M. Mantle. I am a Senior Analyst for the Office of the Public Counsel.
2. Attached hereto and made a part hereof for all purposes is my direct testimony.
3. I hereby swear and affirm that my statements contained in the attached testimony are true and correct to the best of my knowledge and belief.


Lena M. Mantle
Senior Analyst

Subscribed and sworn to me this 9th day of December 2016.



JERENE A. BUCKMAN
My Commission Expires
August 23, 2017
Cole County
Commission #13754037


Jerene A. Buckman
Notary Public

My Commission expires August 23, 2017.

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DIRECT TESTIMONY

OF

LENA M. MANTLE

UNION ELECTRIC COMPANY d/b/a AMEREN MISSOURI

FILE NO. ER-2016-0179

INTRODUCTION

Q. Please state your name and business address.

A. My name is Lena M. Mantle and my business address is P.O. Box 2230, Jefferson City, Missouri 65102.

Q. By whom are you employed and in what capacity?

A. I am employed by the Missouri Office of the Public Counsel ("OPC") as a Senior Analyst.

Q. On whose behalf are you testifying?

A. I am testifying on behalf of the OPC.

Q. Please describe your experience and your qualifications.

A. I was employed by the OPC in my current position as Senior Analyst in August 2014. In this position, I have provided expert testimony in electric and water cases before the Commission on behalf of the OPC. I am a Registered Professional Engineer in the State of Missouri.

1 Prior to being employed by the OPC, I worked for the Staff of the Missouri
2 Public Service Commission ("Staff") from August 1983 until I retired as Manager
3 of the Energy Unit in December 2012. During the time I was employed at the
4 Missouri Public Service Commission ("Commission"), I worked as an Economist,
5 Engineer, Engineering Supervisor and Manager of the Energy Unit.

6 Attached as Schedule LM-D-2 is a brief summary of my experience with
7 OPC and Staff and a list of the Commission cases in which I filed testimony,
8 Commission rulemakings in which I participated, and Commission reports in rate
9 cases to which I contributed as Staff.

10 **Q. Would you provide a summary of the Fuel Adjustment Clause ("FAC") OPC**
11 **is recommending for Union Electric Company d/b/a Ameren Missouri**
12 **("Ameren Missouri") in this case?**

13 **A.** Yes. The FAC recommended by OPC minimizes the complexity of Ameren
14 Missouri's FAC while providing Ameren Missouri with a reduction in risk
15 regarding its recovery of its fuel and purchased power expenses. It also maintains
16 consistency with state law granting the Commission authority to allow Ameren
17 Missouri an FAC. It limits the costs and revenues included in the FAC and
18 increases transparency. Further by removing non-fuel and purchased power costs, it
19 eliminates the disincentive for Ameren Missouri to implement more efficiencies in
20 these cost areas. It reduces the likelihood of errors and increases the ability to

1 conduct a comprehensive prudence review. Lastly, it offers a more meaningful
2 incentive for Ameren Missouri to manage, to the extent it is able, the fuel and
3 purchased power costs and off-system sales revenues through recovery of all the fuel
4 costs included in base rates and 90% of the FAC cost above what is included in base
5 rates. Likewise, it would return 90% of all cost savings to the customers.

6 **Q. Would you provide a summary of your background with respect to the fuel**
7 **adjustment clause?**

8 **A.** After the enactment of Section 386.266 RSMo allowing the Commission to grant
9 the electric utilities a fuel adjustment clause ("FAC"), relevant stakeholders worked
10 together to draft proposed rules for the Commission's consideration to implement
11 the statute. The draft rule development process included many stakeholder meetings
12 where the participants developed proposed wording for draft rules to present to the
13 Commission for its consideration. I attended and participated in all of the
14 stakeholder meetings serving as Staff "scribe" at these meetings and personally
15 recorded the compromise language. I also participated in drafting language
16 regarding Staff's positions for the stakeholders' consideration in this process.

17 After the Commission published its proposed FAC rules I attended, on
18 behalf of the Staff, several of the public hearings the Commission held around the
19 state on its proposed rules in August and September of 2006.

1 Since the rules became effective, in my employment with Staff and OPC, I
2 have either filed testimony or participated in the determination of FAC positions in
3 every general rate case where a Missouri investor-owned electric utility requested
4 the establishment or modification of an FAC under the current statute. In addition, I
5 have reviewed and, sometimes offered testimony, in every FAC rate change,
6 prudence review, and true-up case conducted in Missouri.

7 Drawing on my experience, I have written a white paper providing
8 information on the history of the FAC in Missouri and a general description of the
9 FAC as implemented in Missouri. This whitepaper is attached to this testimony and
10 labeled Schedule LM-D-1.

11
12 **GENERAL OVERVIEW OF OPC'S RECOMMENDED FAC**

13 **Q. Would you outline the FAC OPC is recommending for Ameren Missouri?**

14 **A. OPC is recommending the Commission approve an FAC for Ameren Missouri with**
15 the following features:

- 16 1. Only the following prudently incurred costs shall be included:
- 17 a. Delivered fuel commodity costs including:
- 18 i. Inventory adjustments to the commodities;
- 19 ii. Adjustments to cost due to quality of the commodity; and
- 20 iii. Taxes on fuel commodities;
- 21 b. The cost of transporting the commodity to the generation plants;

- c. The cost of power purchased to meet its native load; and
- d. Transmission cost directly incurred by Ameren Missouri for purchased power and off-system sales.

2. These costs would be offset by:

- a. Off-system sales revenue net of the cost of generation or purchased power to make those sales; and
- b. Net insurance recoveries, subrogation recoveries and settlement proceeds related to costs and revenues included in the FAC.

3. An incentive mechanism that requires changes in Ameren Missouri's fuel adjustment rates ("FARs") to account for 90% of the difference between the actual prudently incurred costs net of off-system sales and the net FAC costs included in its base rates. The other 10% would be absorbed or retained by Ameren Missouri ("90/10 incentive mechanism").

OPC is not proposing any changes to the administration of the FAC, e.g. there would be no change in accumulation and recovery periods.

Q. What are the benefits of the FAC OPC is proposing?

A. OPC's recommended FAC has the following benefits:

1. Assures consistency with Section 386.266.1 RSMo;
2. Increases transparency of the costs and revenues included in the FAC;
3. Limits the disincentive for implementation of efficiencies;

4. Simplifies FAC prudence audits;
5. Simplifies FAC tariff sheets;
6. Recovers the majority of Ameren Missouri's current FAC costs; and
7. Provides an incentive for Ameren Missouri to effectively manage fuel, purchased power and off-system sales.

The remainder of this testimony provides greater detail on each of these benefits.

CONSISTENCY WITH MISSOURI STATUTE

Q. The first benefit you listed is OPC's recommended FAC would be consistent with Section 386.266.1 RSMo. Would you please explain?

A. Yes. Missouri statutes give the Commission the authority to grant regulated electric utilities a mechanism to recover certain costs between rate cases. Specifically, Section 386.266.1 RSMo states:

Subject to the requirements of this section, any electrical corporation may make an application to the commission to approve rate schedules authorizing an interim energy charge, or periodic rate adjustments outside of general rate proceedings to reflect increases and decreases in its prudently incurred fuel and purchased power costs, including transportation. The commission may, in accordance with existing law, include in such rate schedules features designed to provide the electrical corporation with incentives to improve the efficiency and cost-effectiveness of its fuel and purchased-power procurement activities. (emphasis added).

Q. How is OPC's recommendation consistent with Section 386.266.1 RSMo?

1 A. Fuel commodity and the transportation of that commodity to Ameren Missouri's
2 generating facilities is the purest definition of fuel and transportation costs. The
3 statute, however, does not mention fuel adders, fuel handling, contractor costs,
4 spinning reserve costs, startup costs, hedging costs, and a myriad of other costs and
5 revenues that Ameren Missouri is requesting to include in its FAC.

6 Purchased power to meet native load, either through bilateral contracts or
7 through regional transmission organization ("RTO") markets¹ also clearly meets the
8 statute's intent. Accordingly, OPC's recommended FAC limits purchased power
9 costs to the cost of energy from long-term bilateral contracts, capacity charges from
10 bilateral contracts that change annually or more frequently, and capacity and energy
11 purchased through RTO markets to meet native load or to make off-system sales.

12 **Q. Transmission is not mentioned in the statute. Why is OPC recommending**
13 **certain transmission costs be included in Ameren Missouri's FAC?**

14 A. In 2013, the Missouri Appeals Court concluded "the legislature intended the word
15 "transportation" in Section 386.266.1 RSMo to encompass "transmission."² The
16 Commission has defined transmission costs to be included in FACs for all of the
17 electric utilities it regulates beginning with the last Ameren Missouri rate case, ER-

¹ While most of the power purchased by Ameren Missouri would be from the Midcontinent Independent System Operator ("MISO") market, Ameren Missouri has also purchased power from other parties including PJM and AECL.

² Union Electric Company v. PSC, 422 S. W. 3d 358, 367 (Mo. App. 2013)

1 2014-0258. On page 115 of its *Report and Order* of that case, the Commission
2 stated:

3 [Section 386.266.1 RSMo] allows for recovery of transportation
4 costs, which has been determined to include transmission costs, but
5 such transmission costs are limited to those connected to purchased
6 power costs.

7
8 In its *Report and Order* in the Empire District Electric Company ("Empire") rate
9 case, ER-2014-0351, the Commission further defined transmission costs which may
10 be included in the FAC:³

11 Therefore, the costs Empire incurs related to transmission that are
12 appropriate for the FAC, from a policy perspective and by statute,
13 are:

- 14 1) Costs to transmit electric power it did not generate to its
15 own load ("true purchased power"); or
16 2) Costs to transmit excess electric power it is selling to third
17 parties to locations outside of its RTO ("Off-system sales").
18

19 In its *Report and Order* in the Kansas City Power & Light Company ("KCPL") rate
20 case, ER-2014-0370, the Commission stated:⁴

21 [I]t would not be lawful for KCPL to recover all of its [Southwest
22 Power Pool ("SPP")] transmission fees through the FAC. In
23 addition, while KCPL's transmission costs are increasing, those
24 costs are known, measurable, and not unpredictable, so the costs are
25 not volatile. The Commission concludes that the appropriate
26 transmission costs to be included in the FAC are 1) costs to transmit
27 electric power it did not generate to its own load (true purchased
28 power); and 2) costs to transmit excess electric power it is selling to
29 third parties to locations outside of SPP (off-system sales).
30

³ Page 28.

⁴ Page 35.

1 Lastly, the Commission approved a Stipulation and Agreement in the recent
2 KCP&L – Greater Missouri Operation Company (“GMO”) rate case, ER-2016-
3 0156, in which the parties agreed to the following:

4 The cost and revenues in GMO’s FAC will not include transmission
5 costs associated with Crossroads Energy center and will be
6 consistent with those in Kansas City Power & Light Company’s
7 current FAC[.]
8

9 This summer, the Appeals Court upheld the Commission’s decision in the KCPL
10 rate case, ER-2014-0370, affirming the Commission’s decision to allow only
11 transmission costs for “true” purchased power and off-system sales in the FAC.⁵

12 **Q. How did the Commission implement these Reports and Orders?**

13 A. The Commission determined a normalized amount of “true” purchased power
14 mega-watt hours (“MHZ”) using the outputs of the Staff production-cost fuel models
15 for each of the electric utilities. This amount was divided by the utility’s normalized
16 load MWh. This percentage, calculated for each electric utility, is applied to each
17 utility’s non-administrative RTO costs and is included in the electric utility’s FAC.

18 **Q. Is this a measure of the transmission costs directly tied to “true” purchased
19 power and off-system sales?**

20 A. No. This methodology allows a percentage of all non-administrative RTO costs to
21 be included in FACs whether those costs are directly tied to “true” purchased power

⁵ *In the Matter of KCP&L’s Request for Authority to Implement a General Rate Increase, et. al., v. Mo. Pub. Serv. Comm’n*, WD79125 Consolidated with WD79143 and WD79189 (Opinion Affirming Commission’s Report and Order issued on Sept. 6, 2016. KCPL’s motion for rehearing overruled and

1 and off-system sales or not. This is the reason OPC is recommending the
2 Commission restrict the transmission costs included in Ameren Missouri's FAC to
3 the costs of transmission directly tied to purchased power and off-system sales.

4 **Q. Do you have an example of an RTO cost included in the FAC that is not**
5 **directly tied to Ameren Missouri's purchased power or off-system sales?**

6 A. Yes. The current FAC methodology allows Ameren Missouri to include a portion
7 of the Midcontinent Independent System Operator ("MISO") Multi-Value Projects
8 cost, which is Ameren Missouri's largest RTO transmission cost. It is my
9 understanding that all MISO members are charged as these transmission project
10 costs are incurred. Once the line is built, the users of that line are charged to recover
11 the cost of building the transmission. If Ameren Missouri uses this transmission to
12 purchase power or make off-system sales, MISO will charge Ameren Missouri in
13 order to return investment to the members that paid for the line to be built. If the
14 Commission adopts OPC's FAC recommendation this charge would flow through
15 the FAC.

16 **Q. Can Ameren Missouri distinguish which costs are directly tied to true**
17 **purchased power and off-system sales?**

18 A. Yes. Point-to-point ("PTP") and network integration transmission service ("NITS")
19 fees are directly tied to true purchased power and off-system sales. OPC

1 recommends these as the only transmission costs that should be included in Ameren
2 Missouri's FAC.

3 **Q. What is OPC's proposal regarding other MISO costs of which a percentage**
4 **are currently included in the FAC?**

5 A. No other MISO costs and revenues would be included. While all of these costs and
6 revenues are for necessary services, they are not fuel and purchased power costs or
7 revenues.

8 **Q. The statute is silent in regard to off-system sales. Why is OPC**
9 **recommending that the Commission include off-system sales in Ameren**
10 **Missouri's FAC?**

11 A. OPC is recommending the inclusion of off-system sales revenue and the cost to
12 generate or purchase power to make those sales because the determination of costs
13 to make off-system sales is an after-the-fact accounting assignment of costs.
14 Typically, the low cost energy, whether generated or purchased, is assigned to the
15 native load.⁶ Higher cost energy is assigned to off-system sales. Not including off-
16 system sales revenue in the FAC opens an avenue for errors, resulting in parties
17 having different positions regarding the appropriate fuel cost to allocate to off-

Supreme Court is pending).

⁶ Ameren Missouri assigns the cost of its wind energy to its native load regardless due to Missouri renewable energy standards even though it is often not low cost energy.

1 system sales, increasing the potential for improper assignment of fuel and purchased
2 power costs.

3 **Q. Does OPC's recommended FAC include revenues for off-system sales of**
4 **capacity?**

5 A. Yes, it does. Just as capacity cost of purchased power is included, revenues from
6 capacity sales are included.

7 **Q. Why should net insurance recoveries, subrogation recoveries and settlement**
8 **proceeds related to costs and revenues be included in Ameren Missouri's**
9 **FAC?**

10 A. These costs and revenues should be included consistent with the Commission's
11 determination in the KCPL rate case ER-2014-0370 where it found on page 39 of its

12 *Report and Order:*

13 Insurance recoveries, subrogation recoveries and settlement proceeds
14 related to costs and revenues included in the FAC are revenues
15 typically related to an unexpected incident or accident. If these types
16 of revenues do occur, it is likely that at some point in time, prior to
17 the receipt of the recovery or settlement, there were increased costs
18 or reduced revenues due to that circumstance that have been
19 included in the fuel adjustment rates paid by customers.

20 **Q. Is Ameren Missouri requesting costs that are not "fuel and purchased power**
21 **costs, including transportation" in its FAC?**

22 A. Yes, it is. Ameren Missouri provided in Schedule LMB-2 Attachment C to the
23 direct testimony of Ameren Missouri witness Lynn M. Barnes a more detailed list of

1 the costs and revenues that Ameren Missouri currently includes and is proposing to
2 continue to include in its FAC along with a brief description of each cost and
3 revenue. Many of these costs and revenues are not “fuel and purchased power costs,
4 including transportation.” For example, Ameren Missouri proposes to continue
5 include the cost of MISO scheduling system control and dispatch, emergency
6 demand response, and storm restoration costs for Entergy.

7 This leads to the second benefit of OPC’s FAC recommendation: the
8 Commission, Staff, Ameren Missouri, and other interested parties will know exactly
9 what is included in Ameren Missouri’s FAC.

10
11 **INCREASED TRANSPARENCY**

12 **Q. Did Ameren Missouri provide greater detail regarding the costs and**
13 **revenues that it is proposing to be included in its FAC?**

14 **A.** Yes. Schedule LMB-2 Attachment C to Barnes’ direct testimony lists seventy-six
15 different costs and revenues by account, subaccount, and activity code and a
16 description of each.

17 **Q. What conclusion did you draw from reviewing this schedule?**

18 **A.** The additional detail raises questions about why many of these costs should be
19 included in the FAC.

20 **Q. Would you give an example of such a cost?**

1 A. Yes. Ameren Missouri is proposing to continue to include MISO Schedule 42
2 charges in its FAC. The definition provided by Ameren Missouri follows:

3 Charge to Recover Accrued and Paid Interest Associated with
4 Prepayments From Entergy Operating Companies' Pricing Zones.
5 MISO mechanism for collecting accrued and paid interest associated
6 with prepayments for network upgrades to the Entergy Operating
7 Companies. These transmission charges possess the characteristic
8 of, and are of the nature of, the transmission charges assessed to
9 Ameren Missouri by Entergy to serve Ameren Missouri load using
10 Entergy transmission prior to Entergy joining MISO.

11
12 The title of this charge – "Charge to Recover Accrued and Paid Interest Associated
13 with Prepayments From Entergy Operating Companies' Pricing Zones" – and the
14 first sentence in the explanation seem to indicate that this is not a fuel, purchased
15 power, or transmission cost. This seems to be a charge to recover interest on
16 prepayments. However, the last sentence states it is a transmission charge. It is not
17 clear or transparent what this charge is or why it should be considered a
18 transmission charge.

19 Q. Is there any other example of the lack of transparency in the costs Ameren
20 Missouri is including in its FAC?

21 A. Yes. Ameren Missouri's inclusion of a large number of costs and revenues that are
22 not clearly defined obscures transparency. As a part of its monthly filing
23 requirements, Ameren Missouri provides a detailed showing of the costs and
24 revenues it is including in its FAC. My limited review of the September 2016

1 monthly FAC submission revealed at least one cost not found in Ameren Missouri's
2 description provided in its direct filing.

3 **Q. Is this a cost that Ameren Missouri should not currently be including in its**
4 **FAC?**

5 A. I cannot tell. It is recorded in an account approved by the Commission in the last
6 FAC case. The descriptions provided of costs Ameren Missouri was proposing to
7 be included in the last FAC case were very general and brief. It may be an oversight
8 that these costs were not included in the list provided in this case.

9 Having a multitude of costs and revenues in the FAC leads to this sort of
10 confusion and lack of transparency.

11 **Q. How would the FAC proposed by OPC result in more transparency in**
12 **Ameren Missouri's FAC?**

13 A. Limiting the number and types of costs and revenues in Ameren Missouri's FAC to
14 the few large cost and revenue items specified by OPC would result in an FAC that
15 includes costs that clearly meet the statute requirement and are easy to understand
16 that, in turn, leads to greater transparency. While a more comprehensive list costs
17 and revenues included in Ameren Missouri's FAC is now provided, the multitude of
18 complex costs and revenues in Ameren Missouri's FAC makes it less transparent.
19

LIMIT DISINCENTIVES FOR IMPLEMENTATION OF EFFICIENCIES

Q. How does the FAC create a disincentive for implementation of efficiencies?

A. When a cost is included in the FAC it can create a disincentive for the utility to implement cost efficiencies. Consider, for example, there are various products that can be used in Air Quality Control Systems and that the Commission only approves a certain product - \$100 for powder activated carbon ("PAC") but does not allow trona costs in the FAC because the utility is not incurring the cost and has no plans to incur the cost. A disincentive is created if the utility discovers after the approval of its FAC it can accomplish the same air quality using \$80 of trona (\$20 less than what was included in base rates). However, since the Commission approved the inclusion of PAC but not trona, implementing the use of trona would mean the actual costs would be reduced by \$100. If the utility chose to use the more cost effective trona for \$80, the FAC costs would be reduced by \$100 because the utility was not incurring the cost of powder activated carbon lowering the FAC rate. However, the utility would spend \$80 for the trona. The total cost to the utility would be the \$100 that it would no longer collect through the FAC and the \$80 for the trona. Thus, as demonstrated in this hypothetical, including a cost in the FAC can create a disincentive for implementing future efficiencies. If, as OPC is proposing, neither the cost of PAC or trona are included in the FAC, the utility would have an incentive to use the new more cost efficient trona so that it would

1 realize \$20 in savings that would either offset cost increases in other areas or
2 increase shareholder earnings.

3 **Q. Then to avoid this disincentive, should the Commission allow the utility greater**
4 **discretion in what is included in the FAC?**

5 **A.** No, it should not. The Commission addressed this in its *Report and Order* in ER-
6 2014-0370⁷ when it stated:

7 KCPL argues that the FAC should include all costs and revenues
8 relating to net fuel and purchased power costs, whether or not they
9 are currently being incurred. However, allowing a new cost or
10 revenue to flow through an FAC is a modification to that FAC,
11 which under Section 386.266, RSMo, only the Commission has the
12 authority to modify. It is the Commission that should make the
13 determination as to what costs or revenues should flow through the
14 FAC, not the electric utility.

15
16 Expanding the costs included in the FAC to include potential costs the electric
17 utility is not currently incurring but may sometime in the future allows the electric
18 utility to determine what is in the FAC. The proper way to reduce this type of
19 incentive while meeting the statutory requirement of the Commission determining
20 what is included in the FAC is to limit the costs to what is specifically included in
21 Section 386.266 RSMo as recommended by OPC. The fewer the costs included in
22 the FAC, the less likely this type of disincentive would occur.
23

⁷ Page 39.

SIMPLIFY PRUDENCE REVIEWS

Q. The next benefit you list is a simplification of prudency reviews. Would you please explain?

A. Limiting the number and types of costs and revenues included in Ameren Missouri's FAC simplifies the prudence audit. If the Commission approves Ameren Missouri's proposed FAC, the multitude of costs makes a comprehensive prudence review much more difficult and time consuming for all parties involved.

Q. Would you comment on the effectiveness of FAC prudence audits?

A. Ideally, with respect to each of the costs and revenues in an FAC, a prudence audit should identify all instances where an imprudent action resulted in higher costs to customers. In practice, when there is a multitude of costs and revenues to be reviewed, prudence audits are limited in scope. Due to resource constraints and the fact that the utility holds the information, even an experienced auditor's ability to identify and demonstrate imprudence becomes dependent on chance rather than the result of a thorough review.

Q. How would OPC's FAC recommendation increase the effectiveness of FAC prudence audits?

A. While not guaranteeing OPC's FAC recommendation would increase the effectiveness of prudence audits, it would make it more likely. The FAC recommended by OPC would reduce the number and types of costs and revenues

1 included in Ameren Missouri's FAC, thus allowing auditors to concentrate efforts
2 on a few costs.

3
4 **SIMPLIFY FAC TARIFF SHEETS**

5 **Q. How would OPC's recommended FAC simplify FAC tariff sheets?**

6 **A.** The FAC tariff sheets would no longer need to reflect a long list of MISO charges
7 and revenues along with the provision of a process for including charges if MISO
8 makes changes to how it charges.

9 The exemplar FAC tariff sheets provided as Schedule LMB-4 in Barnes
10 direct testimony include two pages that list MISO charge/revenue types that Ameren
11 Missouri flows through its FAC. In addition, two of Ameren Missouri's proposed
12 tariff sheets contain a process for allowing Ameren Missouri to recover a cost if it is
13 "like" an MISO cost listed in the tariff sheets. With the MISO costs limited as
14 proposed by OPC, there would no longer be a need for a process to include new
15 MISO charges and revenues that are "like" MISO costs and revenues already
16 included in the FAC.

17
18 **THE MAJORITY OF CURRENT FAC COSTS ARE INCLUDED**

19 **Q. How does OPC's recommendation impact Ameren Missouri's FAC costs?**

20 **A.** Only the non-fuel and non-purchased power costs now included in Ameren
21 Missouri's FAC would be impacted. Because a large majority of the costs in

1 Ameren Missouri's FAC are fuel commodity, the transportation of that commodity,
2 and purchased-power costs, the impact on total cost recovery is slight. Importantly,
3 OPC's recommendation would still result in Ameren Missouri recovering increases
4 in true fuel and purchased power costs thus reducing the risk to Ameren Missouri of
5 increases in fuel and purchased power costs.

6 In addition, as previously discussed, OPC's recommended FAC would
7 reduce disincentives for cost efficiencies. The removal of these disincentives along
8 with OPC's recommended sharing incentive could actually result in greater earnings
9 for Ameren Missouri.

10 **Q. Would removal of costs from the FAC result in Ameren Missouri not**
11 **recovering the non-fuel and purchased power costs Ameren Missouri is**
12 **proposing to be included in its FAC?**

13 **A.** No, it would not. These costs would still be included in the revenue requirement for
14 Ameren Missouri. Excluding these costs from the FAC would restore the traditional
15 ratemaking incentives to Ameren Missouri in regard to these costs. If Ameren
16 Missouri can find efficiencies that could reduce these costs, then shareholders would
17 see a benefit. Including these costs in the FAC removes Ameren Missouri's
18 incentive to take actions to decrease these non-fuel and non-purchased power costs.

19 Likewise, removal of revenue "types" from the FAC would not result in
20 ratepayers losing the benefits from these revenue sources. Normalized revenues

1 from these sources would still be included in determining the revenue requirement.

2 If Ameren Missouri can increase these revenues (excluded from the FAC), then
3 shareholders could see a greater benefit. In contrast, including non-fuel and
4 purchased power revenues in an FAC may create apathy regarding these increases
5 since Ameren Missouri would see very little benefit.

6
7 **GREATER INCENTIVE FOR COST MANAGEMENT**

8 **Q. Why is OPC recommending a change to Ameren Missouri's FAC incentive**
9 **mechanism?**

10 **A.** OPC's recommendation to change the incentive mechanism from 95 percent
11 recovery/return to 90 percent recovery/return would create a greater incentive for
12 Ameren Missouri to actively strive to reduce fuel and purchased power costs and
13 increase off-system sales revenues.

14 While much of the cost of fuel is out of Ameren Missouri's control, there
15 are several ways Ameren Missouri can influence the cost of fuel. For example,
16 Ameren Missouri has contracts for the coal it burns at its power plants. It has
17 some control over the content of these contracts and should manage the contracts
18 in a manner that minimizes potential waste and cost increases. Ameren Missouri
19 makes decisions on when it is the best time to do maintenance on its power plants.
20 It chooses what maintenance to do. With the shutdown of the Noranda aluminum
21 facility, Ameren Missouri has excess capacity. It has the ability to determine how

1 to best manage this excess capacity. In this case, Ameren Missouri decided that it
2 would change how it managed its capacity within the MISO market. These are all
3 examples of how Ameren Missouri can and does influence its fuel and purchased
4 power costs.

5 **Q. How would a 90/10 incentive mechanism affect Ameren Missouri's cost**
6 **recovery when fuel costs are increasing?**

7 **A.** It depends on the accuracy of base rates and how much the costs increase. If the
8 base is accurate and costs increase 10%, then Ameren Missouri will recover 99.1%
9 of its actual fuel costs. If the costs increase 20%, then Ameren Missouri will still
10 collect 98.3% of its fuel costs. Under either scenario, Ameren Missouri's has little to
11 no risk of not recovering a significant portion of its fuel and purchased power costs.

12 **Q. How would changing the incentive mechanism to 90/10 affect Ameren**
13 **Missouri's cost recovery when fuel costs are decreasing?**

14 **A.** Again, it depends on the accuracy of base rates and how much the costs decrease. If
15 the base is accurate and fuel costs decrease, Ameren Missouri will recover more
16 than its fuel and purchased power costs. If costs decrease 10%, then Ameren
17 Missouri will recover 101.1% of its actual FAC costs. If the costs decrease 20%,
18 then Ameren Missouri will collect 102.5% of its actual FAC costs.

1 **Q. How does that compare to what Ameren Missouri would recover with a 95/5**
2 **incentive mechanism?**

3 **A. The table below summarizes the difference in the percent of costs Ameren Missouri**
4 **would recover with the 90/10 and 95/5 sharing mechanisms.**

5 Comparison of
6 Percent of FAC Costs Recovered
7

Actual Costs as percent of Base Fuel Costs	Incentive Mechanism	
	90/10	95/5
120%	98.3%	99.2%
110%	99.1%	99.5%
100%	100%	100%
90%	101.1%	100.6%
80%	102.5%	101.3%

8
9 **Q. Would you summarize this table?**

10 **A. With the current incentive mechanism which Ameren Missouri proposes to**
11 **continue, Ameren Missouri recovers essentially all of its FAC costs (99.2%) even if**
12 **fuel costs increase 20%. A 95/5 sharing mechanism provides little to no incentive**
13 **for Ameren Missouri to take any actions to keep the FAC costs within 20% of what**
14 **is included in base rates. A 90/10 sharing mechanism actually results in an impact**
15 **(1.7%) on cost recovery when FAC costs increase. It also provides more of an**
16 **incentive to Ameren Missouri to decrease its FAC costs since the amount it would**
17 **recover if FAC costs decrease would be greater with OPC's recommended 90/10**
18 **incentive than with the current 95/5 incentive.**

1 **Q. Would you summarize the benefits of the FAC proposed by OPC?**

2 A. The FAC proposed by OPC would result in the recovery of 90% of the actual cost
3 above what is included in base rates of its fuel commodity (including the
4 transportation of the commodity) and purchased power - net of off-system sales. It
5 maintains consistency with state law granting the Commission authority to allow
6 Ameren Missouri an FAC. It limits the costs and revenues included in the FAC and
7 increases transparency. By removing non-fuel and purchased power costs, it
8 eliminates the disincentive for Ameren Missouri to implement more efficiencies in
9 these cost areas. It reduces the likelihood of errors and increases the ability to
10 conduct a comprehensive prudence review. Lastly, it offers a more meaningful
11 incentive for Ameren Missouri to manage, to the extent it is able, the fuel and
12 purchased power costs and off-system sales revenues.

13 **Q. Does this conclude your direct testimony?**

14 A. Yes.

Electric Utility Fuel Adjustment Clause in Missouri:
History and Application Whitepaper

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Electric Utility Fuel Adjustment Clause in Missouri: History and Application Whitepaper

Introduction

The purpose of this whitepaper is to provide a general description of the history of electric utility fuel adjustment clauses ("FACs") in Missouri prior to and after the passage of Section 386.266 Revised Missouri Statutes ("RSMo") in 2005¹ and provide an understanding of the functionality of the FACs currently implemented throughout the state of Missouri. This whitepaper is not an exhaustive description of the FAC in Missouri but is intended to provide a basic understanding of the history and application of Section 386.266 in a neutral and unbiased manner.

Recovery of Fuel and Purchased Power Costs Prior to Section 386.266 RSMo

In the 1979 Missouri Supreme Court opinion of *Utility Consumer Council of Missouri, Inc. v. P.S.C.*,² the Court concluded FAC surcharges were unlawful because they allowed rates to go into effect without considering all relevant factors. The Court warned "to permit such a clause would lead to the erosion of the statutorily-mandated fixed rate system."³ The Court further explained, "If the legislature wishes to approve automatic adjustment clauses, it can of course do so by amendment of the statutes and set up appropriate statutory checks, safeguards, and mechanisms for public participation."⁴

After this Supreme Court opinion, fuel and purchased power costs for Missouri investor-owned utilities were normalized and included in the determination of the utility's revenue requirement for general rate proceedings. This provided an incentive to the electric utility that, if it managed its activities in a manner that allowed it to reliably serve its customers at a cost lower than what was included in its revenue requirement in the last rate case, all the savings were retained by the electric utility. If costs were greater than the costs included in the revenue requirement, the electric utility absorbed the increased costs. When the electric utility believed that it could no longer absorb the increased costs, the electric utility would ask the Commission for an increase in its rates.

¹ Section 386.266 RSMo was Truly Agreed To and Finally Passed by the Missouri House of Representatives and Senate on April 27, 2005. Governor Matt Blunt signed this legislation on July 14, 2005.

http://www.senate.mo.gov/05info/BTS_Web/Actions.aspx?SessionType=R&BillID=5755

² State ex rel. Utility Consumers Council, Inc. v. P.S.C., 585 S.W.2d 41(MO. 1979)

³ Id. at 57.

⁴ Id.

This incentive worked well for the Missouri electric utilities and their customers for the next twenty-five years. The two largest investor-owned electric utilities, Union Electric Company ("Union Electric") and Kansas City Power & Light Company ("KCPL") went for a period of twenty years without a rate increase request due to the excess generation they built in the 1970's and 1980's. Capital costs of these plants were included in the customers' rates of these electric utilities. Excess generation and capacity from these utilities and other regional providers that over-built was sold through long-term contracts on a cost-plus basis to the smaller investor-owned electric utilities in the state. This resulted in minimal rate increase requests for these smaller investor-owned electric utilities and offset some of the capital costs paid by Union Electric Company and KCPL's customers. Eventually the large utilities' customers load requirements grew into the need for their own capacity and they did not renew the long-term contracts. Then, to meet their customers' needs, the smaller electric utilities began to build the least cost option - natural-gas fired generation plants. While these plants were inexpensive to build, the fuel cost was uncertain.

In the early 1990's, restructuring of the electric utilities began occurring in other parts of the nation. In the mid-1990's the Missouri Legislature considered restructuring Missouri's investor-owned electric utility companies. At the end of 2000, after two months of extraordinarily cold weather and continued reports of extreme storage withdrawals, the commodity price of natural gas spiked to nearly \$10 per thousand cubic feet ("Mcf") in late December after remaining consistently between \$1/Mcf to \$3/Mcf since the inception of the unregulated wholesale natural gas markets in the 1980s.⁵ These wildly fluctuating natural gas prices had little impact on the total fuel costs of KCPL and Union Electric since most of their customers' needs were met through nuclear and coal generation. However, the fluctuating natural gas prices significantly impacted the smaller electric utilities' fuel and purchased power costs.

Overview of Section 386.266 RSMo

The provisions of Section 386.266 RSMo, also known as Senate Bill 179 ("SB 179"), took effect on January 1, 2006.⁶ This section gives the Missouri Public Service Commission ("Commission"), among other things, the authority to approve rate schedules authorizing periodic rate adjustments outside of general rate proceedings to reflect increases and decreases in its prudently incurred fuel and purchased power costs, including transportation costs. An FAC is a mechanism designed to reflect increases and decreases in fuel and purchased power costs, including transportation. The statute, in addition to requiring approval from the Commission for

⁵ Missouri Public Service Commission EFIS Case No. GW2001398XXX, Item no. 44, Final Report of the Missouri Public Service Commission's Natural Gas Commodity Price Task Force, August 29, 2001

⁶ §386.266.12.

the implementation of an FAC, includes other provisions including some consumer protections. It requires the Commission to approve, modify, or reject FACs only as a part of a general rate case proceeding in which all costs and relevant factors are considered. It allows the Commission to include in an FAC features designed to provide incentives to improve the efficiency and cost-effectiveness of the electric utility's fuel and purchased-power procurement activities. If the Commission approves an FAC, the electric utility with the FAC must file a general rate increase case with effective dates of new rates no later than four years after its approval. Prudence reviews of the costs included in an FAC are to be conducted at least every eighteen months and true-ups are required at least annually. Amounts charged/refunded to the customers through an FAC are required to be separately disclosed on each customer's bill.

Section 386.266.1, which is the provision that grants the Commission the authority to approve, reject or modify FACs, applies only to investor-owned electric utilities in Missouri. At the time it became effective, there were four investor-owned electric utilities in Missouri – Union Electric, KCPL, Aquila, Inc. ("Aquila"), and the Empire District Electric Company ("Empire"). Union Electric subsequently did business as AmerenUE and is now doing business as Ameren Missouri. Aquila is now doing business as KCP&L – Greater Missouri Operations Company ("GMO").

Development of Commission Rules Regarding FACs

Section 386.266.9 RSMo gives the Commission the authority to promulgate rules to govern the structure, content, and operation of FACs. The Commission is also given the authority to promulgate rules regarding the procedures for the submission, frequency, examination, hearing, and approval of FACs. Soon after Section 386.266 RSMo went into effect, the Staff of the Public Service Commission ("Staff") began the work of developing rules governing the implementation of this section. It was determined that there would be two rules: one rule, found in *Chapter 3 Filing and Reporting Requirements* of the Commission's rules as *4 CSR 240-3.161 Electric Utility Fuel and Purchased Power Cost Recovery Mechanisms Filing and Submission Requirements*, provides the filing and information requirements necessary for requesting approval, continuation, modification, and discontinuation of an FAC along with filing and submission requirements for changes to the FAC rates and true-ups. It also provides the contents of quarterly surveillance reports and monthly reporting requirement for electric utilities that are allowed an FAC. A second rule, *4 CSR 240-20.090 Electric Utility Fuel and Purchased Power Cost Recovery Mechanisms*, provides the structure and governance requirements for an FAC.

Staff worked diligently with a broad group of stakeholders - including representatives from electric utilities, large customers, AARP, and the Office of the Public Counsel ("OPC") in the development of proposed rules to present to the Commission. Auditors, engineers,

economists, and attorneys worked together in over fifteen workshops collaborating to develop specific language to propose to the Commission rules to implement the provisions of Section 386.266 RSMo pertaining to FACs. The Commission opened Case No. EX-2006-0472 on June 15, 2006 with a finding of necessity for rules to establish and implement an FAC and began the formal rulemaking process with the proposed 4 CSR 240-3.161 and 4 CSR 240-20.090 rules developed through the collaborative workshop process. Public hearings regarding the proposed FAC rules were held in Kansas City, St. Louis, Overland, Cape Girardeau, Jefferson City and Joplin in late August 2006 and early September 2006. Written comments were received from seven individuals and fourteen groups or companies. The Commission issued its final orders of rulemaking on September 21, 2006.⁷ The final order was published in the December 1, 2006 *Missouri Register* effective January 30, 2007.⁸

Key Provisions of the FAC Rules

Despite concerns that an FAC would contribute to over-earnings by electric utilities by the both the non-utility parties that participated in developing the proposed rules and those that provided comments in the formal rulemaking process, the resulting FAC rules do not contain an earnings test. In FAC proceedings, the Commission is only required to review the costs and revenues included in the FAC. Decreases in expenses and increases in revenues not included in the FAC are not considered by the Commission. However, utilities with an FAC are required by the Commission rules to submit quarterly surveillance reports to Staff, OPC, and other parties. These surveillance reports include rate base quantifications, capital quantifications and income statements for the electric utilities as a whole.⁹ The information from these reports includes the earnings of the electric utility for the prior quarter and could be used in an over-earnings complaint case.¹⁰

Because the statute requires adjustments to FAC rates reflect increases and decreases in prudently incurred costs, the rules require that FAC recoveries be based on historical costs.¹¹ Therefore, before the electric utility can begin billing to recover FAC costs, the costs in the utility's FAC must be incurred and any revenues included in the FAC to offset those costs must be received. Interest at the utility's short-term debt rate is applied to the net of these costs and revenues and recovered or returned to the ratepayers through the FAC rate.

⁷ Missouri Public Service Commission, Case No. EX-2006-0472, EFIS Items 27 and 28

⁸ <http://s1.sos.mo.gov/CMSImages/adrules/moreg/previous/2006/v31n23/v31n23b.pdf>

⁹ 4 CSR 240-3.161(6)

¹⁰ However, the Commission, in case no. EC-2014-0223, stated that these surveillance reports alone do not provide a complete or accurate picture of earnings sufficient to reset the utility's rates.

¹¹ 4 CSR 240-20.090(2)(F)

The rules are not prescriptive regarding the design of FAC rates. However, 4 CSR 240-20.090(9) does require that FAC rates reflect differences in losses incurred in the delivery of electricity at different voltage levels for different rate classes based on system loss studies that must be conducted at least every four years.

While Section 386.266.1 allows the Commission to include features in an FAC designed to provide the electric utilities with incentives to improve the efficiency and cost-effectiveness of the utilities fuel and purchased-power procurement activities, the rules are not prescriptive regarding what such an incentive feature would look like. Instead it allows incentive features to be proposed in rate cases in which an electric utility requests the establishment, continuation or modification of an FAC.¹² Incentive features can be proposed for the Commission's consideration by any of the parties in rate cases in which the electric utility is proposing the establishment, continuation, or modification of an FAC.

Section 386.266 is silent regarding the inclusion in an FAC of any fuel related type of revenues. The Commission rules do not require the inclusion of fuel related revenues, such as off-system sales revenues,¹³ in an FAC. The rules do require that if an FAC includes revenues from off-system sales, the FAC include prudently incurred fuel and purchased power costs associated with off-system sales.¹⁴

History of Requests for FACs

Empire was the first electric utility to request cost recovery of fuel costs under Section 386.266 RSMo when it filed Case No. ER-2006-0315 on February 1, 2006. This case was filed while the Commission rules were being drafted. In this case, Empire did not request an FAC. Instead it requested an Energy Cost Rider ("ECR") to recover costs between rate cases. Due to a stipulation Empire had entered into in a prior rate case, the Commission required Empire to remove from its pleadings and other filings its request and support for an ECR.¹⁵ Prior to Empire's next rate case, Case No. ER-2008-0093 filed on October 1, 2007, the Commission rules had been finalized and were effective. The Commission granted Empire an FAC in its July 30, 2008, *Report and Order* in ER-2008-0093. The Commission has authorized continuation of an FAC with modifications in all general rate cases subsequently filed by Empire.

On July 3, 2006 two of Missouri's investor-owned electric utilities filed general rate increase cases in which they requested an FAC. Union Electric, then doing business as AmerenUE,

¹² 4 CSR 240-20.090(11)

¹³ Off-system sales revenues are the revenues from sales of energy by the electric utility above what is needed by the utility's customers.

¹⁴ 4 CSR 240-3.161(1)(A) and 4 CSR 240-20.090(1)(B)

¹⁵ EFIS item 57, *Order Clarifying Continued Applicability of the Interim Energy Charge*, effective May 12, 2006.

requested the Commission grant it an FAC in Case No. ER-2007-0002 and Aquila requested an FAC in Case No. ER-2007-0004. While the FAC rules were not final at this time, the Commission had, just eighteen days earlier, sent proposed rules to the Missouri Office of the Secretary of State for publication in the Missouri Register. The Commission's determination of the final FAC rules occurred while these rate cases were pending.

In its May 22, 2007 *Report and Order* in the AmerenUE case ER-2007-0002, the Commission concluded:

After carefully considering the evidence and arguments of the parties, and balancing the interests of ratepayers and shareholders, the Commission concludes that AmerenUE's fuel and purchased power costs are not volatile enough [to] justify the implementation of a fuel adjustment clause at this time:

AmerenUE filed another general rate increase case on April 4, 2008, again seeking the Commission's approval of an FAC in Case No. ER-2008-0318. In its January 27, 2009 *Report and Order*¹⁶ in this case, the Commission authorized AmerenUE to implement an FAC. The Commission has authorized continuation of an FAC with modifications in all general rate cases subsequently filed by Union Electric now doing business as Ameren Missouri.

The Commission authorized the first FAC for a Missouri investor-owned electric utility under Section 386.266 RSMo in its May 17, 2007 *Report and Order* in Aquila's general rate proceeding in case ER-2007-0004. FAC base rates were approved for each of Aquila's two rate districts, then designated as Aquila Networks-MPS and Aquila Networks-L&P. The actual effective date of Aquila's FAC was delayed when the Commission found that the proposed FAC tariff sheets filed by Aquila were not consistent with its *Report and Order*. Tariff sheets implementing the FAC consistent with the Commission's *Report and Order* were approved on June 29, 2007 effective July 5, 2007. Following this rate case, Great Plains Energy acquired Aquila renamed it GMO. The Commission has authorized the continuation of an FAC with modifications in all general rate cases subsequently filed by GMO.

KCPL was the last Missouri electric utility to be granted an FAC. At the time that SB 179 was being debated at the Legislature, KCPL was negotiating a regulatory plan that would address financial considerations of KCPL's investment in Iatan 2 and other investments and the timeliness of the recovery of the costs of these investments. As a part of the *Stipulation and Agreement*¹⁷ in that case, KCPL agreed, among other items, that prior to June 1, 2015, it would not seek to utilize any mechanism authorized in SB 179. Therefore, KCPL did not request an

¹⁶ EFIS item no. 589, page 70

¹⁷ Case No. EO-2005-0329, EFIS item no. 1

FAC until the general rate case ER-2014-0370 it filed on October 30, 2014. The Commission granted KCPL an FAC in its September 2, 2015 *Report and Order*.¹⁸ Tariff sheets implementing an FAC for KCPL became effective September 29, 2015.

General Structure of FACs in Missouri

While there are some differences in the details of each electric utility's FAC, the general structure of the FACs of each of the electric utilities is the same. An estimate of the FAC costs and revenues, known as Net Base Energy Cost or NBEC, is identified and included in the base rates of each electric utility. The FAC rate is based on the difference between the FAC costs included in base rates and the actual FAC costs incurred. FAC costs are tracked in a designated accumulation period and the difference between actual FAC costs and NBEC is recovered or returned in a designated recovery period.

Even though the rule is not prescriptive regarding the design of the FAC rate, in practice, all of the electric utility's FAC rates are volumetric rates based on customer energy usage. A base factor is calculated in each general rate proceeding as the NBEC divided by the rate case normalized kilowatt-hours ("kWh"). The Commission's rule requires that the FAC is to be based on historical costs¹⁹ so there cannot be an FAC rate until FAC costs are incurred. Therefore the initial FAC rate, ("FAR"), is set at zero when the Commission approves the establishment of an FAC for each of the electric utilities.

To derive a rate to be charged the customers after FAC costs have been incurred, the difference between the actual costs incurred (actual net energy cost or ANEC) and the costs already included in the base rates (NBEC), either positive or negative, is divided by the expected energy use of the utility's customers over the recovery period. Because rule requires voltage losses to be taken into account in the FAC, a FAR is calculated for each of the voltage levels that the utility provides service at based on loss factors derived in the last rate case. These loss-adjusted FARs are the rate used to bill the FAC to the customers.

Accumulation and Recovery Periods

An accumulation period is the time over which the electric utility tracks the ANEC. Commission rule allows up to four accumulation periods a year but requires at least one accumulation

¹⁸ EFIS item no. 592, page 30

¹⁹ 4 CSR 240-20.090(2)(F)

period a year. The Recovery Period is the time period over which the difference between the accumulation period ANEC and NBEC is billed to the utility's customers.

The accumulation periods and recovery periods for the electric utilities are shown in the table below.

<u>Electric Utility</u>	<u>Accumulation Periods</u>	<u>Recovery Periods</u>
Ameren Missouri	February through May June through September October through January	October through May February through September June through January
KCPL	January through June July through December	October through September April through March
GMO	June through November December through May	March through February September through August
Empire	September through February March through August	June through November December through May

The recovery periods are twice as long as the accumulation periods for Ameren Missouri, KCPL, and GMO. The purpose of having recovery periods longer than the accumulation periods is to reduce the FAR and minimize the impact of the change in rates on the customers' bills. Ameren Missouri's accumulation periods are four months and the costs from the four month accumulation period are billed (recovered or returned) over eight months. The accumulation periods of KCPL and GMO are six months while the recovery periods are twelve months. Empire is the only utility where the recovery period is the same length as the accumulation period - both are six months.

The timing of recovery periods for Ameren Missouri, KCPL, and Empire were set to minimize the number of times during a year that changes in rates impact bills. The base rates for all of the electric utilities change twice a year. Base rates are higher in the summer months of June through September for all of the electric utilities because typically the cost to provide electricity is higher in these summer months. The lower, non-summer rates are billed in October through May.

The timing of the recovery periods of Ameren Missouri means that customers see both base rates and FAR changes in June and October and then see another rate change, due to the change in the FAR, in February. Without alignment of the timing of recovery periods,

customers of Ameren Missouri could be impacted by changes in rates up to five times a year – twice in base rates and three times for the FAC rates.

Similarly, the timing of one of the FAC recovery periods for KCPL is October when base rates also change. One of Empire's recovery periods begins in the same month that the base rates change for summer resulting in rates changing for Empire's customers only three times a year. The timing of FAC rate changes for KCPL and Empire results in their customers seeing changes in rates just three times a year instead of four.

Calculation of Fuel Adjustment Rates

At the end of the accumulation period, a NBEC is calculated for the accumulation period based on the Base Rate set in the rate case and the actual energy consumed by the electric utility's customers in the accumulation period. This NBEC is compared to the Actual Net Energy Costs (ANEC) incurred during that accumulation period. The FAR for the accumulation period is then calculated based on the difference between the actual historical costs incurred (ANEC) and the FAC costs billed in the base rates (NBEC) divided by the expected usage of the utility's customers over the recovery period and then adjusting the rate for delivery losses.

This is the FAR that the customer is billed for Empire since the recovery period is the same length as the accumulation period. For the other three electric utilities that have recovery periods that are twice as long as the accumulation periods, the FAR that is billed the customer is actually the sum of the loss adjusted FARs for two consecutive accumulation periods.

Price Signal Resulting From FACs

There is a common misconception that FACs provide customers more accurate price signals than the base rates. There are several reasons Missouri's FAC does not provide accurate price signals to customers. An accurate price signal is timing. Missouri's FAC is based on historical costs so customers are not billed the difference in the FAC costs until months after the costs are incurred. For example, fuel costs incurred in January for KCPL are not billed to its customers until the recovery period that begins in October. At the time that a change in fuel costs is seen on the customers' bills, it may no longer be an accurate representation of the fuel cost the utility is experiencing at that time.

Another reason that FACs in Missouri do not provide accurate price signals is that the accumulation periods bill costs or return savings to customers aggregated over several months.

Increases in FAC costs in one month may be offset by decreases in FAC costs in the next month. In addition, the accumulation periods cross seasons of the year when FAC costs typically vary because the load requirements of the customers vary. For these reasons, the length of the accumulation period mutes any price signal.

Long recovery periods designed to reduce FAC rate volatility to customers also mutes the price signal to customers. For example, for KCPL any increase in costs in January is recovered over the time period of October of that same year through September of the next year. An increase in January is spread out over the twelve months of the recovery period so an increase in January combined with changes for all the months in the accumulation period and then spread over twelve months of estimated usage. This is the price signal that the customer is reacting to – not the actual increase in costs in January. In addition, the customer would not even be billed for the increase in costs in January until the October billing month. If FAC costs are volatile, the customer may be reacting to an increase in cost in the previous year during a time period when costs are actually decreasing. In this case, the FAC is sending the wrong price signal to the customer.

For these reasons the design and application of FACs in Missouri do not send accurate price signals to customers.

True-Up of FACs

SB 179 requires that true-ups of FACs occur at least annually.²⁰ The purpose of a true-up is to make sure that the electric utility recovers all the costs that it is entitled or all amounts due to the customers are refunded. Section 386.266 requires the true-up amount include interest at the electric utility's short-term interest rate.

In practice, true-ups occur after the end of each recovery period. Because KCPL, GMO, and Empire have two recovery periods a year, there are two FAC true-ups a year for these electric utilities. There are three FAC true-ups a year for Ameren Missouri since it has three recovery periods a year. A true-up is simply a comparison of the actual FAC billed the customers in the recovery period to the difference between the actual FAC costs and NBEC in the corresponding accumulation period. This difference, either negative or positive, is added as a true-up amount, including interest, to the FAC costs to be billed in the next recovery period.

The true-up amount is keyed off of the FAC billed not the FAC revenues recovered. This is to reduce complexity of how to deal with under-paid bills. While the FAC amount is separately

²⁰ Section 386.266.4(2)

identified on the customer's bill, the customer that only pays a portion of their bill does not designate what portion of the bill they are paying. The unpaid portion of the bill is included treated uncollectible. The rate case treatment for uncollectibles is determined in the rate case and is not dealt with in the FAC.

Prudence Reviews

Section 386.266.4(4) requires prudence reviews of the costs in the FAC to occur at least every eighteen (18) months. Since the first FAC under section 386.266 was approved for GMO, the first prudence audit was conducted on GMO's FAC, followed by prudence audits on Empire and Ameren Missouri's FACs.²¹ In Ameren Missouri's first prudence audit case, EO-2010-0255, the Commission determined that Ameren Missouri "acted imprudently, improperly and unlawfully when it excluded revenues" derived from power sales agreements from its FAC.²² Because these power sales agreements crossed over two prudence review time periods, the Commission, in Ameren Missouri's second prudence audit, EO-2012-0074, made the same finding.²³ Since then Staff has only recommended one other imprudence finding in an FAC prudence audit. In case no. EO-2011-0390, the third GMO FAC prudence audit case, Staff alleged that GMO had acted imprudently in association with its hedging future purchases of spot market power by buying options to purchase natural gas. The Commission, in its *Report and Order* in this case, found that Staff failed to produce substantial controverting evidence demonstrating serious doubt to rebut the presumption of prudence with regard to GMO's hedging policy.²⁴

There have been no other recommendations by the Staff regarding imprudence with respect to the FAC since the September 4, 2012, *Report and Order* in the third GMO FAC prudence audit case.

Incentive Mechanism

SB 179 allows the Commission to include, in an FAC, incentives to improve the efficiency and cost-effectiveness of the electric utilities' fuel and purchased power procurement.²⁵ The Commission, for each of the electric utilities, found that allowing the utility to have one

²¹ Case Nos. EO-2009-0115, EO-2010-0084 and EO-2010-0255 for GMO, Empire and Ameren Missouri respectively.

²² *Report and Order*, page 2

²³ *Report and Order*, page 2

²⁴ Page 47

²⁵ Section 386.266.1

hundred percent recovery of its FAC costs through an FAC would act as a disincentive for the utility to control FAC costs. The Commission determined that recovering a share of the difference between the NBEC and ANEC allows the electric utility a sufficient opportunity to earn a fair return on equity while protecting customers by providing an incentive to control costs. At the time that this white paper was written, the Commission had set that sharing percentage, for all of the electric utilities, to be 95%/5% - 95% of any increase in FAC costs above NBEC would be billed to the customers and the electric utility absorbs 5% while 95% of a decrease in FAC costs below NBEC would be credited to customers and the electric utility retains 5% of the decrease.²⁶

Given this incentive mechanism, the amount to be billed through the FAC is 95% of the difference between the ANEC and the NBEC. The result of this incentive mechanism is that, when costs are above the amounts included in base rates, the electric utility recovers almost 100% of the FAC costs. If FAC costs are below the amounts included in base rates, the utility recovers greater than 100% of its FAC costs. The table below shows examples of what occurs when actual costs are greater, equal to, and less than what is in the NBEC.

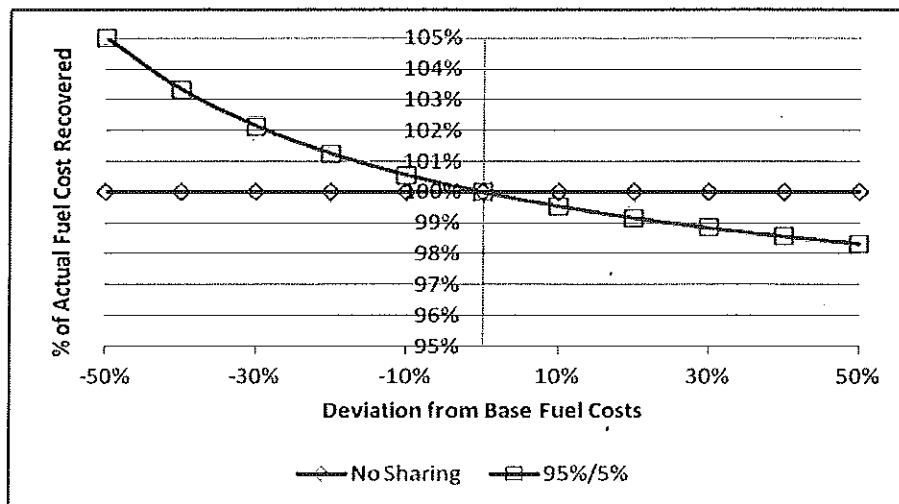
Impact of 95%/5% Sharing Mechanism

NBEC	ANEC	Diff	FAC Amt Billed to Customers	Amt Absorbed/ (Retained) by Company	Total billed to Customers	% FAC Costs Billed
\$100	\$150	\$50	\$47.50	\$2.50	\$147.50	98.3%
\$100	\$110	\$10	\$9.50	\$0.50	\$109.50	99.5%
\$100	\$100	\$0	\$0	\$0	\$100.00	100.0%
\$100	\$90	(\$10)	(\$9.50)	(\$0.50)	\$90.50	100.6%
\$100	\$50	(\$50)	(\$47.50)	(\$2.50)	\$52.50	105%

This table shows incentive mechanism allows the utility to bill its customers for 98.3% of its FAC costs when its ANEC is 50% higher than what is included in base rates, i.e., even if the actual FAC costs incurred are 50% higher than what was included in the base rates, the electric utility recovers 98.3% of its actual FAC costs.²⁷ Likewise, if actual fuel costs are 50% lower than what is included in base rates, the utility will recover 105% of its actual FAC costs. If the utility manages to reduce its actual FAC costs any amount below NBEC, will recover more 100% of its FAC costs. This relationship is shown in the graph below.

²⁶ While parties in rate cases have proposed different sharing percentages and/or different incentive mechanisms, the only incentive mechanism implemented has been a 95%/5% sharing of the difference between ANEC and NBEC.

²⁷ For a utility to bill only 95% of its actual costs, the actual FAC costs would need to be over 1,000 times greater than the costs included in base rates



These relationships hold true regardless of the magnitude of the NBEC.

Importance of Correct NBEC

Because Missouri's FAC is based on the difference between a subset of normalized costs and revenues set in a rate case and actual costs and revenues, it is important the costs and revenues included in the NBEC of the FAC are the same as the costs and revenues included in base rates. The table below shows three different scenarios. To simplify the example, in these scenarios there is no sharing of the difference between ANEC and NBEC. All of the difference between the ANEC and NBEC is billed or returned to the customers.

Net Base Energy Cost (NBEC)	FAC Costs in Base Rates	Actual Net Energy Cost (ANEC)	Billed FAC Costs	Total FAC Costs Billed	Total billed as % of ANEC
Scenario 1 - NBEC Equal FAC Costs in Rates					
\$100.00	\$100.00	\$110.00	\$10.00	\$110.00	100.00%
\$100.00	\$100.00	\$100.00	\$0.00	\$100.00	100.00%
\$100.00	\$100.00	\$90.00	-\$10.00	\$90.00	100.00%
Scenario 2 - NBEC Lower than FAC Costs in Rates					
\$100.00	\$110.00	\$110.00	\$10.00	\$120.00	109.09%
\$100.00	\$110.00	\$100.00	\$0.00	\$110.00	110.00%
\$100.00	\$110.00	\$90.00	-\$10.00	\$100.00	111.11%
Scenario 3 - NBEC Higher than FAC Costs in Rates					
\$100.00	\$90.00	\$110.00	\$10.00	\$100.00	90.91%
\$100.00	\$90.00	\$100.00	\$0.00	\$90.00	90.00%
\$100.00	\$90.00	\$90.00	-\$10.00	\$80.00	88.89%

The first scenario is a correct treatment of NBEC and FAC costs in Rates. NBEC is equal to the FAC costs included in base rates. In this scenario, when ANEC is higher than NBEC, the total FAC costs billed the customer is the \$100 billed in the base rates and \$10 billed through the FAC for a total of \$110. When the ANEC is the same as the NBEC, the customers are billed nothing through the FAC and the utility recovers all of its FAC costs through its base rates. Lastly, when the actual costs are less than the NBEC, the customers' bills are reduced and the utility recovers all of its actual fuel costs.

In Scenario 2, the NBEC designated in the FAC is less than the FAC costs in rates. In this scenario, the customers always pay more than intended. Even when ANEC is the same as the FAC costs included in rates, the customer pays for the difference between the ANEC and NBEC. In this scenario, the customers always paying more than the actual FAC costs because the fuel costs included in the base rates is greater than the costs used to calculate the NBEC.

In Scenario 3, the NBEC is set higher than the FAC costs included in rates. In this scenario, the electric utility does not collect the actual energy costs because the amount of FAC costs included in rates is less than the NBEC set in the FAC. The amount recovered is the lower FAC costs included in rates and the difference between the higher NBEC and ANEC. In this scenario, the company does not receive the revenues that are intended with an FAC.

These scenarios show the importance of insuring that the FAC costs included in base rates are the same as the FAC NBEC. If they are not set correctly, either the customers overpay or the company is not afforded the opportunity to recover its costs as intended.

Future Application of the FAC

The FAC rules have a requirement that the Commission review the effectiveness of the rules by no later than December 31, 2010. On November 12, 2010, the Commission opened a repository file, EW-2011-0139,²⁸ as a repository file for documents and comments regarding effectiveness of the FAC rules. The electric utilities, OPC and other interested parties filed comments regarding the need for revisions to the rules by March 1, 2011. The Commission issued an order on March 27, 2014 directing staff to file a status report on the revision of the rules. Beginning on April 27, 2015, Staff began hosting a series of three workshops for stakeholders to provide input to Staff on its review of the rules and, where possible, prepare

²⁸ EW-2011-0139, *In The Matter Of A Repository File Concerning Staff's Review Of The Commission's Fuel Adjustment Clause Rules*

collaborative revisions to the rules. On February 4, 2015, the Commission directed Staff to complete its review and file its recommendations regarding changes to the rules by September 15, 2015. The Commission later extended that completion date to November 20, 2015 and then to February 15, 2016. At the time that this whitepaper was updated, the Commission had sent its proposed rule to the Department of Economic Development for review prior to it being sent to the Secretary of State to be published in the Missouri Register for comments.

Education and Work Experience Background of

Lena M. Mantle, P.E.

In my position as Senior Analyst for the Office of the Public Counsel ("OPC") I provide analytic and engineering support for the OPC in electric, gas, and water cases before the Commission. I have worked for the OPC since August, 2014.

I retired on December 31, 2012 from the Public Service Commission Staff as the Manager of the Energy Unit. As the Manager of the Energy Unit, I oversaw and coordinated the activities of five sections: Engineering Analysis, Electric and Gas Tariffs, Natural Gas Safety, Economic Analysis, and Energy Analysis sections. These sections were responsible for providing Staff positions before the Commission on all of the electric and gas cases filed at the Commission. This included reviews of fuel adjustment clause filings, resource planning compliance, gas safety reports, customer complaint reviews, territorial agreement reviews, electric safety incidents and the class cost-of-service and rate design for natural gas and electric utilities.

Prior to being the Manager of the Energy Unit, I was the Supervisor of the Engineering Analysis Section of the Energy Department from August, 2001 through June, 2005. In this position, I supervised engineers in a wide variety of engineering analysis including electric utility fuel and purchased power expense estimation for rate cases, generation plant construction audits, review of territorial agreements, and resolution of customer complaints all the while remaining the lead Staff conducting weather normalization in electric cases.

From the beginning of my employment with the Commission in the Research and Planning Department of the in August, 1983 through August, 2001, I worked in many areas of electric utility regulation. Initially I worked on electric utility class cost-of-service analysis, fuel modeling and what has since become known as demand-side management. As a member of the Research and Planning Department under the direct supervision of Dr. Michael Proctor, I participated in the development of a leading-edge methodology for weather normalizing hourly class energy for rate design cases. I took the lead in developing personal computer programming of this methodology and applying this methodology to weather-normalize electric usage in numerous electric rate cases. I was also a member of the team that assisted in the development of the Missouri Public Service Commission electronic filing and information system ("EFIS").

I received a Bachelor of Science Degree in Industrial Engineering from the University of Missouri, at Columbia, in May, 1983. I am a registered Professional Engineer in the State of Missouri.

Lists of the Missouri Public Service Commission rules in which I participated in the development of or revision to, the Missouri Public Service Commission Testimony Staff reports that I contributed to and the cases that I provided testimony in follow.

Missouri Public Service Commission Rules

- 4 CSR 240-3.130 Filing Requirements and Schedule of Fees for Applications for Approval of Electric Service Territorial Agreements and Petitions for Designation of Electric Service Areas
- 4 CSR 240-3.135 Filing Requirements and Schedule of Fees Applicable to Applications for Post-Annexation Assignment of Exclusive Service Territories and Determination of Compensation
- 4 CSR 240-3.161 Electric Utility Fuel and Purchased Power Cost Recovery Mechanisms Filing and Submission Requirements
- 4 CSR 240-3.162 Electric Utility Environmental Cost Recovery Mechanisms Filing and Submission Requirements
- 4 CSR 240-3.190 Reporting Requirements for Electric Utilities and Rural Electric Cooperatives
- 4 CSR 240-14 Utility Promotional Practices
- 4 CSR 240-18 Safety Standards
- 4 CSR 240-20.015 Affiliate Transactions
- 4 CSR 240-20.017 HVAC Services Affiliate Transactions
- 4 CSR 240-20.090 Electric Utility Fuel and Purchased Power Cost Recovery Mechanisms
- 4 CSR 240-20.091 Electric Utility Environmental Cost Recovery Mechanisms
- 4 CSR 240-22 Electric Utility Resource Planning
- 4 CSR 240-80.015 Affiliate Transactions
- 4 CSR 240-80.017 HVAC Services Affiliate Transactions

Office of Public Counsel Case Listing

Case	Filing Type	Issue
ER-2016-0285	Direct	Fuel Adjustment Clause
ER-2016-0156	Direct, Rebuttal, Surrebuttal	Fuel Adjustment Clause, Resource Planning
ER-2016-0023	Direct, Rebuttal, Surrebuttal	Fuel Adjustment Clause
WR-2015-0301	Direct, Rebuttal, Surrebuttal	Revenues, Environmental Cost Recovery Mechanism
ER-2014-0370	Direct, Rebuttal, Surrebuttal	Fuel Adjustment Clause
ER-2014-0351	Direct, Rebuttal, Surrebuttal	Fuel Adjustment Clause
ER-2014-0258	Direct, Rebuttal, Surrebuttal	Fuel Adjustment Clause
EC-2014-0224	Surrebuttal	Policy, Rate Design

Staff Direct Testimony Reports

ER-2012-0175	Capacity Allocation, Capacity Planning
ER-2012-0166	Fuel Adjustment Clause
ER-2011-0028	Fuel Adjustment Clause
ER-2010-0356	Resource Planning Issues
ER-2010-0036	Environmental Cost Recovery Mechanism
HR-2009-0092	Fuel Adjustment Rider
ER-2009-0090	Fuel Adjustment Clause, Capacity Requirements
ER-2008-0318	Fuel Adjustment Clause
ER-2008-0093	Fuel Adjustment Clause, Experimental Low-Income Program
ER-2007-0291	DSM Cost Recovery

Missouri Public Service Commission Staff Testimony

Case No.	Filing Type	Issue
ER-2012-0175	Rebuttal, Surrebuttal	Resource Planning Capacity Allocation
ER-2012-0166	Rebuttal, Surrebuttal	Fuel Adjustment Clause
EO-2012-0074	Direct/Rebuttal	Fuel Adjustment Clause Prudence
EO-2011-0390	Rebuttal	Resource Planning Fuel Adjustment Clause
ER-2011-0028	Rebuttal, Surrebuttal	Fuel Adjustment Clause
EU-2012-0027	Rebuttal, Surrebuttal	Fuel Adjustment Clause
ER-2010-0356	Rebuttal, Surrebuttal	Resource Planning Allocation of Iatan 2
ER-2010-0036	Supplemental Direct, Surrebuttal	Fuel Adjustment Clause
ER-2009-0090	Surrebuttal	Capacity Requirements
ER-2008-0318	Surrebuttal	Fuel Adjustment Clause
ER-2008-0093	Rebuttal, Surrebuttal	Fuel Adjustment Clause Low-Income Program
ER-2007-0004	Direct, Surrebuttal	Resource Planning
GR-2007-0003	Direct	Energy Efficiency Program Cost Recovery
ER-2007-0002	Direct	Demand-Side Program Cost Recovery
ER-2006-0315	Supplemental Direct, Rebuttal	Energy Forecast Demand-Side Programs Low-Income Programs
ER-2006-0314	Rebuttal	Jurisdictional Allocation Factor
EA-2006-0309	Rebuttal, Surrebuttal	Resource Planning
ER-2005-0436	Direct, Rebuttal, Surrebuttal	Low-Income Programs Energy Efficiency Programs Resource Planning
EO-2005-0329	Spontaneous	Demand-Side Programs Resource Planning

Missouri Public Service Commission Staff Case Listing (cont.)

EO-2005-0293	Spontaneous	Demand-Side Programs Resource Planning
ER-2004-0570	Direct, Rebuttal, Surrebuttal	Reliability Indices Energy Efficiency Programs Wind Research Program
EF-2003-0465	Rebuttal	Resource Planning
ER-2002-425	Direct	Derivation of Normal Weather
EC-2002-1	Direct, Rebuttal	Weather Normalization of Class Sales Weather Normalization of Net System
ER-2001-672	Direct, Rebuttal	Weather Normalization of Class Sales Weather Normalization of Net System
ER-2001-299	Direct	Weather Normalization of Class Sales Weather Normalization of Net System
EM-2000-369	Direct	Load Research
EM-2000-292	Direct	Load Research
EM-97-515	Direct	Normalization of Net System
ER-97-394, et. al.	Direct, Rebuttal, Surrebuttal	Weather Normalization of Class Sales Weather Normalization of Net System Energy Audit Tariff
EO-94-174	Direct	Weather Normalization of Class Sales Weather Normalization of Net System
ER-97-81	Direct	Weather Normalization of Class Sales Weather Normalization of Net System TES Tariff
ER-95-279	Direct	Normalization of Net System
ET-95-209	Rebuttal, Surrebuttal	New Construction Pilot Program
EO-94-199	Direct	Normalization of Net System
ER-94-163	Direct	Normalization of Net System
ER-93-37	Direct	Weather Normalization of Class Sales Weather Normalization of Net System
EO-91-74, et. al.	Direct	Weather Normalization of Class Sales Weather Normalization of Net System
EO-90-251	Rebuttal	Promotional Practices Variance
ER-90-138	Direct	Weather Normalization of Net System
ER-90-101	Direct, Rebuttal, Surrebuttal	Weather Normalization of Class Sales Weather Normalization of Net System
ER-85-128, et. al.	Direct	Demand-Side Update
ER-84-105	Direct	Demand-Side Update