BEFORE THE PUBLIC SERVICE COMMISSION OF THE STATE OF MISSOURI

In the Matter of the KCP&L Greater	)	
Missouri Operations Company's Request	)	Case No. ER-2012-0175
for Authority to Implement A General	)	
Rate Increase for Electric Service	)	

<u>THE FEDERAL EXECUTIVE AGENCIES'</u>
<u>INITIAL POST-HEARING BRIEF ON TRANSMISSION TRACKER</u>

COME NOW the Federal Executive Agencies ("FEA"), by and through counsel, pursuant to the Public Service Commission of the State of Missouri's ("Commission") Rules of Practice and Procedure, 4 C.S.R. 240-2.075, in the service area of KCP&L Greater Missouri Operations Company (the Company) hereby submits this Post-Hearing Brief in the above-captioned docket.

1. <u>BACKGROUND</u>

The Company has proposed in its filing to implement a Transmission Tracker. In response to this proposal, FEA filed the direct and surrebuttal testimony of Mr. James Dauphinais. Mr. Dauphinais has been employed as a consultant with the firm of Brubaker & Associates, Inc. since 1997. In this capacity, Mr. Dauphinais has filed and presented testimony before the Federal Energy Regulatory Commission (FERC) and numerous other state utility commissions.[1] The tracking mechanism that the Company seeks to implement will track certain transmission expenses against a specific expense value that will be set in base rates. The expenses that will be tracked are the Southwest Power Pool ("SPP") Schedule 1-A Administration Charge, SPP Transmission Costs and SPP Schedule 12 FERC Assessment Fees. Once these transmission expenses are set at the rate proceeding, any actual expenses that are

[1] Mr. Dauphinais provides a resume as an attachment to his direct testimony which describes his experience as an expert consultant in the electric regulatory industry. (Appendix A)

higher than the determined baseline value will be treated as a regulatory asset and any expenses that fall short of the amount will be treated as a regulatory liability. The regulatory asset or liability would then be amortized in the Company's next rate proceeding over a time equal to the accumulation period between rate cases. The regulatory asset or liability would be included in rate base. The company is also proposing that carrying costs be accrued in amounts that are not yet included in rate base. The carrying costs would be calculated monthly by applying the monthly value of the annual Allowance for Funds Used During Construction (AFUDC) rate to the eligible expenses.[2]

2. FEA ARGUMENT

FEA is opposed to the Commission granting the Company's proposal for a Transmission Tracker. FEA believes that the Commission should deny the Company's request for the following reasons:

A. THE COMPANY HAS NOT DEMONSTRATED A TRUE NEED TO TRACK EXPENSES

The Commission has relied on specific criteria in the past to determine whether a tracking mechanism is necessary to ensure the financial health of a utility. In case ER-2007-0002, AmerenMissouri requested that the Commission implement a tracking mechanism, similar to the Company's requested Transmission Tracker, in the form of a Fuel Adjustment Clause (FAC). In response to Ameren's request, the Commission relied on witness testimony to determine the criteria that the utility needed to show to demonstrate a need for a FAC.[3] The Commission

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[2] Ives direct, 13-16

[3] In ER-2007-0002 the Commission relied on the testimony of State witness Michael L. Brosch in setting out criteria to determine when a fuel adjustment clause is warranted. The Commission found that Mr. Brosch based his criteria on his experience working with expense tracking mechanisms from other proceedings. The Commission found that the criteria proposed by Mr. Brosch appeared to be well accepted throughout the regulatory community. *Report and Order*, Case No. ER-2007-0002 (2007), p. 20-21.

determined that a cost or revenue change should only be recovered through a fuel adjustment clause if such change is:

1. Substantial enough to have a material impact upon revenue requirements and the financial performance of the business between rate cases;
2. beyond the control of management, where utility management has little influence over experienced revenue or cost levels; and
3. volatile in amount, causing significant swings in income and cash flows if not tracked.[4]

The transmission expenses that the Company is proposing to track fail to meet the criteria that the Commission relied on in Case No. ER-2007-0002. The primary reason for this is that none of the expenses which the Company desires to track meet the definition of volatility as viewed by the Commission. The Commission ruled that it was not sufficient for a utility to show that its fuel costs were rising to show volatility. The Commission went on to explain,

> Markets in which prices are volatile tend to go up and down in an unpredictable manner. When a utility's fuel and purchased power costs are swinging in that way, the time consuming ratemaking process cannot keep up with the swings.[5]

In the current case, the Company has only shown that the transmission expenses they wish to track are likely to go up. Furthermore, as Mr. Dauphinais points out in his testimony, the increases in SPP transmission costs that the Company hopes to track are also well forecasted by SPP. This predictability of future expense increases negates any degree of volatility imagined by the Company.[6] The Company has even outlined the specific amounts of transmission cost increases it will face for calendar years 2012 through 2019.[7] These are not volatile expense changes where both the Company and customers need to be protected from the possibility of

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[4] *Report and Order*, Case No. ER-2007-0002 (2007), pp. 20-21.

[5] *Id.* at 23

[6] Dauphinais direct, 8

[7] In the Company's opening statement on the issue of the Transmission Tracker, Company counsel explained that the Company predicted that SPP transmission costs allocated to GMO will be $6.8 million for calendar year 2012 and will increase to $9.2 million in 2014 and peak at over $16.7 million in 2019. Counsel also referred to a schedule in Company witness Mr. Darrin Ives' direct testimony which highlights the expected growth of the Company's transmission expenses over the next three years. (Tr, p. 641)

unforeseen swings in revenues or expenses. Rather, the Company has shown that they forecast transmission expenses to significantly increase between now and its next rate case with no expected decrease. As such, the costs are not volatile and should be recovered through traditional ratemaking mechanisms rather than a Transmission Tracker.

B. THE USE OF A TRACKER WILL ALLOW THE COMPANY TO PURSUE SINGLE-ISSUE RATEMAKING

If the Commission allows the Company to implement a Transmission Tracker the Company will effectively be allowed to pursue single-issue ratemaking. Mr. Dauphinais explains that single-issue ratemaking allows a utility to receive additional revenue in rates based on either an increase in tracked expenses or a decrease in tracked revenues. This allows a utility to protect itself against the risk of losses for one tracked item while simultaneously allowing the utility the opportunity to profit from over-valued items in rate base which might have otherwise offset any revenue shortfall for the tracked item. As Mr. Dauphinais explains, "allowing a tracker can break the synchronism between revenues, expenses and rate base leading to a utility over-recovering its costs."[8] The Missouri Supreme Court has also highlighted the danger of single-issue ratemaking. In *State ex rel. Utility Consumers' Council of Missouri, Inc. v. Public Service Commission*, 585 SW2d 41 (1979) the Supreme Court explained, "By permitting an electric utility to utilize a fuel adjustment clause, the Commission permits one factor to be considered to the exclusion of all others in determining whether or not a rate is to be increased."[9] As the Supreme Court points out, this type of ratemaking essentially allows the Company guaranteed collection of one item without any corresponding benefit passed on to the customers.

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[8] Dauphinais direct, 6

[9] In *State ex rel. Utility Consumers' Council of Missouri, Inc. v. Public Service Commission*, 585 SW2d 41, 56 (1979)

Several aspects of the Company's request for a Transmission Tracker demonstrate the fundamental problems with single-issue ratemaking. First, the Company proposes to track expenses but not revenues. This inconsistency will allow the Company to collect 100 percent of any under recovery in transmission expenses from the customers while at the same time keeping 100 percent of any over recovery in transmission revenues as profit. This omission is especially disconcerting based on the Company's expectation that transmission revenues will increase.[10] Next, the Transmission Tracker will decrease the amount of risk that the Company will incur in earning its required revenue. Despite this, the Company has failed to acknowledge that a corresponding reduction in authorized Return on Equity (ROE) should accompany this reduction in risk. Instead, the Company has requested an increase in their authorized ROE. Finally, many of the transmission expenses that will be tracked are driven by construction of SPP regional transmission projects. These are plant additions that should not be tracked between rate cases, but rather included in rate base in the Company's next rate case. Additionally, the Transmission Tracker fails to account for the benefits that these projects will provide as an offset to tracked expenses.[11] These factors show how single-issue ratemaking associated with the Transmission Tracker has significant potential to create windfall profits for the Company.

C. A TRACKING MECHANISM ELIMINATES THE COMPANY'S INCENTIVE TO MINIMIZE EXPENSES AND MAXIMIZE REVENUES BETWEEN RATE CASES

Each utility has a certain amount of resources that it can expend to keep expenses low and revenues high. If the Company knows that it will automatically recover transmission expenses it will lose all incentive to devote resources to keeping these expenses at the lowest level possible. At the same time, with a tracker in place, the Company will be motivated to

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[10] When Company witness Mr. Ives was asked by Commission Staff counsel whether he believed revenues were projected to go up, he responded by saying, "Assuming our revenue requirement's going up, which I think I testified to, they would be projected to go up." (Tr, p. 695)

[11] Dauphinais direct, 10

devote the majority of its recourses to reducing expenses, or increasing revenues, for items that are not tracked where it stands to earn a profit. Mr. Dauphinais explains that the Company has the ability to manage both the SPP Schedule 1-A Administration Charges and the total SPP Transmission Costs through active participation in the SPP stakeholder process and before the FERC.[12] If the Company is allowed to track these expenses for automatic collection, it will lose all incentive to be an active stakeholder. Instead, the Company will be motivated to devote its resources to untracked expense and revenue items where its shareholders bear the risks and gain the benefits between rate cases.

3. CONCLUSION

The Commission should not grant the Company's request for a Transmission Tracker. The Company's failure to include revenues along with expenses indeed aggravates the problems associated with the proposed Transmission Tracker. However, even an amendment to the Company's requested Tracker to also track revenues would not remedy the inherent problems associated with the Company's proposed tracking mechanism. In *Utility Consumers' Council of Missouri, Inc.* the Missouri Supreme Court warned that the rationale behind a fuel adjustment clause could be used to justify other automatic adjustment clauses for a utility's remaining operating expenses. The Court stated, "... we will not travel further down the 'slippery slope' and risk a dismantling of the carefully balanced fixed rate system established by the legislature."[13] The Company's desire to track transmission expense merely because they expect these expenses to increase is the exact slippery slope that the Supreme Court warned about. To provide a safeguard against this slippery slope, the Commission has since set out specific criteria necessary for a utility to meet in order to show the need for a tracking mechanism. The

[12] Dauphinais direct, 9 and 10
[13] *Utility Consumers' Council of Missouri, Inc.*, 585 SW2d at 57.

Company has failed to meet this burden. Specifically, the Company has failed to show that the expenses it wishes to track are volatile. Instead, the Company has only shown that these expenses are expected to increase which is insufficient to meet the criteria set forth by the Commission in docket ER-2007-0002. The use of the Tracker will allow the Company to pursue single-issue ratemaking and remove the Company's incentive to devote resources to keep transmission expenses low. These are problems that will exist regardless of whether revenues are included in the Transmission Tracker. The Transmission Tracker should be disallowed and the Company should be required to recover its transmission expense on an untracked basis through its base rates as set by the Commission.

Respectfully submitted this 28th day of November, 2012.

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CERTIFICATE OF SERVICE

The undersigned hereby certifies that the foregoing Federal Executive Agencies' Post-Hearing Brief was served on the parties of record as provided on the Commission website via electronic mail on this 28th day of November, 2012.

Capt Samuel T. Miller