

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

In the Matter of the Tariff Filing of Aquila, )  
Inc., to Implement a General Rate Increase for )  
Retail Steam Heat Service Provided to )                      Case No. HR-2005-0450  
Customers in its L&P Missouri Service Area.    )

**STAFF’S SUGGESTIONS IN SUPPORT OF  
NONUNANIMOUS STIPULATION AND AGREEMENT**

**COMES NOW** the Staff of the Public Service Commission of Missouri and submits the suggestions following in support of the Nonunanimous Stipulation and Agreement (Stipulation) filed with the Commission in this case February 17, 2006:

1.     The Staff is a party to the Stipulation, which resulted from extensive negotiations between Aquila, Inc. and Ag Processing, Inc.

2.     Although most of the revenue requirement aspects of the settlement cannot be assigned to specific issues, aspects of the settlement are specific. Those aspects of the settlement are related generally below.

***Effect on Agreement if Modified or Conditioned by Commission***

3.     If the Commission does not accept the Stipulation without modification or condition, then, by the terms of the Stipulation (paragraphs 16 and 17), the Stipulation may neither be used to bar any party from a decision on the merits in this case nor considered as part of the record in this case.

***Conduct of Settlement Negotiations***

4.     After Aquila and Ag Processing, Inc. established the framework of the Stipulation through their negotiations, all parties in the case had opportunity to provide input.

***Pending Commission Cases within Scope of Settlement***

5. The Stipulation addresses only the issues in Case No. HR-2005-0450, Aquila's general steam heat rate increase case.

***Revenue Requirement***

6. Aquila, Inc. initiated a general steam service rate increase case on May 27, 2005 by filing with the Commission tariff sheets it designed to produce, exclusive of gross receipts, sales, franchise and occupational taxes, an additional \$5.0 million in gross annual revenue from Aquila Networks—L&P steam customers (a 44.3% increase).

7. The illustrative tariff sheets of the Stipulation are designed to produce, exclusive of gross receipts, sales, franchise and occupational taxes, an additional \$4.5 million in gross annual revenue from Aquila Networks—L&P steam customers (a 37.5% increase). This increase is within the range of what the Staff anticipates would have been the Staff's post true-up case, although the Staff did not finalize any true-up of its case. For these reasons, the Staff supports the increase.

***Rate Design***

8. The illustrative tariff sheets are also designed to implement the rate increase by increasing each rate component by the same percentage based on the Staff's billing determinants included in the Stipulation as Appendix B. The Staff supports this rate design, which it recommended in the direct testimony of Staff witness Janice Pyatte prefiled in this case October 28, 2005.

***Fuel Adjustment Rider***

9. Aquila and Ag Processing, Inc. developed a fuel adjustment rider for Aquila's Missouri steam operations, operations of Aquila Networks—L&P. Under the Stipulation

(paragraphs 8 through 8.5) Aquila will file new steam rates for Aquila Networks—L&P quarterly. At the end of each quarter Aquila will prepare a rate adjustment based on fuel costs for that quarter to reflect eighty percent (80%) of the change in its natural gas and coal fuel costs above or below a base amount of \$3.005 per million BTU. Thus, when implemented in rates, Aquila will retain twenty percent (20%) of the difference between actual fuel costs and base fuel cost of \$3.005 per million BTU when the actual fuel cost is below the base cost, but, if actual fuel cost exceeds the base cost, Aquila will recover only eighty percent (80%) of the difference, not one hundred percent (100%). Therefore, the fuel adjustment rider gives Aquila an economic incentive to keep fuel costs down.

Each quarterly fuel cost adjustment will be reflected in the steam rates of Aquila Networks—L&P for one year. The sum of these quarterly rate adjustments will be implemented in rates—the fuel rider. Thus, after at the end of the first year, the rider will reflect a rolling twelve-month adjustment, revised quarterly.

The fuel adjustment rider will apply to all Aquila Networks—L&P steam customers.

In determining each quarterly adjustment, and thus rates, Aquila will be deemed to be burning at least a minimum level of coal for purposes of fuel costs, regardless of how much coal it actually burns. If Aquila does not burn the coal minimums then additional coal generation will be imputed up to the agreed to minimum levels, thus reducing the amount of natural gas-fired generation for purposes of determining the rates Aquila Networks—L&P steam customers will pay. This imputation of a minimum level of coal generation for Aquila's steam operations will not result in higher costs to Aquila's electric customers since Aquila commits to not seek recovery from its electric customers of any of the natural gas costs that would be included in costs for setting steam rates but for the minimum coal generation levels. From the Staff's

perspective this provision which protects Aquila's electric customers was an important factor in the Staff executing the Stipulation.

At the end of the twelve (12) months a particular quarterly fuel cost adjustment is reflected in rates, the revenues collected in rates attributable to that quarter will be reconciled with the actual fuel costs Aquila prudently incurred, and the fuel rider adjusted accordingly. Thus, the first reconciliation will take place after the fuel adjustment rider has been in place for one year, and shall be performed quarterly thereafter.

For assurance the fuel adjustment rider is properly executed, there is a two-step review process. In the first step the Staff will review for determination that the rider is working as intended and that no significant level of imprudent costs is apparent. Based on step-one results the Staff may perform a detailed prudence review not more than once every twelve months. Customers may initiate a prudence review through the Commission's existing complaint process. Aquila's steam rates will not change based on the results of a prudence review, unless the prudence adjustment exceeds ten percent (10%) of the total fuel costs incurred during the twelve-month period reviewed.

In the Stipulation at paragraph 14 the parties express their agreement that the foregoing fuel adjustment rider does not constitute approval or acquiescence to Commission implementation of the same or a similar fuel cost rate adjustment mechanism through a rule, promulgated pursuant to Section 386.266 Supp. 2005 or otherwise. Further, in paragraph 13 they agree an absence of a finding of imprudence with regard to the fuel adjustment rider does not prejudice any party or determine the prudence of such fuel costs in an Aquila electric rate proceeding.

In *State ex rel. Utility Consumers Council of Missouri, Inc. v Public Service Commission*, 585 S.W.2d 41 (Mo. banc 1979), on review of a Commission order authorizing electric utilities subject to its jurisdiction to use an automatic fuel adjustment clause for recovery of fuel costs from residential and small commercial customers, the Missouri Supreme Court said, at page 50, generally regarding fuel adjustment clauses the following:

A fuel adjustment clause (FAC), once authorized by the commission as a part of the utility's rate structure, enables the utility to pass on to the consumer any increase (or decrease) in the cost of fuel automatically and without any need for further consideration of compensatory decreases (or increases) in other operating expense. As such, it is a radical departure from the usual practice of approval or disapproval of filed rates, in the context of a general rate case. Even under the file and suspend method, by which a utility's rates may be increased without Requirement of a public hearing, the commission must of course consider all relevant factors including all operating expenses and the utility's rate of return, in determining that no hearing is required and that the filed rate should not be suspended.

The Staff is mindful of Senate Bill 179, codified at section 386.266 RSMo Supp 2005, authorizing fuel adjustment clauses for electric companies. Although Senate Bill 179 (S.B. 179) does not expressly state it is applicable to heating companies (those providing steam service), Section 393.290 RSMo 2000 provides:

All provisions of chapters 386, 387, 390, 392 and 393, RSMo, in reference to . . . electrical corporations . . . in reference to hearings, summoning witnesses, taking of testimony . . . complaints as to quality, price, facilities furnished, the fixing of just and reasonable rates . . . under chapters 386, 387, 390, 392 and 393, RSMo, excessive charges for product, service or facilities, proceedings before the commission, and proceedings in any court mentioned in chapters 386, 387, 390, 392 and 393, RSMo, and in all other sections, paragraphs, provisions and parts of chapters 386, 387, 390, 392 and 393, RSMo, in reference to any other corporations subject to any of the provisions of chapters 386, 387, 390, 392 and 393, RSMo, so far as the same shall be practically, legally or necessarily applicable to heating companies in this state, are hereby made applicable to such heating companies as designated in said chapters, and shall have full application thereto.

Assuming S.B. 179 applies to heating companies, the Commission has not promulgated

rules to effectuate S.B. 179. Thus, even if S.B. 179 applies to heating companies, a fuel adjustment clause (FAC) under S.B. 179 is not at this time available to Aquila Networks—L&P for steam service. Section 386.266.12 states as follows:

The provisions of this section [386.266] shall take effect on January 1, 2006, and the commission shall have previously promulgated rules to implement the application process for any rate adjustment mechanism under this section prior to the commission issuing an order for any rate adjustment.

Regardless, it should not be assumed that a FAC is not otherwise available to Aquila Networks—L&P for steam service. In its 1979 opinion issued in *State ex rel. Utility Consumers Council of Missouri, Inc. v. Public Serv. Comm'n*, 585 S.W.2d 41 (Mo. banc 1979) (*UCCM*), the Missouri Supreme Court recounted the history of the case before it, Commission Case No. 17,730. The Court related that the Commission first authorized a FAC for residential customers with its February 1, 1974 Report And Order in Case No. 17,730 (*In the Matter of the Investigation of the Fuel Adjustment Method for the Recovery of Fuel Costs by Electric Utilities Operating in the State of Missouri*, 18 Mo.P.S.C.(N.S.) 371 (1974) (Emphasis added.)). The Commission had previously permitted FACs for industrial and large commercial electric customers, but the Court expressly noted that matter was not before it, and limited its decision for FACs for residential and small commercial customers:

. . . Such a clause had never before been permitted to become a part of a residential rate schedule in Missouri, although it has been permitted as a part of industrial and large commercial rate schedules, a matter which is not before us in this case. . . .

585 S.W.2d at 44.

We have concluded that application of an FAC to residential and small commercial customers, as was done in this case, was beyond the statutory authority of the commission and that the FAC, roll-in, and surcharge were therefore unauthorized and cannot continue in effect. The question of use of an FAC in regard to other customers is not an issue in this case. . . .

*Id.* at 47.<sup>1</sup>

The Commission commented as follows in its February 1, 1974 Report And Order in Case No. 17,730 regarding the history of FACs for industrial and large commercial electric customers:

For many years the electric utilities in the State of Missouri, pursuant to tariffs on file with the Commission, have made automatic adjustments to the electric bills rendered to certain classes of customers as a result of fluctuations upward or downward, in the cost of fuel used to generate electricity. Generally speaking, all electric utilities apply fuel adjustment to industrial customers but to date the Commission has not allowed fuel adjustments to the bills rendered to residential customers. Various utilities treat the customers in classes other than residential or industrial in different manners. The majority do not apply fuel adjustments to the bills rendered to small commercial customers, however, larger commercial customers electric bills are generally subject to fuel adjustment.

Although the percentages vary slightly from company to company, approximately 50 percent of the kilowatt hours of electricity sold in the State of Missouri are

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<sup>1</sup> There are two other references to industrial and large commercial customers in the Court's decision in *UCCM*: one referring to a distinction in the level of knowledge/expertise between industrial and large commercial customers, on the one hand, and residential customers, on the other, and the second referring to the legal effect of there having been FACs for years applicable to Missouri industrial and large commercial electric customers:

Not only would a fuel adjustment clause permit new "rates" to go into effect without consideration of other factors and thus without a framework in which to determine if overall rates are reasonable, it would also negate the effect of s 393.140(11), by which all rates are printed and open for public inspection. The purpose of thus providing the customer with a method of ascertaining what rates are in effect and enabling him to take the appropriate steps to challenge those rates would be destroyed with a fuel adjustment clause. Upon reference to the filed rate schedule of the utility, the consumer would be confronted with a formula and a rate filed as a result thereof. While it is debatable that representatives of large industrial or commercial customers might understand such a system, the average consumer could not be expected to do so. It is no answer to say that few understand the rates previously filed; this argument merely demonstrates the need to avoid further complication. . . .

585 S.W.2d at 57.

. . . Since FAC's have been used in regard to industrial and large commercial users for 60 years, and because other jurisdictions approve them, it is posited that we should also approve them.

It is for the legislature, not the PSC, to set the extent of the latter's jurisdiction. The mere fact that the commission has approved similar clauses in the past, or that other states permit them, is irrelevant if they are not permitted under our statute . . .

*Id.* at 55; citations omitted.

subject to immediate price adjustment as a result of increases or decreases in the cost of the fuel used to generate the electricity.

For a number of years electric companies in the State of Missouri have, in their applications for rate increases, sought authority from this Commission to file tariffs containing fuel adjustment clauses which would apply to all classes of customers. As recently as December 10, 1971, in Union Electric's Case No. 17,107 and on January 3, 1973, in Arkansas-Missouri Power Company's Case No. 17,405, the Commission has rejected applications to increase revenues by extension of fuel adjustment tariffs to residential electric customers.

18 Mo.P.S.C.(N.S.) at 373-74.

. . . At present utilities implementing the fuel adjustment are required to file little justification for rate changes. There has been infrequent objections to these changes since it is assumed that industrial customers have personnel skilled in the determination of whether or not the fuel clause is being applied correctly. . .

18 Mo.P.S.C.(N.S.) at 376.

In Case No. 17,730, the Commission determined it was appropriate to eliminate disparate treatment to different classes of customers and, therefore, authorized an FAC for all classes of electric customers as an experiment for two years stating that "at the end of the two year experimental period it shall again examine the entire question of extension of fuel adjustment clauses to determine whether it shall be continued on a permanent basis or abandoned." 18 Mo.P.S.C.(N.S.) at 381, 379.

Two years later, in the consolidated cases *In the Matter of the Investigation of the Fuel Adjustment Method for the Recovery of Fuel Costs by Electric Utilities Operating in the State of Missouri* (Emphasis added.) and *Staff vs. Kansas City Power & Light Co.*, Case Nos. 17,730 and 18,663, 20 Mo.P.S.C.(N.S.) 563 (1976), the Commission, among other things, in its Report And Order authorized the use of a revised FAC. The Commission stated that every FAC submitted to the Commission pursuant to the provisions of the Report And Order had to have an expiration date of May 31, 1978 and that prior to the expiration date the Commission would hold further

hearings to determine whether an FAC in its present form or in a modified form should be continued beyond May 31, 1978. The Commission did not preclude reopening the matter at any time prior to May 31, 1978 if it concluded that the objectives of the Report And Order were not being achieved. 20 Mo.P.S.C.(N.S.) at 576. In its *UCCM* decision the Missouri Supreme Court stated the Commission continued the electric residential FAC beyond May 31, 1978. 585 S.W.2d at 45.

The predecessor of Aquila Networks—L&P, St. Joseph Power & Light Company, had an industrial steam FAC in effect when the Missouri Supreme Court issued its *UCCM* decision. That industrial steam FAC stayed in effect until August 1, 1988, the date the tariffs resulting from Commission approval of a Stipulation And Agreement in Case No. HR-88-116 went into effect. Neither the Commission’s Report And Order nor the Stipulation And Agreement approved by the Commission in Case No. HR-88-116 is published in the Commission’s bound volumes of Orders. The Stipulation And Agreement in Case No. HR-88-116, at page 2, includes the following:

1. That the Company be authorized to file revised industrial steam tariffs designed to increase the Company’s Missouri jurisdictional gross annual industrial steam revenues by \$550,000, exclusive of applicable license, occupation, franchise, gross receipts or other similar charges or taxes; that said revised tariffs . . . shall not contain an industrial steam fuel cost adjustment; that said revised tariffs shall become effective for service rendered on and after August 1, 1988 . . .”

In light of the foregoing and Section 536.060 RSMo 2000, which provides that “[c]ontested cases . . . may be informally resolved by consent agreement or agreed settlement or may be resolved by stipulation, consent order, or default, or by agreed settlement where such settlement is permitted by law. . . .,” the Staff believes the fuel adjustment rider in the Stipulation is not unlawful and would not make approval of the Stipulation unlawful.

### ***Moratorium***

10. The Stipulation, in paragraph 10, establishes the period ending December 31, 2006 as a time during which Aquila commits to not file a steam general rate case unless certain criteria are met. Those criteria are if the results of a reliability study or system resource study Aquila commits to perform in paragraphs six (6) and seven (7) of the Stipulation, respectively, result in “actions, improvements, changes in operating procedures, or projects placed in service before September 1, 2007 that would increase the revenue requirements of the Aquila Networks—L&P steam system by ten percent (10%) or more.”

### ***Reliability and System Resource Studies, and Reporting Requirement***

11. In paragraphs six (6) and seven (7) of the Stipulation Aquila commits to study, at its cost, both reliability and system resources of its Aquila Networks—L&P steam system, identifying solutions and economical resource options, respectively. The reliability study results are to be reported to the Staff and interested parties within ninety (90) days of a final order in this case and the system resource study results are to be reported to them within two hundred forty (240) days of a final order in this case. The Staff supports actions taken by utilities to enhance the reliability of their utility systems and to evaluate their resource options to most economically serve their utility customers.

In paragraph 11 of the Stipulation Aquila agrees to provide certain information monthly, quarterly and annually. The Staff supports utilities keeping the Staff informed of information that affects regulated utility operations.

### ***Extension of Ag Processing, Inc. Special Contract***

12. While it has no position on the matter, the Staff notes the Stipulation, at paragraph 12, includes an extension to April 21, 2010 of an existing contract dated April 22,

2004 between Aquila and Ag Processing, Inc. and the continuation of another agreement dated March 22, 2004 between Aquila and Ag Processing, Inc. Aquila agrees that, in future ratemaking cases, Aquila will impute revenues from Ag Processing, Inc. as if Ag Processing, Inc. is paying the full tariff rate.

### ***Tariff and Implementation***

13. In the Stipulation at paragraph 4 the Signatory Parties agree to a goal of tariff sheets conforming to the illustrative tariffs being effective by March 1, 2006, or as soon thereafter as the Commission deems appropriate, and they agree the Commission, if it accepts the Stipulation, should at the same time authorize Aquila to file tariff sheets conforming to the illustrative tariff sheets with an effective date of less than thirty (30) days after the filing date. Because the Staff supports the rate increase the signatory parties agree to in the Stipulation, the Stipulation resolves all issues in the case, and the Staff has already reviewed the illustrative tariff sheets, the Staff supports implementation of the rate increase by March 1, 2006 or soon thereafter.

### ***Cost Allocations***

14. As part of the Stipulation, in paragraph 9, Aquila agrees to continue to use the same allocation methods currently employed to allocate common costs between the electric and steam operations of the Aquila Networks—L&P operating division, and between the Aquila Networks—L&P operating division and other operating entities, such as Aquila, Inc. itself, until, in a general rate proceeding, the parties agree, or the Commission orders, otherwise. Further, in paragraph 13 of the Stipulation, the parties agree the Stipulation does not limit them from advocating or the Commission adopting a different cost allocation approach in other Aquila electric and steam rate cases. The Staff supports use in this case of the allocation factors it

employed and retention of the flexibility to use other factors should changed circumstances warrant doing so.

***Waivers and Limitation of Scope of Effect of Agreement***

15. The Stipulation includes the typical provisions that it is being entered into solely for resolution of the issues in the cases, that does not constitute approval or acquiescence of any party to any ratemaking or procedural principle and that it is not binding, except as expressly specified in the agreement. Further, if the Stipulation is accepted by the Commission, the Stipulation provides for the typical waivers of further contested proceedings and judicial review, and that the testimony prefiled in this case may be made part of the record in the case without the witnesses taking the stand.

***If Unopposed the Stipulation May Be Treated as Unanimous***

16. Commission Rule 4 CSR 240-2.115 provides that parties in a contested case have seven days from the date a stipulation and agreement is filed to object to the agreement. As of the time and date of the filing of these suggestions, no party has filed an objection to the Stipulation. Unless a party objects to the Stipulation, under Commission Rule 4 CSR 240-2.115(2), the Stipulation filed in this case may be treated by the Commission as a unanimous stipulation and agreement. Section 536.060 RSMo 2000 provides that “[c]ontested cases . . . may be informally resolved by consent agreement or agreed settlement or may be resolved by stipulation, consent order, or default, or by agreed settlement where such settlement is permitted by law. . . .”

**WHEREFORE** the Staff submits the foregoing Suggestions in Support of the Nonunanimous Stipulation and Agreement filed February 17, 2006 in Case No. HR-2005-0450.

Respectfully submitted,

/s/ Nathan Williams

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### **Certificate of Service**

I hereby certify that copies of the foregoing have been mailed, hand-delivered, transmitted by facsimile or electronically mailed to all counsel of record this 24<sup>th</sup> day of February 2006.

/s/ Nathan Williams

Nathan Williams