BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the Matter of the Joint Application of Missouri-American Water Company, St. Louis County Water Company, d/b/a Missouri-American Water Company, and Jefferson City Water Works Company, d/b/a Missouri-American Water Company, for an Accounting Authority Order Relating to Security Costs.	))))))	**Case No. WO-2002-273**

REPORT AND ORDER
ON REMAND

Issue Date: November 10, 2004

Effective Date: November 20, 2004

2. The *Sibley* Test:

Under a long-standing test, the Commission has granted AAOs where the expenditures in question are "unusual and nonrecurring, and thus extraordinary."[58] In the present case, the Commission's Staff has urged the Commission to adopt a new four-part test for AAOs. Staff has taken this position in other recent cases involving AAOs and the Commission has not adopted it.[59] Missouri-American strenuously opposes Staff's proposal, while the other parties are willing to accept it.

The leading Commission decision on AAOs concerned a large construction project at Missouri Public Service's Sibley Generating Station.[60] Aquila, then known as Utilicorp United and of whom Missouri Public Service is a division, extensively rebuilt Sibley in order to both extend its life and convert it to the use of low-sulfur, western coal.[61] Also involved were two purchased-power contracts. Aquila sought an AAO in order to defer both costs associated with the Sibley construction project and the purchased power contracts to its next rate case.

In *Sibley,* the Commission noted that it had previously granted AAOs "on a case-by-case basis."[62] The Commission analyzed AAOs in *Sibley* in terms of their ratemaking effect, that is, the consideration of costs from outside the test year:

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[58] *E.g., St. ex rel. Missouri Office of the Public Counsel, supra,* 858 S.W.2d at 811: "The Commission's decision to grant authority to defer the costs associated with the Sibley reconstruction and coal conversion projects . . . was the result of the Commission's determination that the construction projects were unusual and nonrecurring, and therefore, extraordinary. The Commission determined the projects to be unusual because of their size and substantial cost."

[59] *E.g., In the Matter of Missouri Public Service and St. Joseph Light & Power, Divisions of UtiliCorp United, Inc.,* Case No. GO-2002-175, decided by the Commission on November 14, 2002.

[60] *Sibley, supra.*

[61] "Missouri Public Service" is a registered fictitious name under which Aquila does business in Missouri.

[62] *Sibley,* at 204 (punctuation corrected).

> Under historical test year ratemaking, costs are rarely considered from earlier than the test year to determine what is a reasonable revenue requirement for the future. Deferral of costs from one period to a subsequent rate case causes this consideration and should be allowed only on a limited basis. This limited basis is when events occur during a period which are extraordinary, unusual and unique, and not recurring. These types of events generate costs which require special consideration.[63]

Such events, the Commission explained, included extraordinary losses, construction projects of unusual size, costs incurred complying with Commission safety requirements, and such other items as nuclear fuel leases, a coal contract buy-out, pension costs, and an automated mapping system.[64] In fact, in a prior case, the Commission had already permitted the deferral of costs associated with the Sibley rebuild and coal conversion project.

In the *Sibley* decision, the Commission emphasized that it is the extraordinary event that is the "primary focus" in any request for an AAO, considered on a case-by-case basis: "The decision to defer costs associated with an event turns on whether the event is in fact extraordinary and nonrecurring."[65] The Commission emphasized that "[e]xtraordinary means unusual and nonrecurring."[66] Also relevant, but not dispositive, the Commission explained, is "whether the event has a material or substantial effect on a utility's earnings."[67] Another relevant factor is the certainty of the event's occurrence.[68] "Utilities should not seek deferral of speculative events since it is hard to determine whether an event is extraordinary

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[63] *Id.*, at 205 (original paragraph formatting altered).

[64] *Id.*

[65] *Id.*, at 205, 206.

[66] *Id.*, at 207.

[67] *Id.*, at 206.

[68] In *Sibley,* the Commission contemplated the grant of AAOs for future events.

or material unless there is a high probability of its occurring within the near future."[69] Finally, the Commission stated that a utility should be required to file a rate case within a reasonable interval after the granting of an AAO, both to preserve the Commission's practical ability to make a disallowance and because, if the event was truly extraordinary, recovery in rates ought not be delayed.[70]

The *Sibley* Commission considered and rejected other factors raised by Staff and by the Company. Thus, whether or not the utility was earning at or above its authorized rate of return at the time of the deferral was not relevant.[71] Also irrelevant were the prudency of the expenditures and the goals of rate stability, avoidance of rate case expense, mitigation of regulatory lag, and maintaining the financial integrity of the utility.[72] The Commission also rejected the position taken by the Public Counsel, who urged the Commission to adopt a standard similar to that used to determine requests for interim rate relief.[73] "Public Counsel recommends that the Commission only allow deferral of costs associated with acts of God or when the integrity of the service to customers is threatened."[74] The Commission rejected this proposal as "too restrictive."[75]

3. AAOs Since *Sibley:*

Since it issued the *Sibley* decision in 1991, the Commission has generally used the standard announced therein when analyzing AAO requests. For example, when two

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[69] *Id.*

[70] *Id.*

[71] *Id.*

[72] *Id.*, at 206-207. Notice that the Commission's rejection of these purposes is directly contrary to the weight of the academic authorities quoted earlier.

[73] *Id.*, at 204.

[74] *Id.*, at 207.

[75] *Id.*, at 208.

divisions of Aquila, Inc., sought to defer uncollectibles associated with compliance with the Commission's Cold Weather Rule, the Commission stated:[76]

> The test that the Commission has used, and continues to use here, for determining whether or not to grant an AAO is whether the expense to be deferred is extraordinary and not recurring[.] * * * The Commission's initial inquiry is whether the costs sought to be deferred are indeed extraordinary. If they are not, the inquiry is at an end, and the other questions are moot.

However, the Commission's adherence to *Sibley* has not been unwavering. In several cases, particularly those resolved by stipulations and agreements, the Commission has instead resorted to a "not detrimental to the public interest" standard.[77] Thus, in approving an AAO for costs related to storm damage, the Commission stated: "Since the parties are all in agreement that KCPL should be granted an accounting authority order, and are in agreement as to the conditions that should attach to the granting of the authority, the Commission concludes that granting it will not be detrimental to the public interest."[78] In a pair of post-*Sibley* cases, the Commission granted deferral on the basis that the requests were "reasonable."[79]

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[76] *In the Matter of Missouri Public Service and St. Joseph Light & Power, Divisions of UtiliCorp United, Inc.,* 11 Mo.P.S.C.3d 600, 602-3 (November 14, 2002). The requested AAO was denied on the ground that uncollectibles are a normal cost of doing business.

[77] By contrast, elsewhere the Commission has applied the *Sibley* standard in cases resolved by stipulation and agreement. *See In the Matter of Laclede Gas Co.,* 3 Mo.P.S.C.3d 135, 138 (August 22, 1994).

[78] *In the Matter of Kansas City Power & Light Co.,* 11 Mo.P.S.C.3d 419 (July 30, 2002); *and see In the Matter of Missouri Gas Energy,* 11 Mo.P.S.C.3d 317 (June 13, 2002); *In the Matter of UtiliCorp United, Inc.,* 11 Mo.P.S.C.3d 78 (January 10, 2002).

[79] *In the Matter of Missouri Gas Energy,* 3 Mo.P.S.C.3d 201 (September 28, 1994). The deferral requests were (1) costs and expenditures related to gas safety projects undertaken pursuant to the Commission's pipeline repair and replacement rules, and (2) to book as regulatory assets certain regulatory assets acquired from Western Resources upon purchase of its system. *See also In the Matter of Missouri Gas Energy,* 3 Mo.P.S.C.3d 203, 205-6 (September 28, 1994): "The Commission finds the current proposal to be a reasonable and prudent mechanism."

The cases in which the Commission has followed *Sibley* are not entirely consistent. One difficult area has involved successive deferral requests for the same project. In the *Sibley* decision, deferral was granted for costs relating to on-going construction and conversion projects, which had been previously deferred, simply because they had been previously deferred: "The Commission finds that it would be unreasonable to deny deferral of the remainder of the costs associated with this project. The Commission has already found the [life extension] project to be an extraordinary event by allowing deferral of costs associated with the project in Case No. EO-90-114."[80] Elsewhere, the Commission stated: "The Commission also found the coal conversion project to be an extraordinary event in Case No. EO-90-114. . . . Both projects were treated together and both were found to be extraordinary. The Commission is of the opinion it should not now reverse its prior decision[.]"[81] By contrast, when St. Louis County Water Company sought a third AAO with respect to infrastructure replacement costs, the Commission denied the request, stating:

> The record makes it abundantly clear that the Commission should not grant the requested third AAO for infrastructure replacement because the circumstances are recurring, not nonrecurring. The Company has presented ample evidence as to the magnitude of the infrastructure replacement undertaking in terms of cost. However, the record also shows that infrastructure replacement will necessarily continue for years as a series of successive projects. This is not an appropriate case for an AAO.[82]

Another difficult area has been predictability. The Commission permitted the deferral of costs related to upgrading computers for Y2K compliance, stating that "[a]lthough a finding that an event was unpredictable might support the conclusion that the event was

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[80] 1 Mo.P.S.C.3d at 209.

[81] *Id.*, at 210.

[82] *In the Matter of St. Louis County Water Co.*, 10 Mo.P.S.C.3d 56, 68 (February 13, 2001).

extraordinary, an event can be extraordinary even though it was predictable and foreseeable."[83] Previously, however, the Commission had denied the deferral of costs resulting from a mandatory change in accounting methods on the grounds that "UWM's lack of foresight . . . does not justify the issuance of an Accounting Authority Order."[84]

In one case, that has not been followed since, the Commission added a new element to the *Sibley* test:[85]

> However, the simple fact that an expense is extraordinary and nonrecurring is not enough to justify the deferral of that expense. Implicit in the Commission's previous orders regarding requests for AAOs is a requirement that there must be some reason why the expense to be deferred could not be immediately included for recovery in a rate case.

In other cases, the Commission has refused to add to the *Sibley* test. Thus, the Commission has stated that the grant of an AAO need not be supported either by a finding that irreparable harm would result were the AAO not granted or by a finding of materiality.[86] The Commission has reaffirmed that ordinary business expenses are not proper subjects for AAOs.[87]

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[83] *In the Matter of Missouri Gas Energy,* 9 Mo.P.S.C.3d 37, 39 (March 2, 2000).

[84] *In the Matter of United Water Missouri, Inc.,* 8 Mo.P.S.C.3d 124, 128 (April 20, 1999); *see also In the Matter of St. Louis County Water Co.,* 5 Mo.P.S.C.3d 341, 349 (December 31, 1996): "It is also pointed out that the terms 'infrequent, unusual and extraordinary' connote occurrences which are unpredictable in nature."

[85] *In the Matter of St. Joseph Light & Power,* 9 Mo.P.S.C.3d 481, 485 (December 14, 2000). Request to defer purchased power expense resulting from a fire and consequent turbine shutdown denied.

[86] *In the Matter of Missouri Gas Energy,* 9 Mo.P.S.C.3d 37, 39 (irreparable harm), 38 (materiality) (March 2, 2000). For materiality, *see also In the Matter of Missouri Gas Energy,* Case No. GO-99-258 (*Order Regarding Motion to Reject Pleading, Application for Rehearing, and Request for Reconsideration,* issued June 3, 1999), and *Sibley,* 1 Mo.P.S.C.3d at 206.

[87] *In the Matter of Missouri Public Service and St. Joseph Light & Power, Divisions of UtiliCorp United, Inc.,* 11 Mo.P.S.C.3d 600, 602-3 (November 14, 2002), *supra,* No. 76; *In the Matter of St. Louis County Water Co.,* 4 Mo.P.S.C.3d 94, 98 (September 19, 1995).