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March 2, 1987

Mr. Harvey G. Hubbs
Secretary
Missouri Public Service Commission
P. O. Box 360
Jefferson City, Missouri 65102

Re: Case No. AO-87-48

Dear Mr. Hubbs:

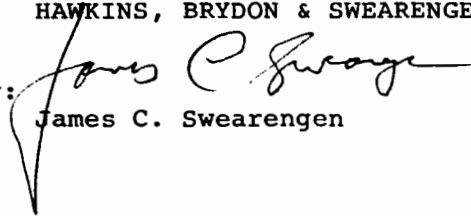
I deliver herewith for filing on behalf of Missouri Public Service Company in the referenced case an original and fourteen (14) copies of Comments in Response to a Missouri Public Service Commission Order Addressing Comments, Granting Interventions and Extending Filing Dates. Copies of this filing have been sent to the parties of record this date.

Thank you for your assistance in this filing.

Very truly yours,

HAWKINS, BRYDON & SWEARENGEN, P.C.

By:


James C. Swearengen

JCS:kh

Enc.

cc: All Parties of Record

FILED
MAR 2 1987
PUBLIC SERVICE COMMISSION

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BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the matter of the)
investigation of the revenue) Case No. A0-87-48
effects upon Missouri Utilities)
of the Tax Reform Act of 1986)

FILED
MAR 2 1987
PUBLIC SERVICE COMMISSION

COMMENTS IN RESPONSE TO A MISSOURI PUBLIC SERVICE
COMMISSION ORDER ADDRESSING COMMENTS, GRANTING
INTERVENTIONS AND EXTENDING FILING DATES

In response to the Commission's Order dated January 30, 1987 in Case No. A0-87-48, Missouri Public Service submits the following comments concerning those factors we believe indicate our rates are not excessive after considering effects of the 1986 Tax Reform Act, as well as our response to Staff's proposals with respect to interim tariffs. This filing does not include calendar year 1986 data. Such information will be provided when it becomes available. The filing is organized into two broad categories addressing legal and theoretical considerations.

LEGAL CONSIDERATIONS

Unconstitutional Taking of Property -

The imposition of interim tariffs, superceding all prior tariffs, providing that charges made and revenues collected thereunder are subject to refund is an unconstitutional taking of property without due process of law. Both the United States and Missouri Constitutions provide that the State may not deprive any

person of property without due process of law. U.S. Const. Amend. XIV; Mo. Const. Art. I, § 10. This principal is applicable to the regulation of public utilities by the State. See, State ex rel. Southwestern Bell Telephone Company v. Public Service Commission, 416 S.W.2d 109 (Mo. 1967). Thus, the Commission is without power to order an act performed or thing done by a public utility if it is tantamount to an appropriation of public utility property.

The suggestions made by Staff with respect to interim tariffs do not withstand constitutional scrutiny. Public utilities in this State have a property interest in money collected from their customers under an established schedule of rates. When the established rate of a utility has been followed, the amounts so collected become the property of the utility, of which it cannot be deprived by either legislation¹ or judicial action without violating the due process provisions of the State and Federal constitutions. Straube v. Bowling Green Gas Co., 227 S.W.2d 666, 671 (Mo. 1950); State ex rel. Barvick v. Public Service Commission, 606 S.W.2d 474, 476 (Mo. App. 1980). The Commission may not redetermine rates already paid without depriving the utility of its property without due process. State ex rel. Utilities Consumers Council of Missouri v. Public Service Commission, 585 S.W.2d 41, 58 (Mo. banc 1979).

¹ In fixing just and reasonable rates, the Commission performs a delegated legislative function. Lightfoot v. City of Springfield, 236 S.W.2d 348, 352 (Mo. 1951).

In Straube, appellants brought an action in equity against respondent, a public utility, to determine the ownership of and recover certain funds received by respondent. One fund represented an amount received by respondent from the Registry of the United States Circuit Court of Appeals of the Eighth Circuit pursuant to its affirmance of a Federal Power Commission rate reduction order. The other fund was an amount representing an alleged excess amount collected by respondent from its customers after the rate reduction order went into effect but prior to the establishment by respondent of an approved revised rate. The Court observed that:

...respondent lawfully came into possession, custody and control of both funds.... Respondent never collected and appellants never paid more than the legally established rate for gas furnished by respondent and appellant's rights were never invaded. (emphasis added).

Id. at 671. The Court held that appellants failed to state a claim upon which relief could be granted. Id. at 672.

The principals articulated in Straube are equally applicable to the present circumstances. Here, as was the case with Bowling Green Gas Company, utilities are collecting revenues pursuant to lawful rates² established by Commission rate fixing orders. Customers are paying no more than the rates that lawfully apply. As such, utilities have a property right in the revenues collected pursuant to those rates. Lightfoot, supra at 353.

² All rates, charges and schedules fixed by the Commission are prima facie lawful and reasonable until found otherwise in a suit brought for that purpose. § 386.270 RSMo 1986.

Either of Staff's interim tariff proposals would radically alter a utility's right to revenues collected pursuant to a Commission rate fixing order. Were the Commission to adopt Staff's proposal, it would be tantamount to a redetermination of rates already paid; an activity clearly held unconstitutional. The Commission may not order refunds of revenues collected based on an after-the-fact determination of reasonableness. Neither may it employ the fiction of an "interim tariff subject to refund," in order to confiscate indirectly what it could not confiscate directly. Furthermore, Staff's proposal is constitutionally deficient whether or not a rate adjustment is subsequently implemented and a refund ordered. If all or a part of the revenues collected pursuant to tariff are made subject to refund, a utility's property interest has been diminished. In short, it has something substantially less valuable than it had before.³

Despite this undeniable deprivation, Staff suggests that the Commission summarily order an industry wide implementation of interim tariffs superceding all prior tariffs. Staff's suggestion, by its terms, does not contemplate the taking of evidence, the opportunity to be heard or the opportunity to cross examine witnesses prior to the issuance of the Commission's order. It is

³ To use an analogy from real property law, a fee simple subject to condition subsequent is a lesser estate than a fee simple absolute.

difficult to imagine a more arbitrary recommendation or one more devoid of the most rudimentary trappings of due process.⁴

For all the foregoing reasons, Staff's interim tariff proposal is constitutionally defective. The Commission should decline to adopt the proposal because it would constitute an act in excess of jurisdiction.

Lack of Statutory Authority -

The Commission does not have the statutory authority to order public utilities to adopt interim tariffs superceding all prior tariffs which make certain revenues collected subject to refund upon the occurrence of a subsequent event. It is axiomatic that the Commission is an administrative agency and, as such, it has only those powers conferred by statute either expressly, or by clear implication as necessary to carry out the express grant. UCCM, supra. at 49; State ex rel. City of West Plains v. Public Service Commission, 310 S.W.2d 925, 928 (Mo. banc 1958). Although the Public Service Commission law should be liberally construed,

"neither convenience, expediency or necessity are proper matters for consideration in the determination of" whether or not an act of the Commission is authorized by statute. (citations omitted).

UCCM, at 49.

⁴ Due process, by Staff's own admission, is either a standard "file and suspend" rate request or a formal complaint proceeding, either determination being based on all relevant factors. Staff Comments, January 9, 1987, at page 2.

As acknowledged by the Office of the Public Counsel and Staff, only two procedures are available to the Commission for the purpose of adjusting rates to be charged by public utilities. State ex rel. Jackson County v. Public Service Commission, 532 S.W.2d 20 (Mo. banc 1975). First, a utility may file revised tariffs incorporating proposed increases or decreases in the charge made for a particular service. The Commission may allow the rate to go into effect by declining to take action within thirty (30) days of the filing or it may suspend the effectiveness of the new rates pending a hearing on the lawfulness or reasonableness of the proposed charges. § 393.140(11) RSMo 1986; § 393.150 RSMo 1986; § 392.230 RSMo 1986. This procedure is commonly known as a "file and suspend" method. Conversely, the Commission may of its own motion initiate a complaint alleging that the rates charged by a utility are unlawful or unreasonable. § 386.390 RSMo 1986. Rates may be revised after a hearing which examine all relevant factors. § 392.240 RSMo 1986; § 393.150 RSMo 1986.

The specificity of the provisions that articulate the procedures to be followed in either a file and suspend rate case or a formal complaint negate the possibility that procedural alternatives exist for the adjustment of rates. Where the statutes prescribe a manner in which proceedings before the Commission are to be initiated, that procedure must be followed. State ex rel. Laclede, supra. at 568. Neither do the statutory provisions giving the Commission general supervisory power over public utilities (i.e. § 393.130 RSMo 1986) give the Commission authority to change the ratemaking scheme created by the legislature. UCCM at 56. The

Staff correctly concluded that: "the only procedural alternative available to address the effects of the TRA is to file complaints..." Staff Comments, January 9, 1987 at page 2.

The Court in State ex rel. Laclede, found that the file and suspend statute contained express language of grant empowering the Commission to adopt an abbreviated rate increase procedure, to wit:

The Commission for good cause shown may allow changes [in rates] without requiring the thirty days notice under such conditions as it may prescribe.

§ 393.140(11) RSMo 1986. The Court observed that:

The "file and suspend" provisions of the statutory sections quoted above [§ 393.140(11) and § 393.150] lead inexorably to the conclusion that the Commission does have discretionary power to allow rates to go into effect immediately...

535 S.W.2d at 566. The Court concluded that the Commission had the authority to order interim rate increases as a necessary incident to its express delegation of power.

We hold that the Commission has the power in a proper case to grant interim rate increases within the broad discretion implied from the Missouri file and suspend statutes and from the practical requirement of utility regulation. (Emphasis added).

Id. at 567.

State ex rel. Laclede is to be distinguished from the instant circumstances in which the Commission is restricted to formal complaint procedures to effect rate adjustments that it may deem appropriate. As such, the statutory language with respect to file and suspend general rate cases is not applicable, that is, the good cause shown exception to the file and suspend procedure does not apply. No such express grant of authority for the use of an expedited procedure can be found in those statutes specifying the

procedure for formal complaints. There being no express grant, there can be no implied power to order the implementation of interim tariffs.

It is apparent from the foregoing that the Commission is not authorized to order utilities to supercede all prior tariffs with interim tariffs pending the determination of company-specific formal complaints. Neither the instant generic investigatory docket nor anticipated formal complaint cases may serve as the host for interim relief. Thus, as a matter of law, the Commission is not empowered to adopt the Staff's proposals.

THEORETICAL CONSIDERATIONS

Isolation of Singular Cost Factor -

The Staff has indicated that voluntary tariff filings should be made by each company affected by this Docket or complaint proceedings will be filed by the Staff for each affected company. Unfortunately, this indication leaves the impression that existing rates of all companies are considered either unlawful or unreasonable as a direct result of one single issue, that being tax reform. Such a presumption requires the conclusion that not only does the Tax Reform Act significantly affect the returns of all utilities, but those returns are so greatly affected as to necessitate a rate adjustment, irrespective of the numerous variations in other factors impacting the Company's return. While this conclusion may be appropriate for some utilities under the jurisdiction of the Missouri Public Service Commission, examination of data indicates that it is not applicable for Missouri Public Service.

As was indicated in Missouri Public Service's December 1986 filing, the maximum estimated first year effect on divisional electric jurisdictional net operating income was an increase of only about 1.1 million dollars. Gas net operating income was actually decreased \$100,000 due to tax reform. These changes are relatively minor in comparison to a number of variances in other items, both increases and decreases, which have occurred since the last full rate proceeding. It is the culmination of all revenue and cost factors, not one in isolation, which must be considered in determining a level of reasonable and equitable rates. This fact has been well established through consistent past Commission use of an annualized test year where all items are normalized. Application of procedures which isolate only one factor would not be appropriate for setting rates or determining an amount subject to refund.

Offsetting Impacts -

In its Order the Commission has required companies to detail cost increases and other factors which offset the impacts of the Tax Reform Act. Because costs are not static (a fact upon which the ratemaking process is generally predicated), a comprehensive list of all cost variances is not practicable. In an effort to provide a meaningful comparison, however, the table below presents the dollar and percentage change on a functional classification basis between the test year revenue and cost levels on which current rates were based and actual twelve month to date amounts through November 30, 1986.

ELECTRIC JURISDICTIONAL

	<u>Increase (Decrease)</u>	<u>% Change</u>
Revenues (1)	21,834	13.5%
Fuel and purchased power	1,045	2.0
Other generating expenses	(4,858)	(41.0)
Transmission	1,236	69.8
Distribution	3,733	68.8
General	8,476	75.0
Depreciation and amortization	1,754	13.8
Other taxes	1,322	9.2
Income taxes	<u>11,203</u>	<u>73.6</u>
Change in net operating income	<u>\$(2,077)</u>	<u>(6.4)%</u>

(1) Includes the tax effected and annualized result of the 1986 rate reduction

There are several significant facts which should be derived from the above table. First, even after reflecting the estimated effects of the Tax Reform Act, annualized net operating income has declined from its level at the time of the utility's last rate proceeding. Secondly, normal operating conditions can and have affected the computation of income tax expense to a far greater extent than has tax reform. Finally, numerous significant individual fluctuations have occurred since 1983 without having been singled out for separate rate consideration as is currently proposed for the Tax Reform Act.

Weather, for example, is a factor totally outside the control of the Company but with far reaching ramifications. Likewise customer growth, fuel costs, payroll changes, plant efficiencies

and many other items are much more significant elements in the causation of earnings fluctuations than is tax reform. In the past, utilities have been guaranteed only an opportunity to earn a reasonable return; with the exception of the now eliminated fuel adjustment clause none of the individual cost items established in rate proceedings were "trued-up." Entering into an era where the achievement of perfect symmetry between costs and rates is attempted is impractical and should not begin with the segregation of tax reform effects.

Effective Current Monitoring -

The Commission has in place an effective method for monitoring and dealing with the combined results of all items impacting the maintenance of reasonable rates. Monthly surveillance reports detailing costs and returns are filed by each utility and monitored by the PSC staff. A significant change in net operating results would be reflected on these monthly reports and investigated by the Staff accordingly. Likewise, if the effects of the Tax Reform Act were so substantial as to significantly affect a company's earnings, that fact would be reflected in the company's monthly surveillance report. This result will not occur in regard to Missouri Public Service because the effects of tax reform are not significant in relation to other cost factor deviations. For example, the estimated \$1.1 million electric jurisdictional effect if new tax legislation had been in effect during 1985 would have represented an increase in electric net operating income of only three percent. Gas net operating income would have decreased over eight percent. Therefore, we do

not believe a tariff filing is in order for Missouri Public Service; however we do endorse the Staff proposal to meet individually with companies to gain a full understanding of the effects of the Tax Reform Act appropriate.

As an example of the operation of the review procedure currently in place, Missouri Public Service reduced its electric jurisdictional rates \$10 million on an annual basis effective September 15, 1986. This decrease was the ultimate result of a Staff review following monthly filings which indicated the utility was earning in excess of its authorized returns. The Company is also aware that the Staff has conducted evaluations of other companies earnings wherein existing rates were reviewed and either proposed to be reduced or left intact.

In the context of Missouri Public Service's rate reduction, no attempts were made to isolate any specific areas of cost causation and implement rate reductions for those specific items only. Rather all elements of cost of service were considered. Furthermore, prior to agreeing to the final stipulated level of rate reduction, Missouri Public Service considered carefully the likelihood of tax reform effects. Missouri Public Service would not have agreed, without a full hearing, to the stipulated reduction in rates had it not been cognizant of estimated short-term tax reform benefits. Therefore, to the extent it is possible to isolate one cost factor, and appropriate to do so, Missouri Public Service has certainly done so in its electric jurisdictional rates, as reflected by the rate decrease of September 15, 1986. This fact is further supported by our December

1986 filing estimating that, using 1985 as a base year and had the tax reform act and the rate reduction been in effect, the utility would not have achieved its authorized return in the initial year of the tax law and likely not in subsequent years.

Other Considerations -

Missouri Public Service is faced with the unique situation of having agreed not to increase rates before September 1988. This action served to provide what was believed to be an appropriate price signal to our customers of stable rates. Effects of tax reform are already reflected in rates. Current rate levels are not excessive. If a rate reduction should ensue it would be shortly followed, in all likelihood, by a comparable increase due to the declining net benefits of the Tax Reform Act in future years and increased financing demands as discussed in our December 1986 filing. Such a "yo-yo" effect would be detrimental to the interests of ratepayers.

There are items which will in the near future increase Missouri Public Service's cost of service. For example, at the request of the Commission Staff following Case Number ER 83-40, Missouri Public Service employed outside consultants to determine an appropriate depreciation level. The results of this study indicated a revenue requirement increase of between three and seven million dollars would be necessary to reflect appropriate depreciation rates in the utility's cost of service. While the possible range of effect can be debated by various parties, there is little question that the negative impact on earnings will be more substantial than the initial benefits of tax reform.

Furthermore, the Staff's suggestion is inequitable because tariffs would be established subject to refund effective July 1, 1987 if they are later found to be excessive. However, no provision is apparently made to implement increased rates retroactive to July 1 if in the subsequent rate proceeding tariffs are determined to be below an authorized return level. It is assumed that the Staff proposes to simply retain established rates superseded only by the tariff statement that revenues are subject to refund, rather than allowing utilities to establish new rate levels either higher or lower than those currently in effect. The inequity is demonstrated by the Staff's example wherein a company whose rates were found to be excessive by \$500,000 retroactive to July 1 would be required to refund that amount. However, if the company had rates in place which were found to result in underearnings of \$500,000, it would not be allowed to instigate new retroactive rates.

Consider, for example, the gas operations of Missouri Public Service. Monthly surveillance reports have indicated that current rate levels are well below those necessary to achieve an authorized level of return. Further, the Tax Reform Act is expected to have a detrimental effect on gas earnings. The Company is precluded from increasing its gas rates prior to the conclusion of a full rate proceeding perhaps eleven months hence; however, the Staff's proposal introduces the possibility that both gas and electric rates could be reduced retroactive to July 1.

Finally, the Staff's proposal that all revenues be considered subject to refund could have other detrimental financial effects.

The quality of earnings would decline due to the added uncertainty. In formulating their opinion, the independent auditors would be required to consider the possible effects and disclosure would be required by the Company in preparing financial statements, which could in turn create difficulties when the Company required outside financing.

Summary -

In summary, Missouri Public Service makes the following comments:

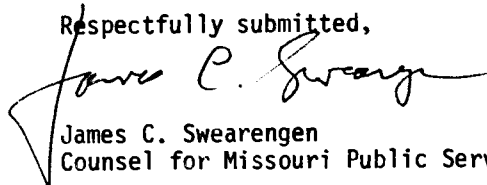
- 1) The interim tariff proposal is an unconstitutional confiscation of property without due process of law.
- 2) The Commission is not empowered to order public utilities to adopt the interim tariff proposal.
- 3) Isolation of one cost item such as the Tax Reform Act, especially when it is not relatively significant in comparison to other cost variances, is not justified. The utility has been affected by many other cost items which have far greater economic impacts than tax reform, without special consideration by the Commission.
- 4) The estimated effect on earnings of the Tax Reform Act, along with other factors, was considered and included by Missouri Public Service in the context of reducing its rates effective September 15, 1986.
- 5) Current earnings on an annualized level are below the authorized return and may continue to decline

subsequent to the implementation of the 1986 Tax Reform Act.

- 6) The Commission has in place a mechanism which is operating effectively to monitor and reduce rates should they become excessive and implement any rate change on a relatively accelerated basis. There is no reason to deviate from a system which is working.
- 7) The utility is precluded by the terms of its stipulation from requesting rate relief for items which may offset the benefits derived from the Tax Reform Act.
- 8) Current depreciation rates are substantially low and if corrected would have a much more significant effect on earnings than would the Tax Reform Act.
- 9) A system which would reduce rates or make revenues subject to refund because of only one cost factor is inequitable unless the utility is afforded the same opportunity to retroactively recover underearnings at the same effective date as the possible reduction/refund.
- 10) Staff's proposals could result in a "yo-yo" effect on rates with immediate reductions followed shortly by rate increases. Such a procedure provides the ratepayer with improper pricing signals.
- 11) Revenues subject to refund raise a cloud of doubt as to the viability of the Company's financial statements and make required financings more difficult.

Missouri Public Service proposes that it be relieved from further requirements as a result of Docket A0-87-48, following its filing of 1986 Tax Reform Act related information. Earnings compared to twelve months earlier have been declining since the institution of a rate reduction in September 1986. This trend is expected to continue. Effects of the Tax Reform Act were considered by the Company in establishment of current tariffs and are not sufficient to return the utility to a condition of excessive earnings. The current monitoring procedure has been operating effectively. If in the future the trend reverses and normalized annual earnings have increased to an excessive level, then it would be appropriate to institute a proceeding designed to investigate and lower rates.

Respectfully submitted,



James C. Swearengen
Counsel for Missouri Public Service



Dennis R. Williams
Director of Rates and Economic Analysis
Missouri Public Service