BEFORE THE MISSOURI PUBLIC SERVICE COMMISSION

In the Matter of a Working Case to Consider the Establishment of a Rate Stabilization Mechanism to Reduce the Need for Frequent Rate Case Filings	))))	Case No. AW-2013-0110

INITIAL COMMENTS OF THE MISSOURI ENERGY DEVELOPMENT ASSOCIATION

The Missouri Energy Development Association (MEDA) is a trade association comprised of the largest, investor-owned and rate regulated public utilities doing business in the State of Missouri. MEDA's purpose is to develop, organize, and promote measures that will advance the ability of investor-owned utilities to build, maintain, protect, and provide the utility infrastructure and services that are critical to the economic well being of all Missourians. MEDA member companies serve a combined total of over 3.8 million customers in Missouri, employ more than 11,500 people, and contribute millions of dollars and thousands of hours in helping others in their communities. On September 20, 2012, the Commission issued an order opening an investigation into the establishment of a rate stabilization mechanism to reduce the need for frequent rate case filings for investor-owned utilities.[1] That order invited suggested solutions to the perceived problem of frequent rate case filings by investor-owned utilities.

MEDA welcomes the Commission's initiative and looks forward to engaging in a dialogue with interested persons that may lead to improvements in the rate case process for all regulated utilities so as to address the perception that rate increase requests are too frequently made. The operational environment across the country has changed, and Missouri should be proactive in addressing why frequent rate cases are occurring in order to adequately plan for the

[1] The order specifically refers to Ameren Missouri, Kansas City Power & Light, KCP&L Greater Missouri Operations Company and The Empire District Electric Company.

future. Customer growth has slowed, new infrastructure is needed, environmental standards are increasingly stringent, renewable energy mandates are driving additional investment requirements, fuel prices are volatile, and there has been no shortage recently of natural disasters which have required rebuilding of damaged facilities and/or limiting the availability generation resources. That being said, MEDA believes there is sufficient flexibility within the existing regulatory structure for the Commission to address the primary drivers of utility rate cases, with the most critical principle being the pursuit of reforms that result in a better, more accurate and timelier matching of rates and actual costs.

Return on Equity (ROE) Determinations

The Commission's September 20th order has invited comment concerning a mechanism employed in New York that utilizes a range of reasonable ROE awards from which the utility may choose depending on whether it commits to not file a rate increase for a specified period of time. MEDA appreciates the Commission's efforts to consider new mechanisms for addressing the regulatory costs and burdens associated with the need for utilities to file frequent rate cases as a result of escalating costs due to environmental mandates, required infrastructure investments and other factors. If properly designed, with a robust and truly competitive ROE range, such a mechanism could be a helpful tool in permitting utilities to defer rate relief for some period of time. To have a significant impact on the frequency of rate case filings, however, MEDA submits that such a mechanism can and should be accompanied by other measures that allow for a better matching of permanent rates and actual costs.

Reducing Regulatory Lag

An extensive regulatory lag of up to eleven (11) months to complete a rate case, combined with an historical test year, is a key driver of regular rate case filings particularly in an era of increasing costs.[2] Until such costs are reflected in rates, a utility under-recovers these increased costs, receives no return on the additional capital investment and its assets depreciate with no recovery of associated depreciation expense even though those assets are being used to provide service. Regulatory lag thus decreases cash flows, increases financing costs and, importantly, erodes earnings on investments that are necessary to provide service. Historically, utilities could expect that additional revenues derived from increased sales would cover much of this shortfall, but this is no longer the case. Today's environment is one characterized as having slower rates of customer growth and slower growth in (or even reduced) usage per customer.

Matching rates more accurately with the underlying costs of providing service in a timely fashion is the single, best tool available to the Commission to control the number of rate case filings. MEDA has sponsored legislation, and worked with the Commission, in the past to make the rate case process more efficient in order to provide permanent rates that are reflective of the actual cost of providing service and thus address the pernicious impact of a structural underearnings problem. The objective of those legislative efforts was to shorten modestly the period of time of suspension while retaining the ability of the Commission's staff to perform a thorough audit.[3]

In addition to shortening the period of suspension, the Commission can employ the use of a temporary rate or rate base adjustment that would enable utilities and customers to be fully compensated for any amounts they have incurred and under collected during the period between the time the rates go into effect and the ending date of the most recent update or trued-up period

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[2] Regulatory lag is by no means the only drag on a utility's earnings. Since most utilities must invest in their systems at a level much greater than their existing assets depreciate, they consistently and systematically lose money.

[3] MEDA has previously observed that the seven states surrounding Missouri average just over nine (9) months to process a litigated case.

in that case. This provides a completely symmetrical approach which embodies the same principles of fairness, restitution and "equal justice for all" that made it possible to enact the same kind of reforms at the appellate level through Senate Bill 48, which was signed into law in 2011. The Commission could further address the problem of regulatory lag by improving the update or true-up process by extending the period nearer to the date new permanent rates will go into effect and, also, by expanding the scope of cost items that are subject to an update or true-up.

The Commission should reconsider its policies concerning when to permit utilities to implement interim rates to reflect some or all of the increases in costs through the pendency of a rate case. Interim rates can be made subject to refund thus safeguarding the public interest of just and reasonable rates. This mechanism is another tool that can be used to better match utility rates to the actual cost to provide service and, therefore, alleviate the problem of persistent under-earnings.

Construction Accounting

An aging infrastructure and increasingly stringent environmental regulations are necessitating significant expenditures by utilities to improve and modernize utility plant. These significant capital expenditure requirements, many of which are not revenue producing, are key rate case drivers. The Commission should consider authorizing construction accounting for ratemaking purposes. Construction accounting has been used for major capital assets for many years in Missouri. It allows a utility to accrue carrying costs on its investment and to defer depreciation on an asset from the asset's in-service date until the time when the investment is reflected in rates. This approach is not entirely new. MEDA contends that it is a viable mechanism to apply to all capital investments between rate cases. Were the Commission to adopt construction accounting for all capital investment between rate cases (or at least that portion that exceeds the associated depreciation expense), the time period between the investment and the return on the investment would be eliminated thus alleviating underearnings due to plant additions which occur between cases.

Ratemaking Considerations

The Commission should also consider a more robust use of ratemaking tools which better match rates with underlying costs within the existing legal framework. There are many possibilities.

One mechanism gaining broader support by state public utility commissions is the cost tracker. This allows a utility to defer its actual costs for a specialized function as a regulatory asset or liability such that they can be considered in a subsequent general rate case. Because they are symmetrical in operation, cost trackers are fair to the utility and its customers; however, trackers can still result in significant cash regulatory lag for the utility.

The Commission should continue to examine rate design proposals which provide for the recovery of capital costs in a manner that reduces the incentive for more frequent rate case filings. A broader use of revenue decoupling rate designs, such as those currently in effect for a number of the state's natural gas utilities, can stabilize earnings and cash flow. They have the additional benefit of moderating seasonal bill fluctuations experienced by consumers.

Other ratemaking tools including the use of formula rates and forward-looking (i.e. budgeted) test years have been implemented to reduce regulatory lag. The states of Arkansas, Illinois, Oklahoma, and Tennessee all utilize proven practices to address regulatory lag that are not incorporated in Missouri.[4]

Other mechanisms that permit utilities to use a portion of the revenues achieved through sales to off-system customers to pay for a portion of the increased costs incurred to serve customers between rate cases or to retain for a longer period of time a share of the savings or other efficiencies achieved by the utility between rate cases should also be considered.

Alternative Rate Mechanisms

MEDA encourages the Commission to remain open to considering alternative ratemaking proposals which can provide an incentive for utilities not to file for rate cases for a designated period of time. In the mid-1990s, the Commission approved an agreement that provided an earnings sharing mechanism for Union Electric Company whereby it made refunds to customers based on by how much the company's achieved earnings exceeded its authorized return on equity.[5] Properly structured, similar proposals can provide for stable rates for a specified timeframe thus providing certainty that benefits regulators, consumers and utilities alike.

Infrastructure Replacement Surcharge (ISRS)

The ISRS mechanisms available for natural gas and water utilities have worked well. These mechanisms have successfully enhanced the ability of such utilities to contemporaneously recover certain capital expenditures and they have moderated the need to file rate cases more often than required by law to maintain the efficacy of the surcharge mechanism. A similar mechanism for electric utilities would moderate the need for rate case filings. Extending the three year rebasing requirement to four or even five years and expanding the scope of availability of the water ISRS also should be considered. Unlike the other topics identified in these comments, these changes would require enabling and remedial legislation.

[4] Source: Edison Electric Institute, "Innovative Regulation: A Survey of Remedies for Regulatory Lag," April 2011

[5] Case No. ER-95-411.

<u>Rate Stabilization Practices/Policies in other States</u>

As noted above, the Commission has referenced a New York plan as the inspiration for commencing the dialogue in this case. That solitary example should not limit the scope of matters considered by the Commission. When assessing ways to reduce rate case frequency, it is important to recognize and analyze mechanisms utilized in other states around the country; especially those right next door. A number of other state regulatory agencies have in place a variety of ratemaking frameworks, the objective(s) of which is to stabilize utility rates. In that regard, MEDA provides the following overview of several ratemaking alternatives currently being utilized that are proving to be of value to all parties involved.

- **<u>Electric Utilities</u>**
  - Rate Impact Mitigation Measures[6]
    - Rate Cap Expiration Plans—AZ, **<u>IL</u>**, MD, PA, VA
    - Adjusting the Timing of Rate Increases—ID, MN, NC, NM, NV, NY, **<u>OK</u>**, SC, TX, VA, WI
    - Securitization Cases—FL, MD, MS, TX, WV
    - Rate Design Changes—CT, **<u>IL</u>**
    - Negotiated Mitigation Plans—**<u>IL</u>**, MD, VA
  - Rate Impact and Regulatory Lag Mitigation Measures[7]
    - Capex Cost Tracker—**<u>AR</u>**, CA, CO, FL, GA, HI, IN, IA, **<u>KS</u>**, **<u>KY</u>**, LA, ME, MA, MN, MS, NJ, NY, OH, **<u>OK</u>**, OR, PA, TX, VT, VA
    - CWIP in Rate Base—CO, FL, GA, IN, LA, MD, MN, MS, NC, SC, TX,

[6] Source: Edison Electric Institute, "State Regulatory Update: Rate Impact Mitigation Measures," June 2010
[7] Source: Edison Electric Institute, "Innovative Regulation: A Survey of Remedies for Regulatory Lag," April 2011

VA, WV, WI

    - Multiyear Rate or Revenue Cap—CA, GA, HI, ME, MA, NY, OH, VT
    - Revenue Decoupling—CA, CO, CT, DC, HI, ID, IN, **KY**, MD, MA, MI, MS, MT, NV, NC, OH, **OK**, OR, SC, VT, WI, WY
    - Retail Formula Rate Plans—AL, **IL**, MS
    - Forward Test Years—AL, CA, CT, FL, GA, HI, **IL**, **KY**, ME, MI, MN, MS, NY, ND, OR, RI, **TN**, UT, WI, WY

- **Gas Utilities**[8]
  - Rate Stabilization Tariffs—AL, GA, LA, MS, **OK**, SC, TX
    - 14 Companies, 6 Million Residential Customers
  - Revenue Decoupling—**AR**, AZ, CA, **IL**, IN, MA, MD, MI, MN, NC, NJ, NV, NY, OR, RI, **TN**, UT, VA, WA, WI, WY
    - 48 Companies, 30 Million Residential Customers
  - Innovative Bad Debt Cost Recovery—CO, CT, DC, **IL**, IN, **KS**, **KY**, MA, MD, ME, MI, NC, NE, NH, NV, NY, OH, **OK**, RI, SC, **TN**, TX, UT, VA, WI, VA
    - 61 Companies, 25 Million Residential Customers
  - Infrastructure Cost Recovery—AL, **AR**, CO, FL, GA, IN, **KS**, **KY**, MA, MI, **MO**, NH, NJ, OH, OR, RI, TX, UT, VA
    - 44 Companies, 20 Million Residential Customers

- **Water Utilities**[9]
  - Distribution System Investment Charge (Non-Revenue-Producing Infrastructure

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[8] Source: American Gas Association, "Innovative Rates, Non-Volumetric Rates, and Tracking Mechanisms: Current List," September 2012

[9] Source: National Association of Water Companies, www.nawc.org/state-utility-regulation/regulatory-practices/defalt.aspx, 11/5/12

Replacement)—CA, CT, DE, **<u>IL</u>**, IN, **<u>MO</u>**, NH, NJ, NY, OH, PA

- Future Test Year—**<u>AR</u>**, CA, CO, FL, HI, **<u>IL</u>**, **<u>KS</u>**, **<u>KY</u>**, NE, NM, NY, OH, PA, **<u>TN</u>**, UT, VA, WI,
- Water Rate Decoupling Mechanisms—CA, NY
- Rate Consolidation (Single-Tariff Pricing)—AZ, CA, CO, CT, DE, FL, ID, **<u>IL</u>**, IN, **<u>KS</u>**, **<u>KY</u>**, LA, MA, MS, **<u>MO</u>**, MT, NH, NJ, NM, NY, NC, OH, OR, PA, SC, TX, WA, WV

<u>Conclusion</u>

MEDA welcomes a dialogue to address mechanisms that will lengthen the time between rate case filings. MEDA's member companies are well aware of the negative public perception associated with frequent rate case filings. Lessening the frequency of such filings would alleviate customer anxiety and, also, reduce regulatory costs and burdens on the Commission, utilities and customers. The key to success in any such undertaking is to put in place a ratemaking process that ensures that permanent rates are reflective of the actual cost of providing service. MEDA submits that in addition to the ROE mechanism highlighted by the Commission, there are many other tools available to the Commission to achieve this objective within the existing regulatory framework. Legislative action to improve and expand upon the successful ISRS model also should be considered.

Respectfully submitted,

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