BEFORE THE PUBLIC SERVICE COMMISSION
STATE OF MISSOURI

In the Matter of the Application of Missouri Gas Energy for the Issuance of an Accounting Order Relating to Its Natural Gas Operations and for a Contingent Waiver of the Notice Requirement of 4 CSR 240-4 020 (2).	)))))	**Case No. GU-2011-0392**

STAFF'S INITIAL BRIEF

Respectfully submitted,

Robert S. Berlin, MBN 51709
Senior Counsel

Sarah L. Kliethermes, MBN 60024
Senior Counsel

Goldie Tompkins, MBN 58759
Legal Counsel

Attorneys for the Staff of the
Missouri Public Service Commission
P. O. Box 360
Jefferson City, MO 65102
(573) 751-6726 (Telephone)
(573) 751-9285 (Fax)
sarah.kliethermes@psc.mo.gov

December 23, 2011

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Introduction

In response to the destruction caused by the tornado which struck Missouri Gas Energy's (MGE) Joplin service area on May 22, 2011, the Company has devoted significant resources to the replacement and repair of its infrastructure used to serve its Joplin residential and commercial customers.

Because of MGE's significant loss of infrastructure from the tornado, MGE has applied to the Commission for an Accounting Authority Order (AAO).

An AAO is an accounting mechanism that allows the Company to defer its costs and expenses incurred from the tornado. As described below, an AAO permits deferral of costs from one period to another. Deferred cost items are booked as a regulatory asset rather than as an expense, thus improving the financial outlook of the utility during the deferral period by allowing the regulatory asset to be amortized to expense. Another benefit of the AAO is that it allows the utility the opportunity to seek recovery of the expenses deferred under the AAO in a future rate case proceeding. Because the accounting treatment moves expenses from one period to another for purposes of considering in future rate cases, utility commissions are advised by prevailing case law to grant AAOs sparingly.

The damage and resulting expenses caused by the Joplin tornado are worthy of an AAO because of their extraordinary and unusual nature. It has been a long-standing practice of this Commission to allow deferral of out-of-pocket costs incurred by utilities to repair damages and restore service to customers following an "Act of God," as such unexpected and nonrecurring costs are not normally included in the ratemaking process. This practice allows the utility to seek rate recognition of the extraordinary repair and restoration costs in its next rate proceeding.

MGE did a good job repairing and replacing the damaged portions of its Joplin distribution system so that MGE may safely resume service to its residential and commercial customers affected by the tornado. In support of that, the Staff recommends that the Commission approve MGE's AAO for the operations and maintenance expenses and associated capital costs related to repairing and restoring its gas distribution system.

At issue here is whether MGE should also be granted an AAO for deferring the revenues that MGE asserts that it lost from Joplin customers that dropped off MGE's system after the tornado. MGE is seeking deferral authority for its quantification of the reduction to its Joplin-area revenue stream ("lost revenues") resulting from some level of customers who were unable to receive service after Joplin's tornado. Staff asserts that any deferral of lost revenues related to Joplin's tornado is improper. MGE's quantification, among other things, wrongly includes customers that dropped off before Joplin's tornado and after the tornado who have since reconnected to the system. Further at issue are: what is the proper amortization period for the AAO and when should the amortization period begin.

Executive Summary

Staff summarizes its positions and rationale on the above issues as follows, but offers the Commission a more detailed explanation and discussion of support for its positions in the main body of its brief.

First, Staff recommends the Commission not grant AAO deferral authority for any reduction to its Joplin-area revenue stream that MGE claims have resulted from Joplin's tornado. The record evidence shows that even MGE's quantification of the alleged reduction to MGE's revenues from its Joplin-area revenue stream is de minimus and of negligible impact

compared to the normal amount of MGE's total annual revenues. MGE's quantification of the reduction to its Joplin-area revenues stream is not accurate because MGE overlooks the critical facts, including recognition that some customers were dropping off the system prior to the tornado, and that customers lost after the tornado have returned and are still returning to the system - only a period of months after the tornado as a result of Joplin's rebuild effort.

Further, the possible granting of deferral authority for lost revenues invokes a major policy consideration. The Commission should not grant AAO deferral for lost revenues on policy grounds that it is not appropriate to look, in isolation, at a single reduction to MGE's revenues at this time for collection from future MGE ratepayers, particularly in light of the fact that MGE continues to collect revenues sufficient to meet its costs of operation and generate some level of profit for its shareholders. This Commission has never before used an AAO to guarantee a defined level of profit, nor has any other state commission allowed an AAO for deferral of similarly unearned profits to be included in the eventual setting of utility rates. The evidence adduced from pre-filed and live testimony offers no compelling policy reason or justification for this Commission to grant MGE deferral authority for reduced customer revenues. If the Commission should do so against the recommendation of Staff and Public Counsel, then it would become the first commission to ever grant deferral authority for lost revenue from customer charges for utility services not provided.

As explained and discussed in detail in the body of this brief, the impact from the reduction to MGE's Joplin-area customer levels has only a negligible effect on MGE's revenues, and does not support a Commission grant of deferral authority. This de minimus reduction to MGE's revenue stream, particularly in light of the fact that MGE continues to collect revenues

sufficient to meet its costs of operation and generate some level of profit for its shareholders, does not rise to the level of convincing Staff that Missouri should be the first utility commission in the United States to depart from the policy that has so well served all other utility commissions faced with catastrophic weather events.

Further addressed below is Staff's support for a ten (10) year amortization period for deferred O&M and capital related tornado costs. Because over 80% of costs incurred in replacement and repair of MGE's distribution system are capital related, these costs should be amortized over a ten year period. Also, Staff supports starting the amortization of deferred costs on January 1, 2012, because this approach begins recognition of these costs for financial reporting purposes a reasonable length of time following the events that gave rise to the costs.

Background:

For the Commission to determine whether it should authorize MGE to defer to Account 182.3, Other Regulatory Assets, its loss of expected revenues related to the May 22, 2011, tornado, including carrying charges equal to its ongoing Allowance for Funds Used During Construction rates, the Commission must consider:

(I) has MGE met its burden with regard to the *Sibley* test (if applicable here) and the USOA?

(II) has MGE met its burden with regard to the USOA requirement of probable recovery?

(III) has MGE requested relief in such a way that the Commission can reasonably prescribe the accounting authority necessary to order such relief?

(IV) has MGE met its burden in asserting that relief is not only possible, but is a worthy exercise of Commission discretion?

(V) does MGE have a right to a certain level of revenue or profit?

and

(VI) should MGE be guaranteed a defined level of revenue or profit?

A Commission finding that MGE has failed any one of these items requires denial of MGE's request for Commission authority to defer purported lost revenues, more accurately described as unearned profits. However, the ultimate question underlying these issues, as well as an important question in is its own right is the simple question: Should MGE be guaranteed a defined level of revenue?

If this Commission does not intend to guarantee a set level of revenue in MGE's next rate case, it is not appropriate for the Commission to grant such deferral authority now. It is important that this Commission take steps to ensure the accurate financial reporting of utilities under its jurisdiction. The accuracy of a utility's financial statements matter; it is not appropriate to mislead investors with inaccurate information by propping up earnings in one period with no intent to allow recovery in a future period. Reporting standards are set by Commission rule adopting the FERC Uniform System of Accounts (USOA). The USOA defaults to booking revenues and losses in the period incurred. That is why the Commission's granting of deferral authority is discretionary. That is why the Commission should not authorize MGE's request to begin the process of dollar-for-dollar recovery of unearned profits associated with Joplin's tornado.

Even if the Commission should desire to guarantee MGE's ability to earn an awarded ROE - as opposed to simply providing MGE the *opportunity* to earn a reasonable return on investment as required by law - MGE has not presented a workable way to do so in this case.

MGE's requested deferral quantification is inaccurate, and if, ordered as requested, the resulting deferral would exceed the actual reduction to its Joplin-area revenue stream that MGE has experienced. Thus the Commission could not simply use MGE's language in granting

deferral authority. The USOA requires probable recovery as a condition precedent to deferral. Whatever decision this Commission might make about guaranteeing a level of revenue, Staff cannot believe it probable that MGE would be given recovery in a future period of excess deferrals related to foregone profits applicable to a past period. The quantification of the relief requested in MGE's application would result in a deferral in excess of any reasonable quantification of MGE's actual tornado-related revenue losses. This is why quantification of the reduction to Joplin-area revenues is important, and this is why precise language is necessary in any order authorizing MGE accounting authority to defer any reduction to Joplin-area revenues associated with Joplin's tornado.

While the proper vehicle to ensure a utility's opportunity to earn a fair return on its investment is the function of a rate case and not of an AAO, MGE has not alleged that it is not earning a reasonable return on its investment. In point of fact, MGE repeatedly testified that its earned ROE is irrelevant to this request. It is not appropriate to look at a single source of revenue or expense in isolation to determine whether such an opportunity is present – that falls under the ambit of a rate case. Rate cases consider annualized and normalized values, and it is a virtual certainty that no particular value used in a rate case will exactly match a particular expense or revenue that is booked during any particular period. In considering MGE's proposal to defer "lost revenues," the Commission should not assume that MGE is earning less than its authorized ROE at this time due to the tornado or for any other reason – MGE certainly has not made this claim.[1], [2], [3], [4], [5], [6]

[1] Trans. p 115 L 17 – 21.
[2] Trans. p 117 L 2 – p 118 L 25.
[3] Trans. p 122 L 18 – 21.

To accept MGE's argument that failing to authorize inclusion of "lost revenues" in an AAO would deny it of an opportunity to earn its authorized ROE, the Commission would have to be willing to engage in single issue ratemaking. Unlike the remediation and reconstruction expenses related to Joplin's tornado, even determining the effect of Joplin's tornado on MGE's revenue requirement would require consideration of all relevant factors. A rate case, not an AAO, is the proper place to address potential changes in revenues. Unlike an AAO, a rate case considers all relevant factors. Recovery in rates of an AAO that focused only on MGE's revenues while necessarily ignoring other factors such as other revenue increases or reductions in expense would be an exercise in single-issue ratemaking. MGE's reluctance to file a rate case, and its belief expressed in testimony that any attempt to resolve any revenue shortfall through a rate case will fail, do not justify that relief is required through an AAO. MGE's testimony simply shows that no relief is required or justified.

MGE's Application properly seeks an AAO for O&M expense and capital costs of system repair but overreaches in seeking deferral authority for reduction to its Joplin-area revenues stream.

MGE has applied for the authority to make certain accounting entries to record on its financial books a regulatory asset set equal in value to their actual O&M expenditures, as well as associated depreciation and carrying charges on tornado-related capital additions, associated with the restoration of service following Joplin's May 22, 2011, tornado ("Joplin's tornado"). Recording this regulatory asset, deferring it altogether for some amount of time, and then amortizing the asset to expense over time, has the effect of moving the expense out of the period in which it occurred, and into one or more subsequent periods.

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[4] Trans. p 122, L 22 – 25.
[5] Trans. p 123, L 1 – 4.
[6] Trans. p 143 L 1 – 6.

MGE has also applied for additional accounting authority to defer a quantification of reduction to its Joplin-area revenues. MGE's request to defer a quantification of its reduction to its revenue stream is not consistent with accounting conventions under the USOA. Therefore identifying the deficiencies associated with each aspect of MGE's request is necessarily tedious.

I. Application of "Extraordinary" Standard of *Sibley* and the USOA:

The granting of an AAO is a discretionary exercise. Governing accounting rules as well as Commission practice, including cases reviewed by Missouri's courts, set out a two prong test regarding grants of deferral authority:

> 1. Events occurring during a period that are extraordinary, unusual and unique, and not recurring; and
>
> 2. The costs associated with the material event are material.

Instruction 7 of the FERC USOA "Extraordinary Items" provides:

> **It is the intent that net income shall reflect all items of profit and loss during the period** with the exception of prior period adjustments as described in paragraph 7.1 and long-term debt as described in paragraph 17 below. **Those items related to the effects of events and transactions which have occurred during the current period and which are of unusual nature and infrequent occurrence shall be considered extraordinary items. Accordingly, they will be events and transactions of significant effect which are abnormal and significantly different from the ordinary and typical activities of the company, and which would not reasonably be expected to recur in the forseeable future.** (In determining significance, items should be considered individually and not in the aggregate. However, the effects of a series of related transactions arising from a single specific and identifiable event or plan of action should be considered in the aggregate. To be considered as extraordinary under the above guidelines, an item should be more than approximately 5 percent of income, computed before extraordinary items. Commission approval must be obtained to treat an item of less than 5 percent, as extraordinary. (See accounts 434 and 435.) [7]

[7] Staff Exhibit 5.

(**emphasis added**)

In its *Report and Order* in Case Nos. EO-91-358 and EO-91-360, cases filed by Missouri Public Service, a division of UtiliCorp United, Inc. (now KCP&L Greater Missouri Operations Company) ("*Sibley*"), the Commission stated its criterion for deferral of **costs** incurred outside a rate case test year. In *Sibley*, the Commission stated that it would consider the appropriateness of granting an AAO on a case by case basis. In doing so, it would approve an AAO for events that it found to be "extraordinary, unusual and unique, and not recurring."[8] The Commission has stated that "the primary focus is on the uniqueness of the event either through its occurrence or its size,"[9] implying separate consideration of the materiality or significance of the item. The reference in *Sibley* to both "occurrence" and "size" requires the Commission's consideration of the USOA's explicit statement of the materiality standard.[10]

The Commission has consistently applied a "materiality" standard since *Sibley*. In *The Matter of the Application of Missouri Gas Energy, a division of Southern Union Company, for an Accounting Authority Order Concerning Environmental Compliance Activities* L 5351369, 2 -6 (Mo.P.S.C.2008), the Commission applied the Sibley test, analyzed the requirements of the USOA, and in denying MGE the accounting authority requested, distilled its analysis to the following factors: for an item to be considered 'extraordinary' it must: (1) be of unusual nature; (2) be of infrequent occurrence; (3) be of significant effect; (4) be abnormal and significantly

[8] *In the Matter of the Application of Missouri Public Service for the Issuance of an Accounting Order Relating to its Electrical Operations. In the Matter of the Application of Missouri Public Service for the Issuance of an Accounting Order Relating to its Purchase Power Commitments.* 1 MPSC 3d 200, 205 (1991).

[9] *See In re Missouri-American Water Co.,* 2002 WL 1425379, Mo.P.S.C., 2002, citing *In the Matter of Missouri Public Service*, Case No. EO-91-358 (*Report & Order*, iss'd December 20, 1991) at 12.

[10] Trans. p 210 L 23 – p 211 L 8.

different from the ordinary and typical activities of the company; and (5) not reasonably be expected to recur in the foreseeable future.[11] The Commission analyzed the materiality of the cost under its consideration of both "unusual nature" and "significant effect".[12]

In an Aquila request for accounting authority related to a 2007 ice storm, the Commission relied on the relative materiality of the cost to repair Aquila's distribution systems in its determination of whether the storm was "extraordinary."

> The Commission concludes that the damage to Aquila's property in the L&P service area as a result of the December 2007 storms squarely fits the "Sibley" standard. An ice storm is unusual, unique and not recurring. In the L&P service area, it was also extraordinary due to the cost of $4.5 million that Aquila must bear in light of the storm damage. However, the cost of $250,000 associated with the damage in Aquila's MPS service area is not extraordinary. The Commission will therefore grant Aquila's request with regard to its L&P service area but will not grant Aquila's request with regard to the MPS service area.[13]

Revenues aren't Expenses and Profit isn't a Cost

In Staff's view, *Sibley* does not provide any support for MGE's requested deferral of "lost revenues," and the Commission must carefully consider any expansion of AAOs beyond deferral of utility expenditures to guarantee utility profit opportunities. In support of its request to defer its quantification of "lost revenues," MGE argues that the *Sibley* test essentially only requires a finding that an event was extraordinary in nature. If so, then in MGE's reasoning approval to defer all financial impacts of the extraordinary event should automatically be

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[11] *In the Matter of the Application of Missouri Gas Energy, a division of Southern Union Company, for an Accounting Authority Order Concerning Environmental Compliance Activities* L 5351369, 2 -3 (Mo.P.S.C.2008).

[12] *In the Matter of the Application of Missouri Gas Energy, a division of Southern Union Company, for an Accounting Authority Order Concerning Environmental Compliance Activities* L 5351369, 4 -5 (Mo.P.S.C.2008).

[13] *In the Matter of the Application of Aquila, Inc., for the Issuance of an Accounting Authority Order Relating to its Electrical Operations* (Mo.P.S.C).

granted, with any other issues involving the deferred financial impacts put off for a subsequent rate proceeding. However, in *Sibley* Missouri Public Service did not seek to defer any amount of alleged lost revenues; it sought deferral authority for O&M expenses and capital related costs associated with major construction projects – equivalent to the types of costs for which Staff is recommending deferral authority in this proceeding. Therefore, *Sibley* wasn't about profits, *Sibley* was about costs. Profits are not costs.[14]

There are big differences between deferral of profits and deferral of expenses.[15] Among other concerns, deferral of a revenue stream requires a tax-gross up, which makes any eventual recovery much more onerous for customers compared to recovery of deferred O&M expenses and capital related costs.[16] This is because, if rate recovery is allowed for lost revenue deferrals, customers will have to reimburse the company not only for lost revenues but also the additional income taxes charged to the company because of that additional income.[17]

MGE has inaccurately portrayed the impact of customers dropping off its system following the tornado as causing it to fail to recover its "fixed costs." This claim is based upon the practice under MGE's current "straight fixed-variable" rate design of aggregating all components of its cost of service (other than purchased gas costs) into the fixed monthly customer charge. Under MGE's unique definition, MGE's profit (return on equity) level included in customer rates is referred to as a "fixed cost." In contrast to any claim that MGE is failing to recover its "fixed costs" due to the tornado, Mr. Oligschlaeger in his rebuttal testimony provided uncontroverted evidence that MGE is not only recovering all of its costs

[14] Trans. p 211 L 11 – 21.
[15] Trans. p 212 L 8 – 17.
[16] Trans. p 212 L 8 – 20.
[17] Trans. p 212 L 8 – 20.

from its revenues collected after the tornado struck, but is earning a positive level of profit.[18], [19] As a consequence, Mr. Oligschlaeger stated any reduction in revenues collected from customers following the tornado represents only a reduction in ROE from what MGE might have earned absent the tornado. Therefore, MGE's requested deferral of its quantification of the reduction to its Joplin-area revenue stream more accurately represents an attempt to defer a reduction in profit margins due to the tornado, and certainly would not constitute a deferral of "fixed costs."

MGE's tortured claim that a utility's profit is a fixed cost controverts established regulatory accounting and financial accounting conventions.[20],[21] While Mr. Noack admits profit is not a cost under the USOA, [22] and contends that MGE follows the USOA,[23] MGE ignores the USOA definition of "cost." Paragraph 9 of the USOA states that "[c]ost means the amount of money actually paid for property or services…."[24] MGE admits that its definition of "cost" is not consistent with the USOA.[25] Again, choosing to call MGE's profit a "cost" simply cannot change fundamental accounting and ratemaking reality.

Even if the Commission *wanted* to give MGE the authority to defer an amount equal to the customer charges not collected from a small number of affected customers for some amount of time, it would be difficult for the Commission to craft such an order. MGE's requested deferral of O&M and capital-related costs can be reasonably quantified and is

[18] Staff Exhibit 2, Oligschlaeger Rebuttal, pp 7 - 8.
[19] Trans. p 122 L 18 -21.
[20] Trans. p 123 L 24 – p 124 L 3.
[21] Trans. p 142 L 17 - 25.
[22] Trans. p 163 L 18 – p 164 L 2.
[23] Trans. p 160 L 20 – 24.
[24] Trans. p 126 L 7 – 13.
[25] Trans. p 164 L 7 – 13.

supported by Staff. The accounts associated with these concepts can be found on a general ledger and traced to the tornado or cause of incurrence. However, "lost revenues" are not easily quantifiable and thus cannot be accurately deferred.[26]

MGE is the applicant and movant. The burden rests on MGE to persuade this Commission that the prerequisites of the *Sibley* test and the USOA are met, and that its request is a reasonable exercise of Commission discretion.[27] MGE has not met its burden. MGE has failed to provide reasonable evidence or argument to meet its burden. Further, MGE has provided no credible evidence or compelling argument for the Commission to extend *Sibley* to allow the deferral of lost revenues as opposed to extraordinary costs permitted under *Sibley*.

Materiality

MGE oscillates between whether it wants the Commission to look at its revenue stream or at the cost of service used for setting rates in its last rate case in considering the materiality of MGE's lost revenues deferral. MGE also directs the Commission's attention to Joplin in isolation because it suits MGE's argument to not consider the impact of the tornado on MGE's total revenues and the remainder of MGE's system. Staff contends it is appropriate to look at MGE's system as a whole, and not Joplin in isolation.

Staff does not deny that Joplin's tornado was an extraordinary event for Joplin. Staff agrees that the O&M costs MGE expended and continues to expend are extraordinary. However, MGE's request begs the question, *what level of materiality is necessary to consider an AAO?*

[26] Trans. p 213 L 7 – p 214 L 16.

[27] *State ex rel. GS Technologies Operating Co., Inc. v. Public Service Com'n of State of Mo*. 116 S.W.3d 680, 693 (Mo.App. W.D.,2003, citing *State ex rel. Tel–Central of Jefferson City, Inc. v. Pub. Serv. Comm'n,* 806 S.W.2d 432, 435 (Mo.App.1991).

Determining what is or is not material in a particular case is an exercise of the Commission's discretion. Staff submits that even giving the doubt to MGE's favor, the reduction to MGE's revenue stream is not material, and the impact on MGE's ability to meet fixed costs is not only non-material, it is non-existent. If the Commission decides to use materiality as an element of the requested relief, then MGE's failure to demonstrate materiality requires denial of that relief. Even if the Commission views materiality as only a consideration, the negligible effect of Joplin's tornado on MGE's revenue stream is so immaterial that relief is not only unnecessary, it is also inappropriate.

MGE's estimated that as a result of Joplin's tornado it failed to receive monthly customer charges from .62% of its Missouri customers.[28] MGE's high end estimate of lost revenues is only $1.167 million.[29] Mr. Noack admitted he doesn't know what the actual reduction to MGE's Joplin customer level is, and that this calculation is only an estimate, and that lost revenues are hard to estimate.[30], [31], [32], [33], [34], [35] Staff has presented evidence that MGE's estimate is inflated, and when adjusted is no greater than $648,000.[36] But even that calculation assumes a full year of customer loss at a level of 100%, and that all of MGE's asserted customer loss is due to the tornado (both assumptions are demonstrably untrue). The Staff's adjusted lost revenues are approximately .341% of Missouri budgeted 2011 net

[28] Trans. p 128 L 14 – 18.
[29] Applicant Exhibit 1, Noack Direct, p 10, L 1 – 3.
[30] Trans. p 170 L 9 – 15.
[31] Trans. p 140 L 18 – 21.
[32] Trans. p 148 L 23 – p 150 L 6.
[33] Trans. p 165 L 4 – 9.
[34] Trans. p 175 L 25 – p 176 L 12.
[35] Trans. p 165 L 4 – 9.
[36] Staff Exhibit 2, Oligschlaeger Rebuttal, pp 15 – 17.

revenues, again assuming a full year of 100% customer loss.[37] As compared to the net income amount reflected in MGE's last general rate case (Case No. GR-2009-0355), MGE's unadjusted quantification of alleged lost revenue impact is approximately 4.7% of net income.[38] With Staff's adjustments, that figure is reduced to approximately 2.6%. Thus, MGE's failure to collect certain revenues is not material or significant for purposes of both USOA instruction 7 and under the *Sibley* standard.

Further, because MGE's revenues meet its expenses and MGE is earning a positive ROE, MGE is not failing to recover its fixed costs. MGE admits that its revenues exceed its expenses.[39] MGE admits that its revenues exceed its expenses even without O&M deferral.[40] MGE admits that its ROE is positive, and deferral of O&M will make it more positive.[41], [42]

MGE's revenues continue to exceed its fixed costs and continue to earn a positive return on equity. Thus, MGE's allegation that it is failing to collect revenues to recover its fixed costs is without merit. Considered under the standards of MGE's own arguments for deferral, the dollar value of MGE's fixed costs not being recovered is $0. There can be no contention that $0 is material or significant for purposes of USOA instruction 7, or the *Sibley* standard.

Finally, OPC presented evidence at hearing that in a prior recent time period, all else being equal, MGE was overearning in an amount greater than the revenues they allege to have

[37] Trans. p 131 L 17 – 22; Staff Exhibit 2, Oligschlaeger Rebuttal, p 16.
[38] OPC Exhibit 1, Lafferty Rebuttal, p 18; Applicant Exhibit 2, Noack Surrebuttal, p 13..
[39] Trans. p 122, L 18 – 21.
[40] Trans. p 122 L 22 – 25.
[41] Trans. p 123 L 1 – 4.
[42] Trans. p 143 L 1 – 6.

subsequently lost due to the tornado.[43] MGE did not apply for an AAO for those apparent overearnings.[44]

The Commission has consistently, whether implicitly or explicitly, considered the materiality of the costs to be deferred in determining whether to grant deferral authority. However, the evidence of this case points toward rejection of MGE's request even under the truncated standard expressed by MGE's counsel at hearing, which would have the Commission totally ignore the materiality requirement. As the party asserting this issue, MGE carries the burden of showing that lost revenues or lost fixed cost recovery are material or significant.[45] MGE has not carried that burden. Therefore, the Commission must conclude that MGE's lost revenues are not of significant effect. Certainly, the Commission should not go against its prior practices and those of all public utility commissions to allow a deferral of lost revenues based upon the immaterial and insubstantial level of loss incurred by MGE in this instance.

II. The USOA Requires a "Probable Recovery" Standard and MGE has not met it.

Concerning Account 182.3 Other regulatory assets, the USOA provides that:

> A. This account shall include the amounts of regulatory-created assets, not includible in other accounts, resulting from the ratemaking actions of regulatory agencies. (*See* Definition No. 30.)
>
> B. The amounts included in this account are to be established by those charges which would have been included in net income, or accumulated other comprehensive income, determinations in the current period under the general requirements of the Uniform System of Accounts **but for it being probable that**

[43] Trans. p 154 L 14 – p155 L 2.
[44] Trans. p 155 L 10 – 12.
[45] *State ex rel. GS Technologies Operating Co., Inc. v. Public Service Commission*, 116 S.W.3d 680 (Mo. App. 2003); *In the Matter of the Application of Missouri Gas Energy, a division of Southern Union Company, for an Accounting Authority Order Concerning Environmental Compliance Activities* L 5351369, 5 (Mo.P.S.C.2008).

such items will be included in a different period(s) for purposes of developing rates that the utility is authorized to charge for its utility services….
(emphasis added)

Thus, even if the Commission determines that MGE meets the *Sibley* test, and Instruction 7 of the USOA, the Commission must decide whether recovery of the deferred amount is probable. As discussed below, and for the reasons that follow in points III – VI, Staff contends that recovery is not probable.

On the simplest level, MGE has not offered a reasonable quantification or method to defer lost revenues or unearned profits. To allow MGE to defer costs according to an unseen and unproven quantification approach would greatly increase the risk of arguments in subsequent rate cases concerning the amounts to be allowed recovery, if they are allowed recovery at all.

MGE assumes that any granted AAO will ultimately be recovered in rates.[46] MGE concedes that they could file a rate case seeking to include the effects of the tornado.[47] However, Mr. Noack admitted that he does not believe MGE would succeed in recovering lost revenues in a rate case.[48], [49] Mr. Noack concedes that the reason for this failure to recover the impacts of the tornado in rate case would be because the tornado was non recurring.[50] Thus, MGE asserts that an AAO is necessary here because any future attempt by MGE to recover for the reduction to MGE's Joplin-area revenue stream (or diminished profits) in a rate case would be unsuccessful.

[46] Trans. p 171 L 5 – 14.
[47] Trans. p 143 L 12 – 20.
[48] Trans. p 143 L 12 – 20.
[49] Trans. p 144 L 1 – 7.
[50] Trans. p 178 L 14 – p 179 L 12.

Staff asserts that the same concerns underlying MGE's contention that it would be unsuccessful in a rate case also reflect the probability that ultimate recovery of any deferred unearned profits would be unsuccessful, and thus not probable. More importantly, however, the ample case law discussed below indicates that MGE's request for latter-period recovery of an earlier period's reduction to revenues (or unearned profits) is unlawful, inappropriate, and certainly not required by the Federal Constitution or any other authority. Thus, since the case law facially requires denial of MGE's ultimate recovery of any deferred amount of "lost revenues," such recovery is not probable, per se.

III. The Commission cannot reasonably prescribe the accounting authority requested.

Narrowly viewed, MGE has applied for the authority to make certain accounting entries to record on its financial books a regulatory asset set equal in value to the monthly customer charges of affected customers, multiplied by the number of customers affected by Joplin's tornado. If it were possible to create **an accurate quantification** of the reduction to MGE's Joplin-area revenue stream to be recorded as a regulatory asset, deferred altogether for some amount of time, and then amortized to expense over time, these transactions would have the following effect: converting the difference between the desired revenue level and the actual revenue level in the current period, to an item of expense in one or more future periods.

By MGE's admission, its current revenues exceed the calculation of fixed costs from its last general rate case, and MGE is making a profit. So narrowly viewed, MGE is requesting that this Commission give it the authority to deviate from the normal rules of USOA accounting to

allow MGE to record additional revenues as profit in the current time period to be treated as an expense in a future rate case.

When viewed as defined in MGE's Application, MGE seeks the authority to make certain accounting entries to record on its financial books a regulatory asset in an amount – all else being equal – that would show MGE's booked revenues to exceed what they would have been absent Joplin's tornado. This is because MGE's Application relies on an inaccurate quantification of the reduction to its Joplin-area revenues. Since MGE's current revenues exceed its fixed costs and MGE is making a profit, MGE's request would allow it to record a level of profit in the current time period to be treated as an expense in a future rate case, in excess of the profit it would have otherwise earned in the present time period.

Thus, even if the Commission wanted to entertain MGE's request, MGE has not provided the information necessary for the Commission to do so. If this Commission ignores Staff's recommendations and decides in favor of granting MGE the authority to defer a quantification of the reduction to its Joplin-area revenues stream, it is imperative that any such order granting MGE authority to deviate from the normal accounting standards prescribed by the USOA must carefully prescribe the boundaries of that accounting authority.

MGE concedes that the customer numbers underlying its request do not tell the whole story. Mr. Noack testified his $1.167 calculation is an estimate, and he testified that the customer count that he used is a "placeholder."[51], [52], [53], [54] While MGE concedes that "lost

[51] Trans. p 140 L 18 – 21.
[52] Trans. p 148 L 23 – p 150 L 6.
[53] Trans. p 165 L 4 – 9.
[54] Trans. p 175 L 25 – p 176 L 12.

revenues" are hard to estimate,[55] and that MGE does not know what level of customer loss is actually attributable to Joplin's tornado at a particular point in time, [56] MGE ignores the fact that any accounting authority order would have to carefully prescribe the authority granted.[57] MGE also fails to address how a loosely-defined deferral would survive external auditor scrutiny.[58]

Errors in MGE's calculation of lost customers and application void its request for authority to defer lost revenues from lost customer charges.

The most obvious problem, even to a non-accountant, with MGE's request is its failure to take into account the return of customers to its system, both throughout its Joplin-area service territory, and also over time. According to Mr. Noack's testimony at hearing, MGE's Data Request response that indicated the return or relocation of 1,900 Joplin area customers subsequent to the tornado is "not reliable for ratemaking."[59] However, this data request response, and Mr. Noack's testimony concerning it at the hearing, are more than sufficiently reliable to thoroughly impeach MGE's proposed quantification of its alleged lost revenues.

Throughout this case it has been clear that MGE is ignoring Joplin's rapid rate of progress and regrowth.[60] MGE has not prepared estimates of how many customers are going to rebuild in the Joplin area.[61] MGE ignores the fact that only 6 months after the tornado nearly half of the homes destroyed by Joplin's tornado are under repair or reconstruction.[62] MGE did not

[55] Trans. p 165 L 4 – 9.
[56] Trans. p 170 L 9 – 15.
[57] Trans. p 213 L 7 – p 214 L 16.
[58] Trans. p 214 L 17 – p 215 L 9.
[59] Trans. p 179 L 16 – 21.
[60] Trans. p 135 L 10 – p 136 L 7.
[61] Trans. p 173 L 23 – 25.
[62] Trans. p 203 L 3 – 16.

account for the customer loss that predated Joplin's tornado in its initial estimate, [63] and MGE has failed to refine that estimate, acknowledging that customers are returning,[64] or taking service elsewhere on system.[65]

Furthermore, MGE's calculation does not reflect the reduction in income tax expense that occurs when a company's revenues decrease. ROE is taxable to business entities. All other things being equal, a reduction in utility revenues will result in a decrease to its ROE, and any reduction to ROE will lead to lower taxes payable to state and federal taxing authorities. In general, a reduction of a dollar in revenue for a utility results in an offsetting reduction of approximately $0.38 to the utility's income tax expense. MGE has totally ignored the offsetting benefit to income tax expense in its quantification of the financial impact of the tornado in its Schedule 3 attached to Mr. Noack's direct testimony. Stated another way, by including the reduction in income tax expense associated with lower revenue levels, MGE's quantification of annual lost revenues from the tornado would decrease from $1.167 million to approximately $720,000. [66]

MGE's quantification of the lost revenue impact on its earnings (in Schedule 3 attached to Mr. Noack's direct testimony) improperly assumes that all of the costs represented in the current monthly customer charge under the "straight fixed variable" rate design are "fixed" costs that do not vary with a reduction in the number of customers. MGE's assumption is not accurate. For example, in response to a Staff Data Request, MGE identified a relatively small amount of costs associated with billing of its customers (postage, envelopes, etc.) that it is not

[63] Trans. p 146 L 24 – p 147 L 3.
[64] Trans. p 147 L 10 – 17.
[65] Trans. p 215 L 19 –p 216 L 13.
[66] Staff Exhibit 2 ,Oligschlaeger Rebuttal, p 15.

presently incurring for customers who left the Company's system following the tornado. MGE's quantification of these costs on a monthly basis is approximately 41.4 cents per customer (MGE Response to Staff Data Request No. 22), or approximately $16,000 on an annual basis.

Correcting for the Company's failure to account for the income tax implications of lost revenues and variable costs associated with the number of customers served results in a calculation of $704,000.[67]

MGE's quantification of the lost revenues impact of the tornado *also includes the loss of customers clearly not associated with the tornado*. Schedule 3, attached to MGE witness Noack's direct testimony, clearly shows that the Company's Joplin area service territory experienced a loss of 169 customers from April 2010 to April 2011, prior to the tornado occurring in May of 2011. Yet, by comparing a September 2010 vs. September 2011 customer count, MGE's quantification of its "lost fixed cost recovery" due to the tornado does not exclude this pre-tornado customer loss impact. Also, MGE Schedule 3 shows a declining level of customers in both August and September 2011 compared to year-earlier totals, and includes these declines in its lost revenues calculation.[68]

Correction of these obvious errors results in annual lost revenues of $648,000. But even that calculation wrongly assumes a full year of customer loss at a level of 100%, and thereby still overstates MGE's actual revenue loss due to the tornado. The morning of the hearing, Staff received MGE's response to a data request that indicated that 1,900 of those displaced by Joplin's tornado had returned to MGE's system by October 31, 2011.[69] While Staff did not have

[67] Staff Exhibit 2 ,Oligschlaeger Rebuttal, p 16.
[68] Staff Exhibit 2 ,Oligschlaeger Rebuttal, p 17.
[69] Staff Exhibit 6.

adequate time to fully analyze the impact of this encouraging new fact on MGE's calculation of unearned profits, it truly is a testament to the people of the Joplin area.

MGE witness Mr. Noack testified that his attempt to quantify what he characterizes as the lost fixed cost component is not accurate in terms of the number of customers from whom MGE alleges it is not collecting its fixed costs. Inflation of that number - if deferral is granted - means that MGE's shareholders would not only be insulated from loss, they would actually see a gain. The accuracy of a utility's financial statement matters and it cannot be ensured with loosely estimated, unverifiable numbers. While incoming expenses and outgoing capital expenditures are easily identified and quantified, no party has been able to develop a reasonably accurate manner of identifying the quantity in a given period of MGE's reduction to its Joplin-area revenues specifically attributable to the tornado that would give MGE sufficient specificity to accurately book them. Even if this Commission makes the decision to defer "lost revenues," effectively guaranteeing MGE's allowed ROE; this means MGE would be booking - all else being equal – lost revenues in excess of actual tornado-related reduction to its Joplin-area revenues. Adoption of MGE's inaccurate method of calculating its profits for purposes of deferral requires that MGE book excess deferrals today, and at the time of its next rate case will either (1) take a loss in the amount of those excess deferrals in a future period, or (2) receive rates in a future period designed to give it recovery of the excess deferrals. To summarize, it is imperative that any deferral of lost revenues authorized by the Commission be based upon a reasonably accurate and reliable quantification of the reduction to revenues to Joplin's tornado. Mr. Noack freely admitted that the quantification approach outlined in his testimony is neither accurate nor reliable in that respect, but promised that a better approach would be

forthcoming sometime in the future. MGE's inability to accurately quantify the reduction in its Joplin-area revenues, ignoring all other arguments against MGE's request, requires rejection of its "lost revenues" deferral.

Should the Commission grant deferral of lost revenues, each of the above issues must be addressed in its order. It should be emphasized again that no utility commission has ever done so, even concerning worse natural disasters than Joplin's tornado.

In the Hurricane Iniki case cited by MGE the utility had sustained damage to over 30 percent of its system. The utility pled facts to justify emergency rate relief. The Hawaii Commission approved a stipulation among the parties that authorized the deferral of lost margins, and ultimately the utility did not get rate recovery of its deferred lost margins because the utility could not prove up the amount. [70]

MGE admits no danger to its provision of Safe and Adequate Service.[71] MGE does not claim to have met Missouri's standard for emergency rate relief, as was the foundation of the Hurrican Iniki case that authorized a deferral by stipulation similar to the deferral of that MGE has requested here.

IV. MGE has not established that guarantee of its unearned profits is a worthy exercise of Commission discretion.

This Commission has said that AAOs should be used sparingly because they can result in ratemaking consideration of items from outside the test year:[72] AAO's necessarily violate the

[70] Trans. p 141 L 15 – p 142 L 10.
[71] Trans. p 127 L 14 – 17.
[72] *see* Missouri American Water Case No. WO-2002-273, referencing *Sibley* at 205, *citing State ex. rel. Union Electric Company v. Public Service Commission,* 765 S.W.2d 618, 622 (Mo. App., W.D. 1988).

matching principle, that expenses should be recovered reasonably close in time from those causing the expense to be incurred. MGE is requesting that future ratepayers not only provide the cost of serving those future ratepayers, but also prop up MGE's earnings in the current time period. MGE has not established any legitimate policy objective for doing so.

Accurate financial reporting informs investors of current period losses and current period revenues. A Commission decision to shield current investors from MGE's actual financial condition should not be taken lightly. If recovery is not granted in a future period, MGE will show today's losses in a future period, passing the cost of Joplin's 2011 tornado onto future ratepayers, stockholders, or both. MGE has not established any legitimate policy objective for shielding today's shareholders from any reduction in profit occasioned by Joplin's tornado.

If MGE needs rate relief, it should file a rate case. If MGE does not believe it would prevail in a rate case, such a belief simply indicates a belief by MGE that it cannot support a request for relief. An AAO does not evaluate all relevant factors because that is not the purpose of an AAO. MGE's reluctance to file a rate case, and MGE's testimony of its certainty that attempts to resolve any revenue shortfall through a rate case will fail, do not prove up that relief is required through an AAO. It indicates that no relief is required. MGE has not established any legitimate policy objective for expanding the use of AAOs in this manner.

The discussions of points V – VI that follow also relate to MGE's failure to establish that its request is a worthy exercise of Commission discretion.

V. MGE does not have the right to a given level of revenue or profit, only the opportunity.

MGE has no right to a return, much less a particular level of return. It is very well established that the law does not require that rates yield any particular return.[73], [74], [75], [76], [77], [78], [79] As stated in a 2006 MGE appeal of a rate case before the Western District, there is no statute, rule, or case supporting that utilities have a property right to a defined level of revenue.[80] MGE simply does not have any sort of right to collect revenues – or defer an amount in lieu of collection of revenues – from any particular customer or set of customers. Thus MGE has no right to a guarantee of a defined level of profit.

This same body of law indicating that MGE has no right to an AAO to guarantee a defined level of profit also implicitly points toward denial of MGE's request. MGE certainly hasn't brought forth any evidence or argument that granting the requested authority is good regulatory practice in absence of any right to a defined stream of revenues from Joplin's tornado victims. There is nothing to suggest that the tragedy of Joplin's tornado marks an appropriate occasion to vary from the foundational regulatory principle that a utility has – between rate cases – only the opportunity to earn the ROE allowed in rates set in the preceding rate case.

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[73] *State ex rel. Capital City Water Co. v. Public Service Commission of Missouri* 252 S.W. 446, 456 (Mo. 1922).
[74] *State ex rel. Missouri Gas Energy v. Public Service Com'n* 186 S.W.3d 376, 383 (Mo.App. W.D.,2005).
[75] *State ex rel. Missouri Office of Public Counsel v. Public Service Com'n of State* 293 S.W.3d 63, 80 -81 (Mo.App. S.D.,2009).
[76] *Straube v. Bowling Green Gas Co*. 360 Mo. 132, 141-142, 227 S.W.2d 666, 670 - 671 (Mo.1950).
[77] *Reinhold v. Fee Fee Trunk Sewer, Inc.* 664 S.W.2d 599, 603 -604 (Mo.App. E.D. 1984).
[78] *Lightfoot v. City of Springfield* 361 Mo. 659, 669, 236 S.W.2d 348, 352 (Mo.1951).
[79] *State ex rel. Missouri Gas Energy v. Public Service Com'n* 210 S.W.3d 330, 334 -335 (Mo.App. W.D.,2006).
[80] State ex rel. Missouri Gas Energy v. Public Service Com'n 210 S.W.3d 330, 334 -335 (Mo.App. W.D.,2006).

MGE's risk of revenue shortfall and diminished profit is a business risk for which shareholders are properly compensated. Missouri courts have held that "it is a well-accepted principle of regulation that common stockholders contribute what is known as 'risk capital' to the utility company for which they receive a compensatory rate of return. Among the uncertainties that common stockholders accept in return for this added compensation is the danger of earnings shortfall, for whatever reason."[81] Further, "risks are part of the utility business and that even the risk of economic catastrophe may be properly assigned to owners of the utility rather than to its customers."[82] This is proper, because if a stockholder could be assured a return of his investment under all circumstances, it would make the investment practically risk-free.[83] Thus, it is not appropriate to guarantee a defined level of profit.

Essentially, case law makes it clear that the Commission is under no obligation to grant an AAO to provide a utility with any level of profit, much less the precise ROE used to set rates in the proceeding general rate case. Further, since shareholders are compensated for the risk of decreased profit, it is inappropriate to guarantee MGE any level of profit through an AAO.

VI. The Commission should not grant deferral authority to guarantee a utility a defined level of revenue or profit.

MGE's shareholders do not have a right to any defined level of revenue or profit. Moreover, the MGE's level of profit even after accounting for the full level of reduction following Joplin's tornado, is still within the zone of reasonableness used in setting rates in

[81] *State ex rel. Union Elec. Co. v. Public Service Com'n of State of Mo.* 765 S.W.2d 618, 622 -623 (Mo.App. W.D. 1988).
[82] *State ex rel. Union Elec. Co. v. Public Service Com'n of State of Mo.* 765 S.W.2d 618, 626 (Mo.App. W.D. 1988).
[83] *State ex rel. Union Elec. Co. v. Public Service Com'n of State of Mo*. 765 S.W.2d 618, 622 -623 (Mo.App. W.D. 1988).

MGE's last case – all else being equal. This analysis ignores customers returning to MGE's system that has occurred and continues to occur, since the tornado.

MGE acknowledges that rates stay the same though investment fluctuates.[84] MGE acknowledges that in the last case, the Commission's zone of reasonableness was 9.1 to 11.11,[85] with an ROE of 10.0% being what the Commission decided to give them an opportunity to earn for purposes of setting rates.[86] MGE, however, at least for purposes of this request views their rates on a granular basis. They believe that rates were set to provide them with a fixed cost of profit of 12% of every dollar collected.[87]

In addition to the general business risk discussed above, MGE's Form 10K specifically mentioned risk of catastrophic tornado.[88] Expert evidence was presented at hearing that acts of god are taken into account in setting ROE,[89] and that investors are compensated for risks equal to the Joplin tornado.[90] Experts further testified that hurricane risk is accounted for in MGE's ROE,[91] and that catastrophic events are included in business risk for which shareholders are compensated.[92] Finally, *Sibley* acknowledges that consideration should be given to whether shareholders were compensated through ROE.[93]

Ratemaking strikes a balance between the risks occasioned by doing business, and the return shareholders have an opportunity to earn on their invested capital. It is not appropriate

[84] Trans. p 181 L 25 – p 182 L 11.
[85] Trans. p 172 L 11 – 14.
[86] Trans. p 173 L 6 – 9.
[87] Trans. p 177 L 21 – 25.
[88] Trans. p 158 L 24 – p 159 L 9.
[89] Trans. p 191 L 14 – 18.
[90] Trans. p 226 L 22 – p 227 L 1.
[91] Trans. p 209 L 17 – 210 L 5.
[92] Trans. p 227 L 7 – 13.
[93] see *Sibley*; Trans. p 198 L 16 – 199 L 10.

for the Commission to reduce that risk without reducing the risk premium received by the shareholders. The proper context for such decisions is not an AAO, which is necessarily limited in scope.

An AAO does not evaluate all relevant factors because that is not the purpose of an AAO. MGE's reluctance to file a rate case, and MGE's testimony of its belief that any attempt by it to resolve any revenue shortfall through a rate case will fail, are not indicators that relief is required through an AAO. They indicate that no relief is required. MGE has not established any legitimate policy objective for extending the application of an AAO in this manner.

Conclusion:

There are many reasons that the Commission should not grant MGE's request at any level. As discussed under section III above, there are many problems with MGE's quantification of the reduction to their Joplin-area revenue stream related to Joplin's tornado. However, setting those deficiencies aside, the facts are such that the Commission can legitimately deny MGE's request on the basis of MGE's failure to meet the *Sibley* and USOA requirements - even if the Commission is willing to extend the applicability of these tests from expenses and costs to revenues and profits.

MGE is the movant, and the burden rests on MGE to persuade this Commission that it has met the prerequisites of the *Sibley* test and the USOA's requirements; and MGE must also demonstrate that the requested relief is appropriate.[94] Even if the Commission should determine that the requirements of the Sibley test and the USOA standards are met, the

[94] *State ex rel. GS Technologies Operating Co., Inc. v. Public Service Com'n of State of Mo.* 116 S.W.3d 680, 693 (Mo.App. W.D.,2003, citing *State ex rel. Tel–Central of Jefferson City, Inc. v. Pub. Serv. Comm'n,* 806 S.W.2d 432, 435 (Mo.App.1991).

Commission has discretion to deny the requested accounting authority. An AAO is neither required nor appropriate for deferral of a quantification of the reduction to MGE's Joplin-area revenues following Joplin's tornado. In short, MGE has no right to a defined level of revenue or profit, and it would be inappropriate for the Commission to grant deferral authority to guarantee MGE a defined level of revenue or profit.

MGE may argue that this analysis is premature. However, it is within the Commission's discretion to reject MGE's request for deferral authority of lost revenues at this time. Not only does MGE have no right to an AAO, but, as discussed above, it is inappropriate to defer an item unless its recovery in a future period is probable. Under the circumstances of MGE's current application, rate recovery of deferred lost revenue amounts definitely cannot be considered "probable."

Length and Start Date

If the Commission grants MGE's requested AAO, Staff recommends that the deferral period for the amortization on any expense related to the AAO be amortized over a period of ten years.[95] MGE has incurred expense related costs and capital related costs due to the tornado.[96] Expense related costs are typically amortized over a period of five years, whereas capital related costs are typically amortized over a twenty year period.[97] Since 83.5% of the costs subject to deferral in this case are capital related, per Michael Noack, MGE's expert, a ten year amortization period is an appropriate period.[98]

[95] Staff Exhibit 3, McMellen Rebuttal, p. 3.
[96] Staff Exhibit 3, McMellen Rebuttal, p. 3.
[97] Staff Exhibit 3, McMellen Rebuttal, p. 3.
[98] OPC Exhibit 1, Lafferty Rebuttal, p. 8, L 17-21.

If an AAO is granted, the Staff recommends that the deferral period begin on January 1, 2012.[99] MGE requests a start date effective with the date of new rates set by the Commission. The problem with MGE's request is that there is no guarantee when MGE will file its next rate case. A start date of January 1, 2012 is more appropriate because it is a guaranteed start date and because it is closer in time to the date of the event.[100] The benefit of the January 1, 2012 start date is that the cost would then be appropriately recognized in MGE's financial reporting, and in addition, it would eliminate the near-certainty tha MGE will over recover these costs in rates if the start date for the amortization coincided with the Company's next rate case).[101]

Recommended Findings of Fact

1. On May 22, 2011, a tornado struck Joplin, Missouri, and the surrounding area, and resulted in tremendous loss of life and property.
2. MGE expended and continues to expend significant amounts in operations and maintenance activities associated with securing its distribution system and restoring service in the Joplin area.
3. Some of those who lost their lives, homes, and businesses in the Joplin were MGE customers.
4. Some properties that sustained such damage that they were not immediately safe for occupation took gas service from MGE.
5. Following the tornado, MGE received monthly customer charges from fewer customers in the Joplin area than MGE had previously received.
6. Prior to the tornado, MGE experienced customer loss in the Joplin area.[102]
7. Since the tornado, MGE has experienced customer growth in the Joplin area as customers rebuild in the tornado area or relocate elsewhere.[103]

[99] Staff Exhibit 3, McMellen Rebuttal, p. 3.
[100] Staff Exhibit 3, McMellen Rebuttal, p. 4.
[101] Staff Exhibit 3, McMellen Rebuttal, pp. 4-5.
[102] Trans. p 175.
[103] Staff Exhibit 6; Trans. p 147.

8. Approximately 1,900 of those displaced by Joplin's tornado returned to MGE's system by October 31, 2011.[104]

9. In spite of MGE receiving monthly customer charges from fewer customers in the Joplin area than MGE had previously received, statewide, MGE is able to meet its fixed costs of operation.[105]

10. In spite of MGE receiving monthly customer charges from fewer customers in the Joplin area than MGE had previously received, statewide, MGE is making a profit in excess of its fixed costs.[106]

11. MGE did not consider whether or not it was currently making a profit to be relevant to its request.[107], [108], [109], [110], [111], [112]

12. MGE filed an application for accounting authority, it has not filed a general rate case.

Recommended Conclusions of Law

1. Missouri Gas Energy is a gas corporation under Missouri law. As a gas corporation, the Commission has jurisdiction over MGE. The Commission further has the jurisdiction "to prescribe by order the accounts in which particular outlays and receipts shall be entered, charged or credited."[113]

2. An AAO allows a utility to defer certain costs for later consideration in a general rate case. The deferral of costs in an AAO does not guarantee the utility a right to ultimately recover the amounts deferred in that future rate case.[114] Rather, the Commission must consider all other relevant factors when determining in the rate case the appropriate rate the utility may charge.[115]

3. As a gas company subject to the Commission's jurisdiction, MGE is required by regulation to keep all its accounts in conformity with the Uniform System of Accounts (USOA) prescribed

[104] Staff Exhibit 6.
[105] Trans. p 122 L 18 – 125.
[106] Trans. p 123 L 1 – 4.
[107] Trans. p 115 L 17 – 21.
[108] Trans. p 117 L 2 – p 118 L 25.
[109] Trans. p 122 L 18 – 21.
[110] Trans. p 122, L 22 – 25.
[111] Trans. p 123, L 1 – 4.
[112] Trans. p 143 L 1 – 6.
[113] See Section 386.020 (18).
[114] *Missouri Gas Energy v. Pub. Serv. Comm'n*, 978 S.W.2d 434 (Mo. App. W.D. 1998).
[115] *Public Counsel v. Pub. Serv. Comm'n*, 858 S.W.2d 806 (Mo. App. W.D. 1993).

by the Federal Energy Regulatory Commission.[116] In general, the USOA requires that a company's net income reflect all items of profit or loss occurring during the period. The USOA, however, recognizes that special accounting treatment, what this Commission refers to as an AAO, may be appropriate when accounting for extraordinary items of profit or loss. The question then becomes, what is an extraordinary item?

4. The USOA indicates that an extraordinary item for which special accounting treatment would be appropriate is ”of unusual nature and infrequent occurrence.”‘ Furthermore, ”they will be events and transactions of significant effect which are abnormal and significantly different from the ordinary and typical activities of the company, and which would not reasonably be expected to recur in the foreseeable future.” In addition, the USOA requires that to be considered extraordinary, the item ”should be more than approximately 5 percent of income, computed before extraordinary items.”[117]

5. In a 1991 decision, often referred to as the Sibley case,[118] the Commission stated that it would consider the appropriateness of granting an AAO on a case by case basis. In doing so, it would approve an AAO for events that it found to be ”extraordinary, unusual and unique, and not recurring.”[119] The Commission's decision in the Sibley case was subsequently affirmed by the Missouri Court of Appeals.[120] In the Sibley case - the case in which the Commission set out its standards for the granting of an AAO - the Commission approved an AAO for the deferral of costs relating to refurbishment of the company's coal-fired generating plant.[121]

6. Under *18 CFR part 201, General Instruction 7*, income shall reflect all items of profit and loss during the period in which such profit and loss occurs, unless such item is extraordinary. The instruction defines extraordinary as follows:

> Those items …which are of unusual nature and infrequent occurrence …[and are] events and transactions of significant effect which are abnormal and significantly different from the ordinary and typical activities of the company, and which would not reasonably be expected to recur in the foreseeable future. (In

[116] 4 CSR 240-40.040. The USOA for gas companies is found at 18 CFR part 201.
[117] 18 CFR part 201, general instruction 7.
[118] *In the Matter of the Application of Missouri Public Service for the Issuance of an Accounting Order Relating to its Electrical Operations*. *In the Matter of the Application of Missouri Public Service for the Issuance of an Accounting Order Relating to its Purchase Power Commitments*. 1 MPSC 3d 200 (1991).
[119] *Id*. at 205.
[120] *State ex rel. Public Counsel v. Public Service Commission*, 858 S.W. 2d 806 (Mo. App. W.D. 1993)
[121] In the Matter of the Application of Missouri Public Service for the Issuance of an Accounting Order Relating to its Electrical Operations. In the Matter of the Application of Missouri Public Service for the Issuance of an Accounting Order Relating to its Purchase Power Commitments. 1 MPSC 3d 200 (1991).

> determining significance, items should be considered individually and not in the aggregate. However, the effects of a series of related transactions arising from a single specific and identifiable event or plan of action should be considered in the aggregate.) To be considered as extraordinary, an item should be more than approximately 5 percent of income, computed before extraordinary items. Commission approval must be obtained to treat an item of less than 5 percent as extraordinary.

7. Thus, for an item to be considered ”extraordinary” it must be material or significant in relation to the utility’s income.

8. Having made the above findings of fact and conclusions of law the Commission determines that any reduction to MGE's Joplin-area revenues are not extraordinary, material, or significant. The Commission will therefore deny MGE's application for an accounting authority order for “lost revenues.”

9. Even if MGE satisfied the *Sibley* test,for the reasons that follow, the Commission concludes that it is not proper to use an AAO as a vehicle to guarantee a utility a profit, much less a particular level of profit.

10. MGE is the movant, and the *burde*n rests on MGE to persuade this Commission that not only are the prerequisites of the Sibley test met, but also that the requested relief is appropriate. [122]

11. The law does not require that rates yield any particular return.[123]

12. There is no statute, rule, or case supporting that utilities have a property right to a defined level of revenue.[124]

13. MGE has no right to a return, much less a particular level of return.[125], [126], [127], [128], [129], [130], [131]

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[122] *State ex rel. GS Technologies Operating Co., Inc. v. Public Service Com'n of State of Mo.* 116 S.W.3d 680, 693 (Mo.App. W.D.,2003, citing *State ex rel. Tel–Central of Jefferson City, Inc. v. Pub. Serv. Comm'n,* 806 S.W.2d 432, 435 (Mo.App.1991).

[123] *State ex rel. Capital City Water Co. v. Public Service Commission of Missouri* 252 S.W. 446, 456 (Mo. 1922); *State ex rel. Missouri Gas Energy v. Public Service Com'n* 186 S.W.3d 376, 383 (Mo.App. W.D.,2005); *State ex rel. Missouri Office of Public Counsel v. Public Service Com'n of State* 293 S.W.3d 63, 80 -81 (Mo.App. S.D.,2009); *Straube v. Bowling Green Gas Co.* 360 Mo. 132, 141-142, 227 S.W.2d 666, 670 - 671 (Mo.1950); *Reinhold v. Fee Fee Trunk Sewer, Inc.* 664 S.W.2d 599, 603 -604 (Mo.App. E.D. 1984); *Lightfoot v. City of Springfield* 361 Mo. 659, 669, 236 S.W.2d 348, 352 (Mo.1951); *State ex rel. Missouri Gas Energy v. Public Service Com'n* 210 S.W.3d 330, 334 -335 (Mo.App. W.D.,2006).

[124] *State ex rel. Missouri Gas Energy v. Public Service Com'n* 210 S.W.3d 330, 334 -335 (Mo.App. W.D.,2006).

14. MGE simply does not have right to collect revenues – or defer an amount in lieu of collection of revenues – from any particular customer or set of customers.

15. MGE hasn't brought forth any evidence or argument that granting the requested authority is good regulatory practice in absence of any right to a defined stream of revenues from Joplin's tornado victims.

16. "It is a well-accepted principle of regulation that common stockholders contribute what is known as 'risk capital' to the utility company for which they receive a compensatory rate of return." [132]

17. "Among the uncertainties that common stockholders accept in return for this added compensation is the danger of earnings shortfall, for whatever reason."[133]

18. "Risks are part of the utility business and that even the risk of economic catastrophe may be properly assigned to owners of the utility rather than to its customers."[134]

19. If a stockholder could be assured a return of his investment under all circumstances, it would make the investment practically risk-free.[135]

20. MGE's risk of revenue shortfall and diminished profit is a business risk for which shareholders are compensated.

21. It is not appropriate to guarantee a profit, much less a defined level of profit.

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[125] *State ex rel. Capital City Water Co. v. Public Service Commission of Missouri* 252 S.W. 446, 456 (Mo. 1922).
[126] *State ex rel. Missouri Gas Energy v. Public Service Com'n* 186 S.W.3d 376, 383 (Mo.App. W.D.,2005).
[127] *State ex rel. Missouri Office of Public Counsel v. Public Service Com'n of State* 293 S.W.3d 63, 80 -81 (Mo.App. S.D.,2009).
[128] *Straube v. Bowling Green Gas Co*. 360 Mo. 132, 141-142, 227 S.W.2d 666, 670 - 671 (Mo.1950).
[129] *Reinhold v. Fee Fee Trunk Sewer, Inc.* 664 S.W.2d 599, 603 -604 (Mo.App. E.D. 1984).
[130] *Lightfoot v. City of Springfield* 361 Mo. 659, 669, 236 S.W.2d 348, 352 (Mo.1951).
[131] *State ex rel. Missouri Gas Energy v. Public Service Com'n* 210 S.W.3d 330, 334 -335 (Mo.App. W.D.,2006).
[132] *State ex rel. Union Elec. Co. v. Public Service Com'n of State of Mo.* 765 S.W.2d 618, 622 -623 (Mo.App. W.D. 1988).
[133] *State ex rel. Union Elec. Co. v. Public Service Com'n of State of Mo.* 765 S.W.2d 618, 622 -623 (Mo.App. W.D. 1988).
[134] *State ex rel. Union Elec. Co. v. Public Service Com'n of State of Mo.* 765 S.W.2d 618, 626 (Mo.App. W.D. 1988).
[135] *State ex rel. Union Elec. Co. v. Public Service Com'n of State of Mo.* 765 S.W.2d 618, 622 -623 (Mo.App. W.D. 1988).

22. It is within the Commission's discretion to refuse to place its imprimatur upon MGE's request to guarantee a level of profit.

Recommended Ordered Paragraphs

1. MGE is authorized to defer actual incremental O&M expenses associated with repair and restoration activities associated with the May 22, 2011, tornado, and depreciation and carrying charges equal to its ongoing AFUDC rates associated with tornado-related capital expenditures, to Account 182.3, Other Regulatory Assets.

2. Nothing in the Commission's order shall be considered a finding by the Commission of the reasonableness of the costs and/or expenditures deferred, and the Commission reserves the right to consider the ratemaking treatment to be afforded all deferred costs and/or expenditures.

3. Any and all offsets including, but not limited to, insurance claim proceeds or government payments or credits applicable to incremental operation and maintenance expense or capital expenditures shall be used to offset the total amount of costs to be deferred.

4. MGE shall not seek to recover any tornado related capital costs for which it is deferring depreciation and carrying charges pursuant to this AAO through its Infrastructure System Replacement Surcharge rate mechanism.

5. MGE shall begin, as of January 1, 2012, ratably amortizing to expense, over a ten-year (120-month) period, the appropriate amount of all costs it is authorized to defer, which are directly related to the May 2011 tornado. Thus, the ten-year amortization period will conclude December 31, 2021.

6. MGE shall maintain detailed supporting records, work papers, invoices and other documents to support the amount of costs deferred under this AAO, including any related deferred taxes recorded as a result of the cost deferral. Such records shall be made available for review by the Commission Staff, The Office of the Public Counsel and other intervenors, pursuant to 4 CSR 240-2.085 and Section 386.480.

7. MGE's request for authority to defer the fixed cost components of the Company's rates resulting from sales lost due to the tornado be denied.

Respectfully submitted,

/s/Sarah Kliethermes
Robert S. Berlin, MBN 51709
Sarah L. Kliethermes, MBN 60024
Goldie Tompkins, MBN 58759
Attorneys for the Staff of the
Missouri Public Service Commission
P. O. Box 360
Jefferson City, MO 65102
(573) 751-6726 (Telephone)
(573) 751-9285 (Fax)
sarah.kliethermes@psc.mo.gov

Certificate of Service

I hereby certify that copies of the foregoing have been mailed, hand-delivered, or transmitted by facsimile or electronic mail to all counsel of record this 23rd day of December, 2011.

/s/ Sarah L. Kliethermes