BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of Spire Missouri Inc.'s d/b/a Spire Request for Authority to Implement a General Rate Increase for Natural Gas Service Provided in the Company's Missouri Service Areas	))))))	Case No. GR-2021-0108

INITIAL BRIEF OF THE MISSOURI OFFICE OF THE PUBLIC COUNSEL

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Introduction

Spire began this case seeking an increase of approximately $112 million. Of this amount, nearly $47 million constituted the rebasing of investments currently being recovered through Spire's infrastructure system replacement surcharge ("ISRS"). However, the OPC's investigation of Spire's books and records quickly showed that Spire could not justify the requested increase. In fact, the OPC's investigation showed that Spire had failed to support many of the changes and revenue increases it was recommending, including the requested modifications to its WNAR, depreciation rates, and tariff provisions along with the recovery of its new ultrasonic meters. The OPC further discovered severe problems with the manner in which Spire was operating that included failing to actively manage its capital structure to achieve the most economically efficient financing available, failure to abide by the instructions of the Uniform System of Accounts adopted by the Commission in relation to the capitalization of overheads, and grievous violations of the Commission's affiliate transaction rules that resulted in Spire Missouri paying nearly all the costs to operate its affiliated parent company, Spire Inc.

Based on its investigation, the OPC concluded that Spire could not justify an increase to its base rates at this time (including the rebasing of ISRS plant), and is thus recommending that the Commission not order such an increase. The primary driving force behind the OPC's recommendation is the need to prevent Spire Missouri from subsidizing its parent company, Spire Inc., and associated non-regulated business enterprises by:

1. Maintaining a capital structure that includes much more common equity than is necessary and further manipulating its debt ratio for the purpose of excluding short-term debt financing;

2. Committing to extensive gold-plating of its distribution system through an unjustified switch in metering technology; and

3. Purposely developing affiliate transaction allocation factors designed to exclude Spire Inc. from being charged for the goods and services Spire Missouri produces on Spire Inc.'s behalf, with those costs instead being allocated primarily back to Spire Missouri itself.

The OPC argues that the adjustments necessary to correct for this current subsidization outweighs the increase to revenue required to cover plant additions that Spire has made since its last rate case. Moreover, it is important to understand that these are issues that could not be raised during the intervening ISRS cases due to the limited scope of those proceedings. In fact, this is the very reason why the ISRS statute requires a natural gas utility to come before the Commission for a rate case every three years. It is necessary to ensure that plant additions included in an ISRS case are periodically reconsidered in the context of the natural gas utility's **entire** cost of operation (*i.e.* a general rate proceeding). Such a review can, as is the case here, show that the utility was already overearning before the ISRS was implemented, with the result being that just and reasonable rates require that rates remain at pre-ISRS levels. That is what has happened in this case and that is why the OPC is recommending that Spire's rates remain static.

Executive Summary

Of the nearly fifty issues originally included in the jointly filed list of issues, all but nine have been resolved through a series of stipulations and agreements filed by the parties to this case. The OPC will now lay out, at a very high level, its arguments for the nine issues that remain. This section will not include any citation to the record. Citation to the supporting facts and law may be found in the full discussion of each issue included in this brief.

Issue 1: Cost of Capital

The proper, just, and reasonable capital structure to be used for the purpose of setting Spire Missouri's allowed rate of return is comprised of 45.00% common equity, 48.00% long-term debt and 7.00% short-term debt. This is the only capital structure recommendation that directly addresses the fact that Spire Missouri's capital structure consisted of approximately 7% short-term debt for 19 out of the 20 months that make up the combined test-year and true-up period. It is also the only capital structure offered that recognizes that Spire Missouri is not actively managing its capital structure to achieve the lowest reasonable cost of capital without jeopardizing financial stability. Instead of managing its capital structure for its own best interest, Spire Missouri's capital structure is being managed for the best interest of its parent company, Spire Inc. This has resulted in Spire Missouri maintaining much more common equity than is prudent or necessary and thus Spire Missouri customers paying much more than is just and reasonable. Adopting the OPC's proposed capital

structure will align Spire Missouri with the actively managed capital structure of its own parent, and will thereby force the utility to behave similar to a competitive business. In addition, the Commission should order an allowed return on equity of 9.25%, a cost of long-term debt of 3.99%, and a cost of short-term debt of 0.29% based on the testimony of OPC witness David Murray. Unlike Spire's witness, Mr. Murray's analysis is based on the actual parameters that third-party equity analysts use in practice, is consistent with Spire's own internal evaluations, and is supported by common rule-of-thumb methods taught as basic tests of reasonableness to professional financial analysts in the field of investing and finance.

Issue 8: Cash Working Capital

The Commission should not order rates that calculate cash working capital ("CWC") for income tax purposes based on assumed quarterly income tax payments because Spire does not – and will not – make quarterly income tax payments to the IRS. Instead, the Commission should order its Staff to calculate CWC for income tax purposes using a 365-day expense lag (*i.e.* one full year) to properly account for the fact that Spire collects money to pay income taxes from customers but does not thereafter pay income taxes to a taxing authority during the course of the year. Customers should not have to pay for the day-to-day expenses needed to cover a cost that is not actually incurred by the Company and should instead receive the benefit derived from having to pay for taxes that are never actually remitted.

Issue 13: Incentive Compensation

Spire should not be permitted to recover the cost of its incentive compensation program through rates because those programs will pay for themselves through positive regulatory lag (if properly designed). Therefore, allowing Spire to simultaneously recover the cost of the program through rates will consequently result in double-recovery. This is the same logic that the Staff employed in recommending that Spire not recover the cost of severance payments. Because a properly designed incentive compensation program will necessarily increase a utility's bottom line by more than it costs to operate, there is no need to pay the utility to undertake the program. Spire will engage in the incentive compensation program regardless of whether it is awarded cost recovery in rates because it will result in a marginal increase to Spire's revenue between rate cases. There is no justifiable reason for allowing Spire to double-recover its costs by also including the costs to operate the incentive compensation program in rates. The Commission should thus disallow the costs.

Issue 15: Capitalization of Overheads

Spire Missouri's current capitalization policies are not in compliance with the Commission's rules adopting the Uniform System of Accounts. This is primarily because Spire is capitalizing overheads that do not bear a definite relationship to construction and is instead using an arbitrary percentage (the ratio of direct labor to total labor) to justify capitalization. Both Staff and OPC witnesses agree that this is violation of the USOA. Staff has further identified several other violations that have

occurred. For this reason, the Commission should order Spire to cease capitalizing general overheads that do not have a definite relationship to construction and further order a tracker to ensure that Spire Missouri's general overheads are not being over-recovered.

Issue 16: Net Operating Loss Carryforward application

The Commission should not order the Net Operating Loss ("NOL") recorded by Spire to be included as an offset to reduce the amount of Accumulated Deferred Income Tax ("ADIT") included in the Company's rates as a reduction to rate base. It is not necessary to offset the ADIT because the NOL can instead be offset by the amount of current income tax expense that is included in rates but not remitted to the IRS. This amount of current income tax expense creates a distinct pool of "free money" that is being generated for the utility that is separate and aside from the amount of ADIT included in the Company's books. This second pool of "free money" deserves to be recognized. If the Commission nevertheless does allow Spire's NOL to be included as an offset to ADIT, then the Commission should also order a tracker or regulatory liability to account for this second pool of money.

Issue 19: Affiliate Transactions

Spire Missouri is currently being charged for the cost of goods and services it produces for the benefit of Spire Inc. At the same time, Spire Inc. is paying nothing for the cost of goods and services that Spire Missouri produces on its behalf. This is a clear, open, and flagrant violation of the Commission's affiliate transaction rule. The Commission

should therefore order the OPC's recommended adjustment to account for this violation of its rules.

Issue 24: Depreciation

Spire's current position on depreciation is uncertain as it has filed conflicting recommendations for its position. Spire's recommendation is further confused by the fact that its own witnesses have contradicted one another and have consequently called the integrity of its own study into question. Staff has similarly filed testimony that includes several self-contradictions and has further confused the record as a result. Because of the scale and scope of inaccuracies and contradictions included in the depreciation recommendations of both Staff and Spire, the Commission should side with the OPC and order an extension of Spire's existing rates (save for the OPC's recommended adjustments), with this issue to be more fully resolved in the next rate case. If the Commission nevertheless decides to order new rates in this case, then it should order the depreciation rates proposed by Staff subject to the adjustments laid out in this brief. In either event, the Commission should not order general plant amortization, or, at a minimum, order the conditions proposed by the OPC and Staff.

Issue 26: Ultrasonic Meters

Spire cannot substantiate or support the prudency of its decision to switch from diaphragm to ultrasonic meters. Spire failed to perform any cost benefit analysis or other due diligence prior to making the decision to switch. There are no safety features unique to ultrasonic meters that cannot also be achieved with diaphragm

meters. The degree of increased accuracy between diaphragm and ultrasonic meters is suspect and there is nothing to indicate what cost benefits the minuscule marginal accuracy increases would bring. The claim that ultrasonic meters are more reliable and less likely to break down is fundamentally undermined by the fact that Spire has simultaneously argued that ultrasonic meters will last anywhere from half as long to as long as diaphragm meters on average. Asserting that diaphragm meters are obsolete is false, as the OPC has shown. The switch from diaphragm to ultrasonic meters is, simply put, gold-plating of Spire's distribution system. Moreover, this unabashed build-out of rate base will significantly exacerbate a major stranded asset problem that Spire has already negligently allowed to develop. Spire customers should not have to shoulder the burden of paying for multiple meters they are not using; one meter for one account. Therefore, regardless of what action the Commission orders with regard to the ultrasonic meter question, the Commission should also order an adjustment to the plant accounts related to Spire's existing diaphragm meters to address the massive reserve deficiency that has already been created and which **will grow worse** with further diaphragm meter retirements.

Issue 30: Weather Normalization Adjustment Rider

Spire has failed to put forth any real evidence supporting why the Company should be allowed to maintain its existing Weather Normalization Adjustment Rider ("WNAR"). The Commission should therefore order Spire to discontinue this rate mechanism. If the Commission nevertheless decides to allow Spire to continue to use the mechanism that Spire has shown it cannot be bothered to maintain correctly,

then the Commission should also order the adjustments offered by the OPC's witness Ms. Lena Mantle. The Commission should not order the Rate Normalization Adjustment mechanism ("RNA") proposed by the Company as it is not authorized by statute and is thus beyond the Commission's power to grant. Further, such a mechanism will actually disincentivize conservation. Finally, if the Commission does order an RNA mechanism regardless, it should only do so with the modifications and conditions proposed by Staff and the OPC.

Issue 1. Cost of Capital

The Commission should order a capital structure to be used for the purpose of setting Spire Missouri's allowed rate of return comprised of 45.00% common equity, 48.00% long-term debt and 7.00% short-term debt and further order an allowed return on equity of 9.25%, a cost of long-term debt of 3.99%, and a cost of short-term debt of 0.29%.

Analysis

When considering the matter of the proper rate of return there are two essential elements that must be discussed. Those are (1) the rates appropriate for the allowed return on common equity and the cost of debt and (2) the common equity ratio and the debt ratio (also known as the capital structure) to which the rates are applied. We shall discuss these two components separately, beginning with the capital structure.

Capital Structure

The proper, just, and reasonable capital structure that should be used for the purpose of setting Spire Missouri's allowed rate of return is 45.00% common equity, 48.00% long-term debt and 7.00% short-term debt, as set forth in the true-up testimony of OPC witness Mr. David Murray. Exhibit 241, *True-up Direct Testimony of David Murray*, pg. 7 lns. 19 – 22. Instead of engaging in a protracted analysis of how these numbers were developed (which may be reviewed in the testimony Mr. Murray filed in this case), the OPC will focus on how this capital structure differs

from those proposed by either Staff or Spire. In particular, the OPC intends to prove that its capital structure needs to be adopted to mitigate the impact of Spire Missouri's unjust manipulation of its own capital structure through the unwarranted exclusion of short-term debt and the direct targeting of an unnecessarily equity-rich capital structure. Let us begin with the issue of short-term debt.

Spire's Capital Structure Should Reflect the Amount of Short-term Debt it Actually Carried on its Books During the Test-year Period

During the evidentiary hearing, both Staff and the OPC's witness agreed that short-term debt should be included in a utility's capital structure to the extent that the amount of short-term debt exceeds the short term assets (including or with the addition of CWIP). Tr. pg. 799 ln. 12 – 17, pg. 830 ln. 10 – 14. This is nothing new. The Commission has actually recognized this very point before:

> The Commission is persuaded by OPC witness Trippensee, who has some thirty years regulatory experience, when he states that the primary reason that short-term debt is not normally included in the capital structure used to determine revenue requirement is because short-term debt is used to support CWIP (construction work in progress), and the related interest cost is capitalized and subsequently built into rates via the process referred to in the Uniform System of Accounts as Allowance for Funds Used During Construction (AFUDC). The result is that when the CWIP becomes plant-in-service, the total original cost will include AFUDC which, in turn, includes the short-term interest cost. Stated another way, the short-term interest costs are capitalized and included in future rate cases as depreciation expense and as rate base upon which a return is earned. Including short-term interest costs in the revenue requirement would result in double recovery of those costs. **Only in the event that short-term debt balances exceed CWIP investments would it be appropriate to consider the increment short-term debt costs in the revenue requirement**.

Case ER-2007-0291, *Report and Order*, pg. 69, 2007 Mo. PSC LEXIS 1438, *69 (emphasis added). The whole point is quite clearly this: short-term debt that is supporting CWIP (or other short-term assets) is a form of temporary bridge financing that does not get reflected in a capital structure, but the short-term debt that **exceeds** CWIP and other short-term assets **is** supporting rate base and, therefore, should be included in the capital structure. *See* Tr. pg. 829 lns. 7 – 11 ("I understand the notion and I think some people try to get short-term debt eliminated by saying it's a bridge. Well, **the amount up to CWIP is a bridge**. Anything above that, that's being constantly maintained with gas companies." (David Murray speaking) (emphasis added)); Tr. pg. 797 lns. 13 – 17 ("So there is a kind of matching principle. The proposal with short-term debt should recover short-term expense and asset. **If that exceed portion of debt, it's actually debt served for capital, so that should be include in capital structure**." (Dr. Won speaking)). The question to answer is thus quite simple: did Spire's short-term debt balances exceed its CWIP (or CWIP plus other short-term asset balances). The answer is plainly yes.

The fact that Spire's short-term debt balances greatly exceeded its short-term assets (including CWIP) is extremely obvious and easy to prove. Consider the schedule attached to the surrebuttal testimony of Spire witness Adam Woodard that shows the short-term debt balances Spire carried on its books during the test year. Exhibit 45C, *Surrebuttal Testimony of Adam Woodard*, Schedule AWW SR-2. Let us use the September 19th date as an example. The short-term assets listed are: $10,724,244.20 in Propane, ($25,362,367.38) in Unamortized PGA, $9,073,493.60 in

deferred purchased gas costs, and $96,011,894.09 in CWIP. *Id*. at pg. 1 of 7. The total assets supported by short term debt is thus listed as $90,447,264.51. *Id*. The amount of short-term debt being carried, however, is $386,415,000.00. *Id*.; Tr. pg. 840 ln. 7. By subtracting the $90,447,264.51 in short term assets (including CWIP) from the $386,415,000.00 in short-term debt, we see that, for September 2019, short-term debt balances exceed short-term assets (including CWIP) by $295,967,735.49. Tr. pg. 839 lns. 19 – 21 ("taking that 386 million of short-term debt outstanding minus that 90 million to determine the net short-term debt balance for that month is 296 million."). Another way to look at this is to say that the short-term assets only account for approximately 23% of the overall short-term debt issued. This is the reason that the OPC is arguing that Spire's capital structure should reflect the other roughly 70% of short-term debt that consistently supports the capital structure. *See* Tr. pg. 799 ln. 12 – 17, pg. 830 ln. 10 – 14.

There is another adjustment to Schedule AWW SR-2 that has not yet been discussed. That is the "proforma long term debt issue" line. This is an erroneous adjustment, as will be explained shortly. For now, though, let us consider the impact on all the other months. For the Commission's convenience, the OPC has prepared a table that takes the "Assets Supported by STD" and "Average Notes Payable" values from Spire's Schedule AWW SR-2 and shows how much short-term debt exceeded short-term assets (including CWIP) during the test year.

Period	(A) Assets (including CWIP) supported by Short-term debt[1]	(B) Short-term debt[1]	= (B) – (A) Short term debt in excess of short-term assets (including CWIP)
September 2019	$90,447,264.51	$386,415,000.00	$295,967,735.49
October 2019	$50,645,687.59	$411,915,000.00	$361,269,312.41
November 2019	$57,865,070.61	$288,115,000.00	$230,249,929.39
December 2019	$45,544,587.28	$288,115,000.00	$242,570,412.72
January 2020	$31,065,208.01	$309,865,000.00	$278,799,791.99
February 2020	$8,390,018.74	$270,715,000.00	$262,324,981.26
March 2020	$3,934,103.62	$224,720,790.23	$220,786,686.61
April 2020	-$489,610.02	$218,415,000.00	$218,904,610.02
May 2020	$10,676,456.82	$189,325,000.00	$178,648,543.18
June 2020	$5,950,763.87	$218,325,000.00	$212,374,236.13
July 2020	$389,291.94	$240,775,000.00	$240,385,708.06
August 2020	$13,494,908.83	$257,225,000.00	$243,730,091.17
September 2020	$43,832,781.84	$301,225,000.00	$257,392,218.16
October 2020	$32,038,583.10	$325,725,000.00	$293,686,416.90
November 2020	$47,338,880.72	$364,475,000.00	$317,136,119.28
December 2020	$45,076,614.25	$393,675,000.00	$348,598,385.75
January 2021	$33,491,006.31	$418,125,000.00	$384,633,993.69
February 2021	$82,567,601.67	$295,225,000.00	$212,657,398.33
March 2021	$294,246,108.50	$619,375,000.00	$325,128,891.50
April 2021	$285,393,961.83	$632,725,000.00	$347,331,038.17
May 2021	$253,274,719.12	$433,525,000.00	$180,250,280.88

Exhibit 45C, *Surrebuttal Testimony of Adam Woodard*, Schedule AWW SR-2. As is readily apparent, there is a **tremendous** amount of short-term debt in excess of

[1] Taken directly from Exhibit 45C, *Surrebuttal Testimony of Adam Woodard*, Schedule AWW SR-2.

short-term assets (including CWIP) for each month. This amount should be included in Spire's capital structure. *See* Tr. pg. 799 ln. 12 – 17, pg. 830 ln. 10 – 14.

The OPC's expert witness Mr. David Murray identified that approximately 10% of Spire Missouri's capital structure has been supported by short-term debt for the period from September 30, 2017 through September 30, 2020. Exhibit 216, *Rebuttal Testimony of David Murray*, pg. 15 lns. 1 – 3. More importantly, 7.3% of that amount **remained** after deducting short-term debt assets (including CWIP). *Id* at lns. 4 – 7. In true-up, this number increased to 8.51%. Exhibit 242, *True-up Rebuttal of David Murray*, pg. 4 lns. 22 – 27. That is 8.51% of Spire's capital is thus being directly supported by short-term debt. In order to capture the cost of capital that Spire Missouri incurs to support its investment, the Commission needs to recognize the reality of how Spire Missouri's assets are financed. This includes recognizing the very real and very significant short-term debt ratio Spire **consistently** maintains. Therefore, the capital structure the Commission sets to determine Spire Missouri's authorized ROR must include short-term debt.

Since the evidence clearly shows Spire is carrying far more short-term debt than short-term assets on a regular basis, why does Spire argue that short-term debt should be excluded from its capital structure? Spire's argument is that the short-term debt Spire held during the test year should not be included in its capital structure because it was re-financed with a $305 million long-term bond issued on May 20, 2021. Exhibit 44, *Rebuttal Testimony of Adam Woodard*, pg. 7 lns. 9 – 10. Mr. Woodard insists that the Commission must exclude the short-term debt refinanced

by the long-term bond because of what he refers to as the "point-in-time" rule. *See Id*. at lns. 6 – 7, Exhibit 45C, *Surrebuttal Testimony of Adam Woodard*, pg. 17 lns. 13 - 15. This May 20, 2021, issuance is what gives rise to the $250 million "proforma long term debt issue" found in Mr. Woodard's Schedule AWW SR-2. Exhibit 45C, *Surrebuttal Testimony of Adam Woodard*, pg. 17 lns. 7 – 9, Schedule AWW SR-2. However, Spire's argument is fatally flawed for three reasons:

1. The "point in time" analysis that Mr. Woodard refers to is not customary or traditional for the Commission and has been expressly rejected by the Commission multiple times in the past

2. The long-term debt issuance is a non-recurring or unusual event that is not representative of Spire Missouri's actual capital structure either in the past or expected in the future

3. This long-term debt issuance and argument is a blatant attempt to manipulate the Company's debt balances for ratemaking purposes as demonstrated by repeated behavior.

We will now address each of these reasons in turn and thereby establish firmly why Spire's cost of capital should include the short-term debt in excess of short-term assets it actually carries on its books.

We begin with the first point. At various times, Spire witness Mr. Woodard refers to the "point in time" analysis as "customary," "historical," or as a "rule." *See* Exhibit 44, *Rebuttal Testimony of Adam Woodard*, pg. 7 lns. 6 – 7, Exhibit 45C, *Surrebuttal Testimony of Adam Woodard*, pg. 17 lns. 13 – 15, Exhibit 62C, *True-up rebuttal of Adam Woodard*, pg. 6 lns. 20 – 21. It is none of these things. Starting with the obvious, there is no rule in the code of state regulations related to the PSC that includes a "point in time" analysis that Mr. Woodard describes. As to it being

"customary" or "historical," the **only** evidence to substantiate this claim is the finding of fact from the immediately preceding Spire general rate case that reads:

> The average level of construction work in progress and other short-term assets exceeds the amount of short term debt outstanding during the true-up period after taking into consideration a September 15, 2017 funding of $170 million of long-term debt instruments. Mr. Murray's proposal to add short-term debt to the capital structure ignores this fact by using a three-year average rather than the customary "point in time" analysis of short term debt.

GR-2017-0215 and GR-2017-0216, *Amended Report and Order*, pg.42 ¶ 29. This finding is supported by only **one** citation, which is to the surrebuttal of Spire's own witness Steven P. Rasche. *Id*. fn. 150. Mr. Rasche's testimony contains no legal or factual citation to support the "point in time analysis" **whatsoever** and instead references Spire witness Glenn Buck. GR-2017-0215 and GR-2017-0216, *Exhibit 37 - Rebuttal testimony of Steven P Rasche*, pg. 3 ln. 1 – 4 ("I also agree with Mr. Buck that witness Murray's attempt to ignore this fact by using an unorthodox three-year average rather than the customary "point in time" analysis of short term debt is equally flawed - which conclusively demonstrates the impropriety of his approach - not to mention inappropriately selective."). Mr. Glenn Buck filed four rounds of testimony in GR-2017-0215, **but not a single one mentions the "point in time" analysis**. *See* GR-2017-0215 and GR-2017-0216, *Exhibit No. 19 - Direct Testimony of Glenn W. Buck*; GR-2017-0215 and GR-2017-0216, *Exhibit No. 20 - Rebuttal Testimony of Glenn W. Buck*; GR-2017-0215 and GR-2017-0216, *Exhibit No. 21 - Surrebuttal Testimony of Glenn W. Buck*; GR-2017-0215 and GR-2017-0216, *Exhibit*

No. 22 - True-Up Direct Testimony of Glenn W. Buck. Moreover, the OPC has undertaken a search of Commission decisions and related case-law but has found no mention of a "point in time" analysis that Mr. Rasche refers to **anywhere**. It appears that outside of this **one** sentence in **one** witness's testimony, there is no actual evidentiary support for the existence of this purported "customary" analysis. In fact, the OPC was able to find **numerous** Commission decision that expressly rejected a point in time analysis in one form or another.

In case EO-85-185 and EO-85-224, the Commission addressed costs related to Kansas City Power and Light (now known as Evergy)'s Wolf Creek nuclear plant. *See* EO-85-185 and EO-85-224, 75 Pub. Util. Rep. 4th (PUR) 1, 1986 Mo. PSC LEXIS 33 (April 23, 1986). One contested issue in that case was the determination "of what period should be used to calculate the value of the fuel inventory in the reactor." *Id*. at 142. "Staff ha[d] utilized a 13-month average of the balance of unburned nuclear fuel in the reactor and included that amount in rate base." *Id*. "Staff assert[ed] it is a known fact that the level of nuclear fuel in the reactor core will decrease throughout the first year of operation[,]" and therefore claimed "the use of any amount greater than Staff's average would overstate nuclear fuel inventory." *Id*. at 142-43. The "Company disagree[d] with Staff's methodology and recommend[ed] the Commission **adopt a point-in-time concept instead**." *Id*. at 143 (emphasis added). "That concept would include in rate base the value of nuclear fuel in the reactor as of the date Wolf Creek is declared by the Commission to be in service." *Id*. In deciding the case, the Commission stated as follows:

> Contrary to the arguments put forth by Company, the Commission finds Staff's average to be a reasonable method of determining the value of fuel inventory in the reactor. **The Commission finds that the point-in-time calculation recommended by the Company would overstate the nuclear fuel inventory, since the fuel would be at its highest level when the plant is declared in service**. The Commission does not believe that the initial level adequately reflects the fact that the fuel in the reactor will steadily decline during the first year of operation.

Id at 143-44 (emphasis added). This means that the Commission **expressly rejected the point in time analysis** because it found that looking at the fuel inventory as of a **single** date was not a realistic representation of the fuel inventory due to the fact that inventory would naturally decrease over time. *Id*. The exact same logic applies to the present case. Spire is arguing the Commission must base its capital structure off a debt issuance that did not exist until the last eleven days of the rate case true-up period. This debt issuance does not accurately reflect how the capital structure was being supported during the other 19 months of the original test-year and true-up period, nor will it reflect how the capital structure is going to be supported moving forward given the fact that 10% of Spire Missouri's capital structure has been supported by short-term debt for the period from September 30, 2017 through September 30, 2020. Exhibit 216, *Rebuttal Testimony of David Murray*, pg. 15 lns. 1 – 3.

Another case to consider is TR-80-235, TR-81-151 and TR-81-166, which was a telephone rate case. TR-80-235, TR-81-151 and TR-81-166, 24 Mo. P.S.C. (N.S.) 152, 1981 Mo. PSC LEXIS 57 (February 3, 1981). One of the issues before the Commission

was the amount of cash working capital to be included in rate base. *Id* at *22 – 23. "The Company ha[d] computed a cash working capital requirement of ($190,706)." *Id*. at *22. "Staff ha[d] computed a cash working requirement of ($1,498,687)." *Id*. at *22 – 23. "The Company computed its cash working capital requirement using the balance sheet approach, while Staff used a lead lag study to determine the cash working capital requirement." *Id*, at *23. The Commission found that there were "numerous defects inherent in the Company's balance sheet approach" with the very first one being that "[i]t provides **only a point in time level of working capital** which ignores fluctuations within a given month." *Id*. at *26. The Commission contrasted this with Staff's lead-lag study, which it found "examines the source of the cash working capital associated with each normalized expense item over 365 days." *Id*. The Commission subsequently found that Staff's methodology was more appropriate. *Id*. Again, we see in this case the Commission expressly rejecting an argument because it relied on a **point in time** and thus ignored the fluctuations that normally occur in any given month. The Commission instead determined that the correct answer was to use an average or normalized amount by looking at the whole 365 day period at issue. If the same logic is applied to the present case, then the result would be recognizing that 10% of Spire Missouri's capital structure has been supported by short-term debt for the period from September 30, 2017 through September 30, 2020. Exhibit 216, *Rebuttal Testimony of David Murray*, pg. 15 lns. 1 – 3.

The third case is an electric rate case for Kansas City Power and Light (now known as Evergy). Case Nos. 18,433, 18,463, 18,494 and 18,495, 20 Mo. P.S.C. (N.S.)

592, 1976 Mo. PSC LEXIS 31 (April 23, 1976). One of the issues in the case concerned depreciation reserve. *Id* at *18. Staff was proposing to increase the actual depreciation reserves under the rationale that the adjustments "were necessary to have a proper regulatory matching of rate base and revenues and expenses" *Id* at *19. Kansas City Power and Light y took the position that "any increase in the depreciation reserve over the actual amount thereof as of December 31, 1975, would result in depriving the Company of the opportunity to earn the rate of return allowed by the Commission because the Company would earn no return on the amount by which its new plant as of that date were reduced by the increase in the depreciation reserve proposed by the Staff." *Id*. at *19 – 20. In deciding the issue, the Commission found as follows:

> The Commission finds the adjustments inappropriate in this case. The Commission further finds that the purpose of "year ending" various data is to get a "snapshot" of the Company as of a particular point in time. **It is hoped that this "snapshot" will accurately reflect the Company's situation on a continuing basis** and that rates determined on the basis of the "snapshot" **will reflect the Company's continuing situation**. In this case, an increase in the Company's depreciation reserve as of December 31, 1975, does not give us a "snapshot" that is reflective of the Company's situation on a continuing basis. While the Staff treatment and rationale might be appropriate for companies in a static situation or for companies having a declining rate base this Commission would be ignoring realities if it were to accept Staff's treatment for Kansas City Power & Light, a company whose investments in plant are rapidly increasing. If this Commission is to establish rates over a period of time for expanding utilities, **it must have a "snapshot" reflective of the Company's situation over a period of time**. While the Staff's position may be technically correct with respect to **one time** or piece of equipment **it is not conceptually sufficient for this Commission for ratemaking purposes** for this Company at this time.

Id. at *20 – 21 (emphasis added). The message is clear: the Commission plainly states that rates should not be set according to a single point in time, but rather, need to be based on a "snapshot" that reflect the Company's situation over an entire **period** of time. *Id*. In this case, that would mean recognizing that, for 19 out of the 20 months in the test-year and true-up period, 10% of Spire's capital structure was short-term debt. Exhibit 216, *Rebuttal Testimony of David Murray*, pg. 15 lns. 1 – 3.

The thing that all three of these decisions have in common is the idea that the Commission cannot blind itself to the full picture of a given situation by simply focusing on one single "point" in time. There are still more cases that support this same proposition. Case Nos. ER-82-39 and WR-82-50, 25 Mo. P.S.C. (N.S.) 139, 170, 1982 Mo. PSC LEXIS 36, *86 (June 21, 1982) ("However, the Commission cannot accept an across-the-board 10% increase in allowable return on equity as an attrition allowance, based upon any inflation rate **at a given point in time** which may not be reasonabl[y] representative of either historic or reasonably expected future inflation rates, given the uncertainties of the current economy." (emphasis added)); Case No. ER-78-252, 28 P.U.R.4th 398, 1979 Mo. PSC LEXIS 49, *64-65 (March 5, 1979) ("The Commission has, from time to time, selected capital structures other than the specific capital structure existed at test year end because the Commission concluded that the specific capital structure would not be representative of the typical capital structure which the company involved would actually face during future financing cycles."). Moreover, OPC witness Mr. David Murray argued the same in testimony:

> Mr. Woodard's statement refers to the Commission's evaluation of the reasonableness of a company's rate levels as of the test year and any potential updates of this test year. However, **an audit of a company's books and records should never be restricted to accepting a company's financial position as of a "point in time" as being representative of a company's potential earnings during the period rates will be in effect**. **A test year should not cause regulators to put on "blinders" and ignore a company's typical financial position over a ratemaking cycle**. This is especially true for a company such as Spire Missouri that is allowed to collect surcharges on investments between rate cases. Therefore, the capital structure should be examined over the rate case cycle to determine how Spire Missouri typically finances its infrastructure investments.

Exhibit 217C, *Surrebuttal Testimony of David Murray*, pg. 11 ln. 18 – pg. 12 ln. 3. The logic espoused by Mr. Murray is identical to the logic this Commission has applied in the cases previously discussed and is the logic that this Commission should apply in this case as well.

Spire is asking this Commission to "put on 'blinders' and ignore the reality of how Spire Missouri routinely and consistently finances its investments." *Id* at pg. 12 lns. 24 – 25. Their argument is predicated on tricking the Commission into believing the existence of a "custom" or "tradition" that has never actually existed and which is wholly unsupported – and is actually contradicted by – the Commission's decisions that directly address the logic of the issue. Asking the Commission to behave in this manner, to ignore the relevant facts of the case, because of a false claim that it is "custom" is the height of arbitrariness. The Commission should not permit itself to be misled in this manner.

The second point is similar to the first and touches on the underlying rationale for why the so-called point in time analysis makes no sense. That rationale is that the Commission should base its decision on the "average" or the "normal" behavior of a utility, and not on single, isolated, and non-recurring event. *See* EO-85-185 and EO-85-224, 75 Pub. Util. Rep. 4th (PUR) at 143-44; TR-81-151 and TR-81-166, 1981 Mo. PSC LEXIS 57 at *26; Case Nos. 18,433, 18,463, 18,494 and 18,495, 1976 Mo. PSC LEXIS 31 at *20 – 21. In this case, the single, isolated, and non-recurring event is the issuance of $305 million of long-term debt on May 21, 2021. Mr. Murray explained the problem with this adjustment in his true-up rebuttal testimony:

> Mr. Woodard's adjustment to Spire Missouri's average short-term debt balance inaccurately assumes that the $305 million of long-term debt issued on May 21, 2021 had been issued in September [2019]. Mr. Woodard characterized his backdating of the hypothetical replacement of short-term debt with long-term debt as a "pro forma long-term debt issue." This characterization is misleading. Pro-forma adjustments to financial statements are intended to reflect a company's expected financial position going-forward. Companies typically make pro-forma adjustments to exclude extraordinary issues, similar to Spire Inc.'s adjustments to its Generally Accepted Accounting Principle ("GAAP") financial results, to determine net economic earnings per share ("NEEPS"). This formed the basis for Spire Inc.'s exclusion from its 2020 earnings of its write-down of its Spire Storage assets by $140.8 million and Spire compressed natural gas fueling stations by $7.8 million, equivalent to $2.89 in EPS. Spire Inc. considered this a non-recurring or unusual circumstance that is not likely to occur in the future.
>
> If Spire Missouri's issuance of long-term debt in May 2021 to refinance short-term debt resulted in capital structure ratios expected to be maintained over future periods, then it could be argued this is a reasonable adjustment. However, considering the decline in the short-term debt ratio as of May 2021 is a non-recurring or unusual event, this "point-in-time" capital structure is not representative of Spire Missouri's expected revenues or costs. Therefore, Spire Missouri's capital structure

> as of the true-up date introduces a non-recurring or unusual event that is not reflective of a normal level of Spire Missouri's cost of capital over the period in which rates will be in effect.

Exhibit 242, *True-up Rebuttal of David Murray*, pg. 4 lns. 1 – 21. Spire Missouri's "point in time" analysis is dependent on the Commission ignoring evidence of historical use of short-term debt by the Company and basing its **entire** capital structure decision off **one** debt issuance that occurred just 11days before the end of the true-up period of the test-year. This is a ridiculous proposition.

The evidence in the record makes it extremely clear that Spire (and even its parent Company Spire Inc.) has made heavy use of short-term debt that was well in excess of short-assets like CWIP. Besides the evaluation of the schedule included in Mr. Woodard's surrebuttal (discussed previously), there is also the following explanation from the testimony of OPC witness Mr. Murray:

> **[B]oth Spire Inc.'s and Spire Missouri's capital structures have consisted of at least 11% short-term debt, on average, for the last 3 to 5 years**. I used Spire Inc.'s and Spire Missouri's fiscal year (FY) ended balance sheet information (shown on Schedules DM-D-9-2 and DM-D-9-3) to determine the proportion of their capital structures supported by short-term debt.
>
> Although this information shows Spire Inc.'s and Spire Missouri's propensity to use a significant amount of short-term debt over several years, I recognized that this yearly information was a "snapshot," or "point-in-time" as Mr. Woodard characterizes such, based on FY-ending balances for each year over the last several years. For this reason, for purposes of determining whether and how much short-term debt to include in my recommended capital structure, I analyzed Spire Inc.'s and Spire Missouri's average quarterly short-term debt balances **over the entire test year** (9/30/2019 through 9/30/2020). This approach allowed me to evaluate the decline in short-term debt balances that

> should occur due to receipt of payments from customers after the 2019/2020 heating season. My findings from this analysis are shown on Schedules DM-D-10-1 and Schedule DM-D-10-2. As can be seen on Schedule DM-D-10-1, both Spire Inc.'s and Spire Missouri's quarterly-average capital structures for the test year consisted of at least 10% short-term debt. **Even after excluding construction work in progress ("CWIP") from the short-term debt balances, over 7% of each company's capital structures was supported by short-term debt**.

Exhibit 217C, *Surrebuttal Testimony of David Murray*, pg. 13 ln. 5 – pg. 14 ln. 7 (emphasis added). It is this actual 10% average short-term debt (7% after CWIP is removed) that the Commission should base its capital structure decision on.

If the Commission truly has an interest in setting rates according to the **normal** state of affairs for a utility, then it needs to include the short-term debt that Spire carried on its books for more than 19 out of the 20 months in the test-year and true-up. This idea is even alluded to in the filed *Joint Stipulation of Facts* which states:

> A normalization adjustment is an adjustment made to a cost or revenue to reflect normal, on- going operations of the utility. Revenues or costs that were incurred in the test year that are determined to be atypical or abnormal will get specific rate treatment and generally require some type of adjustment to reflect normal or typical operations. **The normalization process removes abnormal or unusual events from the cost of service calculations and replaces those events with normal levels of revenues or costs**.

Joint Stipulation of Facts, pg. 4 ¶ 20 (emphasis added). The Commission should therefore not do as Spire suggest and set the Company's entire capital structure for

rates moving forward based on the capital structure that was only in place for the last 11 days of the true-up:

> **Q. Does Mr. Woodard's capital structure recommendation accurately capture Spire Missouri's use of short-term debt to fund its rate base?**
>
> A. No. Mr. Woodard employs what he refers to as a "point-in-time" analysis. Specifically, he used common equity and long-term debt balances as of May 31, 2021, but excluded short-term debt. Mr. Woodard justifies his exclusion of short-term debt by claiming the "average" of Spire Missouri's short-term debt for the thirteen months ended May 31, 2021 was less than the average of short-term assets that are assigned short-term debt carrying costs. **However, what he has actually done is manipulated the short-term debt balances by assuming the long-term debt issue in May 2021 was issued 20 months ago (September 2019) to replace short-term debt**. **But for this manipulation, Spire Missouri's average short-term debt balance would have far exceeded the average balance of short-term assets assigned short-term debt carrying costs**.

Exhibit 242, *True-up Rebuttal of David Murray*, pg. 2 lns. 9 – 20. This, incidentally, brings us to the third and final point, which is that Spire is blatantly manipulating its debt balances using this phony "point in time" analysis.

This is not the first time that this issue has come up, nor is it the first time that Spire has included a convenient long-term debt issuance at the last moment in a rate case so as to purposefully eliminate short-term debt:

> **Q. Did Spire Missouri time its long-term debt issuance in the last rate case during the final month of the true-up period?**
>
> A. Yes. Spire Missouri's true-up period in its 2017 rate case was September 30, 2017. Spire Missouri issued $170 million of long-term debt on September 15, 2017. Spire Missouri's capital structure witness in that case, Glenn Buck, claimed that if this pro forma amount of long-

> term debt were deducted from short-term debt for the prior 13-months to the true-up date, the net balance would be less than short-term asset balances for the same 13-months, which he testified justified the exclusion of short-term debt from the authorized ROR.

Exhibit 217C, *Surrebuttal Testimony of David Murray*, pg. 15 lns. 10 – 17. The first thing that the Commission should notice is that this is the **exact same behavior** as what has occurred in the present case. Spire has clearly developed a system wherein it waits until the very end of the test-year to issue long term-debt that it then claims invalidates **all** the short-term debt that it has carried on its books prior to that point. This allows the Company to have rates set using just long-term debt costs – which is generally more expensive than short-term debt – after which the Company goes back to using short-term debt to finance up to 10% of all its capital needs. *Id*. at pg. 13 ln. 5 – pg. 14 ln. 7. This is a cheat code; an obvious abuse of the ratemaking process designed to raise Spire's income:

> Q. It sounded like you have agreed with Dr. Won that the cost for short-term assets and CWIP and whatever is excess of that should go into short-term debt, and the second answer that Dr. Won had, I asked him why not this rate case. He said they're going to look at it for the future. Is that correct? Is it ready to be looked at now?
>
> A. Definitely needs to be looked at now. They did the same thing -- The Company did the same thing in this case they did in the 2017 case. I disagreed with it then. I disagree with it now. What they do is they issue long-term debt right in time for the end of the true-up period. So in this case May 20, 2021. In the 2017 case, they issued the long-term debt. I believe the true-up was September 30, 2017, issued the long-term debt and then pretended like that long-term debt reduced the short-term debt going back 19, 20 months. **That is inappropriate. That is not -- It's fictitious. It does not reflect how they are supporting their investments. It is improper. It's manipulation right now**.

> Q. So you're saying that this rate case is the second example and two is too many?
>
> A. **<u>One was too many, in my opinion</u>**.

Tr. pg. 831 ln. 5 – pg. 832 ln. 2 (bench questioning of David Murray) (emphasis added). While the OPC is glad to hear that Staff had conceded that it will at least *look into* this problem in the next rate case,[2] the OPC agrees with its witness's observation: **<u>allowing this manipulation once was one time too many</u>**.

As the OPC has now demonstrated, employing Spire's supposed "point in time" analysis in order to pretend that long-term debt issued in May of 2021 was issued in September of 2019 (20 months earlier than it actually was) is patently absurd. This application is not supported by logic, contradicts Commission practice, is contrary to basic normalization principles, does not reflect the actual state of Spire's capital structure, and results from an attempt to game the system by creating a false impression of Spire's debt issuance and a false impression of past Commission practice. The Commission should therefore deny this misleading argument and calculate short-term debt for each month of the test year as if the long-term debt that had not yet been issued had in fact not been issued.[3] Should the Commission view short term debt in this fashion, it will find that Spire Missouri's average short-term

[2] Tr. pg. 783 lns. 5 – 10 ("Q. What would you look for to determine when to recommend a different capital structure? A. So one of the main thing is about the short-term debt. We needed to check that is intentionally Spire Missouri manipulate short-term debt level. I needed to check that." (Dr. Won speaking)).

[3] Compare this to Spire's position that calls for long-term debt that had not yet been actually issued to be treated as if it **<u>had</u>** been issued. Exhibit 242, *True-up Rebuttal of David Murray*, pg. 2 lns. 9 – 20.

debt balance far exceeded the average balance of short-term assets that are assigned short-term debt carrying costs (including CWIP). Exhibit 242, *True-up Rebuttal of David Murray*, pg. 2 lns. 9 – 20. The Commission should therefore include the short-term debt Spire carried during the test year that was in excess of CWIP and other short-term assets in Spire's capital structure. *See* Tr. pg. 799 ln. 12 – 17, pg. 830 ln. 10 – 14.

Spire Missouri's Capital Structure Should be Guided by Spire Inc.'s Dynamically Managed Capital Structure to Account for the Fact that Spire Missouri is Currently Targeting an Unnecessarily Equity-rich Capital Structure

There are two parts to this issue. The first is to establish that Spire Missouri is currently targeting an unnecessarily equity-rich capital structure and explain why that is a problem. The second is to explain why Spire Inc.'s dynamically managed capital structure is the better proxy and the one that should guide the Commission's decision.

To start at the beginning, let us establish that Spire Missouri is targeting its capital structure. This is easy to establish, as Spire Missouri has acknowledged in its data responses that it is targeting the capital structure approved by the Commission in the last rate case. *See* Exhibit 216, *Rebuttal Testimony of David Murray*, pg. 3 lns. 1 – 7. Spire Missouri has made no attempt to hide this fact and has openly acknowledged it. Exhibit 45C, *Surrebuttal Testimony of Adam Woodard*, pg. 5 ln. 14 – pg. 6 ln. 5. There is no question that Spire Missouri is targeting the capital structure

that the Commission approved in the last rate case. Let us now turn to why that is a bad thing.

The single, simplest reason for why Spire Missouri's decision to purposefully target the capital structure approved by the Commission in the last case is a bad thing is that the Company is now maintaining more equity than is necessary. *See* Exhibit 215C, *Direct Testimony of David Murray*, pg. 50 ln. 22 – pg. 51 ln. 4; Tr. pg. 817 ln. 8 – pg. 819 ln. 8. This has resulted in Spire ratepayers paying far more than they otherwise would need to in rates:

> Q. I feel like we need to break things down on a most basic level. What is the impact of having a high equity ratio on customer rates?
>
> A. They're higher. It's a higher revenue requirement assuming using the same ROE but it's as high a revenue requirement plus you have a tax gross-up factor on equity which makes it even more magnified.
>
> Q. How does that factor into your concern regarding maintaining the existing Spire equity to debt ratio?
>
> A. Based on my analysis of Spire Missouri's credit metrics which produce healthy cash flows consistent with apparently a higher economical credit rating, which they don't receive credit for, that customers are paying at least 20 million. With true-up it's going to be even higher. Let's just say in the $20 to $25 million range higher rates per year to achieve credit metrics that they don't get credit for from specifically Standard & Poor's.

Tr. pg. 837 ln. 12 – pg. 838 ln. 5; *see also* Tr. pg. 819 lns. 9 – 11 ("Q. Can you identify any damage to ratepayers? A. Yes, sir. They're being charged too much. Over $20 million a year."). There are, however, other consequences, as Mr. Murray explained:

> **Q. Are there any other consequences of maintaining a high common equity ratio on Spire Missouri's revenue requirement**

other than charging a higher return for a higher proportion of the capital structure?

A. Yes. Although the common equity ratio has been my primary point of contention as to how Spire Inc. inflates Spire Missouri's cost of service, because debt yields have been very favorable, reaching all-time lows recently, Spire Inc.'s strategy also prevents Spire Missouri ratepayers from realizing lower cost of debt capital. Spire Inc.'s decision to issue holding company debt clearly impacts Spire Missouri's debt issuance strategies.

Exhibit 215C, *Direct Testimony of David Murray*, pg. 53 lns. 3 – 10. Therefore, by specifically targeting a capital structure with higher-than-necessary equity ratios, Spire Missouri is hurting its customers. That begs the question: why is Spire doing this?

Spire Missouri is targeting its equity-rich capital structure to the detriment of its customers so as to benefit Spire Inc., its parent company, as discussed by OPC witness David Murray:

> Since Spire Inc. acquired Alagasco (now Spire Alabama) on September 2, 2014, Spire Inc.'s main goal relative to its capitalization strategy has been to reduce the amount of leverage it carries on a consolidated basis in order to show improvement in Spire Inc.'s consolidated credit metrics. Obviously, this can't be achieved if Spire Missouri used more leverage for its own benefit or else this would cancel any benefit to Spire Inc. reducing leverage at the holding company. Consequently, **Spire Missouri's capital structure is not managed for the best interest of Spire Missouri, but rather for the best interest of Spire Inc**. Spire Missouri's targeting of a higher common equity ratio for ratemaking, rather than for changes in business risk and/or economic conditions, **contradicts one of the primary purposes of managing a capital structure – to achieve the lowest reasonable cost without jeopardizing financial stability**. As I will discuss later in my testimony, Spire Missouri's lower business risk affords it the ability to utilize more leverage, but for its affiliation with Spire Inc. and its

> decisions to use significant leverage to pursue and execute its acquisitions of other companies.

Exhibit 215C, *Direct Testimony of David Murray*, pg. 40 lns. 1 – 14. Spire Inc. has been taking advantage of the debt capacity afforded by its low-risk regulated utility subsidiaries to manage its own capital structure. *Id*. at pg. 41 lns. 3 – 4. For example, "Spire Inc. issued a significant amount of holding company debt for purposes of acquiring Alagasco in 2014." *Id*. at lns. 5 – 6. Spire Inc. was only able to do this, however, because it was able to take advantage of Spire Missouri's and Spire Alabama's low risk regulated utility operations. *Id*. at lns. 11 – 13. "In essence, Spire Inc. has used Spire Missouri's (and Spire Alabama's) debt capacity to enhance its shareholder returns utilizing a sizeable amount of leverage to acquire Spire Alabama." *Id*. at lns. 21 – 23.

One of the ways that we can tell Spire Missouri is not being managed for its own best interest (but rather for the interests of its parent) is to directly compare the Company to its parent. For example, consider this statement by OPC witness David Murray:

> If Spire Missouri's capital structure were being managed for its own benefit, then one would expect that it would have a carefully managed dividend payment policy, similar to how Spire Inc. manages its dividend payments to a targeted payout ratio in the range of 55% to 65%. However, Spire Missouri's dividend payout ratio was approximately 80% in the 2016 FY, 25% in the 2017 FY and has averaged around 32% over the 2018 through 2020 FYs. If Spire Missouri were financially managed as a stand-alone entity accountable to third-party equity investors, it would be required to maintain a higher and more consistent payout ratio, similar to how Spire Inc. manages its dividends. Spire

> Missouri's retention of a significant amount of its earnings in recent years results in Spire Missouri's capital structure not receiving the benefit of the use of debt rather than retaining equity to meet it cash deficiencies.

See Exhibit 215C, *Direct Testimony of David Murray*, pg. 52 lns. 5 – 15. In a similar vein, one can also argue that, if 54.2% is a desirable equity ratio for purposes of maintaining credit, Spire Inc. would be moving its own capital structure to this target through the true-up period in this case (May 31, 2021). However, Spire Inc.'s common equity ratio has actually declined from 42.58% at the beginning of the test year, to 39.85% as of the end of the true-up date, May 31, 2021. Exhibit 241, *True-up Direct Testimony of David Murray*, Schedule DM-TD-4. Stop for a moment and consider the meaning of this. At the same time Spire Missouri is arguing that it should have a 54.2% equity ratio, its **own** parent is currently moving in the **opposite** direction. This is the difference between a capital structure that is being managed to maximize rate-making rate of return and one being managed to achieve a lower cost of capital for the best interests of its shareholders.

The fact that Spire Inc. has so much more leverage (less equity) than its own regulated subsidiary utility is a major concern, as expressed by Mr. Murray:

> **Q. Considering Spire Inc.'s operations other than its regulated LDC operations have more business risk, would it not be prudent for Spire Inc.'s consolidated capital structure to have less leverage than its regulated utility subsidiaries?**
>
> A. Yes. Actually, this is how Spire Inc. managed its capital structure prior to the commencement of its acquisition strategy. Prior to Spire's acquisition of Alagasco, Spire Inc. typically had a higher common equity ratio in its consolidated capital structure as compared to the common

equity ratio at its regulated utility subsidiary, Laclede Gas Company (assets now known as Spire Missouri East).

The only assets Spire Inc. owns are its subsidiaries. Spire Inc.'s other subsidiaries have not been able to operate without Spire Inc.'s credit support. The only assets that provided significant and dependable cash flows to allow Spire Inc. to provide parental guarantees of up to ** _____ _____ ** are those of its regulated utilities. This is not theory. This is fact.

Exhibit 217C, *Surrebuttal Testimony of David Murray*, pg. 8 ln. 22 – pg. 9 ln. 8.

Moreover, Spire's own internal documents show that its other business segments should be supported by a more economical capital structure:

As it relates to Spire Inc.'s investments in ** _____ _____ _____ _____** Considering the fact that Spire Inc. had to write-down its Spire Storage investment by $140.8 million last year, **it is illogical to assume Spire Storage's business risk can allow a higher proportion of leverage than Spire Missouri**. As I will explain when addressing Dr. Won's discussion of the four factors to consider when evaluating a fair and reasonable capital structure, **this demonstrates the lack of a logical relationship between business risk and financial risk (i.e. the use of a higher proportion of debt to finance lower-risk assets)**.

Id. at pg. 9 lns. 11 – 19. Similar testimony was further elicited on the stand with regard to Spire's STL business:

Q. Thank you. If the Commission does not accept OPC's proposed capital structure, do you have any recommendations for an appropriate capital structure outside of the Staff and the Company's proposal?

A. At a bare minimum, STL is a new pipeline, and obviously folks are aware of the issues there and that there's risk to whether or not it even continues. It was a brand new pipeline and they were authorized a

> higher rate of return as part of getting their certificate. FERC gave them a 50/50 capital structure, 50 percent equity, 50 percent debt. A brand new pipeline versus a company that's been in existence since the late 1800s and has fairly predictable ongoing investments for the foreseeable future within structure replacement, I don't understand how anybody can with a straight face say that Spire Missouri should have an equity ratio that's higher than what's assigned to the FERC STL pipeline.

Tr. pg. 862 ln. 15 – pg. 827 ln. 7 (bench questioning of David Murray). This is the point that the OPC wants to stress the most to the Commission.

There **should** be an inverse relationship between business risk and debt capacity. Exhibit 217C, *Surrebuttal Testimony of David Murray*, pg. 8 lns. 17 – 18. A riskier business should have a harder time acquiring debt financing and, consequently, need to rely on more equity financing when compared to a less risky business. *Id*. In this case, though, we have the opposite occurring. The OPC has shown how three entities in the Spire enterprise: Spire Inc., Spire Storage, and Spire STL, have argued or assumed less equity and more debt than the relatively more safe and secure Spire Missouri. This indicates that Spire Missouri has contradicted one of the primary purposes of managing a capital structure: to achieve the lowest reasonable cost without jeopardizing financial stability. Exhibit 215C, *Direct Testimony of David Murray*, pg. 40 lns. 8 – 11. Why would Spire Missouri do this? Why would Spire Missouri vehemently fight to maintain the 54.2% common equity ratio allowed by the Commission in the last rate case? Because doing so allows Spire Inc. to receive another $34 million/year from Spire Missouri's ratepayers. *Id*. at pg. 51 ln. 28 – pg. 52 ln. 2. It also allows Spire Inc. to misappropriate the debt capacity

of Spire Missouri in order to fund acquisitions and guarantee obligations for its non-regulated subsidiaries such as Spire Storage, Spire Marketing, and Spire STL. *Id.*, at pg. 42 lns. 11 – 24. Let us take a moment to consider this last point in detail.

The fact that Spire Inc. is effectively leveraging the debt capacity of Spire Missouri (through the preservation of a higher-than-necessary equity ratio) to fund its other interests has been recognized by both Moody's and Standard and Poor's (the two most prolific rating agencies in the world):

> **Q. What proof do you have that Spire Missouri's debt capacity is impaired by the holding company's use of leverage?**
>
> A. The rating agencies observations of the impact Spire Inc.'s holding company debt has on Spire Missouri's financial flexibility. For example, in Moody's recent ratings report on Spire Missouri it explicitly indicated that Spire Inc.'s substantial amount of holding company debt puts pressure on Spire Missouri to provide upstream dividends to support the holding company's debt serviced needs. S&P assigns Spire Missouri a corporate credit rating of 'A-' rather than its hypothetical stand-alone credit profile of 'A+' because of its association with Spire Inc.'s higher financial risk associated with its use of leverage, as well as its higher-risk non-regulated operations.

Id. at pg. 42 lns. 1 – 10. Mr. Murray also includes direct quotes from both Moody's and S&P in his testimony:

> Moody's indicated the following about Spire Inc.'s ability to service this debt:
>
> > The roughly $31 million of annual parent level interest expense is essentially a fixed obligation **that is generally serviced by the utilities**, since the unregulated net income and distributable cash of Spire Inc.'s other unregulated businesses, such as Spire Marketing, can be

> more volatile, less certain and insufficient to service the debt.

Id. at pg. 41 lns. 13 – 19 (emphasis added).

> Standard & Poor's ("S&P") Ratings Direct indicated the following about Spire Missouri's lack of sufficient separation from Spire Inc. to justify being rated based on its own stand-alone credit quality:
>
> > Under our group rating methodology, we assess Spire Inc. as the parent of the group that includes Spire Alabama Inc. and Spire Missouri Inc. We assess the group credit profile as 'A-' which leads to a long-term issuer credit rating of 'A-'. **Our view is that the current insulation measures are not sufficient to warrant separation between the parent and its subsidiaries.** .

Exhibit 217C, *Surrebuttal Testimony of David Murray*, pg. 6 lns. 12 – 19. This last quote from S&P is particularly important as is shows how Spire Missouri's Standard & Poor's corporate credit rating is rated 'A-', which is two notches below its Stand Alone Credit Profile ("SACP") of 'A+', because of its affiliation with Spire Inc.'s more leveraged capital structure. *Id*.; *see also* Exhibit 234C, *Response to OPC's DR 304*. This lower corporate credit rating causes Spire Missouri's bond rating to be two notches below what it would be absent its affiliation with Spire Inc. Exhibit 234C, *Response to OPC's DR 304*. **Therefore, Spire Missouri's capital structure does not support its own bond rating**.[4]

[4] In addition, while Moody's does assign Spire Missouri's First Mortgage Bonds a stronger rating of "A1" when compared to "Baa2" for Spire Inc.'s senior unsecured bond, this is because the former is secured debt while the latter is unsecured debt. *See* Tr. pg. 776 lns. 6 – 16.

In the absence of its relationship with Spire Inc., Spire Missouri would have a stronger bond rating and would be able to acquire even cheaper debt financing. *See generally*, Exhibit 215C, *Direct Testimony of David Murray*, pg. 42 lns. 1 – 10. Further, Spire Missouri currently has the capacity to issue more debt, but is being prevented from doing so by Spire Inc., who needs the high cash-flow generated by Spire Missouri to meet its consistent dividend payouts. Exhibit 217C, *Surrebuttal Testimony of David Murray*, pg. 5 lns. 11 – 20. ** _____

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_____ ** This is not the appropriate outcome. Spire Missouri **should** receive credit for the debt capacity that its assets support:

> **Q. Mr. Woodard claims that your capital structure recommendation is based on your "theory that Spire Missouri should receive credit for the debt capacity its assets support." Is this theory?**
>
> A. No. **This is reality**. It is a fact that lower business risk assets can support more financial risk, i.e. debt. Spire Missouri, Spire Alabama and Spire Gulf have low business risk as demonstrated by the rating agencies' evaluation of such. This is also supported by Spire's own internal evaluations of events likely to have caused a decline in Spire Inc.'s equity value and the volatility of its stock, which was not its regulated utilities.

Exhibit 217C, *Surrebuttal Testimony of David Murray*, pg. 8 lns. 14 – 21. The only way to achieve this is to deny Spire Missouri the unrealistically high equity ratio that

it has purposefully maintained at the behest of its parent Spire Inc. and instead order a new capital structure based on a company that **is** being dynamically managed: Spire Inc.

"Spire Inc. has managed its own consolidated capital structure for purposes of taking advantage of debt capacity afforded by Spire Inc.'s low-risk regulated utility subsidiaries." Exhibit 215C, *Direct Testimony of David Murray*, pg. 41 lns. 3 – 4. Further, Spire Inc.'s internal financing documentation show ** _____

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_____ ** Spire Missouri, by contrast, shows no such considerations because it, as has already been firmly established, is not actively managing its capital structure to achieve the most cost effective outcome.

One clear example of how Spire Inc. is actively managing its capital structure can be found in its issuance of mandatory convertible equity units[5] in February of 2021. Exhibit 216, *Rebuttal Testimony of David Murray*, pg. 8 lns. 3 – 7. Such convertible equity units are considered attractive compared to common equity or traditional debt "[t]o avoid incurring immediate dilution to existing shareholders' earnings per share ("EPS"), but at the same time not incurring additional leverage (i.e. debt) that will cause pressure on a company's credit quality through further strain on its credit metrics." *Id.* at lns. 18 – 20. In this case Spire Inc. issued the convertible equity units:

> Because its stock price had declined considerably for much of 2020, reaching a low in the fall of 2020. If it had issued traditional common equity either through its at-the-market ("ATM") program or through an overnight issuance, it would have had to issue a higher number of shares than it anticipates issuing in the future to settle the investors' commitment to purchase shares at an expected higher price. Spire will avoid excess dilution to its existing shareholders to the extent it stock price increases over the next three years.

Exhibit 216, *Rebuttal Testimony of David Murray*, pg. 8 lns. 23 – pg. 9 ln. 2. The contradiction here should be obvious. Although issuing more common equity (thus

[5] Mandatory convertible equity units are:

> a type of security that offers the investor a fixed yield/dividend for the first few years from purchase (three years for Spire Inc.'s equity units) conditioned on an underlying commitment to purchase common stock in the future (in three years for Spire Inc.). The investor receives the certainty of a higher yield on the security for the first three years in exchange for foregoing potential increases in the value of the common stock over the same period (the first 20% of stock price appreciation over the next three years under the terms of Spire Inc.'s equity units).

Exhibit 216, *Rebuttal Testimony of David Murray*, pg. 8 lns. 9 – 15.

bringing Spire Inc. closer to the 54.2% common equity ratio Spire Missouri is requesting) would provide for more financial stability, this financial stability comes at a cost that Spire Inc. considered too high for its current shareholders. However, Spire Inc. does not have the same concern about requesting Spire Missouri's ratepayers pay for this higher cost.

Mr. Murray summed up Spire's rationale regarding the issuance of the mandatory convertible equity units succinctly as follows:

> During 2020, Spire Inc. recognized it needed to raise capital to fund various capital needs, but due to its stock trading at 5-year lows, it did not want to issue traditional common equity because doing so would cause too much dilution in value to existing shareholders. However, it also recognized issuing traditional debt would further strain its consolidated credit quality and reverse the progress it had been making in reducing the amount of holding company debt. Therefore, because S&P, and to some extent Moody's, would not treat the equity units as debt for purposes of evaluating the Company's financial risk, Spire considered the alternative of issuing equity units as the most cost efficient without sacrificing financial stability.

Exhibit 216, *Rebuttal Testimony of David Murray*, pg. 11 lns. 17 – 25. The problem is that "Spire Inc. does not carefully manage Spire Missouri's capital structure to achieve these same goals." *Id*. at lns. 26 – 27. Instead, "Spire Inc. manages Spire Missouri's capital structure for a desired equity ratio for ratemaking." *Id*. at lns. 27 – 28. This needs to change.

Summation

This Commission should **<u>want</u>** Spire Missouri to actively pursue the most cost efficient capital structure possible so that the Company's customers can pay the least amount while still maintaining a good credit rating for the Utility. Exhibit 215C, *Direct Testimony of David Murray*, pg. 40 lns. 8 – 11 ("[O]ne of the primary purposes of managing a capital structure [is] to achieve the lowest reasonable cost without jeopardizing financial stability."). However, this is not what has occurred. Instead, Spire Missouri is simply targeting the capital structure this Commission approved in its last rate case. *See* Exhibit 216, *Rebuttal Testimony of David Murray*, pg. 3 lns. 1 – 7. Customers have ended up paying substantially more than is necessary as a result. Tr. pg. 837 ln. 12 – pg. 838 ln. 5; *see also* Tr. pg. 819 lns. 9 – 11. Moreover, Spire Inc.'s misappropriation of Spire Missouri's excess debt capacity has impaired the latter's debt rating. Exhibit 215C, *Direct Testimony of David Murray*, pg. 42 lns. 1 – 10; Exhibit 217C, *Surrebuttal Testimony of David Murray*, pg. 6 lns. 12 – 19. It would be far less offensive if Spire Missouri's ratepayers were charged for a more costly capital structure that allowed for it to have a credit rating consistent with this lower-risk, but this is sadly not the case. Instead, the higher costs paid by Spire Missouri ratepayers is used to support Spire Inc.'s less credit worthy businesses. Exhibit 215C, *Direct Testimony of David Murray*, pg. 42 lns. 11 – 24. This should not be seen as acceptable.

There is yet a further problem, though, that has not been fully addressed. That is the fact that almost all of Spire (and for that matter Staff's) arguments simply rely

on their having not been significant changes from the previous case. *See* Exhibit 217C, *Surrebuttal Testimony of David Murray*, pg. 2 lns. 22 – 24 ("Q. Does Mr. Woodard claim that nothing has changed to cause the Commission to reconsider Spire Missouri's authorized capital structure? A. Yes. This is a main theme to Mr. Woodard's rebuttal testimony."), pg. 16 lns. 4 – 6 ("Q. What is the basis for Dr. Won's disagreement with your capital structure recommendation? A. Dr. Won cites several of the Commission's reasons from the 2017 rate case . . . ."). First, there have been no changes since the last case because Spire has been targeting the capital structure this Commission approved in its last rate case. *See* Exhibit 216, *Rebuttal Testimony of David Murray*, pg. 3 lns. 1 – 7. Second and more importantly, if the Commission accepts this line of reasoning it ensures that Spire's capital structure will **never** change. If Spire keeps targeting what the Commission sets and Staff keeps recommending what the Company targets on the basis that it hits that target, it ensures that no change will occur **no matter what happens to the capital market**. This is a problem:

> Q. . . . Can you explain to me and for the record simple terms what is the problem of a company targeting or trying to keep its debt, equity to debt ratio fairly constant?
>
> A. The same, static. Well, I think what happened in this case is proof of what the problem is. I mean, I'll venture to say that I think the Commission when it authorized the 54.2 percent equity ratio in the 2017 case that it didn't believe that it was setting what the company should use going forward. I don't know if there's anything in writing on that. I don't think that was the intention of the Commission, but the Commission knows what its intention was there. Anyway, point being is that **you definitely expect and it does happen at Spire[] Incorporated level for a company to adjust its capitalization**

> **policies based on changes in the capital markets**. Whether it's common equity valuation levels, changes in debt costs, lower business risk, issues going on with affiliates, which is very much an issue with Spire, Incorporated, and trying to keep the cost of capital low.

Tr. pg. 817 ln. 8 – pg. 818 ln. 5 (emphasis added). This is the **whole** point: a properly managed utility will "adjust its capitalization policies based on changes in the capital markets" and that is **not** what Spire Missouri is doing. *Id.*; Tr. pg. 819 lns. 1 – 8 ("So with Spire Missouri, which is set for ratemaking purposes, which we verified, it's just a matter of, you know, let's plow ahead with the highest equity ratio because that's what's going to be put into rates. They are not focusing on it for purposes of managing the financial risk, the credit metrics of Spire Missouri to achieve the most efficient capital structure which would allow for a lower cost of capital situation.").

The simplest, easiest, fastest way for the Commission to fix this problem and force Spire Missouri to actively manage its capital structure as one would expect a normal, competitive business to do is to order a capital structure that is "consistent with Spire Inc.'s consolidated capital structure ratios, net of short-term debt adjusted for CWIP balances." Exhibit 215C, *Direct Testimony of David Murray*, pg. 39 lns. 21 – 22. "This capital structure best represents the amount of debt capacity Spire Inc. considers reasonable and appropriate for its regulated utility assets, including Spire Missouri." *Id.* at lns. 22 – 24. Further, "[u]se of this capital structure ensures that Spire Missouri receives credit for the debt capacity its assets actually support." *Id.* at lns. 24 – 25. The Commission should therefore order the recommend capital structure

of OPC witness Mr. David Murray, as laid out in the beginning of this subsection, because it achieves these goals. *Id.* at lns. 21 – 25.

Return on Equity

The Commission should award Spire Missouri an allowed return on equity (ROE) of 9.25%, which is a point recommendation based on Mr. Murray's ROE range of 8.5% to 9.5%. Exhibit 215C, *Direct Testimony of David Murray*, pg. 3 lns. 5 – 6. This range in consistent with Mr. Murray's recommended ROE range of 9.0% to 9.5% in Spire Missouri's last rate case; Case No. GR-2017-0215. *Id.* at pg. 7 ln. 25 – pg. 8 ln. 2. However, this ROE recommendation is dependent on the Commission adopting Mr. Murray's capital structure recommendation. *Id.* at pg. 55 lns. 5 – 6. If the Commission adopts Staff's and Spire Missouri's recommended capital structure, Spire Missouri should instead be awarded an allowed ROE of 8.5%. *Id.* at pg. 55 lns. 6 – 8.

The OPC's witness David Murray performed a cost of equity ("COE") analysis on Spire Inc. and a local gas distribution company ("LDC") proxy group consisting of the same companies used by Spire Missouri's ROR witness, Dylan D'Ascendis. *See Id.* at pgs. 23 – 28. Mr. Murray applied two primary methodologies, a discounted cash flow ("DCF") method and the Capital Asset Pricing Model ("CAPM"), commonly used by investors to estimate the COE and fair values for utility stocks. *Id.* at pg. 23 lns. 1 – 9. Mr. Murray applied the multi-stage version of the DCF to his LDC proxy group because he determined utility industry equity investment analysts use this version in practice. *Id.* at lns. 17 – 21. Mr. Murray's DCF analysis explicitly emphasized

"equity analysts' consensus estimated dividends and the modeled growth of dividends." *Id*. at pg. 6 lns. 27 – 28. "When the DCF method is applied to dividends as the proxy for cash flow, it is more specifically defined as the dividend discount model ("DDM")." *Id*. at pg. 7 lns. 1 – 2.

Mr. Murray used equity analysts' discrete annual dividends per share ("DPS") estimates for the first stage of his analysis, then he estimated the transitionary growth rate in DPS for each company during the second stage in order for all companies to achieve a perpetual DPS growth rate in the final stage. *See Id*. at pgs. 30 – 32. This ensures the assumptions of sustainable growth are met, which are a constant dividend payout ratio (DPS/EPS) with dividends, earnings and book value growing at the same rate. *Id*. at pg. 35 lns. 4 – 11. Mr. Murray's approach and assumptions are similar to those of analyses that equity investment analysts actually use and, thus, **are similar to the type of analyses upon which investors actually rely**. *See Id*. at pg. 23 lns. 15 – 16 ("This has allowed me to test the theory of cost of capital estimation in utility ROR testimony as it compares to how utility stocks are actually valued."). The result of Mr. Murray's study was a COE of approximately 6.5% to 7.5%. *Id*. at pg. 5 lns. 6 – 7. This is the same ballpark as the 6% to 7% COE estimates utility equity analysts actually use, which further underlines how Mr. Murray's method is consistent with the **actual practice** of real equity investors. *Id*. at pg. 24 lns. 1 – 2. Even more importantly though, Mr. Murray's COE estimate **

** Exhibit 216, *Rebuttal Testimony of David Murray*, pg. 11 lns. 6 – 8.

Mr. Murray also applied the CAPM to Spire Inc. and the LDC proxy group. *See* Exhibit 215C, *Direct Testimony of David Murray*, pgs. 34 – 37. Once again, Mr. Murray used equity risk premiums consistent with the consensus **that equity investment analysts actually use**. *Id*. at pg. 34 ln. 20 – pg. 35 ln. 4. As a result, his CAPM COE estimates in the range of 5.5% to 6.75% are consistent those used by the investment community and Spire Inc. itself. *See Id*. at pg. 37 lns. 5 – 10. *Compare Id*. with Exhibit 216, *Rebuttal Testimony of David Murray*, pg. 24 lns. 6 – 7.

Staff arrived at COE estimates for Spire Missouri of 6.40% to 8.10% using a DCF method and the CAPM. Exhibit 101, *Staff Cost of Service Report*, pg. 5 lns. 15 – 16, 1 – 4. These are obviously very close to the OPC witnesses' values of 6.5% to 7.5%. *Id*. at pg. 5 lns. 6 – 7. Staff's higher DCF COE estimate of 8.10% is attributed to its assumption that LDCs can grow perpetually at a CAGR of 4.41% compared to the OPC's more modest perpetual growth rates of 0% to 3.3%. *Compare Id*. at Appendix 2, Schedule SJW-13 *and* Exhibit 215C, *Direct Testimony of David Murray*, Schedules DM-D-2 – DM-D-6. It should be noted that the OPC's assumed perpetual growth rates are consistent with those utility equity analysts (likes Wells Fargo) use in making stock recommendations. Exhibit 215C, *Direct Testimony of David Murray*, pg. 28 lns. 1 – 5. Staff's CAPM results were in the range of 5.87% to 6.85% range. Exhibit 101,

Staff Cost of Service Report, Appendix 2, Schedule SJW-14. Again, this is very similar to the OPC's result of 5.5% to 6.75%.

In contrast to both Staff and the OPC's witnesses, Spire Missouri's ROR witness, Dylan D'Ascendis, estimates a COE of 9.94% to 12.07%. Exhibit 5, *Direct Testimony of Dylan W. D'Ascendis*, pg. 5 lns. 22 – 24. The high-end of Mr. D'Ascendis COE estimates increased to 12.75% based on his opinion that the COE increased from when he filed his Direct Testimony (December 11, 2020) and his Rebuttal Testimony (June 17, 2021). Exhibit 6, *Rebuttal Testimony of Dylan W. D'Ascendis*, pg. 8 Table 1. Mr. D'Ascendis used three methodologies—a constant-growth DCF, CAPM (a standard version and an "empirical" version), and a risk premium methods applied to both a LDC proxy group and a non-price-regulated proxy group. Exhibit 5, *Direct Testimony of Dylan W. D'Ascendis*, pg. 6 ln.14 – pg. 7 ln. 4.

Because Mr. D'Ascendis' average adjusted constant-growth DCF results are around 9.95% (which is consistent with his final recommendation), it is clear that he decided to give more weight to this method as opposed to the other methods. *Id*. at Schedule DWD-D-3 pg. 1. Assuming use of reasonable inputs, utility stock prices provide valuable and logical information about utility companies' current COE. However, Mr. D'Ascendis' assumed constant/perpetual growth rates for investors' expected cash flows (through dividends) are neither reasonable nor corroborated by those actually used by investors. For example, his COE estimate of 9.95% depends on assumed perpetual growth rates of up to 10.44%. Exhibit 216, *Rebuttal Testimony of*

David Murray, pg. 19 lns. 13 – 18. **Not even the S&P 500 has achieved compound gains of this level**. *Id*.

Another problem with Mr. D'Ascendis's analysis is that he assumes DPS can grow **in perpetuity** at the same rate as a projected 5-year CAGR in EPS because, in his opinion, earnings expectations have more influence on stock prices than dividends. However, his opinion is drastically undercut by the simple fact that **

** *Id*. at pg. 20 lns. 6 – 10. Mr. D'Ascendis's argument is further weakened by a review of the relevant financial literature, which supports the position that equity analysts' stock recommendations (buy, sell, hold) influence stock prices. *See* pg. 21 ln. 15 – pg. 22 ln. 22. "To assume that investors utilize the information provided by equity analysts in a way that is wholly inconsistent with how these analysts use the data in their own analysis, is not credible." *Id*. at pg. 22 lns. 11 – 13. This would explain why ** ** *Id*. at pg. 21 lns. 5 – 14. In addition, Mr. Murray researched equity analysts' reports since January 1, 2019, provided by Spire Inc. in response to Public Counsel Data Request

No. 3005, as well as equity research reports provided in the context of past utility rate cases and through email distribution lists. Exhibit 215C, *Direct Testimony of David Murray*, pg. 24 lns. 17 – 20. However, Mr. Murray has **never** seen a professional equity analyst use his/her own projected CAGR in EPS in the context Mr. D'Ascendis assumes. Exhibit 216, *Rebuttal Testimony of David Murray*, pg. 21 lns. 1 – 4. To the extent equity analysts perform a DCF analysis, they use perpetual growth rates of around 2.7% to 3.3%, with some even assuming a decline in the LDC industry in perpetuity, *i.e.* no terminal value. Exhibit 215C, *Direct Testimony of David Murray*, pg. 23 ln. 25 – pg. 24 ln. 2, pg. 15 lns. 1 – 6.

Yet another problem with Mr. D'Ascendis's argument is the discrepancy between the market risk premiums he used and the ones used by Spire to determine the fair market value of its own assets. "Spire uses a market risk premium of ** ** for purposes of determining if the value of its assets are fairly reported on its financial statements." Exhibit 216, *Rebuttal Testimony of David Murray*, pg. 24 lns. 6 - 7. Mr. D'Ascendis, on the other hand, estimated Spire Missouri's market risk premium at 10.69%. *Id*. at pg. 23 lns. 20 – 22. As the OPC's witness Mr. Murray pointed out:

> [I]f Spire Inc. continues to view the market risk premium estimate of ** ** to be reasonable for purposes of reporting to investors the fair value of its assets, it is disingenuous for Spire Inc. to sponsor a ROR witness that estimates a much higher market risk premium for the alternate purpose of requesting a ROR for ratemaking. Considering the repercussions that would result from Spire Inc. misrepresenting its financial condition on its financial statements, the Commission should

> heavily scrutinize the discrepancy between Mr. D'Ascendis' cost of capital opinion and that of Spire's for financial reporting.

Id. at pg. 24 ln. 29 – pg. 25 ln. 4. This should be a major problem for the Commission. Spire's witness is literally recommending a position that is directly contrary to what Spire itself has used for reporting a fair carrying value of its assets on its financial statements. On the other hand, compare Spire's **actual** estimate risk premium of ** ** to the risk premium that the OPC's witness developed, which is 5.5% to 6.07%. *Id*. at pg. 24 ln. 3. The choice here should be obvious.

The key difference between the OPC's witness and Spire's witness that the OPC has been driving at is that the OPC's witness considered the fundamental issues affecting Spire Inc. and the LDC industry as a whole in his analysis instead of just regurgitating canned responses. For example, Mr. Murray specifically considered a scenario in which Spire Inc. would have a 0% perpetual growth rate, but not as pessimistic as a declining growth rate, which would be the assumption if the LDC industry becomes obsolete. *See* Exhibit 215C, *Direct Testimony of David Murray*, pg. 15 ln. 10 – pg. 16 ln. 2. Mr. Murray also analyzed the assumption of no higher than an inflationary growth rate of 2% for his LDC group. *Id*. at pg. 27 lns. 11 – 13. All of Mr. Murray's scenarios are based on issues specifically being debated by investors in evaluating the fair value of LDCs compared to electric utility companies. The 6.5% to 7.5%. COE estimates that resulted from Mr. Murray's study are corroborated by the cost of Spire Inc.'s mandatory convertible equity units (yield of 7% as of May 28, 2021). *Id*. at pg. 5 lns. 6 – 7; Exhibit 216, *Rebuttal Testimony of David Murray*, pg. 10 lns.

15 – 18. **These equity units should serve as a test of reasonableness for the various equity estimates in this case**. Exhibit 216, *Rebuttal Testimony of David Murray*, pg. 10 lns. 19 – 21.

There are yet further examples that corroborate the accuracy of the OPC's COE estimates, such as the bond-yield-plus-risk premium that Mr. Murray explains in direct:

> [A] simple rule of thumb the Chartered Financial Analyst ("CFA") suggests in its curriculum to estimate the COE is to add 3% to 4% risk premium to a company's bond yield to provide a fairly simple, but objective cost of equity. Being that the investment community views utility stocks as bond surrogates/substitutes, it is logical and reasonable to not add a risk premium any higher than 3% to the bond.

Exhibit 215C, *Direct Testimony of David Murray*, pg. 37 lns. 20 – 25. This method was applied in practice by Mr. Murray in rebuttal:

> Spire Missouri issued $305 million in aggregate principal amount 30-year bonds on May 20, 2021 at a coupon of 3.3%. Adding a 3% equity risk premium (consistent with the bond-yield-plus-risk premium level I described in my direct testimony) to this coupon implies a COE of 6.3%.

Exhibit 216, *Rebuttal Testimony of David Murray*, pg. 11 lns. 3 – 6. Mr. Murray further pointed out that his 6.5% to 7.5%. COE estimates were ** _____ _____ _____ ** and that "Wells Fargo used a 6.5% COE to estimate a fair price to pay for local gas distribution company ("LDC") stocks when it

evaluated several scenarios related to potential declines in the LDC industry." *Id*. at lns. 6 – 10. Finally, Mr. Murray pointed out that "based on Spire Inc.'s dividend yield of 3.45% as of June 1, 2021, and the expectation that utility stock capital gains are not likely to be in excess of the dividend return, a 6.9% expected return on Spire Inc.'s stock going forward is likely the high end of an expected range." *Id*. at 10 – 13. All of these factors support the OPC's witness Mr. David Murray's COE estimates of 6.5% to 7%.

Although security prices overwhelming support a low cost of capital environment, Mr. Murray recognized the Commission recently awarded The Empire District Electric Company ("Empire") a 9.25% ROE. Exhibit 215C, *Direct Testimony of David Murray*, pg. 4 ln. 23 – pg. 5 ln. 3. Mr. Murray had estimated the utility industries' COE to be even lower at that time, but accepted the Commission's zone of reasonableness standard, which dictates that the Commission will not award an ROE 100 basis points below the national average. *See Id*. at pg.5 lns. 8 – 23. Therefore, Mr. Murray compared and contrasted the electric utility industry and the LDC industry to determine if market conditions warranted a different authorized ROE for an LDC such as Spire Missouri. Mr. Murray eventually determined that LDCs stocks had been trading at a discount to electric utilities during most of 2020, despite the fact that they had traded at a premium to electric utilities from January 1, 2015 through December 31, 2019. *Id*. at pg. 12 lns. 1 – 8. Consequently, and although he recommends Spire Missouri be authorized an ROE similar to that which the Commission awarded Empire, he increased the upper-end of his recommended ROE

range by 25 basis points due to his comparative analysis of the LDC and electric utility equity market conditions. *Id*. at pg. 2 ln. 28 – pg. 3 ln. 6. Finally, as a safeguard, Mr. Murray analyzed the impact that his recommended 9.25% ROE as applied to his recommend capital structure would have on Spire Missouri's FFO/debt ratios (one of the key benchmark credit ratios followed by rating agencies) and determined that it "would be approximately 15.45%." *Id*. at pg. 51 ln. 27. "This FFO/debt ratio is consistent with that which Spire targets on a consolidated basis." *Id*. at lns. 27 – 28. "Therefore, if Spire Missouri was allowed to use its own debt capacity, it would still be able maintain a strong credit rating while charging ratepayers approximately $34 million/year less in revenue requirement." *Id* at pg. 51 ln. 28 – pg. 52 ln. 2.

Cost of Debt

Spire Missouri's cost of long-term debt is 3.99% as of May 31, 2021. Exhibit 241, *True-up Direct Testimony of David Murray*, pg. 7 lns. 24 – 27. Spire Missouri's cost of short-term debt is 0.29% as of March 31, 2021. *Id*. This was provided by the Company in an update to a Staff data request. *Id*. In addition, the OPC's witness noted the following in true-up rebuttal:

> Spire Missouri did not provide a cost of short-term debt for the period through May 31, 2021 in response to Staff Data Request No. 110. However, Spire Inc.'s recently released June 30, 2021 SEC Form 10-Q, Note 5. to the Financial Statements indicates that Spire Missouri's weighted average cost of commercial paper for the nine months ended June 30, 2021, was 0.2%. The same note indicates that Spire Missouri's weighted-average interest rate on a $250 million term loan is 0.8%.

Exhibit 242, *True-up Rebuttal of David Murray*, pg. 5 lns. 7 – 12. No other party appears to have filed testimony regarding Spire's cost of short-term debt.

Conclusion

There are three issues at play with regard to Spire's rate of return. The first is the inclusion of short-term debt. In this case, the amount of short-term debt that Spire is carrying on its books greatly exceeds the amount of short-term assets (including CWIP). *See* Exhibit 216, *Rebuttal Testimony of David Murray*, pg. 15 lns. 1 – 7; Exhibit 217C, *Surrebuttal Testimony of David Murray*, pg. 13 ln. 5 – pg. 14 ln. 7; Exhibit 242, *True-up Rebuttal of David Murray*, pg. 2 lns. 9 – 20. The amount of short-term debt that exceeds the short-term assets (including CWIP) should therefore be included in the authorized ratemaking capital structure. *See* Tr. pg. 799 ln. 12 – 17, pg. 830 ln. 10 – 14. The second is the fact that Spire Missouri is currently targeting its previously approved capital structure to the benefit of Spire Inc. and the detriment of its customers. Exhibit 216, *Rebuttal Testimony of David Murray*, pg. 3 lns. 1 – 7; . pg. 837 ln. 12 – pg. 838 ln. 5, pg. 819 lns. 9 – 11; Exhibit 215C, *Direct Testimony of David Murray*, pg. 40 ln. 1 – pg. 41 ln. 23. This has resulted in Spire Missouri having more equity and less debt than three of its substantially more risky affiliate entities, which contradicts the basic principles of finance. Exhibit 217C, *Surrebuttal Testimony of David Murray*, pg. 8 ln. 22 – pg. 9 ln. 19; Tr. pg. 862 ln. 15 – pg. 827 ln. 7; Exhibit 217C, *Surrebuttal Testimony of David Murray*, pg. 8 lns. 17 – 18. It has also resulted in Customers paying tens of millions of dollars more per year than they need to. Tr. pg. 819 lns. 9 – 11; Exhibit 215C, *Direct Testimony of David Murray*, pg.

51 ln. 28 – pg. 52 ln. 2. The simple answer to this problem is to set a new capital structure guided by the actively managed capital structure of Spire Inc., the parent company of Spire Missouri. Exhibit 215C, *Direct Testimony of David Murray*, pg. 39 lns. 21 – 25.

The third issue is the question of what return on equity the Commission should order. The answer is the 9.25% recommended by the OPC's witness. Exhibit 215C, *Direct Testimony of David Murray*, pg. 3 lns. 5 – 6. This was developed using an approach and assumptions that mirrored those that equity investment analysts actually use and rely upon. *Id*. at pg. 23 lns. 15 – 16. Moreover, the methods and inputs used resulted in outcomes that are largely consistent with the same conclusions drawn by Staff. *Compare Id*. at Appendix 2, Schedule SJW-13 *and* Exhibit 215C, *Direct Testimony of David Murray*, Schedules DM-D-2 – DM-D-6. The recommendation offered by Spire, by contrast, relies on unrealistic assumptions that sometimes even contradict the Company's own internal metrics. *See* Exhibit 216, *Rebuttal Testimony of David Murray*, pg. 19 lns. 13 – 18; Exhibit 216, *Rebuttal Testimony of David Murray*, pg. 24 ln. 29 – pg. 25 ln. 4. Therefore, the Company's recommendations should not be used.

Based off all this analysis, the outcome that the Commission should order is a capital structure comprised of 45.00% common equity, 48.00% long-term debt and 7.00% short-term debt; a return on equity of 9.25%; a cost of long-term debt of 3.99%; and a cost of short-term debt of 0.29%. Exhibit 241, *True-up Direct Testimony of*

David Murray, pg. 7 lns. 19 – 27; Exhibit 215C, *Direct Testimony of David Murray*, pg. 3 lns. 5 – 6.

Issue 8. Cash Working Capital

The Commission should not accept the position offered by the Company, and accepted by Staff, to calculate CWC for income tax purposes based on assumed quarterly income tax payments because Spire does not – and will not – make quarterly income tax payments to the IRS. Instead, the Commission should order its Staff to calculate CWC for income tax purposes using a 365-day expense lag (*i.e.* one full year) to properly account for the fact that Spire collects money to pay income taxes from customers but does not thereafter pay income taxes to a taxing authority during the course of the year.

Analysis

The error committed by Spire and Staff with regard to this issue is clear and simple. The Company has argued, and Staff has accepted, CWC calculations related to state and federal income taxes based on the assumption that Spire will make quarterly income tax payments. Exhibit 26, *Rebuttal Testimony of Timothy S. Lyons,* pg. 4 lns. 11 – 14; Exhibit 119, *Rebuttal Testimony of Antonija Nieto*, pg. 3 lns. 14 – 17. The IRS does not require a corporation to make quarterly income tax payments if the Corporation does not expect to incur taxes in excess of $500. 26 USC §6655(f); *see also* Exhibit 49, *IRS Publication 542*, pg. 6 ("Generally, a corporation must make installment payments **if it expects its estimated tax for the year to be $500 or more**." (emphasis added)). Spire will consequently not make quarterly income tax payments because they will not have to remit any tax at any point in the near future.

Tr. pg. 525 lns. 13 – 21; pg. 624 lns. 12 – 15. This is corroborated by the fact that "Spire Inc.'s state and federal income tax returns, the Company's annual report filed with the Commission, and the public 10-K reports all indicate that both the parent company and Spire Missouri have not been required to pay income tax in at least the last three years." Exhibit 209, *Direct Testimony of John S. Riley*, pg. 9 lns. 4 – 6. It is further corroborated by the fact that **

** Exhibit 211, *Surrebuttal Testimony of John S. Riley*, JSR-S-03, pg. 11 lns. 1 – 4. Finally, it is corroborated yet further by the fact that Spire's net operating loss carryforward balance has been steadily increasing, which is consistent with statements made "in the Company['s] most recent 10-K, which eliminated past and future tax liabilities." Tr. pg. 647 lns. 6 – 8; Exhibit 211, *Surrebuttal Testimony of John S Riley*, pg. 11 fn. 10; Exhibit 209, Direct Testimony of John S Riley, JSR-S-03, pg. 9 fn. 7.

The overwhelming and uncontroverted evidence demonstrates that Spire will not need to make quarterly income tax payments. Therefore, assuming quarterly income tax payments when calculating the Company's income tax CWC requirement is a clear error. Exhibit 211, *Surrebuttal Testimony of John S Riley*, pg. 4 lns. 9 – 10. A utility does not need "a rate base component that represents a measurement of the amount of funds, on average, required for the payment of a utility's day-to-day expenses" to account for paying income taxes **if that utility does not pay income taxes**. Exhibit 209, *Direct Testimony of John S Riley*, JSR-S-03, pg. 8 lns. 5 – 7, pg. 9 lns. 6 – 10. Neither Spire nor Staff have provided any real response to this argument,

or, indeed, have even attempted to rebut the basic factual point that the Company will not make quarterly income tax payments. This raises the serious question of why Spire, and more importantly Staff, even adopted this position in the first place.[6]

It would appear that Staff did eventually realize the error in its own position, because it attempted to raise a completely new argument for the first time during the hearing. Tr. pg. 520 ln. 17 – pg. 521 ln. 9. Having finally recognized that calculating CWC based on assumed quarterly tax payments made no sense when Spire did not make quarterly tax payments, Staff effectively sought to adopt Spire's *alternative* argument raised in the rebuttal testimony of Company witness Mr. Timothy Lyons. *Id*. Mr. Lyon's argued that "if the Commission determines in this rate case proceeding that the Company has no income tax expenses, then the Company's cash working capital requirement related to income tax payments would be zero." Exhibit 26, *Rebuttal Testimony of Timothy S. Lyons,* pg. 4 lns. 19 – 22. It is immensely dishonest for the Company to even take this position given that it knows **full well** that it will not pay income taxes at any point in the near future. Tr. pg. 525 lns. 13 – 21; pg. 624 lns. 12 – 15. In doing so, Spire is effectively claiming that: "if the Commission realizes that the Company misled the Commission about having to make quarterly income tax payments (because it does not actually pay any taxes), then the Commission should just overwrite the amount of income tax expense included in Spire's rates and

[6] It would appear that Staff's position was really just born out of inertia. In other words, Staff adopted this position simply because that is what it had always done. Tr. pg. 493 lns. 11 – 12 ("Well, Staff has traditionally used this approach to develop the expense lag for income taxes.").

fudge the CWC calculations so that the result comes out to be zero." The inequity and inaccuracy with this argument is obvious.

Due to IRS normalization requirements, Spire's rates must be set using an assumed amount of current income tax expense – even if that same amount may end up being deferred and thus not paid to any federal or state government. 510 ln. 18 – pg. 511 ln. 19, pg. 259 lns. 22 – 24; Exhibit 209, *Direct Testimony of John S Riley*, pg. 9 ln. 14 – pg. 109 ln. 18. Therefore, the calculation of Spire's revenue requirement includes a non-zero amount of current income taxes. Exhibit 102, Full Staff Accounting Schedule, Accounting Schedule 1 pg. 1 of 1 ln. 7; Exhibit 209, *Direct Testimony of John S Riley*, pg. 7 lns. 16 – 17. To simply change the dollar amount included for state and federal income taxes to be zero dollars in the CWC calculation would thus be inconsistent with reality. Tr. pg. 510 ln. 18 – pg. 511 ln. 24. Moreover, such a result would not be supported by – and would directly contradict – the factual record. Exhibit 102, Full Staff Accounting Schedule, Accounting Schedule 1 pg. 1 of 1 ln. 7. Thus, the Commission cannot just "put zero in for the income tax portion of CWC" as Staff and Spire suggest.[7]

[7] One point to note is that Mr. Lyon's statement that "if the Commission determines in this rate case proceeding that the Company has no income tax expenses, then the Company's cash working capital requirement related to income tax payments would be zero" is *technically* correct. Exhibit 26, *Rebuttal Testimony of Timothy S. Lyons,* pg. 4 lns. 19 – 22. However, that is only because Mr. Lyon only refers to "income tax **expenses**." Income tax "expenses" are different from income tax "payments." The former refers to what the Company collects from customers, the latter to what the Company pays to the relevant taxing authority. This is a subtle **but important** difference. If Spire's income tax **expenses** were zero, then the Company would not collect **any** income tax expense from customers and thus the CWC calculation really would be zero. In this case, though, the income tax expense is not zero. Exhibit 102, Full Staff Accounting Schedule, Accounting Schedule 1 pg. 1 of 1 ln. 7. Therefore, Mr. Lyon's statement is largely meaningless. The OPC's position, on the other hand, is based on the fact that Spire's income tax **payments** are zero. That means that Spire is collecting money from its

We have now established the only two necessary points required to demonstrate the error committed by the Company and Staff, which are:

1. Spire has included current income tax expense in its revenue calculations (as required by IRS rules) and is thus going to collect an amount to cover income taxes from its customers. Exhibit 102, Full Staff Accounting Schedule, Accounting Schedule 1 pg. 1 of 1 ln. 7.

2. The uncontroverted evidence shows that Spire will not actually pay income taxes at any point in the near future. Tr. pg. 525 lns. 13 – 21; pg. 624 lns. 12 – 15.

Given these two points, it should become clear that the only logical option when calculating the income tax component of CWC is the one presented by the OPC. "If you have no cost (payments) at any time during the year, then your lag would be an entire year." Exhibit 209, *Direct Testimony of John S Riley*, pg. 9 lns. 12 – 13. Stated in a different way, the expense lag for the income tax component of CWC should be 365 days.[8] *Id*. at ln. 13. As explained by OPC witness John Riley:

> There [] needs to be a 365 day lag to reflect the inflow, yet nonpayment of, the calculated income tax built into the Company revenue requirement. There is no other rational view. The Company is afforded an income tax expense in rates but does not have to pay and will not

customers to pay taxes but then not paying taxes out to the relevant taxing authority. Exhibit 209, *Direct Testimony of John S Riley*, pg. 9 ln. 14 – pg. 109 ln. 4.

[8] Please note, Mr. Riley refers to a "negative 365 day" expense lag in testimony. This may cause some confusion due to how the net lag is calculated. The expense lag is normally offset against the revenue lag to produce the net lag that is used in the calculation of CWC. This can be done by either adding a negative expense lag (which is what Mr. Riley refers to) or subtracting a positive expense lag. In either case, the expense lag should end up reducing the revenue lag. With regard to the OPC's calculation, this results in a "change to the Company's working capital requirement for income taxes from a positive $446,136 to a negative $12,643,686." Exhibit 209, *Direct Testimony of John S Riley*, pg. 10 lns. 23 – 24.

> have to pay the money to a taxing authority through the period that these rates will be in effect. This is a negative CWC requirement.

Exhibit 211, *Surrebuttal Testimony of John S Riley*, pg. 10 lns. 12 – 16. To do anything different would be to ignore the plain reality of the situation and deny customers what little benefit they will receive for paying to cover taxes that are not actually remitted by Spire.

As on final point, the OPC would make two observations. First, the OPC would note that having such a large expense lag is not entirely out of the ordinary. The expense lag for property taxes, for example, is also quite large to account for the fact that property taxes are not paid until the end of the year. Tr. pg. 513 ln. 17 – pg. 514 ln. 21. The OPC's argument regarding income taxes is hence nothing more than a logical extension of the practices already in place. *Id*. The only real exception is that, because income taxes are **never** paid out, the expense lag should be the **entire** year. *Id*. The second issue to address is the possible concern that some change in circumstances might mean that Spire would have to start paying income taxes again in the future. To begin with, there is no actual evidence that any such change is going (or is even likely) to occur. Second, the existing ISRS statutes make it very likely that Spire will be back before this Commission for another rate case in three years. RSMo. § 393.1012.2. Thus, the likelihood of some change in circumstance requiring Spire to begin paying taxes again within the time before Spire will almost certainly be back for another general rate case is **extremely small**. Moreover, *even if such a change did occur*, Spire is at liberty to just file another rate case and thus correct the problem. Tr. pg. 252 lns. 6 – 9. There is consequently no logical reason to assume that the

proffered highly unlikely and easily fixable hypothetical scenario should impact the Commission's decision on this point to any degree whatsoever.[9]

Conclusion

The uncontroverted evidence shows that spire has not and will not pay income taxes on a quarterly basis. Therefore, the Company and Staff's calculation of the expense lag for income taxes (for CWC purposes) based on assumed quarterly income tax payments is a clear error. Exhibit 210, *Rebuttal Testimony of John S Riley*, pg. 4 lns. 6 – 16; *see also* Exhibit 211, *Surrebuttal Testimony of John S Riley*, pg. 10 lns. 8 – 9. Instead, the correct calculation would require including "a 365 day lag to reflect the inflow, yet nonpayment of, the calculated income tax built into the Company revenue requirement." Exhibit 211, *Surrebuttal Testimony of John S Riley*, pg. 10 lns. 12 – 13. The Commission should thus issue an order requiring Staff to recalculate the CWC related to income tax expenses based on a 365-day expense lag.

[9] This is to say nothing of the legal error that would be committed by requiring the party who does **not** bear the burden of proving the just and reasonable nature of Spire's rates to disprove a hypothetical. In other words, because Spire has the burden of proving that its rates are just an reasonable, Spire must prove that the OPC's adjustment to the CWC calculation would result in rates that are not just and reasonable, not the other way around. RSMo. § 393.150.2. This would include proving the likelihood of any presumed change in circumstances.

Issue 13. Incentive Compensation

A properly designed incentive compensation program will result in Spire receiving and retaining earnings in excess of the cost to run the program. Therefore, a properly designed incentive compensation program will generate positive regulatory lag that will cover the cost of the program itself. To allow Spire to simultaneously recover the cost of the program through rates will consequently result in double-recovery: first through positive regulatory lag, and then again through rates. The Commission should not allow Spire to double-recover the cost of its incentive compensation programs by including those costs in rates.

Analysis

Let us begin by stressing one important point: no party is arguing for the discontinuation or modification of Spire's incentive compensation plans. Instead, the argument presented comes down to how to **pay** for these plans. This is important because Spire (and likely Staff) will almost certainly attempt to justify the cost recovery for these plans based on the benefit the plans generate for customers. **Any argument based on the benefits of these plans is wholly and completely irrelevant**. The fact that Spire's customers will ultimately benefit from these plans should not be used to justify double-recovery of the cost of the plans. If, however, the Company is allowed to recover the cost of these plans in rates, it **will** double-recover the cost of these plans. Such double-recovery would violate Missouri statute, as it will result in rates that are not just and reasonable. RSMo. § 393.150.2.

Before our analysis goes any further, we should stop and establish exactly why allowing cost recovery of the incentive plan in rates will result in double-recovery. The answer comes down to two simple facts:

1. A prudently designed incentive plan will generate earnings (through either increased revenue or decreased expense) for the utility in an amount greater than the cost to operate the plan itself. Tr. pg. 559. lns. 15 – 18; Tr. pg. 542 lns. 22 – 25; Tr. pg. 552 lns. 2 – 25; Tr. pg. 576 lns. 3 – 17.

2. The earnings generated by an incentive plan between rate cases will be retained by the utility and thus increase the utility's bottom line. Tr. pg. 560 ln. 22 – pg. 561 ln. 12.

Based on these two facts, it is clear that a prudently designed incentive plan will cause a utility to generate and retain more earnings than the plan costs to operate between rate cases. The earnings that are generated and retained by the utility between rate cases are what pays for the plan.[10] Tr. pg. 576 lns. 11 – 17. If customers where then required to *further* pay for the plan a **second** time (*i.e.* through rates), it would result in the utility recovering twice: once through the generated and retained earnings and a second time through the rates collected from customers. Tr. pg. 576 ln. 25 – pg. 577 ln. 3. Because the utility has recovered twice, it has double-recovered the cost of the incentive plan.

There is a specific name for the phenomenon where a Company recovers costs for a program through the time delay between when revenue is generated and when

[10] We obviously know that these earnings pay for the **entire** plan because they exceed the cost of the plan per the first point.

that revenue is reflected in rates. Exhibit 136, *Surrebuttal Testimony of Antonija Nieto*, pg. 6 lns. 6 – 7. The name of that phenomenon is "positive regulatory lag." Tr. pg. 560 ln. 22 – pg. 561 ln. 12. In this circumstance, the OPC's argument is that Spire will recover the cost of the incentive programs through positive regulatory lag, and thus, the cost of those programs do not need to be included in rates. The tremendous irony of the present situation is that Staff raised nearly the **exact same argument** in relation to a different form of cost expense *in this same case*, which Staff sought to disallow. Exhibit 136, *Surrebuttal Testimony of Antonija Nieto*, pgs. 6 - 7. With regard to severance compensation, Staff stated as follows:

> In this case[,] the Company could have experienced what's commonly known as a "positive regulatory lag," meaning that by the time current rates are changed from this rate case, Spire will have recovered directly in rates more dollars from terminated employee salary and benefits compensation than it expended in severance costs. Staff did not confirm if those specific positions freed by severed employees were filled.

Exhibit 136, *Surrebuttal Testimony of Antonija Nieto*, pg. 6 lns. 19 – 23. Staff went on to provide a specific numerical example as to how that recovery might look and concluded by stating "[s]everance costs would be significantly over-recovered by the time new rates are implemented." Exhibit 136, *Surrebuttal Testimony of Antonija Nieto*, pg. 7 lns. 1 – 7. Staff consequently argued the Commission should disallow recovery of severance compensation. Tr. pg. 562 lns. 1 – 4; Exhibit 101, *Staff Cost of Service Report*, pg. 69 ln. 5.

The OPC's position on this issue is literally nothing more than the application of Staff's own logic to the issue of incentive compensation. In other words, if one takes

the **exact same logic** Staff applied to argue that severance costs should be disallowed and applies it to the incentive compensation, the outcome should be the exact same: incentive compensation should also be disallowed to prevent significant over-recovery. There is only one real difference between severance expense and incentive compensation with regard to this argument, which is that, for severance expense, positive regulatory lag is only a **possibility**, while, for incentive compensation, positive regulatory lag is **guaranteed** to occur.[11] However, this difference only makes the OPC's argument *more* compelling because it means that Spire is literally guaranteed recovery of its compensation incentive plan through positive regulatory lag.

There is no legitimate logical reason for why Staff would argue to disallow the cost of severance compensation based on a *possible* threat that positive regulatory lag would result in double-recovery while still advocating for the inclusion of incentive compensation for which positive regulatory lag *guarantees* double-recovery.[12] Nor is

[11] In the case of severance compensation, it is possible for the Company to not experience positive regulatory lag if another employee (at the same salary and benefits) immediately fills the position of the individual leaving the company. Under that circumstance, there is no way for Spire to "recovered directly in rates more dollars from terminated employee salary and benefits compensation than it expended in severance costs" because it is paying the same amount of salary and benefits compensation to the new employee. Exhibit 136, *Surrebuttal Testimony of Antonija Nieto*, pg. 6 lns. 21 – 22. This is why Staff had to explicitly note that it "did not confirm if those specific positions freed by severed employees were filled." Exhibit 136, *Surrebuttal Testimony of Antonija Nieto*, pg. 6 lns. 22 – 23. When it comes to incentive compensation, however, the exact opposite occurs. Because an incentive compensation plan does not pay out **until** benefits are achieved, the revenue increase or expense reduction occurs **before** the cost is incurred. Thus, there is no way for the Company to not earn more than it is paying, **as long as the program is prudently designed**. Tr. pg. 559. Lns. 15 – 18; Tr. pg. 542 lns. 22 – 25; Tr. pg. 552 lns. 2 – 25; Tr. pg. 576 lns. 3 – 17. Consequently, positive regulatory lag is quite literally **guaranteed** to occur with a prudently designed compensation incentive plan.

[12] While there is no **logical** reason, there is an obvious practical reason. Once again, Staff's position in this case is nothing more than inertia at work. This is made quite evident in the surrebuttal testimony of Staff witness Jeremy Juliette who expressly based his decision on the fact that the

there any real argument that the incentive plans will not result in double-recovery. In fact, the only real effort made to rebut this fact is a single line from Staff Witness Juliette's testimony that reads, "'Double recovery' is not an issue as the savings from the plan achievements are included in the cost of service as reductions in cost or increases in revenue. . . ." Exhibit 131, *Surrebuttal Testimony of Jeremy Juliette*, pg. 9 lns. 9 – 10. However, this point was demonstrated to be inaccurate during cross-examination. The problem lies with the fact that the double-recovery stems from the positive regulatory lag that occurs **before** "the savings from the plan achievements are included in the cost of service." The savings that have already been achieved, on the other hand, have also already been paid for, so there is no need to include the cost of *those* plans in rates:

> Q. Okay. So the benefits that have already been achieved, they're built into rates. We do not need to worry about them. Right?
>
> A. When you say benefits, you're talking about the cost savings?
>
> Q. Either reduced O&M or -- just reduced costs or increased revenue. Either way, the ones that have already achieved, they are already in rates. We don't need to worry about them?

Commission has allowed recovery of certain incentive plan costs in the past. Exhibit 131, *Surrebuttal Testimony of Jeremy Juliette*, pg. 9 lns. 1 – 3. This is, of course, meaningless from a legal standpoint because it is well established law that the Commission is not bound by the doctrine of *stare decisis*. *See*, *e.g.*, *State ex rel. Laclede Gas Co. v. PSC*, 392 S.W.3d 24, 36-37 (Mo. App. WD 2012) ("The Commission 'is not bound by stare decisis based on prior administrative decisions.'" (citing *State ex rel. Aquila, Inc. v. Pub. Serv. Comm'n of Mo.*, 326 S.W.3d 20, 32 (Mo. App. WD 2010); *State ex rel. GTE North, Inc. v. Mo. Pub. Serv. Comm'n*, 835 S.W.2d 356, 371 (Mo. App. WD 1992))). What is even **more** compelling, however, is the fact that Mr. Juliette goes on to acknowledge that the OPC's argument regarding double-recovery "has never been presented in the context of incentive compensation issues." Exhibit 131, *Surrebuttal Testimony of Jeremy Juliette*, pg. 9 lns. 6 – 7. Thus we see the problem whole. Staff has literally never been presented with or forced to consider the OPC's argument regarding incentive compensation before now and has therefore decided to steadfastly ignore the argument because it is inherently incapable of doing otherwise. Staff has instead adopted a position that directly contradicts the logic it applied to other issues in this case simply and solely to conform with what the Commission has ordered in the past. This is not how Staff should operate.

A. As long as they are in the test year. Yes.

Q. We don't have to include costs to pay for those benefits we've already achieved. We're looking for cost to achieve new benefits. Right?

A. That is correct.

Tr. pg. 559 lns. 1 – 14 (emphasis added). This is a very important point, so let us review it again. The idea that double-recovery is not an issue because the savings from the plan have already been included in rates is wrong. What has been included in rates are the benefits that have been **previously achieved**. Tr. pg. 559 lns. 1 – 10. Those benefits have already been paid for. *Id*. The issue before the Commission is the inclusion of costs to achieve **new** benefits. Tr. pg. 559 lns. 11 – 14. These **new** benefits have not yet been included in rates and will thus result in positive regulatory lag and add to Spire's bottom line:

Q. Okay. So in your surrebuttal testimony you acknowledge the fact that the Company is going to increase its bottom line in between rate cases because of the incentive plan. Do you agree with that?

A. Yes.

Q. Would you qualify that increase to bottom line as regulatory lag?

A. As my surrebuttal stated, if the Company recognizes revenues greater than what is built into rates, then yes, they would get to keep that in between rate cases.

Q. So would you agree with me that we could use the term positive regulatory lag to describe that phenomenon?

A. Positive for the Company?

Q. Yes.

A. Yes.

Tr. pg. 560 ln. 22- pg. 561 ln. 12. Thus, the existence of positive regulatory lag and the double-recovery that stems from it is effectively uncontroverted.

This point cannot be stressed enough. Both Staff and Spire's witnesses acknowledged that a prudently designed incentive plan will generate earnings (either through increased revenue or decreased expense) for the utility in an amount greater than the cost to operate the plan itself. Tr. pg. 559. lns. 15 – 18; Tr. pg. 542 lns. 22 – 25; Tr. pg. 552 lns. 2 – 25. As we have just seen, Staff fully agrees that these earnings will be retained by the Company and increase Spire's bottom line. Tr. pg. 560 ln. 22- pg. 561 ln. 12. Because the earnings from the incentive plan are greater than the cost of the incentive plans and because the incentive plans do not trigger payments (*i.e.* costs) until *after* the cost savings are achieved, Spire's incentive plans will necessarily pay for themselves. Tr. pg. 576 lns. 11 – 17. Because the incentive plans will necessarily pay for themselves, asking customers for further payment for the plans will necessarily result in double-recovery: once through the generated and retained earnings and a second time through the rates collected from customers. Tr. pg. 576 ln. 25 – pg. 577 ln. 3. There is no evidence in the record to contradict this very basic premise.

Given that double-recovery has been more or less unquestionably established, there remains only the question of whether Spire should be permitted to double-recover the cost of its incentive programs. The only perceivable argument that the Company (or Staff) may be expected to muster for why Spire should be permitted to double-recover is that these incentive compensation programs provide benefits to

customers. Needless to say, the fact that customers benefit from the Company's incentive compensation plan does not justify double-recovery of those program costs by Spire. Customers also benefit from Spire having a natural gas distribution system, from having a customer call center, or from engaging in necessary pipe replacements, yet for none of these things is the Company allowed to double-recover its costs. In fact, there is **no** other cost incurred by Spire for which the Company is allowed to double-recover, regardless of what "benefits" might be achieved for customers. This includes severance costs that, again, even Staff sought to disallow recovery of due, in part, to the need to prevent double recovery. Exhibit 136, *Surrebuttal Testimony of Antonija Nieto*, pg. 6 lns. 19 – 23; pg. 8 lns. 1 – 2. There is just no logical argument for allowing Spire to double-recover the cost of the incentive compensation program.

Conclusion

Spire's incentive program improves Spire's bottom line. Tr. pg. 559 lns. 1 – 14. In its filed revenue requirement report, Staff cited the Commission's *Report and Order* from Spire West's 2004 rate case to support its position. Exhibit 101, *Staff Cost of Service Report*, pg. 66 ln. 30 – pg. 67 ln. 17. That Commission decision stated, "[i]mprovements to the company's bottom line chiefly benefit the company's shareholders, not its ratepayer." GR-2004-0209, *Report and Order*, pg. 43; Exhibit 101, *Staff Cost of Service Report*, pg. 66 ln. 30 – pg. 67 ln. 17. The Commission further went on to state:

> If the company wants to have an incentive compensation plan that rewards its employees for achieving financial goals that chiefly benefit

shareholders, it is welcome to do so. **However, the shareholders that benefit from that plan should pay the costs of that plan**.

GR-2004-0209, *Report and Order*, pg. 43 (emphasis added); Exhibit 101, *Staff Cost of Service Report*, pg. 66 ln. 30 – pg. 67 ln. 17. Because the incentive compensation programs in this case will improve the Company's bottom line, they also chiefly benefit the Company's shareholders and not its ratepayers. The cost of these incentive programs should therefore be borne by Spire's shareholders, just as the Commission decided in 2004. GR-2004-0209, *Report and Order*, pg. 43. However, the rationale for not allowing cost recovery of these programs is even more compelling than just that. The incentive programs not only benefit shareholders by increasing the bottom line; they also pay for themselves by producing earnings in excess of their cost. Tr. pg. 559. lns. 15 – 18; Tr. pg. 542 lns. 22 – 25; Tr. pg. 552 lns. 2 – 25; Tr. pg. 576 lns. 11 – 17.Forcing ratepayers to cover the cost of these programs will consequently result in Spire double-recovering its costs. Tr. pg. 576 ln. 25 – pg. 577 ln. 3. There is no rationale justification for allowing this, so the Commission should not allow it. The Commission should issue an order disallowing cost recovery of all incentive compensation plans because those costs are already recovered through positive regulatory lag.

Issue 15. Capitalization of Overheads

Spire Missouri is improperly capitalizing overheads to construction projects because Spire cannot establish a definite relationship between the overhead costs and the construction projects. This is a violation of the Commission's rule requiring the gas company to operate in accordance with the Uniform System of Accounts. To resolve this problem, the Commission should order Spire to cease capitalizing general overheads that do not have a definite relationship to construction and further order a tracker to ensure that Spire Missouri's general overhead are not being over-recovered.

Analysis

The underlying argument for this issue is remarkably simple. Commission rules prohibit a utility from capitalizing overheads to construction projects absent a definite relationship to that project. Spire is violating that rule because it is capitalizing overheads to construction projects without showing a definite relationship. To properly examine this issue, it is best to break it down into parts.

What are Capitalized Overheads?

Staff witness Mr. Matthew R. Young provides the following explanation of capitalized overheads in his rebuttal testimony:

> The most basic description is capitalized overheads are costs that are indirectly related to a capital project. Overheads of this type are allocated to construction work orders and are ultimately reflected in the plant-in-service component of rate base. Some examples of capitalized

> overheads are provided by the Uniform System of Accounts ("USOA"), which identifies engineering, supervision, general office salaries and expenses, construction engineering and supervision by others than the accounting utility, law expenses, insurance, injuries and damages, relief and pension, taxes, and interest as indirect capital costs.

Exhibit 125, *Rebuttal Testimony of Matthew R. Young*, pg. 1 ln. 23 – pg. 2 ln. 5. The OPC's witness Mr. Robert Schallenberg notes that Spire ** _____

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_____ ** Exhibit 203C, *Direct Testimony of Robert E. Schallenberg*, pg. 23 lns. 26 – 28. This is the issue in this case.

<u>What is the USOA and What does it Require?</u>

The OPC's expert witness explained the intricacies of the USOA as it relates to this issue in his direct testimony: **

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** *Id*. at pg. 22 ln. 20 – pg. 23 ln. 22. This excerpt will largely form the basis of the rest of our analysis.

What are the Concerns Regarding Spire and the USOA in this case?

The concerns related to overhead costs Spire Missouri charges to construction projects are laid out in Mr. Schallenberg's direct testimony: **

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** *Id*. at pg. 23 lns. 31 – 36. These are reflected in Staff witness Young's testimony. Exhibit 125, *Rebuttal Testimony of Matthew R. Young*, pg. 2 lns. 7 – 10 ("Mr. Schallenberg identifies two concerns about capitalized overheads. First, OPC is concerned with the risk of Spire over-capitalizing costs to the extent it would be an abuse of the ISRS surcharge mechanism. Second, OPC is concerned that Spire would use a capitalization methodology that is prohibited by the USOA."). Mr. Young further elaborates on these concerns in his rebuttal:

> Q. Regarding OPC's first concern, are there any risks regarding the amount and timing of Spire's overhead capitalization?
>
> A. Yes, there are risks that are present with or without an ISRS surcharge and are driven by rate-base regulation as well as accounting methodology. Since the size of a utility's rate base drives the utility's earnings, Spire may find an incentive to increase the amount of capitalized costs for the sole purpose of maximizing it rate of return. Under rate-base regulation, a utility that increases its rate base value can increase the amount included in rates for its opportunity for earnings.
>
> Additionally, Spire can alter its net income through changes to its methodology for accounting for overheads. For example, if Spire were to remove an overhead expense from the income statement (by charging the cost to plant-in-service), the immediate impact would be a reduction to expenses, which leads to an artificial increase in earnings. In other words, rather than increasing its earnings by controlling costs or increasing revenue, there is a risk Spire would increase its earnings by manipulating its capitalization accounting methodology and at the same time, increase the size of its regulated rate base.

Q. Is there an audit risk that is specific to the ISRS surcharge?

A. Yes. A consequence of the single-issue ratemaking nature of the ISRS surcharge is that it creates an incentive for Spire to maximize the costs charged to ISRS eligible work orders. The ISRS surcharge presents an opportunity for Spire to increase its revenue without the need of a rate case, which would consider all relevant factors to establish a holistic cost of service. Additional incentive is added through the mitigation of regulatory lag that the ISRS surcharge provides. As such, Spire has an incentive to maximize its ISRS revenue which can be achieved by inflating the cost of ISRS-eligible rate base via excessive capitalized overheads.

Id. at pg. 2 ln. 11 – pg. 3 ln. 12. Now that the issue has been properly laid out, the next step is to examine the evidence to see if Spire can prove that it is meeting the requirements of the USOA.

Spire has been Unable to Prove that it is Meeting the Requirement of the USOA

Spire cannot prove that it is in compliance with the requirements of the USOA regarding the capitalization of overheads to construction projects. This was the conclusion reached independently by both the OPC and Staff's expert witnesses. For example, the OPC's expert witness stated as follows in direct: **

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** Exhibit 203C, *Direct Testimony of Robert E. Schallenberg*, pg. 24 lns. 1 – 19. Mr. Schallenberg expressed a similar sentiment on the stand:

> Q. Other than labor and materials directly assigned to a capital project, is there any way, based upon the information provided by Spire to determine if any of the overhead allocations to the capital projects are in compliance with the USOA?
>
> A. **I'd say if you want to play it by the precision and say do they have that kind of detail supporting on their overhead the answer's no**.

Tr. pg. 178 ln. 21 – pg. 179 ln. 3 (emphasis added). As previously indicated, Staff came to nearly the same conclusion in its own investigation.

In its Class Cost of Service report, Staff identified significant problems with regard to the capitalization policy Spire employs. For example Staff noted that "that the overhead capitalized in Spire East's ISRS rate base exceeds 50% of the total capital costs[.]" Exhibit 101, *Staff Cost of Service Report*, pg. 32 lns. 3 – 4. "[I]t is not a reasonable expectation for half of Spire East's construction projects to be comprised

of costs that are not directly related to any particular construction project." *Id*. lns. 10 – 12. "To discover if Spire's overhead construction costs are equitably assigned to each capital job or unit as required by the USOA, Staff submitted a series of data requests regarding Spire's capitalization practices." *Id*. at 12 – 14.

> In response to a data request asking for test year overhead employee costs and the related benefits that are capitalized, Spire notes that it does not maintain records of such information. Furthermore, Spire states that the allocation of costs to capital orders has dozens of steps and is a complex systematic process. As such, **Staff cannot accurately discern the origin of overhead costs that Spire is booking to its capital projects and including in its rate base**. For example, the information regarding overheads provided to Staff does not, or cannot, differentiate between supervisory labor from a Spire Missouri employee, unrelated overhead labor from a Spire Alabama employee, an employee of Spire Inc.'s unregulated businesses, an executive employee, and so on. **Staff is concerned that the complexity of Spire's processes obfuscate the nature and amount of overheads Spire Missouri has booked to rate base**.
>
> For this reason, **Staff is unable to affirm that Spire is in compliance with USOA requirements found in Gas Plant Instructions 3 and 4 that limits a project's assigned overhead to an equitable proportion, since Spire cannot show where the overhead originated**. **Additionally, there are costs currently capitalized by Spire that appear to conflict with the guidance set forth in the USOA**.

Id. at pg. 23 ln. 19 – pg. 33 ln. 2. This was repeated by Staff witness Mr. Young in surrebuttal:

> In Staff's Cost of Service Report, I described Spire's capitalization processes as opaque and not in compliance with the USOA. I recommended that the Commission order Spire to cease capitalizing non-operational overhead costs or, as an alternative, cease capitalizing costs Spire receives from Spire Services Inc., until such a time Spire can show the nature and relationship of its overhead costs to capital projects.

Exhibit 140, *Surrebuttal Testimony of Matthew R. Young*, pg. 12 lns. 11 – 15. Mr. Young also identified several other problems with Spire's capitalization process in surrebuttal.

In addition to the issues concerning USOA instruction 4, which Mr. Schallenberg identified in direct testimony and which is included above, Staff also found that Spire faced compliance issues with USOA instruction 3:

> Q. Do you agree with Mr. Krick that Spire is in compliance with Instruction 3?
>
> A. **No**. As previously mentioned, **Spire cannot show how the costs identified in Instruction 3 are accounted for in its capitalization process** so Staff cannot agree that Spire is in compliance with the USOA. To the contrary, Staff is aware of two accounting procedures that are in contradiction with the USOA's guidance.
>
> Q. What two procedures are you referring to?
>
> A. The first procedure relates to Gas Plant Instruction 3(A)(8), which describes the injuries and damages transactions that are eligible for capitalization. In summary, injuries to a person or damages to property that are in connection with construction work is includable in the gas plant accounts and insurance-related recoveries related to those incidents "shall be" credited to the accounts charged with the cost. Spire books the loss from the injury or damage to construction accounts but contrary to the USOA guidance, books insurance proceeds to the income statement accounts. When compared to the USOA's method, Spire's method inflates rate base and increases its earnings (through reduced expense).
>
> The second procedure I'm aware of relates to Gas Plant Instruction 3(A)(19), which describes the training costs that are eligible for capitalization. This Instruction provides for capital eligibility of training costs related to construction with the provision that the related facilities must be unconventional in nature or new to the company's operations. However, Staff understands that Spire makes no such distinction in training activity and charges its construction projects for generic training activities. The effect of this accounting method produces

> the same inflated rate base and increased earnings when compared to the USOA's guidance.

Exhibit 140, *Surrebuttal Testimony of Matthew R. Young*, pg. 15 lns. 1 – 21. However, that does not mean that Staff did not also find considerable problems related to the previously discussed USOA instruction 4.

With regard to USOA instruction 4, Staff noted that Spire could not show compliance with either paragraphs A, B, or C. *Id*. at pg. 16 lns. 3 – 4 ("Instruction 4 has paragraphs A, B, and C, and Spire has not shown compliance with any of them."). As to paragraph A, Staff noted that "Spire's responses to Staff's inquiries give general overviews of *how* overhead costs are capitalized but do not attempt to explain *why* any particular overhead is applicable to a construction job or unit or why the end result is an equitable allocation of overheads." *Id*. at lns. 9 – 12.

> Instead, Spire comes to the conclusion that costs are not unique in nature and are equally eligible for capitalization. For example, Spire applies the same capital transfer rate to injuries and damages insurance, nearly the entire office supplies account, and directors and officers insurance despite the varying relationship of those costs to construction.

Id. at lns. 13 – 16. This is inappropriate. Without Spire completing a study of the supervisor timecard distributions, there would be no way to determine an appropriate capital transfer rate based on the USOA requirements. Tr. pg. 161 lns. 16 – 24. Moreover, Spire should not simply be assuming that the same transfer rate applies

to **all** overhead costs "despite the varying relationship of those costs to construction." Exhibit 140, *Surrebuttal Testimony of Matthew R. Young*, pg. 16 lns. 13 – 16.

Paragraph B of USOA instruction 4 covers what may be the most important violation. As Staff points out: "paragraph B, describes how the indirect payroll of supervisors should be capitalized, '… to the end that only such overhead costs as have a definite relation to construction shall be capitalized.'" *Id*. at lns. 18 – 20. It also "prohibits the use of arbitrary percentages to cover assumed overhead payroll costs." *Id*. at lns. 20 – 21. Finally, it "requires the use of time card distributions as a basis of assigning overhead payroll to construction." *Id*. at pg. 17 lns. 6 – 7. Spire is not in compliance with any of these provisions.

> Instead of conducting studies of the time charged to clearing accounts by its employees, Spire uses the direct labor charges as the basis of distributing overhead payroll costs. While direct labor charges are based on time card distributions, **the USOA intended the time reporting of the supervisory labor to be the basis of distribution, not the time cards of their direct reports**. To explain further, Spire has assumed there is a relationship between how construction employees use their time and how a supervisor's time is used. However, the USOA intended each supervisor's time reporting to be the basis of capitalizing overhead payroll, or when that is not practicable, supervisory time reports should be studied to make an appropriate allocation.

Id. at pg. 17 lns. 8 – 16 (emphasis added). As a result, Spire allocates overheads using the ratio of direct labor to total labor. *Id*. at lns. 18 – 19. This constitutes the use of arbitrary percentages to cover assumed overhead payroll costs prohibited by the USOA, as Staff's witness recognizes. *Id*. at pg. 19 lns. 1 – 6 ("Rather than examining the time of supervisors, Spire has relied exclusively on an arbitrary relationship

between direct and indirect labor to account for overhead payroll costs, and the related payroll benefits that follow payroll.").

Mr. Young further explained the arbitrary nature of Spire's cost allocation methodology during the evidentiary hearing:

> Q. And I think you further explain that Spire has assumed there is a relationship between how construction employees use their time and how a supervisor's time is used?
>
> A. **Yes, and that's what makes it an arbitrary sentence**.
>
> Q. Well, that's my question for you. Doesn't the method used by Spire use reason or judgment? It's just not the reason or judgment that you think they should use?
>
> A. It's not the -- **it's not reasonable to just assume that the supervisors and their supervisors and all the way up to who knows how far up the hierarchy of the employees, that their time is dictated by how the time is reported by the field employees**.
>
> Q. But let's back up a second. I mean you're making an assumption as to how this plays out down the road. But at the fundamental level, there is reason or judgment in terms of how Spire Missouri approaches these overheads, the capitalization of overheads; correct?
>
> A. **No**. We won't know until we see how their –
>
> COURT REPORTER: (Asked for clarification.)
>
> THE WITNESS: How Spire's reasoning was laid out.

Tr. pg. 148 ln. 21 – pg. 149 ln. 19 (emphasis added). This is a problem that the OPC's witness Mr. Robert Schallenberg also identified:

> Spire Missouri acknowledges its use of these formulas in its fiscal year 2020 Annual Report submitted to the Commission and to FERC as a required Form 2 filing:

> "The transfers to construction are intended to cover that portion of those accounts which is attributable to construction on a general basis but which is not directly applicable to a particular work order"
>
> "The amount capitalized is determined by apportionment of administrative and general expenses for the year based on the percentage of construction labor to total labor charges."

Spire Missouri indicates that it is using a prohibited method. Mr. Young seems to be indicating the same conclusion.

Exhibit 204C, *Rebuttal Testimony of Robert E. Schallenberg*, pg. 9 lns. 5 – 16; *see also* pg. Exhibit 205, *Surrebuttal of Robert E. Schallenberg*, pg. 26 lns. 18 – 21 ("The Company continues to be unable to show that it will comply with the requirements to capitalize overheads. The Company cannot satisfy these requirements just by having employees repeatedly state they are in compliance. The compliance must be **shown** to be in existence, not told it exists.").

Paragraph C, the final paragraph of instruction 4 to the USOA, sets forth the recording and reporting requirements for capitalization of overheads. Staff witness Mr. Young explained the problem with Spire's attempt to comply this paragraph quite simply as follows:

> Paragraph C requires records of construction work orders and utility plant accounts to be maintained so that the total amount of each overhead, the nature and quantity of each overhead that is charged to each work order and each plant account, as well as the bases of distributing the overhead costs, can be shown. To track the amount and nature of overheads, Spire uses a concept called 'cost elements' to charge work orders. Unfortunately, by the time construction work-in process is unitized to the FERC plant accounts, those cost elements are lost. Accordingly, Spire does not keep records sufficient to show each

> overhead costs in its utility plant account and also has not provided support to show the bases used to distribute its overheads. As such, Staff concludes that Spire is unable to show how costs are recorded so that each job or unit is charged overheads that are reasonably applicable to the construction so that the job or unit will bear an equitable proportion.

Exhibit 140, *Surrebuttal Testimony of Matthew R. Young*, pg. 19 lns. 8 – 18. There is really nothing else to say about this third paragraph.

What is the Proper Remedy for this Situation?

Two separate remedies have been proposed to resolve the issue of Spire's violation of the USOA capitalization instructions. The first was proposed by the Commission's staff and is explained by Mr. Young as follows:

> I recommended: 1) that the Commission either order Spire to cease capitalizing non-operational overhead costs or 2) order Spire to cease capitalizing costs received from Spire Services until Spire shows the nature and relationship of capital overhead costs. Lastly, 3) order accounting adjustments to reflect the Commission's decision on the appropriate capitalization.

Id. at pg. 20 lns. 6 – 10. The OPC's witness Mr. Robert Schallenberg offered his own recommendation in direct testimony: **

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** Exhibit 203C, *Direct Testimony of Robert E. Schallenberg*, pg. 23 lns. 26 – 28. Both witnesses had very different responses to the proposal offered by the opposing party.

The OPC, for the most part, agreed with the Staff's position. *See* Exhibit 204C, *Rebuttal Testimony of Robert E. Schallenberg*, pg. 22 lns. 3 – 12. Specifically, OPC's witness expressly agreed "that Spire should be expressly ordered to cease capitalizing overhead where it cannot show a definite relationship to construction" and further offered that the "order should be effective October 1, 2019, the beginning of the test year." *Id*. Staff, on the other hand, vehemently disagreed with the OPC's proposal to create a tracking mechanism. *See* Exhibit 125, *Rebuttal of Matthew R young*, pg. 4 ln. 14 – pg. g ln. 5. However, Staff did tentatively agree to the OPC's proposal to require Spire to submit ongoing reports on capitalized overheads and their relationship to ISRS eligibility. *Id*. at pg. 5 lns. 13 – 19. In response, the OPC's expert witness noted the following:

> It is my personal opinion that the tracker is simple and should be established to prevent Spire Missouri from double recovery of the overhead costs. The amount of overheads placed in current rates can be established in this case and compared to actual amount of overheads being capitalized on the books. The importance of the tracker is to alert

the interested parties if Spire Missouri is capitalizing money in base rates.

Q. Are you willing to forego your reporting proposal?

A. No. Mr. Young's rebuttal testimony notes that Staff found the definition, identification, and quantification of capital overhead costs is not readily in Spire's books and records. I hold the position that Spire Missouri should be required to report such information monthly or no longer than a quarterly basis. I am not comfortable in recommending that the situation where the definition, identification, and quantification of capital overhead costs is not readily in Spire's books and records continue.

Exhibit 205C, *Surrebuttal of Robert E. Schallenberg*, pg. 27 lns. 1 – 12. The importance of this tracker was only further cemented when Staff's witness acknowledged that Staff cannot say, for certain, that the amounts being expensed currently and included in base rates will not be further capitalized in a future ISRS project. Tr. pg. 158 ln. 23 – pg. 159 ln. 6.

Based on these recommendations, the OPC requests the Commission issue the following orders with regard to Spire's capitalization of overheads:

1. Order Spire to cease capitalizing either non-operational overhead costs or costs received from Spire Services until Spire shows the nature and relationship of capital overhead costs in its next rate case;

2. Order a tracker designed to ensure that Spire Missouri's general overhead is not allowed to be over-recovered by transferring overheads to construction by an amount causing overhead expense to be less than the amount included in base rates in this case;

3. Order Spire to create policies and procedures that: track in the greatest detail the Company's practice for selection of overheads for capitalization, tracks the criteria needed to prove a definite relationship, and explains why the basis of the relationship is not being used to assign

costs that will include an examination of the cost assignment based on hours worked vs salary/wages costs that support the use of the method utilized;

4. Order Spire to report quarterly information regarding overhead capitalization to allow monitoring of the dollar impact of Spire Missouri's practices; and

5. Order Spire to report each fiscal year the amount of overhead capitalization and show the definitive relationship to construction for that capitalization.

Exhibit 140, *Surrebuttal Testimony of Matthew R. Young*, pg. 20 lns. 6 – 10; Exhibit 203C, *Direct Testimony of Robert E. Schallenberg*, pg. 23 lns. 26 – 28.

Conclusion

Spire cannot establish the definite relationship between its construction projects and the overhead costs it is booking to those construction projects. Exhibit 203C, *Direct Testimony of Robert E. Schallenberg*, pg. 24 lns. 1 – 19; Tr. pg. 178 ln. 21 – pg. 179 ln. 3. Spire has instead resorted to simply using a general allocator that compares the ratio of direct labor to total labor. Exhibit 140, *Surrebuttal Testimony of Matthew R. Young*, pg. 17 lns. 18 – 19. This is an example of the use of an arbitrary percentage to cover assumed overhead payroll costs, which is prohibited by the USOA. *Id*. at pg. 16 lns. 20 – 21, pg. 19 lns. 1 – 6. This is not appropriate. Nor is this the only manner by which Spire is violating the USOA. *See generally,* Exhibit 140, *Surrebuttal Testimony of Matthew R. Young*, pg. 15 lns. 1 – 21; pg. 16 lns. 3 – 4. The Commission should therefore order Spire to cease capitalizing overhead where it cannot show a definite relationship to construction. Exhibit 204C, *Rebuttal Testimony*

of Robert E. Schallenberg, pg. 22 lns. 3 – 12; Exhibit 140, *Surrebuttal Testimony of Matthew R. Young*, pg. 20 lns. 6 – 10. The Commission should further order a tracker and other recommendation proposed by the OPC's expert witness. Exhibit 203C, *Direct Testimony of Robert E. Schallenberg*, pg. 23 lns. 26 – 28. Such a tracker is necessary to ensure that Spire is not capitalizing money in base rates. Exhibit 205C, *Surrebuttal of Robert E. Schallenberg*, pg. 27 lns. 1 – 12.

Issue 16. Net Operating Loss Carryforward application

The Net Operating Loss ("NOL") recorded by Spire should not be included as an offset to reduce the amount of Accumulated Deferred Income Tax ("ADIT") that is reducing rate base. The argument presented by Spire and Staff that an NOL deferred asset should be included in rate base because the available tax deductions created by such an asset cannot offset Spire's income tax liability and thus no "free" cash is generated by the ADIT is incorrect because it fails to account for the free cash generated due to the inclusion of income taxes in the revenue requirement that are not being paid to the taxing authorities because of that same NOL. If, however, the Commission nevertheless does allow Spire's NOL to be included as an offset to ADIT, then the Commission should also order a tracker or regulatory liability to account for the unspent income tax expense that the OPC argues would otherwise offset the NOL.

Analysis

It is no secret that this issue can become quite confusing quite quickly. To prevent this from happening, we need to break the issue down into parts. The first part is the fact that there are **two** "piles" or "buckets" of money at issue here.

There are Two Piles of Money

There are two different piles of money related to this issue. The first is the "current income tax" pile, and it refers to the money that the utility is expected to pay to the relevant taxing authorities. The second is the "deferred income tax" pile, which refers to an amount of tax that the utility collects from customers but is able to

temporarily avoid paying to a taxing authority due to differences between how certain deductions are treated for ratemaking (book) versus taxation (tax) purposes. The "deferred income tax" pile is important because it represents "free" cash that ratepayers have provided to the utility in the form of an interest free loan. You may have noticed that this paragraph has been absent of citations. That was to ensure that the information was relayed neatly. Let us now review the record to show the support for everything that was just stated.

Let us begin our analysis with the surrebuttal of Staff witness Mr. Matthew Young who states the following:

> As a preliminary point, remember that utility income tax expense for ratemaking purposes is divided into two categories: (1) current income tax expense which is paid in cash by the utility to taxing authorities, and (2) deferred tax expense which represent amounts of "free" cash to the utility provided by customers related to normalization of certain income tax deductions.

Exhibit 140, *Surrebuttal of Matthew R young*, pg. 7 lns. 22 – 26. This should be sufficient to establish the point that there are two piles of money (income tax expense) that are at issue: the "current income tax" pile and the "deferred income tax" pile. This also establishes the point that the "deferred income tax" pile is important because it represents "free" cash that ratepayers have provided to the utility in the form of an interest free loan. *Id*. We can add to this understanding by referencing the definition of ADIT that Mr. Young provided in rebuttal:

> The ratemaking concept of ADIT is a measurement of the tax savings Spire has received from the Internal Revenue Service ("IRS") but has

> not passed onto ratepayers through the ratemaking process. ADIT is the summation of normalized book/tax timing differences (caused by tax deductions) that are temporary in nature and will become a tax liability to Spire in future periods. Since Spire is able to use book/tax timing differences to avoid paying current income taxes, the ADIT balance represents an amount of cash Spire has avoided spending on its past income tax liabilities and is considered a cost-free loan from the federal government.

Exhibit 125, *Rebuttal of Matthew R young*, pg. 6 lns. 12 – 18. Between these two statements, we have established everything stated in the first paragraph. Let us now further develop our understanding by applying some actual numbers to these concepts.

Schedule 11 of Staff's combined accounting schedules shows the Income Tax Calculations that Staff preformed for Spire Missouri. Exhibit 102, *Full Staff Accounting Schedules*, Accounting Schedule 11. For purpose of this brief, we will focus on this except from the bottom of the first page of schedule 11.

42	SUMMARY OF CURRENT INCOME TAX				
43	Federal Income Tax	$23,112,941	$33,040,24	$34,034,791	$35,022,019
44	State Income Tax	$4,104,381	$5,867,26	$6,043,876	$6,219,188
45	City Income Tax	$0	$	$0	$0
46	TOTAL SUMMARY OF CURRENT INCOME TAX	$27,217,322	$38,907,51	$40,078,667	$41,241,207
47	DEFERRED INCOME TAXES				
48	Deferred Income Taxes - Def. Inc. Tax.	-$7,471,955	-$7,471,95	-$7,471,955	-$7,471,955
49	Amortization of Deferred ITC	-$202,545	-$202,54	-$202,545	-$202,545
50	Amortization of Protected Excess ADIT (TCJA)	-$1,939,752	-$1,939,75	-$1,939,752	-$1,939,752
51	Amortization of Unprotected Excess ADIT (TCJA)	-$6,517,877	-$6,517,87	-$6,517,877	-$6,517,877
52	Amortization of Protected Excess ADIT (MO)	-$372,850	-$372,85	-$372,850	-$372,850

Exhibit 102, *Full Staff Accounting Schedules*, Accounting Schedule 11 pg. 1 of 2 (annotations added). For clarity's sake, the OPC has supplied a box highlighting column (E) of the original, which is where we will focus our discussion. Please note first line 46, which is labeled "Total Summary of Current Income Tax." Under column

(E), this value is approximately $40 Million. *Id*. at line 46. This represents the first of the two piles, the "current income tax" pile, referenced in Mr. Young's surrebuttal. Exhibit 140, *Surrebuttal of Matthew R young*, pg. 7 lns. 22 – 26. The inclusion of this amount in the revenue requirement (which is necessary to make the payments to the taxing authorities) is found at line 7 of Schedule 1 of the Full Accounting Schedules. Exhibit 102, *Full Staff Accounting Schedules*, Accounting Schedule 1 pg. 1 of 1 ln. 7.

The second number to consider is at line 48, which is labeled "Deferred Income Taxes." Exhibit 102, *Full Staff Accounting Schedules*, Accounting Schedule 11 pg. 1 of 2 ln. 48. This line shows a value of approximately $7.5 Million for column (E). *Id*. This is the second pile, the "deferred income tax" pile, referenced in Mr. Young's surrebuttal. Exhibit 140, *Surrebuttal of Matthew R young*, pg. 7 lns. 22 – 26. This is the amount that is supposed to represent the interest free loan, as identified during cross-examination of Mr. Young:

> Q. And that seven and a half million, that reduces rate base because it is considered an interest-free loan. Right?
>
> A. Correct.
>
> Q. It's an interest-free loan because the IRS doesn't require the Company to pay taxes immediately. It allows them to hold onto the tax money that they collect from customers. Correct?
>
> A. Correct.

Tr. pg. 653 ln. 24 – pg. 654 ln. 7. Obviously, this tracks with what Mr. Young said in rebuttal and surrebuttal. The $7.5 Million in line 48, which is labeled "Deferred Income Taxes" is the "deferred tax expense which represent amounts of 'free' cash to

the utility provided by customers related to normalization of certain income tax deductions." Tr. pg. 653 ln. 24 – pg. 654 ln. 7; Exhibit 140, *Surrebuttal of Matthew R young*, pg. 7 lns. 24 – 26.

At this point, everything should be relatively simple and clear. There is an amount of "current income tax" that Spire is expected to pay to the taxing authorities and an amount of "deferred" income taxes that Spire is not going to pay right away. Exhibit 140, *Surrebuttal of Matthew R young*, pg. 7 lns. 22 – 26; Exhibit 125, *Rebuttal of Matthew R young*, pg. 6 lns. 12 – 18. We even have a rough idea of how much those two figures should be. *See* Exhibit 102, *Full Staff Accounting Schedules*, Accounting Schedule 11 pg. 1 of 2. However, we are now going to move to the second part of the analysis, which is going to cause a significant problem. To put it simply, Spire is not paying the current income taxes to the relevant taxing authorities due to book/taxing timing differences. This means that **both** the "current income tax" pile and the "deferred income tax" pile are being deferred.

Both Piles of Money are being Deferred

As was just stated, Spire has not paid the amount previously included in its rates to cover current income taxes to the relevant taxing authorities. Exhibit 209, *Direct Testimony of John S Riley*, pg. 9 lns. 4 – 6. ("Spire Inc.'s state and federal income tax returns, the Company's annual report filed with the Commission, and the public 10-K reports all indicate that both the parent company and Spire Missouri have not been required to pay income tax in at least the last three years."). Nor is it likely that Spire will pay income taxes in the near future. *See* Tr. pg. 525 lns. 13 – 21;

pg. 624 lns. 12 – 15. The current income tax that **will not be paid** is instead deferred, as Spire's own witness Mr. Charles J. Kuper testified:

> Q. So you are saying all current income tax is deferred?
>
> A. I'm saying all current income tax is deferred. That's correct.
>
> [. . .]
>
> Q. But you would include all current income taxes as deferred income taxes?
>
> A. Well, I would look at the activity that we have for that respective year and determine if we are going to have a current tax liability or not. If we don't feel that we are going to have a current tax liability, we would classify it out as deferred tax.
>
> Q. Do you feel like Spire is going to have a tax liability in the next year?
>
> A. In the next year, the likelihood is remote that we would have a current tax payment.
>
> Q. So again, you would treat all current income tax as deferred income tax next year?
>
> A. Correct.

Tr. pg. 623 lns. 16 – 19, pg. 624 lns. 5 – 18. The Commission's Staff also acknowledged that the Company was collecting current income tax expense from customers that was not being remitted to the IRS. Tr. pg. 654 lns. 16 – 19. ("Q. The Company is currently collecting $40 million and not remitting all of it -- not remitting any of it to the IRS? A. Correct.").

There really is not much more to this idea than what has already been stated. Current income taxes are included in rates but are not being paid to any taxing

authority (at least temporarily) and are therefore deferred. The OPC's witness Mr. John Riley has explained this repeatedly in testimony and on the record:

> I mean, it's -- actually, you know, we call it deferred and Mr. Kuper had mentioned it and I believe that he said that current income taxes are all deferred. I believe they are too. That is my whole contention is that this money is not necessarily going to pay taxes down the road. It's certainly not going to pay them anytime soon.

Tr. pg. 667 lns. 9 – 14; *see also* Exhibit 210, *Rebuttal Testimony of John S Riley*, pg. 3 lns. 5 – 20; Exhibit 211, *Surrebuttal Testimony of John S Riley*, pg. 4 ln. 9 – pg. 6 ln. 21. As a result, both the "current income tax" and "deferred income tax" piles are currently being deferred. This brings us to the next part of the problem, which is that current income taxes are currently not being recognized as deferred.

The Current Income Tax Pile is not being Recognized as Deferred

Again, this is a very simple point to prove. For example, consider this discussion during the cross-examination of Staff witness Mr. Young:

> Q. When you started off and the Judge was walking through how he understood this, I think we came to a head. This I believe is the critical part to understanding at least our arguments. The $40 million that the Company is collecting in income taxes, is that amount being -- is the ADIT reducing rate base being increased by a dollar for dollar by that 40 million?
>
> A. No.
>
> Q. [. . .] There is an amount of money collected by the Company that is not paid to a taxing authority which is also not being used to reduce rate base?
>
> A. Correct. That's not paid to a taxing authority and something else is used to reduce rate base.

Q. So some part of 40 million is not being put into ADIT?

A. I don't think there is any link between the 40 million and ADIT.

Q. The amount of money that the Company is collecting, but not remitting, that is supposed to be the interest-free loan that is the basis of ADIT, is it not?

A. No. The 40 million, I mean, it's income tax expense collected from customs but the ADIT we put in rate base comes from tax returns which flows through to the balance sheet of the Company.

Tr. pg. 652 ln. 24 – pg. 653 ln. 23. In fact, Staff directly states this very point in surrebuttal where Mr. Young states: "[t]he difference between current income tax expense collected from customers and cash paid to the IRS **does not factor into the ADIT component of rate base**." Exhibit 140, *Surrebuttal of Matthew R young*, pg. 8 lns. 20 – 22 (emphasis added). Instead, the current income tax is simply treated as cash to the Company, as explained during cross of Mr. Young:

Q. What happens to the $40 million the Company collects an[d] doesn't remit to the IRS? What does the Company do with it?

A. It collects it as a revenue and I don't -- I would be surprised if they earmark it for any specific purpose.

Q. It's just cash to the Company?

A. Correct.

Q. So customers are currently paying $40 million in cash to the Company?

A. Well, these accounting schedules have 40 million. I don't know what they are currently paying.

Q. Fair enough.

A. Yeah.

Q. If these accounting schedules are approved, the Company will be just collecting 40 million in cash?

A. Correct.

Tr. pg. 654 ln. 24 – pg. 655 ln. 14. We have now come to the root of the whole problem. The current income tax included in Spire's revenue requirement (approximately $40 million worth) is effectively forming a pile of free cash for the Company in the same manner as the deferred income tax, **but it is not being recognized as such**.

Putting the Pieces Together

So far, we have established three important points that are, effectively, uncontroverted. Those three points are:

1. There is an amount (somewhere in the range of $40 million) of "current income tax" that is separate and distinct from the amount of "deferred income tax" that has been included in Spire's proposed revenue requirement, which has been included for the purpose of paying taxes to the relevant taxing authorities. Exhibit 140, *Surrebuttal of Matthew R young*, pg. 7 lns. 22 – 26; Exhibit 102, *Full Staff Accounting Schedules*, Accounting Schedule 11 pg. 1 of 2 ln. 46; Exhibit 102, *Full Staff Accounting Schedules*, Accounting Schedule 1 pg. 1 of 1 ln. 7.

2. This amount of "current income tax" is actually being deferred because Spire will not pay income taxes in the near future. Tr. pg. 623 lns. 16 – 19, pg. 624 lns. 5 – 18, pg. 525 lns. 13 – 21, pg. 624 lns. 12 – 15, pg. 667 lns. 9 – 14; *see also* Exhibit 210, *Rebuttal Testimony of John S Riley*, pg. 3 lns. 5 – 20; Exhibit 211, *Surrebuttal Testimony of John S Riley*, pg. 4 ln. 9 – pg. 6 ln. 21.

3. Even though the amount of "current income tax" is being deferred, it is not being included in ADIT and is instead simply being treated as cash to the Company. Exhibit 140, *Surrebuttal of Matthew R young*, pg. 8 lns. 20 – 22 ("[t]he difference between current income tax expense collected from customers and cash paid to the IRS **does not factor into the ADIT component of rate base**." (emphasis

> added)); Tr. pg. 652 ln. 24 – pg. 653 ln. 23, pg. 654 ln. 24 – pg. 655 ln. 14.

These three points, which the OPC stresses are uncontroverted, establishes one exceedingly crucial fact that forms the entire basis of the OPC's argument. The amount of current income tax that is: (1) included in rates, (2) not paid to the relevant taxing authority, and (3) not included in the ADIT component of rate base is forming a separate and distinct "pile," "bucket," or "pool" of free money. This "current income tax" pile of free money is itself important because it invalidates the underlying rationale for why the NOL should be included as an offset to ADIT.

The justification that the Commission has accepted in the past for the inclusion of an NOL to offset ADIT can be found in the *Report and Order* issued in case ER-2014-0258, which both Staff and OPC witnesses cite to. Exhibit 140, *Surrebuttal of Matthew R young*, pg. 7 lns. 2 – 11; Exhibit 210, *Rebuttal Testimony of John S Riley*, pg. 2 ln. 6 – 15. That rationale is this:

> However, when bonus depreciation and other tax deductions grow so large as to push the company's taxable income into the negative, the available tax deduction cannot offset any liability and no "free" cash is generated. In that circumstance, the company must record an offsetting deferred tax asset for Net Operating Loss Carryforward (NOLC). The NOLC offsets the ADIT, which would decrease the company's rate base, and therefore, the NOLC has the effect of increasing the rate base.

Id. The OPC argues that the logic presented here is flawed, however, because the Commission is ignoring the pile of "current income tax" related "free" money, as Mr. Riley explains:

> The logic of this argument is flawed, however, when considering regulated utilities. The Commission's belief hangs on the premise that "**no 'free' cash is generated**" by the ADIT because of the NOL, but there is free cash generated due to the inclusion of income taxes in the revenue requirement that are not being paid to the taxing authorities (ironically due to the existence of the same NOL). Income tax expense is included in Spire's revenue requirement for every year and is not being spent on income taxes. That is free cash in my book.

Exhibit 210, *Rebuttal Testimony of John S Riley*, pg. 2 ln. 16 – 21 (emphasis in original). Neither Staff nor Spire have been able to refute the basic premise that there **is** "free" cash generated for the utility, and Staff's witness has openly acknowledged it. Tr. pg. 654 ln. 24 – pg. 655 ln. 14. The statement that the Commission has previously relied upon to say 'the available tax deduction cannot offset any liability and no 'free' cash is generated" is simply not true and is directly contradicted by the record now before the Commission. Exhibit 140, *Surrebuttal of Matthew R young*, pg. 7 lns. 2 – 11; Exhibit 210, *Rebuttal Testimony of John S Riley*, pg. 2 ln. 6 – 15; Tr. pg. 654 ln. 24 – pg. 655 ln. 14. Therefore, the NOL should **not** be included as an offset to ADIT because it is itself already being offset by the "current income tax" expense included in Spire's revenue requirement. *See* Exhibit 210, *Rebuttal Testimony of John S Riley*, pg. 3 ln. 5 – 20.

OPC's Alternative Proposal: Order a Tracking Mechanism

As already laid out, the fact that there are current income taxes included in Spire's rates that are being deferred but not account for as such is well established. In his surrebuttal testimony, Staff witness Mathew Young argued as follows:

> The cash obtained by the utility through tax strategy is entirely different from the income tax costs included in rates intended to cover current tax payments. Mr. Riley has confused these two sources of cash in his arguments although they are in fact separate. If rate base contained a component that represented the difference between cash collected from ratepayers for current income tax expense and actual tax payments paid by the utility, it would not be appropriate to label the balance as accumulated deferred taxes; **it would instead represent an income tax expense tracker balance**.

Exhibit 140, *Surrebuttal of Matthew R young*, pg. 8 lns. 6 – 13 (emphasis added). In his surrebuttal testimony, OPC witness John Riley stated:

> **Q. Is there an alternative revenue requirement adjustment that the Commission could consider?**
>
> A. There is, but eliminating the NOL from rate base would be my preferred course of action. Given the fact that the income tax expense paid by the ratepayers until the next rate case will total more than the NOL itself, coupled with the fact that the deferred tax balance is shrinking, **the Commission could consider a regulatory liability or install a tracker to offset the NOL**.
>
> Conventional wisdom concludes that Spire will not file another general rate case for three years. **The Commission could establish a regulatory liability for three years' worth of income tax expense to recognize the interest free use of the normalized expense.** Again, however, I believe that the best course of action would be for the Commission to eliminate the NOL from rate base

Exhibit 211, *Surrebuttal Testimony of John S Riley*, pg. 9 lns. 1 – 12 (emphasis added). During the hearing, Mr. Riley also testified as follows:

> Q. And in the alternative, you would say well the Commission should order the tracking of that [unspent income tax expense]?
>
> A. Yes. They can do that. That was brought up by Mr. Young and it certainly is a viable option. I had not thought about it before but if you

> do a tracker, I still believe that offsetting the NOL is the way to go. But if the Commission thinks maybe a tracker is position -- that brings up some interesting points is that a [tracker] would probably not be under the IRS's decision-making in a private letter ruling. Trackers are trackers. So if you set something up for the $40 million for each year and put a tracker on that and make a decision down the road that it needs to offset rate base, that is probably not an IRS thing.

Tr. pg. 20 ln. 20 – pg. 667 ln. 7. Based on this evidence, if the Commission ultimately decides to include Spire's NOL as an offset to the ADIT reducing ratebase, the Commission should also order a tracker to track the amount of unspent current income tax included in rates but not in ADIT. While this would not give customers immediate relief, it would allow for the Commission to be better informed in the next rate case and ensure that all deferred income taxes are either booked to ADIT or else booked properly somewhere else. It would also provide a way to avoid any potential lingering threat of a normalization violation. Tr. pg. 668 lns. 8 – 12 ("Q. So tacking on to that, no risk of a normalization violation whatsoever if you go with a tracker? A. Yeah. That is my -- that would be my understanding as to what the IRS usually does and what ratemaking usually does.").

Conclusion

There is an amount (somewhere in the range of $40 million) of "current income tax" that is separate and distinct from the amount of "deferred income tax" that has been included in Spire's proposed revenue requirement, which has been included for the purpose of paying taxes to the relevant taxing authorities. Exhibit 140, *Surrebuttal of Matthew R young*, pg. 7 lns. 22 – 26; Exhibit 102, *Full Staff Accounting*

Schedules, Accounting Schedule 11 pg. 1 of 2 ln. 46; Exhibit 102, *Full Staff Accounting Schedules*, Accounting Schedule 1 pg. 1 of 1 ln. 7. This amount of "current income tax" is actually being deferred because Spire will not pay income taxes in the near future. Tr. pg. 623 lns. 16 – 19, pg. 624 lns. 5 – 18, pg. 525 lns. 13 – 21, pg. 624 lns. 12 – 15, pg. 667 lns. 9 – 14; *see also* Exhibit 210, *Rebuttal Testimony of John S Riley*, pg. 3 lns. 5 – 20; Exhibit 211, *Surrebuttal Testimony of John S Riley*, pg. 4 ln. 9 – pg. 6 ln. 21. Even though the amount of "current income tax" is being deferred, it is not being included in ADIT and is instead simply being treated as free cash to the Company. Exhibit 140, *Surrebuttal of Matthew R young*, pg. 8 lns. 20 – 22 ("[t]he difference between current income tax expense collected from customers and cash paid to the IRS **does not factor into the ADIT component of rate base**." (emphasis added)); Tr. pg. 652 ln. 24 – pg. 653 ln. 23, pg. 654 ln. 24 – pg. 655 ln. 14. This amount of free cash should be used to offset any claimed NOL experienced by Spire instead of allowing that NOL to offset ADIT. *See* Exhibit 210, *Rebuttal Testimony of John S Riley*, pg. 3 ln. 5 – 20. The Commission should therefore not include any NOL as an offset to reduce the amount of ADIT that is reducing rate base. If the Commission nevertheless decides to include an NOL to offset the amount of ADIT reducing rate base, the Commission should also order a tracker to track the amount of unspent current income tax included in rates but not in ADIT. *See* Exhibit 140, *Surrebuttal of Matthew R young*, pg. 8 lns. 6 – 13; Exhibit 211, *Surrebuttal Testimony of John S Riley*, pg. 9 lns. 1 – 12; Tr. pg. 20 ln. 20 – pg. 667 ln. 12.

Issue 19. Affiliate Transactions

Spire Missouri is currently being charged for the costs that it incurred to produce goods and services that were used by Spire Inc. Spire Missouri is therefore providing a financial advantage to Spire Inc. Because Spire Missouri is providing Spire Inc. a financial advantage as defined by the Commission's affiliate transaction rule, Spire Missouri is engaging in a prohibited transaction. The OPC recommended adjustments is necessary to correct this violation.

Analysis

Before delving too deeply into the heart of this issue, let us take one moment to consider the proper nomenclature of this discussion. In the list of issues, this topic has been dubbed "Corporate Allocations/Affiliate Transactions." This is a problem as explained in the rebuttal testimony of OPC witness Robert Schallenberg:

> [Staff and Company] testimonies mischaracterize their discussion of Spire Missouri's transactions with its affiliates as a corporate or cost allocation mechanics matter. The importance of understanding this mischaracterization cannot be understated. The Commission has an affiliate transaction rule for its gas utilities that establish the requirements that must be satisfied before a utility can participate in such transactions with its affiliates. This rule prohibits affiliate transactions if they are not consistent with the Commission's Affiliate Transaction Rule. The term "cost allocations" is only meant to address the assignment of costs totally within Spire Missouri (e.g. cost assignment to Spire Missouri East vs Spire Missouri West of Spire Missouri total costs or a customer class cost of service). Cost allocations are not covered by a Commission rule in the same manner as affiliate transactions. Thus, **by mischaracterizing Spire's affiliate transactions using the "cost" or "corporate" allocation nomenclature, Spire and Staff are effectively seeking to reduce**

> **or remove these affiliate transactions from scrutiny under the Commission's rules**.

Exhibit 204C, *Rebuttal Testimony of Robert E. Schallenberg*, pg. 9 lns. 5 – 16. For this reason, the OPC will refer to this issue only as the "affiliate transaction" issue throughout this brief.

As explained in the excerpt above, Spire's transactions with its affiliate entities are governed by the Commission's affiliate transaction rule: 20 CSR 4240-40.015. Spire is currently violating the plain language of this rule. The OPC's proposed adjustment is designed to correct the violation of the affiliate transaction rule ("ATR"), which will be explained shortly. Before establishing how Spire is violating the rule, however, we must first examine the ATR itself.

Evaluation of the Commission's Affiliate Transaction Rule

The Commission's ATR contains eleven separate subsections and covers more than two pages in the published code of state regulations. Fortunately, our discussion will only require consideration of a very small portion of the whole rule. That portion is subsection (2)(A), which sets out the prohibition on provision of a financial advantage by a utility to an affiliate entity:

> (2) Standards.
>
> (A) A regulated gas corporation shall not provide a financial advantage to an affiliated entity. For the purposes of this rule, a regulated gas corporation shall be deemed to provide a financial advantage to an affiliated entity if—

> 1. It compensates an affiliated entity for goods or services above the lesser of—
>
> > A. The fair market price; or
> >
> > B. The fully distributed cost to the regulated gas corporation to provide the goods or services for itself; or
>
> 2. It transfers information, assets, goods or services of any kind to an affiliated entity below the greater of—
>
> > A. The fair market price; or
> >
> > B. The fully distributed cost to the regulated gas corporation.

20 CSR 4240-40.015. The central premise and purpose of this rule is found in the first sentence: "A regulated gas corporation shall not provide a financial advantage to an affiliated entity." *Id*. This is a very basic, blanket prohibition. Under the plain language of the rule, a utility that provides a financial advantage to an affiliated entity has violated the rule. *Id*.

Following the blanket prohibition found in the first sentence, the rest of the rule just defines what the term "financial advantage" means. *Id*. For our discussion, we will focus on (A)2, which states that a utility has provided a financial advantage if "it transfers information, assets, goods or services of any kind to an affiliated entity below the greater of A. The fair market price; or B. The fully distributed cost to the regulated gas corporation." *Id*. If a utility has made such a transfer to an affiliate, then it has provided the affiliate with a financial advantage and thus violated the rule. The OPC's argument in this case is that Spire Missouri is providing its parent company Spire Inc. a financial advantage in the form of "information, assets, goods

or services" for which Spire Inc. is paying **nothing**. Thus, the question of whether the cost is "below the greater of A. The fair market price; or B. The fully distributed cost to the regulated gas corporation" is largely irrelevant. This is because a cost of $0 is always going to be **below** the greater of "A. The fair market price; or B. The fully distributed cost to the regulated gas corporation." Therefore, the OPC's argument need only establish two points to show a violation of the ATR has occurred: (1) that Spire Missouri has provided Spire Inc. with information, assets, goods or services" and (2) that Spire Inc. paid Spire Missouri **nothing** for said "information, assets, goods or services." Let us now consider the facts establishing these two points.

Spire is violating the Commission's Affiliate Transaction Rule

"Spire Missouri has developed and implemented a system where rates charged to Spire Missouri's customers include the costs of goods and services provided to Spire Missouri's parent company, Spire Inc." Exhibit 204C, *Rebuttal Testimony of Robert E. Schallenberg*, pg. 10 lns. 10 – 12. "Spire Missouri is therefore providing financially advantageous and preferential treatment to Spire Inc." *Id*. at lns. 12 – 13. Examples of all the goods and or services provided to Spire Inc. and its other subsidiaries by Spire Missouri can be found in the CAM annual report filed by the Company. The CAM annual report for fiscal year ending September 30, 2020, lists the following goods and services provided by Spire Missouri to Spire Inc. and its subsidiaries: **

ral

** Exhibit 203C, *Direct Testimony of Robert E. Schallenberg*, schedule RES-D-6 part 1, PDF pgs. 40 – 69.

Given the extensive list of functions that Spire Missouri performs for Spire Inc. and its subsidiaries, it should be clear what the OPC's witness Mr. Schallenberg meant when he stated as follows in direct: **

** Exhibit 203C, *Direct Testimony of Robert E. Schallenberg*, pg. 9 lns. 22 – 24. The total cost Spire Missouri incurs to produce or procure all these goods and services is ** ** Exhibit 205C, *Surrebuttal of Robert E. Schallenberg*, pg. 11 lns. 3 – 15. Of this amount, only ** ** was charged to Spire Inc. *Id.* **

** Exhibit 203C, *Direct Testimony of Robert E. Schallenberg*, pg. 15 lns. 6 – 9. ** ** *Id.* at pg. 15 ln. 25 – pg. 16 ln. 2. (** **).

The OPC's expert witness Mr. Robert Schallenberg included a matrix in his direct testimony that identified just some of the work products created by Spire Missouri during the test year that Spire Inc. received at no cost:

**

asis	

** *Id*. at pg. 16 ln. 5 – pg. 17 ln. 1. The provision of these goods and services by Spire Missouri to Spire Inc. at no cost constitutes the provision of a financial advantage. *Id*. at pg. 17 ln. 1 – 3. This fact was further substantiated by Staff's witness during cross-examination.

During the evidentiary hearing, the OPC engaged Staff's witness Mr. Matthew R. Young in discussion regarding a demonstrative exhibit prepared by the OPC. That demonstrative was offered as OPC exhibit 229:

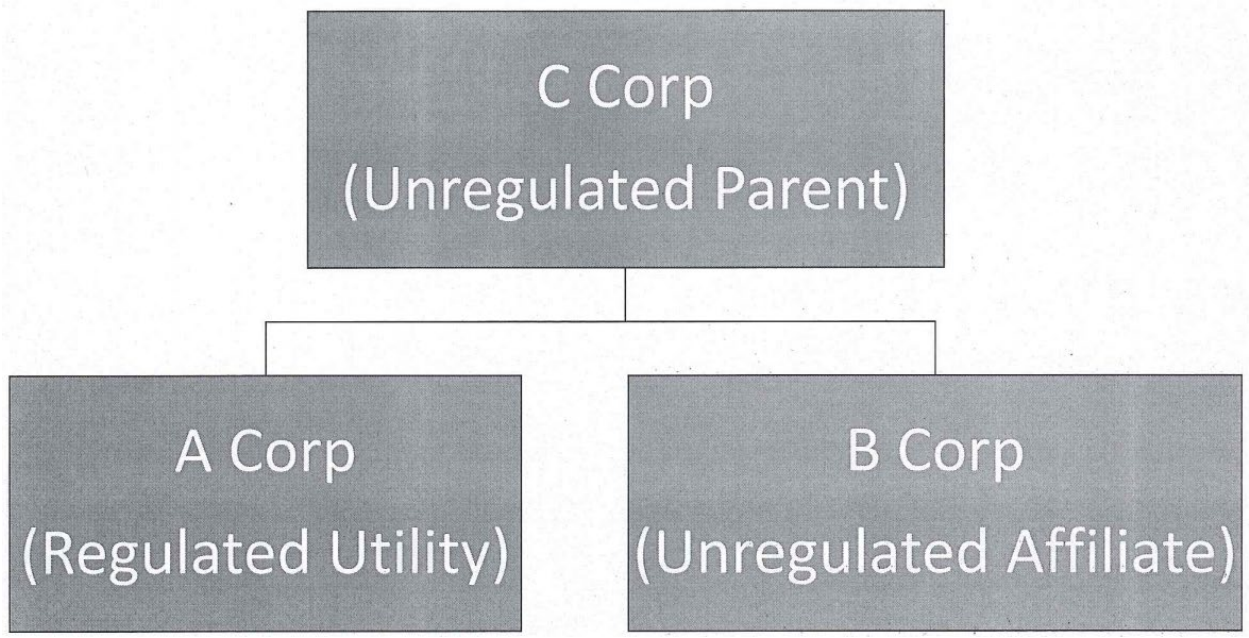

Exhibit 229, *Demonstrative Exhibit Re: A, B, C Corps*. The conversation held regarding this demonstrative went as follows:

> Q. All right. So, let's walk through this really quick so we all are on the same page. Here we see three corporations in a fairly simple corporate family structure. You have the A Corp., that's the regulated utility; the B Corp., the unregulated affiliate; and C Corp., is an unregulated parent. And both A Corp. and B Corp. are fully owned subsidiaries of C Corp. Does that make sense?
>
> A. Yes.
>
> Q. Okay. Thanks. I'm just going to refer back to this for the purposes of this discussion to make things simple. All right. I want you to assume for a second that A Corp. is providing personnel to manage B Corp. Is the provision of management personnel a service, in your opinion, as it would be defined under the Affiliate Transaction Rule?
>
> A. Yes.
>
> Q. If B Corp. does not provide any compensation to A Corp. following the provision of this service, would you agree with me that it has received a financial advantage, if I define a financial advantage as the transfer of information, assets, goods or services of any kind to an affiliate entity below the greater of fair market price or fully distributed costs to produce?

A. You're saying that A gave to B at no cost that would violate the rule?

Q. I'm asking whether or not you would consider that to be a financial advantage?

A. Oh, yes.

Q. Yes. Now, if I give the exact same situation, but instead A is providing management personnel to manage C. And, again, C provides no compensation to A. Has A provided C with a financial advantage, if I define financial advantage as a transfer of information, assets, goods or services below the greater of fair market price or the fully distributed cost to produce?

A. Yes.

Q. And if I changed out the term management personnel and instead replaced it with auditing services, would the same situation hold?

A. Yes.

Q. And if I changed out the term auditing services then for preparation of income taxes, would the same hold?

A. It would.

Q. Thank you.

Tr. pg. 385 ln. 3 – pg. 386 ln. 21. What do we learn from this? Well, if we substitute "Spire Missouri" for "A Corp" and substitute "Spire Inc." for "C Corp" – which is consistent with the actual Spire enterprise corporate structure[13] – we see that Staff's witness agrees that Spire Missouri has provided Spire Inc. with a financial advantage (as that term is defined in the ATR) whenever Spire Missouri provides a service (such as the provision of management personnel, auditing services, or the preparation of income taxes) without compensation. *Id*. Given our previous discussion of the rule,

[13] *See* Exhibit 203C, *Direct Testimony of Robert E. Schallenberg*, schedule RES-D-6 part 1, PDF pg. 81.

this means that Staff's witness agrees that the evidence necessary to establish a violation of the ATR occurs under those same circumstances just described. As we have already established that Spire is providing these types of goods and services without compensation,[14] Staff's witness effectively conceded that an ATR violation has occurred in this case.

At this point, the basic nature of the OPC's argument has been fully developed: Spire Missouri is providing goods and services to its parent Spire Inc. well below cost (primarily for free) and is thus violating the Commission's ATR. *See* Exhibit 205C, *Surrebuttal of Robert E. Schallenberg*, pg. 2 lns. 22 – 24. Beyond that, there is one other issue that is worth further elaboration. That is the interplay between Spire Missouri, Spire Services, and the rest of the Spire enterprise including Spire Inc. To understand this, we need to first examine the history of the present organization.

Laclede Gas Company (the entity by which Spire Missouri was formerly known) underwent a restructuring in 2001. Exhibit 226, *Verified Application GM-2001-0342*. However, ** ** Exhibit 203C, *Direct Testimony of Robert E. Schallenberg*, pg. 10 lns. 1 – 3. In particular, **

[14] **
**

** *Id*. at pg. 11 lns. 2 – 4. **

** *Id*. at lns. 4 – 6. ** **

Id. at pg. 12 ln. 5. Instead, **

** *Id*. at lns. 5 – 6. The creation of this shared services company represents its own problems,[15] but its existence is not itself the issue here. Rather, the point of this discussion is to explain how Spire's system works.

To explain it briefly, the Spire Services system works like this: **

[15] Among other things, **
** Exhibit 203C, *Direct Testimony of Robert E. Schallenberg*, pg. 12 lns. 18 – 21. Even more import, though, is the problem Mr. Schallenberg explained in direct regarding the cost of operating Spire Services: **

** Tr. pg. 12 lns. 6 – 17.

** Exhibit 205C, *Surrebuttal of Robert E. Schallenberg*, pg. 10 lns. 3 – 5, 20 – 21. The principle problem here is that ** ** *Id*. at pg. 2 lns. 23 – 24. This means that Spire Missouri's affiliates, specifically Spire Inc., are ** ** *Id*. at pg. 3 lns. 1 – 2; *see also Id*. at lns. 10 – 12 (** **). As a result, ** ** This can be easily seen in this graph from OPC witness Schallenberg's surrebuttal testimony: **

** *Id.* at pg. 4 ln. 1. Again, it is this method of re-allocation of costs that is allowing for Spire Inc. to avoid being charged for any of the goods and services it uses to operate. This is a violation of the ATR as explained by Mr. Schallenberg: **

** *Id*. at pg. 10 ln. 19 – pg. 11 ln. 2.

If there is any doubt regarding the idea that Spire Services is nothing but a tool designed to ensure the disproportionate allocation of costs to Spire Missouri, just consider the explanation provided by Ms. Ellen Theroff, the secretary to all Spire entities, as given in the surrebuttal testimony of the OPC's expert witness: **

_____
_____
_____
_____

** *Id*. at pg. 8 lns. 20 – 23, pg. 10 lns. 3 – 5. Based on this, we can confirm: Spire Missouri is providing goods and services to Spire Inc. without just compensation (or really any compensation) and is thus violating the affiliate transaction rule. *Id*. at pg. 10 ln. 19 – pg. 11 ln. 2.

Redressing this Violation of the Commission's Affiliate Transaction Rule

OPC witness Robert Schallenberg proposed an adjustment to correct the affiliate transaction violation that is presently occurring. His recommendation was not addressed in the rebuttal of either Staff or Spire, as Mr. Schallenberg explains: **

_____
_____
_____
_____
_____
_____
_____

** Exhibit 205C, *Surrebuttal of Robert E. Schallenberg*, pg. 23 ln. 5 – pg. 24 ln. 19. Mr. Schallenberg further explained what this adjustment would actually account for and what its impact would be on the revenue requirement: **

_____
_____
_____
_____
_____
_____
_____
_____
_____
_____

** *Id*. at pg. 24 ln. 21 – pg. 25 ln. 5. The OPC requests that the Commission make the adjustment as proposed in the surrebuttal of Mr. Robert Schallenberg to address the ATR violation thus far described.

Conclusion

Spire Missouri is currently being allocated a portion of the costs that Spire Missouri incurred to produce goods and services used by Spire Inc. As such, Spire Missouri is providing goods or services to Spire Inc. below either Spire Missouri's fully distributed cost to produce the product or its fair market values. Because Spire Missouri is providing goods and services to Spire Inc. below Spire Missouri 's fully distributed cost to produce the product or its fair market values, Spire Missouri is providing a financial advantage to Spire Inc. Under the plain language of the

commission's affiliate transaction rule, Spire is thus engaging in a prohibited transaction.

In order to rectify this situation, costs need to be disallowed from Spire Missouri's revenue requirement to account for the goods and services that Spire provided to Spire Inc. without compensation. The OPC's expert witness identified that this would require the removal of ** _____ _____ _____ ** Exhibit 205C, *Surrebuttal of Robert E. Schallenberg*, pg. 24 ln. 21 – pg. 25 ln. 5. By making this adjustment, the Commission will ensure that Spire is held to the commitments it made during its re-organization to ensure Spire Missouri would not be used to subsidize the Company's unregulated business activities and thereby preserve the integrity of the affiliate transaction rule.

Issue 24. Depreciation

The Commission should order Spire East to maintain its current ordered depreciation rates and should further order Spire West to adopt the depreciation rates of Spire East so that both systems are on a consolidated set of depreciation rates. Failing this, the Commission should order Spire to adopt consolidated depreciation rates based on the average service lives and net salvage values determined by Staff and calculated using the formula presented in Staff's cost of service report. Regardless of what depreciation rates the Commission sets, it should also order specific adjustments to account 376.2 mains – cast iron, 376.3 mains – plastic, 381.1 smart meters, 382.1 smart meter installation, and 391.95 EMIS as set forth in this brief. The Commission should not order general plant amortization for Spire. If the Commission decides to nevertheless order general plant amortization, it should also order the conditions proposed by the OPC.

Analysis

The record regarding the issue of depreciation that is now before this Commission is an absolute mess. It should be important to the Commission to understand why this mess has occurred and how it can be avoided in the future. To that end, the OPC is going to take some time to fully explain the situation.

The problem begins with the fact that Spire failed to provide any direct testimony with evidence supporting its request for new depreciation rates. The Direct testimony of Spire Witness Wesley E. Selinger states on page 13 that he included a

schedule (H-11) that "details the adjustment to annualize depreciation expense based upon the depreciation rates supported by the Company's depreciation study and the level of plant investment at September 30, 2020 compared to test year expense levels." Exhibit 34, *Direct Testimony of Wesley E. Selinger*, pg. 13 lns. 16 – 18. However, the depreciation study Mr. Selinger refers to was never filed with his direct, thus leaving his statement completely unsupported. Later on in the testimony, Mr. Selinger does provide a *description* of the depreciation study that the Company did not file. *See Id*. at pg. 17. Though, nearly all of Mr. Selinger's discussion centers on the regulatory requirements to file a study and thus gives the *apparent* purpose of proving the Company did not actually need to file a study. *Id*. at lns. 9 – 17. The fact that Spire's direct testimony *appears* to be laying the groundwork for why it did not need to file a study is a point that we will return to later. For now, let us focus on the fact that Spire states it "has engaged the services of Gannett Fleming to provide an updated depreciation study in this proceeding, which will be provided to Commission Staff and OPC." *Id*. at pg. 18 lns. 1 – 3. Again, this study was not included **anywhere** in Spire's direct testimony, which caused significant problems as will be shown shortly.[16]

Having covered what little Spire had to say in direct, let us take a moment to examine the actual depreciation rates that Spire proposed. These can be found in the aforementioned schedule H-11. Exhibit 34, *Direct Testimony of Wesley E. Selinger*,

[16] Not least of which is the fact that Spire is, once again, demonstrating that it does not understand the importance of meeting its burden of proof. *See* RSMo. § 393.150.2.

Schedule WES-1 H11-Depr Adj (pg. 38 of 45). Please note at the outset that this schedule does not contain a list of either the average service lives or net salvage amounts used to calculate these rates (this will be important later). *Id*. There are quite a few rates to consider, but for the purpose of our discussion, please focus on the following:

Account	Proposed Rate
376.2 Mains - Cast Iron	3.12%
391 Furniture & Fixtures	4.71%
391.1 Data Processing Systems	12.12%
391.2 Mechanical Office Equipment	5.47%
391.3 Data Processing Software	See adj. H-13
391.95 Ent Software - EIMS	See adj. H-13
392.1 Transportation Eq - Automobiles	10.00%
392.2 Transportation Eq - Trucks	7.69%
393 Stores Equipment	2.16%
394 Tools, Shop & Garage Equipment	3.62%
395 Laboratory Equipment	3.63%
396 Power Operated Equipment	6.07%
397.0 Communication Equipment	6.24%
397.1 Communication Equipment - ERTs	5.67%
397.1 Communication Equipment - AMR Devices	13.33%
398 Miscellaneous Equipment	4.58%

Id. In particular, please note the rates for 376.2 Mains - Cast Iron (3.12%) and 391 Furniture & Fixtures (4.71%). *Id*. These two rates are going to form the sort of benchmark for this discussion.

Having reviewed Spire's direct, let us now consider Staff's direct. To do this, we must look to the Staff cost of service report. *See* Exhibit 101, *Staff Cost of Service Report*, pg. 112 – 113. According to the report, "Staff conducted its own depreciation

study for the assets of Spire using the straight-line method, broad group-averaging life procedure, and whole life technique for its depreciation study." *Id*. at pg. 112 lns. 26 – 27. The report goes on to state that "Staff used the following formula to calculate the depreciation rates for each plant account: $Depreciation\ Rate = (100\% - Net\ Salvage\ \%) \div (Average\ Service\ Life)$." *Id*. at lns. 28 – 29; pg. 113 ln. 27 – 28 ("These estimates of average life and net salvage were used in the equation noted above to calculate depreciation rates."). The resulting rates (according to Staff) are found in Appendix 3, Schedule DTB-d1, which are what Staff recommends. *Id*. at pg. 114 lns. 1 – 2. This is incorrect, however, in that the accounts under the label "general plant" found in Appendix 3 of Staff's report clearly do not use the formula Staff describes.

One of the key difference between Staff schedule 3 and Mr. Selinger's schedule H-11 is that Staff included the average service lives and net salvage amounts used to calculate rates. This means that Staff's calculations can be verified. The table below shows the same accounts referenced above (in relation to Mr. Selinger's schedule H-11) but uses the information taken from Staff's appendix three (Schedule DTB-d1) with one important addition.[17] The OPC has added a column showing what the average service life should have been if the exact formula Staff **claims** it used in the report is actually used.

[17] Please note that, for some reason, the general plant account numbers for 391.1 and 391.2 have been transposed between Staff and Spire's respective direct testimonies. Please see footnote 20 for more detail.

Account	Average Service Life	Net Salvage Percentage	Depreciation Rate according to Staff's Schedule	Depreciation Rate if using the calculation Staff claims to have used
376.2 Mains - Cast Iron	80	-150	3.12%	3.12%
391 Office Furniture and Equipment	20	0	4.71%	5.00%
391.1 Mechanical Office Equipment	15	0	5.47%	6.67%
391.2 Data Processing Software/Systems	5	0	12.12%	20.00%
391.3 Data Processing Equipment	10	0	6.44%	10.00%
391.95 Enterprise Software	10	0	10.00%	10.00%
392.1 Transportation Equipment - Autos	8	20	10.00%	10.00%
392.2 Transportation Equipment - Trucks	11	15	7.69%	7.73%
393 Stores Equipment	30	0	2.16%	3.33%
394 Tools, Shop and Garage Equipment	25	0	3.62%	4.00%
395 Laboratory Equipment	20	0	3.62%	5.00%
396 Power Operated Equipment	14	15	6.07%	6.07%
397.0 Communication Equipment	15	0	5.81%	6.67%
397.1 Communication Equipment - ERTs	15	0	5.67%	6.67%
397.1 Communication Equipment - AMR	7.5	0	13.33%	13.33%
398 Miscellaneous Equipment	20	0	4.58%	5.00%

Exhibit 101, *Staff Cost of Service Report*, Appendix 3 (Schedule DTB-d1). For all but a few accounts under the "general plant" heading, the number Staff presented for the depreciation rate is **not** the same number that would have been calculated had Staff actually used the calculation it claims to have used. At the same time, the numbers Staff **did** present are largely consistent with what Spire requested in its direct

testimony. *Compare Id. with* Exhibit 34, *Direct Testimony of Wesley E. Selinger*, Schedule WES-1 H11-Depr Adj (pg. 38 of 45). This is a point that Staff itself noted in surrebuttal. Exhibit 128, *Surrebuttal testimony of David T. Buttig*, pg. 3 included table. In other words, the evidence shows that Staff did **not** perform the calculations it claimed it performed (with regard to "general plant" accounts) and instead it largely adopted the general plant depreciation rates that Spire itself had requested.

The fact that Staff's depreciation rates for general plant accounts are largely just copy and pasted from Spire's request (and not calculated as Staff claims) is a problem in and of itself.[18] However, the situation only becomes worse the closer one examines it. Despite the fact that Staff had effectively adopted Spire's rates, Spire choose in rebuttal to criticize the rates Staff proposed:

> Q. DOES STAFF'S PROPOSED RATES FOR THESE ACCOUNTS PROPERLY REFLECT THE FULL RECOVERY AND APPLICATION OF THE METHODOLOGY?
>
> A. No.
>
> Q. PLEASE EXPLAIN THE ISSUE WITH AN EXAMPLE.
>
> A. I will use Account 391.00, Office Furniture and Equipment as an example. This asset class has an amortization period of 20 years. Therefore, the rate should be 5 percent for the appropriate aged assets. The account has $10,824,779.94 in service as of September 30, 2020, however, only $10,195,581.10 is within the 20-year amortization 21 period. Therefore, the surviving plant of $629,198.84 is older than 20 years and should have a rate of 0 percent and the $10,195,581.10 and future plant should have a rate of 5.00 percent. Staff has proposed a rate of 4.71 percent for the entire $10,824,779.94. 24 Although the total

[18] During cross examination of Staff witness, the OPC was able to elicit responses that showed Staff's method for calculating **all** depreciation rates largely consisted of just using the numbers Spire supplied with only minor alterations. Unfortunately, nearly the entire portion of this cross-examination was lost due to technical difficulties. Tr. pg. 116 lns. 24 – 25.

> amount of depreciation expense as of September 30, 2020 is the same, the impact of depreciation expense going forward is not when new assets are added to the account. Thus, the new assets will be under-recovered, a reserve deficiency will develop and swings in depreciation expense will be excessive. Therefore, Staff's proposal of 4.71 percent for all the existing assets and to be applied to future assets is not appropriate based on the recovery methods for these accounts. The 5 percent rate is the proper rate for the assets in Account 391.00. This same issue occurs in the other general plant accounts represented by amortization accounting.

Exhibit 35, *Rebuttal Testimony of John J. Spanos*, pg. 18 ln. 12 – pg. 19 ln. 7. To be clear, Spire is arguing that Staff's proposed 4.71% rate for account 391 will result in an under-recovery of new assets and that the proper rate should be 5%. However, if one looks at the proposed rate included in Spire's direct schedule H-11, you will find that Spire requested **the same** 4.71% that Spire is now claiming would result in an under-recovery. Exhibit 34, *Direct Testimony of Wesley E. Selinger*, Schedule WES-1 H11-Depr Adj (pg. 38 of 45). Moreover, if one looks at the depreciation rate that Staff **would** have calculated if it used the calculation found in its class cost of service report (as seen in the above table), one will see that it is the very same 5% that Spire now claims it should be.[19]

The Commission really needs to stop for a moment and consider what is occurring here. Spire is actually accusing Staff of not calculating the proper depreciation rates even though Staff just adopted the same rates that Spire originally

[19] Just in case there is any concern regarding the table the OPC has presented please note the following: Staff's claimed calculation is $Depreciation\ Rate = (100\% - Net\ Salvage\ \%) \div (Average\ Service\ Life)$. According to Staff's Schedule 3, the average service life for account 391 is 20 years and the net salvage percentage is 0. Therefore, the depreciation rate calculated using Staff's calculation would be (100%-0%)/20. The answer to this equation is 5%.

proposed. On the other hand, the rates that Spire argues are correct are the ones that Staff **would** have gotten had they calculated their rates in the manner they **claim** to have used. To put the matter another way, Spire has filed rebuttal testimony that contradicts its own position from direct and Staff filed direct testimony that was self-contradictory. This is a colossal failure on the part of both parties, and it could have been easily avoided if Spire had properly filed direct testimony to support its depreciation rates. Let us take a moment to consider why.

The whole problem here comes down to the depreciation study prepared by Gannett Fleming. This report was, again, not filed with Spire's direct case nor was any attempt made in direct to explain or interpret it. Exhibit 201, *Rebuttal Testimony of John A. Robinett*, pg. 2 ln. 17 – pg. 3 ln. 2. The following is an excerpt taken from page VI-6 of the report, which is attached to Spire witness Spanos' rebuttal testimony:

Gannett Fleming

SPIRE MISSOURI, INC.

TABLE 1. SUMMARY OF ESTIMATED SURVIVOR CURVE, NET SALVAGE PERCENT, ORIGINAL COST AND CALCULATED ANNUAL AND ACCRUED DEPRECIATION RELATED TO GAS PLANT AS OF SEPTEMBER 30, 2020

	DEPRECIABLE GROUP	SURVIVOR CURVE	NET SALVAGE PERCENT	ORIGINAL COST AS OF SEPTEMBER 30, 2020	CALCULATED ANNUAL ACCRUAL AMOUNT	CALCULATED ANNUAL ACCRUAL RATE	CALCULATED ACCRUED DEPRECIATION
	(1)	(2)	(3)	(4)	(5)	(6)=(5)/(4)	(7)
	GENERAL PLANT						
390.20	STRUCTURES AND IMPROVEMENTS	35-S0	0	1,041,497.59	28,456	2.73	437,916
391.00	OFFICE FURNITURE AND EQUIPMENT						
	FULLY ACCRUED	FULLY ACCRUED		629,198.84	0	-	629,198
	AMORTIZED	20-SQ	0	10,195,581.10	509,779	5.00	2,998,221
	TOTAL OFFICE FURNITURE AND EQUIPMENT			10,824,779.94	509,779	4.71	3,627,419

Exhibit 35, *Rebuttal Testimony of John J. Spanos*, Schedule JJS-R2, pg. 52 of 396. If one looks at account 391.0, here labeled Furniture and Equipment, one will see that there are several entries for Fully Accrued, Amortized, and Total Office Furniture and Equipment. Moving to the column "Calculated Annual Accrual" and looking under the sub-heading "Rate" one can see three separate rates. First, for the "Fully

Accrued" a rate of null (-) or no rate; second, under "Amortized," a rate of 5.00% (which is what Spire says should be the rate for the account); and then third there is the "Total Office Furniture and Equipment" line which shows the same 4.71% that Spire initially proposed in direct and which Staff adopted. This probably would lead one to wonder what in the world is going on here. The answer, as OPC witness John Robinett explains in surrebuttal, is that the "4.71% for Account 391 Total Office Furniture and Equipment, . . . **is a dollar weighted rate** in which Mr. Spanos sets 'fully accrued plant' to 0.00% depreciation rate and utilizes a depreciation rate consistent with the proposed amortization period for all not fully accrued plant." Exhibit 202, *Surrebuttal of John A Robinett*, pg. 8 lns. 9 – 12 (emphasis added); *see also* Exhibit 128, *Surrebuttal testimony of David T. Buttig*, pg. 4 ln. 14 – pg. 5 ln. 14. Unfortunately, Spire never bothered to explain this point in direct, and thus created the mess now before the Commission.

We now know how we got to where we are. Spire had a depreciation study performed that listed rates for general plant on both an amortized and dollar weighted "total account value" basis. Spire's expert witness (Mr. Spanos) apparently failed to indicate to Spire what his actual recommendation was because Spire ended up recommending the "total account value" rate for all the general plant accounts in direct.[20] Exhibit 202, *Surrebuttal of John A Robinett*, pg. 8 lns. 14 – 16. Staff then

[20] If one compares Spire witness Selinger's WES-1 H11-Depr Adj schedule from direct with page VI-6 of John Spanos' Schedule JJS-R2, one will see that account 391.1 is labeled Data processing Systems and given a rate of 12.12% in the former and given the label Mechanical Office Equipment with a rate of 6.67% (5.47% total account) in the latter. Conversely, account 391.2 is labeled Mechanical Office Equipment and given a rate of 5.47% in the former and is called Data processing Systems with a rate of 20.00% (12.12% total account) in the latter. It would appear that these two accounts were

went on to adopt all of Spire's requested depreciation rates from the Company's filed direct position, which, again, are the "total account values" found in Spire's own depreciation study. Exhibit 101, *Staff Cost of Service Report*, Appendix 3 (Schedule DTB-d1); Exhibit 35, *Rebuttal Testimony of John J. Spanos*, Schedule JJS-R2, pg. 52 through 53 of 396. In rebuttal, however, the same Spire witness who prepared the actual depreciation study argued that it should be the "amortized" rate that are applied to the accounts and that applying the "total account values" will result in an under-recovery. Exhibit 35, *Rebuttal Testimony of John J. Spanos*, pg. 18 ln. 12 – pg. 19 ln. 7 ("The 5 percent rate is the proper rate for the assets in Account 391.00."). As if this problem needed even *more* confusion, all that Spire's position statement has to say with regard to depreciation rates is that "The Commission should adopt the rates set forward in Schedule JJS-R2 because they reflect more current information and analysis." Spire Missouri, *Position Statement*, pg.14. The problem here is that both the "amortized" rate and the "total account value" rate for each account can arguably be said to have been "set forward in Schedule JJS-R2" because the schedule contains both sets of rates. This begs the very simple and important question: exactly which set of depreciation rates for general plant is Spire even requesting?

Spire botched the depreciation recommendation for general plant in this case. The company prepared and offered to Staff and OPC a depreciation study that had two sets of rates but did not file in direct either the study **or any testimony**

transposed. As was noted in a previous footnote, the same transposition occurs in Staff's schedule 3 of the class cost of service report. Given this information, the OPC presumes that 391.1 is meant to be correctly labeled Mechanical Office Equipment and that 391.2 should be labeled Data processing Systems.

supporting or explaining it. Exhibit 201, *Rebuttal Testimony of John A. Robinett*, pg. 2 ln. 17 – pg. 3 ln. 2. Instead, the Company filed a single schedule that included proposed rates that matched **one** of the two rates found in the depreciation study. Exhibit 34, *Direct Testimony of Wesley E. Selinger*, Schedule WES-1 H11-Depr Adj (pg. 38 of 45). Staff then filed its direct that just adopted the proposed rates found in Spire's request instead of performing the calculations Staff said it performed. Exhibit 101, *Staff Cost of Service Report*, Appendix 3 (Schedule DTB-d1). In rebuttal, Spire decides to file its depreciation study for the first time and then criticizes Staff for using the rates it requested in direct because, apparently, Staff was supposed to use the *other* set of rates in the depreciation study. Exhibit 35, *Rebuttal Testimony of John J. Spanos*, pg. 18 ln. 12 – pg. 19 ln. 7. Moreover it is now unclear exactly *which* set of rates Spire actually is requesting (the ones it originally requested that it claims will now result in under-recovery or the other set) because both are found in its depreciation study and Spire's positon statement just says to use the rates "set forward" in that study. Spire Missouri, *Position Statement*, pg.14. So there are basically two possibilities here: either Spire is requesting rates that its own expert witness argues are wrong and would result in under-recovery, or Spire has changed its position somewhere in the middle of the case and never bothered to tell anyone or modify its original request. Neither of these should be acceptable to the Commission.

Unfortunately, this was just the beginning of the depreciation errors. Please recall that there were two accounts noted earlier in this discussion as the sort of benchmarks to watch for: account 376.2 Mains - Cast Iron and account 391 Furniture

& Fixtures (also called office furniture and equipment). We have examined account 391 at some length, and we must now turn to account 376.2 Mains – Cast Iron. As with our previous discussion, one must start by pointing out that both Staff and Spire's **direct** testimony argued for the same 3.12% depreciation rate for this account. Exhibit 34, *Direct Testimony of Wesley E. Selinger*, Schedule WES-1 H11-Depr Adj (pg. 38 of 45); Exhibit 101, *Staff Cost of Service Report*, Appendix 3 (Schedule DTB-d1). However, Spire witness John Spanos provided significant discussion of why this rate was wrong in his rebuttal testimony:

> Q. PLEASE DISCUSS ACCOUNT 376.2, MAINS – CAST IRON.
>
> A. The assets in this account are distribution cast iron mains and accessories. Both Staff and I recommend an 80-year average service life for these assets, however, Staff disregards the impact going forward of the cast iron main replacement program. Therefore, it is necessary to include the truncation component that incorporates that all cast iron mains and their accessories will be retired by the end of 2030. The truncation date is a second life component that matches the full life cycle of cast iron mains with the recovery of these same mains. In other words, based on the information we know related to cast iron mains, all plant in service will be retired by end of 2030 so the depreciation rate must include this life component in order to ensure the full recovery by end of 2030. Staff does not oppose this program but neglects to reflect in their proposed rates the impact on annual depreciation.
>
> Q. SHOULD THE TRUNCATED SURVIVOR CURVE FOR CAST IRON MAINS INCLUDE THE ENCAPSULATION ASSETS?
>
> A. Yes. The encapsulation assets are part of the cast iron main plant in service and will be retired when the cast iron mains are retired by the end of 2030. Although, the encapsulation assets are of a more recent vintage than the cast iron mains themselves, these assets were necessary in order for the cast iron mains to reach the life they have to date. Therefore, the 2030 truncation year is appropriate for all assets in Account 20 376.2, Mains – Cast Iron. Again, Staff's report does not reflect the proper recovery of all cast iron main assets by end of 2030.

> Staff's proposed rate and 80-year average service life estimates that cast iron mains and the encapsulation assets will last on average another 70 years.

Exhibit 35, *Rebuttal Testimony of John J. Spanos*, pg. 14 ln. 1 – 23. The adjustments Mr. Spanos' references are included in his depreciation study at page III-5. Exhibit 35, *Rebuttal Testimony of John J. Spanos*, Schedule JJS-R2, pg. 38 of 396. However, there is no mention of the cast iron **encapsulations** that Mr. Spanos refers to in his testimony in the depreciation study, which is a point that will become relevant shortly. On page VI-5 of the depreciation report, Mr. Spanos' lays out the actual rate he proposes for cast iron mains, which is 12.35%. Exhibit 35, *Rebuttal Testimony of John J. Spanos*, Schedule JJS-R2, pg. 51 of 396.

Again, one must note that the rate Mr. Spano's rebuttal testimony recommended for account 376.2 (12.35%) is completely different than the rate Spire witness Wesley Selinger requested in direct testimony (3.12%). *Compare* Exhibit 35, *Rebuttal Testimony of John J. Spanos*, Schedule JJS-R2, pg. 51 of 396 *and* Exhibit 34, *Direct Testimony of Wesley E. Selinger*, Schedule WES-1 H11-Depr Adj (pg. 38 of 45). And, once again, the rate Staff adopted (which Mr. Spanos harshly criticizes for failing to take into account the end of life for the cast iron mains) is the same as what Spire actually requested in direct. Exhibit 101, *Staff Cost of Service Report*, Appendix 3 (Schedule DTB-d1). However, the point at which this starts to get *really* difficult is when the OPC gets involved. Unlike either Staff or Spire, the OPC **did** address the

issue of cast iron mains and encapsulations at some considerable length in direct testimony:

> **Q. What are you recommending as a change in depreciation rates for Account 376.2 – Mains- Cast Iron and why?**
>
> A. Since Case No. GR-2010-0171, the plant account balance for Account 376.2 Mains - Cast Iron has continued to increase. In Schedule 3 of Staff's Accounting Schedules in Case No. GR-2010-0171, the Staff reflected the plant in service balance for Account 376.2 Mains - Cast Iron at $14,241,880. Spire Missouri East's direct workpapers (excel file name: Rate Base at 9-30-20 MOE MOW Actuals w plant bal detail) provided by Spire to support the present case, however, indicates Account 376.2 Mains - Cast Iron has a plant in service balance of $32,999,803 as of September 30, 2020. OPC has previously outlined serious concerns with the fact that, despite plant being continuously removed from service under Spire Missouri East's Infrastructure System Replacement Surcharge ("ISRS"), the plant-in service is actually growing in amount on Spire's balance sheet. 20 CSR 4240- 40.030 (15)(D) describes the replacement program to be developed by each operator. Specifically 20 CSR 4240- 40.030 (15)(D)2 states:
>
> > A long-term, organized replacement program and schedule shall also be established for cast iron pipelines not identified by the operator as being high priority.
>
> Once the cast iron replacement program was implemented by the utility, the cast iron mains sub-account should have been considered a holding account in which little to no additions would be expected. When a utility begins replacing and retiring the cast iron mains, the associated plant in service balances should be decreasing with every retirement that occurs, but that is not what has been occurring for plant-in-service. Throughout the course of several ISRS cases that arose since Spire's last general rate case (Case No. GR-2017-0215), I became aware that the Cast Iron Mains account was being driven by joint encapsulations that were being capitalized on cast iron mains to allow for existing mains to continue to operate while new infrastructure was being installed in the adjacent areas. The large capitalizations of joint encapsulations in the cast iron account has drastically changed how the account has historically functioned. The vast majority of the asset values in the account no longer are expected to last 80 years as the cast iron pipe with these joint encapsulations are expected to last 10 years or less. Given the latest update to the ISRS legislation, which included a sunset provision set for 2029, **I would recommend using a remaining life**

> **technique for this account of 8 years with a net salvage percentage of -188% based on the average of the last 10 years of cost of removal experience.** Based on the work papers provided by Spire and their depreciation study sent to OPC, **I recommend a depreciation rate of 35.87% in order to collect the plant-in-service value and needed cost of removal values based on the most recent 10 year average.** This recommendation will result in a revenue requirement increase of approximately $23.2 3 million dollars on an annual basis for just this one account. Utilizing the current authorized depreciation rates for Spire Missouri East will require 35 more years of recovery with no additional additions just to recover the original investment. For Spire Missouri West to recover original cost using current depreciation rates will require 49 years assuming no further investment or retirements.

Exhibit 200, *Direct Testimony of John A Robinett*, pg. 3 ln. 11 – pg. 5 ln. 7. There is a lot to go over here, so let us take a moment to break this down.

First, it should be noted that the OPC was the **first** party to raise the issue of cast iron joint encapsulations. These encapsulations are, again, mentioned neither in Spire's depreciation study nor anywhere in Spire's direct discussion of depreciation (what little of it there is).[21] Despite this, Spire still accuses Staff of failing to consider

[21] In what is perhaps the ultimate of impolitic ironies, Spire responds to the OPC in surrebuttal with the following:

> Q. MR. ROBINETT STATES THAT THE COMPANY'S RECOMMENDED DEPRECIATION RATE OF 3.12% FOR CAST IRON MAINS IS NOT SUPPORTED BY ITS DEPRECIATION STUDY. DO YOU AGREE WITH THIS CONCLUSION?
>
> A. No. In the 2020 Depreciation Study the cast iron mains represents not only the remaining cast iron mains that are being replaced as part of the cast iron replacement program but also the cast iron main encapsulation assets. The 12.35% for Cast Iron mains is appropriate for all related cast iron assets in Account 376, however, the 3.12 percent that Mr. Robinett cites as the rate for cast iron mains is only for the mains themselves from the 2016 study and does not reflect the cast iron encapsulation assets. Both the main and the encapsulations will be replaced as part of the cast iron main replacement program.

To begin with, this answer obviously contradicts itself. The question is whether Spire's depreciation rate of 3.12% is supported by the depreciation study. Mr. Spanos indicates that he disagrees with Mr.

the importance of the joint encapsulations in Mr. Spanos' rebuttal Exhibit 35, *Rebuttal Testimony of John J. Spanos*, pg. 14 ln. 13 – 23. It is the OPC's position that Spire did not actually even *consider* the joint encapsulation problem until after the OPC pointed it out in direct. This would help to explain the significant difference between Spire and the OPC's adjustments to account for the cast iron main issue. Mr. Spanos recommended a 12.35% average service life for account 376.2 based on a truncation of the survivor cure to terminate in 2030. Exhibit 35, *Rebuttal Testimony of John J. Spanos*, Schedule JJS-R2, pg. 38 and 51 of 396. The OPC, on the other hand, used an 8 year remaining life technique with a net salvage percentage of -188% based on the last 10 years of cost removal experience. Exhibit 200, *Direct Testimony of John A Robinett*, pg. 4 lns. 19 – 21. This resulted in a depreciation rate of 35.87%. *Id*. at 22 – 23. This led to the following exchange at the evidentiary hearing offered by OPC witness John Robinett:

> Q. Is your adjustment designed to make sure that Spire recovers the outstanding balance of cast-iron main plants by the end of the -- I know 2030 is not around but I'm going to say the ISRS Sunset Provision?

Robinett's statement – thus implying that the depreciation study **does** support the 3.12% – but then goes on to discuss the 12.35% that the depreciation **actually** supports and claims the 3.12% Mr. Robinett is citing is from a 2016 study. **This means that Mr. Robinett was correct.** The current depreciation study does **not** support the 3.12% that spire originally requested because it actually supports 12.35%, **as Mr. Spanos himself points out**. Therefore, Mr. Spanos should be agreeing with the claim that the "rate of 3.12% for cast iron mains is not supported by [Spire's] depreciation study" not attempting to refute it. Moreover, the language in the reply seems to be attempting to tie the 3.12% recommendation to Mr. Robinett and suggests Mr. Robinett did not consider the joint encapsulations. As we now know, however, Mr. Robinett was literally the **first** person in this case to discuss joint encapsulations in testimony and he has recommended a 35.87% rate to account for them. Exhibit 200, *Direct Testimony of John A Robinett*, pg. 3 ln. 11 – pg. 5 ln. 7. Yet, despite all of this, **Mr. Spanos never even addresses the OPC's proposed 35.87% rate in either rebuttal or surrebuttal**.

A. Yes. If you look at my testimony on page four of my direct I spell out the math. I'm actually recommending the depreciation rate, which is almost three times what the Company did.

Q. Is Mr. Spanos's recommendation going to recover all of the outstanding cast-iron plants by the end of the ISRS Sunset Provision period?

A. I don't know. Mine accounts for not only the original cost but the cost of removal with an eight year life.

Tr. pg. 121 ln. 16 – pg. 122 ln. 4. The ultimate irony of this situation is that the OPC is now actually arguing for the highest depreciation rate, and thus the highest depreciation expense included in rates, related to this account. This will ultimately increase Spire's revenue requirement, which OPC witness John Robinett addressed in his testimony. Exhibit 200, *Direct Testimony of John A Robinett*, pg. 5 lns. 8 – 19.

To summarize the issue with the cast iron main account, there are three rates the Commission has to choose from. The first is the 3.12% that Spire originally requested and which Staff ultimately adopted. This rate is wrong, as both Spire and the OPC pointed out, because it fails to account for the termination of the cast iron accounts that will be brought on by Spire's pipe replacement program. Exhibit 35, *Rebuttal Testimony of John J. Spanos*, pg. 14 ln. 1 – 23; Exhibit 200, *Direct Testimony of John A Robinett*, pg. 3 ln. 11 – pg. 5 ln. 7. Then there is the 12.35% that Spire changed to be its request in the middle of the case. This number is wrong because it most likely fails to take into account the cast iron encapsulations and is based on just truncating the life of the account without considering changes in the net salvage percentage. Exhibit 35, *Rebuttal Testimony of John J. Spanos*, Schedule JJS-R2, pg. 38 of 396; Tr. pg. 121 ln. 16 – pg. 122 ln. 4. Finally, there is the OPC's recommendation

of 35.87% which is the only one made with the cast iron joint encapsulations specifically in mind and which has included modifications to account for changes in the net salvage percentage based on historical data. Exhibit 200, *Direct Testimony of John A Robinett*, pg. 3 ln. 11 – pg. 5 ln. 7. Given these factors, the OPC's recommendation is the obvious choice.

We are, unfortunately, still not done addressing errors regarding depreciation. The next issue to discuss is a problem that Staff has created of its own accord. In the surrebuttal testimony of Staff witness Buttig, he states that Staff's recommendation is to maintain the currently ordered depreciation rate for Account 391.95 Enterprise software. Exhibit 128, *Surrebuttal of David T. Buttig*, pg. 7 lns. 1 – 2. Mr. Buttig further states that the current rates for this account are the same as those set in case GO-2012-0363. *Id.* at lns. 4 – 5. The rate set in GO-2012-0363 was 7% based on a 15 year average service life.[22] GO-2012-0363, *Report and Order*, pg. 10 ¶ 2, pg. 8 ¶ 16. This is not what Staff has actually recommended in Appendix 3 of its cost of service report, which shows a 10% depreciation rate based on 10 year average service life an 0% net salvage. Exhibit 101, *Staff Cost of Service Report*, Appendix 3 (Schedule DTB-d1). Staff's Appendix 3 recommendation is consistent with Spire's depreciation study while Spire's direct testimony did not list a depreciation rate for this account and instead directed the reader to a different schedule that did not list any deprecation rates. Exhibit 35, *Rebuttal Testimony of John J. Spanos*, Schedule JJS-R2, pg. 52 of

[22] Based on Staff's calculation of $Depreciation\ Rate = (100\% - Net\ Salvage\ \%) \div (Average\ Service\ Life)$, this would imply a -5% net salvage percentage. {7% = (100% - (-5%)) ÷ 15}.

396; Exhibit 34, *Direct Testimony of Wesley E. Selinger*, Schedule WES-1 H11-Depr Adj (pg. 38 of 45). Now, the odd part here is that Mr. Buttig's surrebuttal argues that the 7% should be maintained because the "depreciation study as provided by the Company does not provide the evidence for a shortened average life for these assets[,]" which the OPC completely agrees with. Exhibit 128, *Surrebuttal of David T. Buttig*, pg. 7 lns. 21 – 22.There is no evidence to support changing the depreciation rate for account 391.95 from 7% ordered in GO-2012-0363, which is based on a 15 year average service life and a negative 5% net salvage percentage, to the 10% Spire has requested based on a 10 year life and 0% salvage. *Id*. Thus, the OPC supports Staff's surrebuttal position, which has now been changed from its direct position.[23]

The next error relates to accounts 381.1 and 382.1 (Smart Meters and Smart Meter Installations, respectively). Fortunately, this issue seems to have been largely resolved. When Spire first filed direct, it requested these accounts be changed from the existing 5% to 6.67%. Exhibit 34, *Direct Testimony of Wesley E. Selinger*, Schedule WES-1 H11-Depr Adj (pg. 38 of 45). This was consistent across both the direct testimony and the depreciation study and was based on a change to a 15 year average service life from a 20 year average service life (no net salvage percentage in both cases). *Id*.; Exhibit 35, *Rebuttal Testimony of John J. Spanos*, Schedule JJS-R2, pg.

[23] During opening statements, counsel for the OPC repeatedly stated that the average service life for the enterprise software should be 10 years. This is incorrect and should be disregarded. Counsel for the OPC had become confused due to the disconnect between Staff's report and its recommendation as laid out in this paragraph. The correct average service life is 15 years with a -5% salvage value to yield a final rate of 7% as ordered in GO-2012-0363. GO-2012-0363, *Report and Order*, pg. 10 ¶ 2, pg. 8 ¶ 16.

51 of 396. Staff initially adopted these changes in its recommended depreciation rates. Exhibit 101, *Staff Cost of Service Report*, Appendix 3 (Schedule DTB-d1). In rebuttal, the OPC pointed out that the Commission had just recently (September 16, 2020) ordered the depreciation rates for these accounts at 5% based on a 20 year average service life. Exhibit 201, *Rebuttal of John A. Robinett*, pg. 7 lns. 8- 10. This 20 year average service life was based on the actual expected battery life of the internal battery found in the meter. *See* Exhibit 32, *Rebuttal Testimony of James Rieske*, Schedule JAR-R3 pg. 4 of 4 (Battery Life 20 year for meter, RF and valve using recommended parameters"). "Staff [] filed no supportive direct testimony that addresses why it [] recommend[ed] a change in depreciation rates for [these accounts,]" and also failed to provide "any sort or regional/state study of depreciation rates authorized for similar accounts in its Cost of Service Report that could be a basis for changing rates." Exhibit 201, *Rebuttal of John A. Robinett*, pg. 7 lns. 11 – 14. Moreover, the OPC pointed out that "these are new accounts and have yet to experience any retirements let alone enough retirements to even attempt to perform a statistical analysis of account lives experienced." *Id.* at lns. 15 – 17; *see also Id.* at pg. 8 lns. 2 – 6. Having pointed out these problems, Staff changed its position in surrebuttal back to the original 5%. Exhibit 128, *Surrebuttal of David T. Buttig*, pg. 8 lns. 13 – 15 ("Staff is correcting an inadvertent error made in its Direct filing. Staff became aware of the need for this correction in the Rebuttal Testimony of OPC witness John A. Robinett"). Staff then went on to agree with the OPC that Spire had

presented no evidence to support the proposed change. *Id*. at pg. p lns. 11 – 12. In its filed position statements, Spire stated as follows:

> While the Company's depreciation study supports a depreciation rate change for accounts 381.1 and 382.1, the Company will maintain depreciation rates as ordered in Case No. GO-2020-0416 at this time. The Company reserves the right to request adjustment of the depreciation rate for these accounts in future rate cases.

Spire Missouri, *Position Statement*, pg.15. Therefore, as previously indicated, it would appear that this issue has been fully resolved at this time as all parties agree that the correct depreciation rate for accounts 381.1 and 382.1 (Smart Meters and Smart Meter Installations, respectively) should be 5%.

The discussion of smart meters brings us to another major issue in this case; the problem with account 381 - Meters.[24] In fact, this one error might possibly be the single most alarming problem with the entire depreciation issue. In this circumstance Spire's direct position, Spire's depreciation study, and Staff's recommendation are all largely aligned. Spire's direct position requested a rate of 2.77%. Exhibit 34, *Direct Testimony of Wesley E. Selinger*, Schedule WES-1 H11-Depr Adj (pg. 38 of 45). Spire's deprecation study recommended a rate of 2.77% based on a 35 year average service life and 3% net salvage percentage. Exhibit 35, *Rebuttal Testimony of John J. Spanos*, Schedule JJS-R2, pg. 51 of 396. Staff recommended a rate of 2.85% based on a 34 year average service life and 3% net salvage rate. Exhibit 101, *Staff Cost of Service Report*, Appendix 3 (Schedule DTB-d1). The problem is that the record now suggests that the

[24] Account 381 – Meters is distinct from account 381.1 – Smart Meters and consist primarily of Spire's existing diaphragm meter infrastructure.

meters in this account are **not** lasting 34 – 35 years on average and are actually being retired much sooner than that. Moreover, the evidence clearly shows that Spire **knew** about this problem, did **nothing** about it for **years**, and is still not trying to actively correct the problem.

Let us begin with a review of the facts. Spire made a request in this case to recover the cost of ultrasonic meters used to replace existing diaphragm meters. This is a massive issue that will be discussed at length later in this brief. As part of the investigation of this issue, the OPC came to discover that there was a discrepancy between the depreciable life of Spire's diaphragm meters and the actual average service life. Of particular importance was Spire's response to Staff data request 0443 question 14:

> 14. Has Spire Missouri retired the existing diaphragm meters that were removed for testing within the meter sampling process which meet the accuracy standard? Explain and cite any adjustments Spire Missouri made within this case to account for the retirements.
>
> **Spire has been retiring most existing diaphragm meters that were removed for testing and met the accuracy standard for years**. This has been the case in all regions and is consistent across the industry. **For some time, there has been a disconnect between the asset depreciation and the practical life of a meter**. Spire agrees that this needs to be analyzed and that further conversations and discussions with Staff and other interested parties are beneficial. . . .

Exhibit 202, *Surrebuttal Testimony of John A. Robinett*, pg. 14 lns. 5 – 15 (emphasis added). This was further confirmed during the evidentiary hearing as part of the cross-examination of Spire witness James Rieske:

Q. And you previously testified that the average service life you are seeing is -- I wrote them down, but I want to make sure I get these correct -- 18.8 for the East and 22.1 for the West?

A. That's correct.

Q. So is that at a high level, roughly, when you are going to be doing these replacements, they are going to be that old?

A. So, yes, that would be a good starting point. I think -- you know, we recognize we need to more aggressively replace our metering populations because there are a lot of underperforming populations. So I would expect that to continue to slightly trim downward, but that is where we're at historically.

Q. Have you reviewed -- have you reviewed the testimony filed by John J. Spanos in this case?

A. I have not.

Q. All right. That is the depreciation testimony that Spire has submitted for evidence in this case. So you have not reviewed his recommended average service life for diaphragm meters?

A. I have not.

Q. You're not aware that he's recommending a 35-year life again in this case?

A. I'm not.

Q. Have you reviewed the testimony of Mr. John Robinett?

A. I have not.

Q. So you're not aware that Mr. Robinett points out that Mr. Spanos has also recommended that same 35-year life on average over the past four cases?

A. I would tell you that I am an operational expert in metering technology and I do not set or manage the way that we depreciate our assets.

Q. But, according to you, the average service life for diaphragm meters is substantially less than what Spire's other witness has claimed? For reference, they are claiming 35 years.

A. In this case, yes, I became aware of that discrepancy.

> Q. How long would you see that average service life for meters has actually been in that 18- to 20-year range?
>
> A. I don't know.

Tr. pg. 253 ln. 19 – pg. 255 ln. 12. To his credit, the numbers cited by Mr. Rieske do match the response Spire gave to OPC data request 8521. Exhibit 202, *Surrebuttal Testimony of John A. Robinett*, pg. 15 lns. 2 – 4. This fact does **not**, however, help to alleviate the problem.

This should be a **major** concern for the Commission. On the one hand, you have Spire's touted expert in the field of depreciation with a study that says Spire's meters should last **on average** at least 35 years. Exhibit 35, *Rebuttal Testimony of John J. Spanos*, Schedule JJS-R2, pg. 51 of 396. On the other hand you have a Spire witness and self proclaimed "operational expert in metering technology" stating that they will only last between 18 and 22 years. Tr. pg. 253 ln. 19 – pg. 255 ln. 12. Obviously one of these two people is wrong. The Commission is **necessarily** going to have to find one of Spire's two experts to not be credible. Once that occurs, why would the Commission consider **anything** that witness had to say to be credible moving forward? After all, this is not some minor error. Account 381 has $188,721,499 worth of plant-in-service across both systems. Exhibit 102, *Staff Accounting Schedules*, Accounting Schedules 3, page 1 of 2, ln. 23. A timing difference somewhere between 13 to 17 years could lead to depreciation expense differences in the multiple millions

of dollars range.[25] Moreover, there is a major timing element that needs to be considered here.

As OPC witness Mr. John Robinett points out in his surrebuttal testimony, the 35 year average service life for account 391 has been a fairly **consistent** recommendation by Spire witness John Spanos:

> In Laclede Gas Company's depreciation study for plant as of September 30, 2003, the average service life recommendation for the meters account was 37 years with a positive 5% net salvage. In Laclede Gas Company's depreciation study for plant as of September 30, 2009, the average service life recommendation for the meters account was 37 years with a positive 5% net salvage. In Laclede Gas Company's depreciation study for plant as of September 30, 2012, the average service life recommendation for the meters account was 33 years with a positive 3% net salvage. In Laclede Gas Company's depreciation study for plant as of September 30, 2016, the average service life recommendation for the meters account was 35 years with a positive 3% net salvage. In Spire Missouri's depreciation study for plant as of September 30, 2020, the average service life recommendation for the meters account was 35 years with a positive 3% net salvage. **Consistently Mr. Spanos has recommended average service lives for diaphragm meters ranging from 33-37 years** . . .

Exhibit 202, *Surrebuttal Testimony of John A. Robinett*, pg. 15 lns. 19 – pg. 16 ln. 10 (emphasis added). Despite this, Spire claims that it has known about the discrepancy between depreciable life and actual average service life "for some time." Exhibit 202, *Surrebuttal Testimony of John A. Robinett*, pg. 14 ln. 12; Tr. pg. 255 lns. 9 – 12 ("Q.

[25] For illustration. Staff's current depreciation rate for meters is 2.85% based on a 34 year average service life and 3% net salvage (2.85% = (100% - 3%) / 34). Multiplying this by the amount of plant in service yields depreciation expense of $5,378,563. Exhibit 102, *Staff Accounting Schedules*, Accounting Schedules 5, page 1 of 3, ln. 23. If we change the average service life to 20 years, the depreciation rate changes to 4.85% (4.85% = (100% - 3%) / 20). At 4.85%, the depreciation expense is $9,152,993. This results in an increase of $3,774,429 to Spire's revenue requirement.

How long would you see that average service life for meters has actually been in that 18- to 20-year range? A. I don't know."). This implies that Spire has **knowingly** allowed this problem to persist over the course of what could be almost a **decade** without doing anything about it. This should not be considered acceptable.

What is really and truly galling about this massive inaccuracy that Spire's own witnesses have developed is the degree to which Spire witness Spanos criticizes Staff (and to a lesser extent OPC) for failing to engage in a detailed boots-on-the-ground investigation of Spire's system. *See* Exhibit 35, *Rebuttal Testimony of John J. Spanos*, pgs. 3 – 8. In fact, "Mr. Spanos even discusses the importance [of] relying on conversations with management to gain an understanding of how plans of the utility may affect the retirement date and rate of a particular asset class at page III-3 of his depreciation study (page 36 of 396 of Schedule JJS-R2)." Exhibit 202, *Surrebuttal Testimony of John A. Robinett*, pg. 21 lns. 17 – 20. Apparently, Mr. Spanos does not actually practice what he preaches – or else Spire has been knowingly misinforming its own expert witness for years. This is the only explanation for why Mr. Spanos would **continue** recommending a 35 year average service life for an asset that Spire's other expert claims may only last half that long. Further, there are plenty of other areas where Mr. Spanos either does not follow his own advice or else appears to have just ignored the actual historical evidence in developing his recommended rates. For example, with regard to the proposed change to 15 years for accounts 381.1 and 382.1 (Smart Meters and Smart Meter Installations, respectively) OPC witness John Robinett notes the following:

> OPC asked data request number 8511 which sought Mr. Spanos' rational[e] for changing the lives of the smart meters and smart meters installations accounts with no historical retirement data for Spire Missouri. Spire's answer, which is signed by Mr. Weitzel, indicates that:
>
> > The 15 year life is based on the understanding of the nature of the smart meters and informed judgment of the life cycle of smart meters which includes the life estimates of other utilities in the industry that have experienced more defined life characteristics for smart meters.
>
> In this answer, which I will assume was at least informed by Mr. Spanos, he seems to indicate no reliance on experience by Spire. This answer appears to be only based on what Mr. Spanos has seen at other utilities, of which there is no evidence in his testimony or attached schedules that would support what other gas utilities have done or are doing with ultrasonic meters. Moreover, it is unclear what type of utilities are being referenced in this answer.

Exhibit 202, *Surrebuttal Testimony of John A. Robinett*, pg. 21 lns. 17 – 20. There are yet still more examples:

> Page 380 of 396 of Schedule JJS-R2 is a generated report from the software that used Spire's recommended rate and net salvage parameter to determine the annual accrual based on the vintage additions. One important note is there are no output files from the retirement rate calculation function that analyzes the historical retirement and remaining original investment in order to determine the average service life based on the retirement rate. No retirement data once again means Mr. Spanos is relying on what other utilities are doing for their enterprise software but doesn't present any information about what the other utilities are doing or if their systems are using the same software platforms as Spire. Again, this account seems to be driven by other utilities actions and has zero historical retirement basis of Spire that would have driven a change in depreciation rates.

Exhibit 202, *Surrebuttal Testimony of John A. Robinett*, pg. 23 lns. 3 – 12. One of the larger examples though relates to the average service life for plastic mains.

"Spire Missouri consultant Mr. John J. Spanos' depreciation study attached to his rebuttal testimony [] recommends a 60-year life for plastic mains." Exhibit 202, *Surrebuttal Testimony of John A. Robinett*, pg. 3 lns. 20 – 21. "Spire's direct testimony is a recommendation of 2.34% with no detail on the average service life or net salvage percentages that make up the depreciation rate." *Id*. at pg. 3 ln. 21 – pg. 4 ln. 2. This recommendation represents a significant decrease in rates as Mr. Robinett explains:

> The depreciation study for Laclede Gas Company for gas plant at September 30, 2003 indicated a 70 year average service life with a -15% net salvage. The depreciation study for Laclede Gas Company for gas plant at September 30, 2009 indicated a 70 year average service life with a -15% net salvage. The depreciation study for Laclede Gas Company for gas plant at September 30, 2012 indicated a 75 year average service life with a -25% net salvage. The depreciation study for Laclede Gas Company for gas plant at September 30, 2016 indicated a 75 year average service life with a -30% net salvage. The depreciation study for Spire Missouri for gas plant at September 30, 2020 indicated a 60 year average service life with a -40% net salvage.

Id. at pg. 4 lns. 5 – 13. This is a problem because the decline in life rates for this asset is being driven by the accelerated, premature retirement of plastic mains due to Spire's ongoing ISRS projects and is thus an inaccurate representation of the actual life of these assets. *Id*. at pg. 4 ln. 16 – pg. 5 ln. 32 ("[The] distortion in the average service life on [plastic pipe] by continuous early retirements may result in a skewed and abnormal relationship between the plant and reserve balance. This skewed and abnormal relationship, if not noted and removed from the depreciation study, will likely indicate an increase in depreciation rates when no increase is actually

needed."). This is an issue the OPC had pointed out over four years ago, but which had been largely ignored at the time. *Id*. at pg. 5 lns. 29 – 30.

The failure of Spire's so-called expert to address the issue related to the premature retirement of plastic pipes despite all his testimony regarding the importance of making site visits and talking with company personnel is just another example of the inherent failure of Spire's depreciation recommendation. It is especially ironic given Spanos' report discusses the accelerated replacement of plastic services due to Spire's ISRS program. Exhibit 35, *Rebuttal Testimony of John J. Spanos*, Schedule JJS-R2, pg. 37 of 396 ("Management has established replacement of the majority of copper services with plastic services and increased its capital budget for installing new plastic services when the associated main is replaced, particularly the replacement of cast iron main."). Of particular importance here is the fact that, again, Spire's own witnesses have provided testimony that shows these assets should have a different service life than what Mr. Spanos is now recommending:

> In addition, over past several ISRS cases Spire made a compelling argument for extending the lives of plastic (polyethylene) mains to lives that exceed metallic mains as they lack the inherent flaw of corrosion that exists in the other main types.
>
> > Q. Is it your opinion that plastic is going to last longer than the cast iron 4 or unprotected steel?
> >
> > A. Yeah. The industry right now, no indication that there will be any issues with the plastic. Early on when the plastic was first involved there were some issues with what's called legacy plastic. We do not have any of that, for instance, in Missouri East. Other companies may have a little bit of that. They're going to replace it. **But the**

plastic we're putting in, the polyethylene, it should last indefinitely.

Exhibit 202, *Surrebuttal Testimony of John A. Robinett*, pg. 20 ln. 19 – pg. 21 ln. 10. Stop and consider this for a moment. Spire's witness Mr. Spanos is now arguing the life of an asset that Spire witness Craig R. Hoeferlin previously testified should "last indefinitely" should be shortened. This is wrong. The decreased average service life being seen for the plastic mains account is being driven by premature retirement caused by Spire's ISRS program, which is a factor that Spire's purported depreciation expert has either overlooked or ignored. The Commission thus needs to step in and modify the plastic mains rate as proposed by OPC witness John Robinett to account for this premature retirement problem. *Id.* pg. 6 lns. 12 – 18. ("I recommend utilizing a 75 average service life, which is consistent with the September 30, 2012 and 2016 depreciation studies performed by Mr. Spanos . . . . Consistent with the current depreciation study that has seen an increase in cost of removal, I recommend utilizing the -40% net salvage as calculated by both Staff and Mr. Spanos. Utilizing the -40% net salvage and 75-year average service life, I recommend a depreciation rate of 1.87% for Account 376.3 Mains- Plastic.").

With that, we come to the end of our exhaustive discussion of the problems necessary to understand how the absolute mess that is the depreciation issue came about. To summarize those problems again briefly:

1. Spire failed to file either its depreciation study or any testimony properly explaining the depreciation rates that it was seeking (and how they had been developed) in direct.

2. Instead, Spire filed a single schedule that just listed its proposed depreciation rates, not all of which were actually supported by its own study.

3. Staff filed a recommendation that **claimed** to be the product of an independent study but actually largely adopted what Spire had proposed even when the rates were inconsistent with the calculation that Staff claimed to have used.

4. Spire then filed rebuttal that criticized Staff for adopting the rates Spire had originally proposed and effectively sought to change its position in the middle of the case without modifying its original testimony.

5. Spire's position statement makes it unclear which set of rates found in its depreciation study the Company is actually requesting.

6. Both Staff and Spire's original positions called for a depreciation rate of 3.12% for account 376.2 mains – cast iron, but Spire then changed its position to argue for a 12.35% rate due to the need to recover the balance before the end of the ISRS sunset period (the OPC meanwhile is recommending an even more aggressive 35.87% based on joint encapsulations and increased net salvage costs).

7. Staff adopted Spire's proposed rates for account 391.95, despite there being no evidence for a change, and then filed surrebuttal that changed its position and argued that Spire's proposed change should not be adopted because it pointed out correctly that there was no evidence to support the change.

8. Both Spire and Staff sought to change the depreciation rates for accounts 381.1 and 382.1 without any evidence to support the change and then recanted that position through the position statement and surrebuttal respectively.

9. Staff and Spire recommended very similar rates for account 381 meters based on a 34 and 35 year average service life respectively, only for another Spire witnesses to argue that this average service life was wrong and that the actual service life should be between 18 and 22 years, which calls Spire's entire depreciation study into question.

10. The evidence shows that Spire has known about the discrepancy between the depreciable life of meters and their actual life "for some time" and did nothing to fix it (including requesting different rates at any point in the last four rates cases), thus further calling their depreciation study into question.

11. Finally, both Spire and Staff have reduced the average service life of plastic mains despite prior Spire testimony saying those mains should "last indefinitely" because both parties have ignored the fact that the mains are being prematurely retired due to the ISRS and thus driving down the lives, as the OPC's witness warned the Commission about four years ago.

After going through all of this we may, at long last, finally come to the OPC's recommendation in this case.

To fully understand the OPC's position in this case, one must understand two things: (1) the timing of the testimony and (2) the limitations of our office. We shall start with the latter. No OPC witness performed a depreciation study in this case because the OPC does not have the technological capabilities to do so. Exhibit 202, *Surrebuttal Testimony of John A. Robinett*, pg. 19 lns. 17 – 18. ("I did not perform a study, as OPC does not have depreciation software needed to perform a study.") That is the simple, candid truth. Now we pivot to the first point. When it came time to file direct, the OPC had the following: (a) a depreciation study that was not in the record, (b) a filed schedule requesting rates that were not consistent with the depreciation study, and (c) specific issues with specific rates based on accumulated knowledge and understanding of Spire's system. Based on the problems that were already beginning to appear, and given the limitations presented, the OPC chose to recommend maintaining Spire East's existing rates (with several modifications to address specific

issues) and to have Spire West adopt Spire East's rates. Exhibit 200, *Direct Testimony of John A. Robinett*, pg. 3 lns. 6 – 10; pg. 1 lns. 18 – 19.

When it came time to file rebuttal, the OPC still did not have Spire's depreciation study in the record (Spire did not file the depreciation study until its rebuttal which was filed concurrently with the OPC's rebuttal) and so the OPC's witness began his testimony by attempting to explain **why** it appeared Spire was not filing its depreciation study. *See* Exhibit 201, *Rebuttal Testimony of John A. Robinett*, pgs. 1 – 2. This discussion was based on the testimony of Spire witness Selinger that was mentioned at the very beginning of this analysis and focused on the fact that Spire appeared to be arguing that it was not required to file a depreciation study because it had already filed one within the last five years. *Id.* at pg. 2 lns. 1 – 3. ("As Mr. Selinger points out on page 17 of his direct testimony, Spire has submitted depreciation studies, databases, and property unit catalogs in its most recent general rate cases, GR-2017-0215 and GR-2017-0216, less than five years ago."). The OPC further pointed out that the depreciation study did not support the rates being sought as we have already explored at length. *Id.* at pg. 3 lns. 12 – 20. Based on the proposed rates in Spire's direct, the OPC assumed (much as Staff appears to have done) that Spire was requesting the weighted average (or total account value) rates, which are the same rates found in Spire's direct and Staff's recommendation. The OPC recognized the same problem that Spire would ultimately point out in its own rebuttal, which is that these rates will result in under-recovery. *Id.* at pg. 5 lns. 13 – 19. ("Spire's recommended actions for these general plant accounts will result in new

investments not being fully recovered by the time the assets in the accounts are to be retired based on the allowed amortization period because the new recommendation of depreciation rates does not reflect the full life of the assets since it is being weighted and reduced by assets that have been fully recovered by Spire. To simplify and re-state, Spire's recommendation is setting the Company up for under recovery of all general plant accounts that are amortized."). The OPC's witness therefore recommended that Spire's proposed rates (which at this point both Staff and OPC thought were those actually listed in Spire's direct filing) should be rejected.[26] *Id*. at pg. 5 lns. 22 – 23.

Spire filed its rebuttal at the same time as the OPC's rebuttal. Spire's rebuttal criticized the OPC for not engaging in "informed judgement" *i.e.* looking at specific factors beyond the mathematical.[27] Exhibit 35, *Rebuttal Testimony of John J. Spanos*, pg. 3 lns. 18 – 21. Specifically Mr. Spanos states: "The statistical component of life and net salvage analyses should include all of the forces of retirement and drivers for replacement at that time so developing lives or net salvage estimates need to include different practices or policies if they existed." *Id*. at lns. 21 – 24. The OPC has already shown that Mr. Spanos ignored his own advice here in a number of ways, most importantly with regard to account 381 Meters and account 376.3 Mains- Plastic. *See*

[26] The OPC also addressed several other issues in direct including the change to accounts 381.1 and 382.1. Exhibit 201, *Rebuttal Testimony of John A. Robinett*, pgs. 6 – 7.

[27] Needless to say, this is obviously false given the fact that the OPC's direct made specific adjustments based on thorough analysis of the actual behavior of Spire's business including most importantly the adjustment to cast iron mains that Spire would also go on to recommend. *See* Exhibit 200, *Direct Testimony of John A Robinett*, pg. 3 ln. 11 – pg. 5 ln. 7.

generally, Exhibit 201, *Surrebuttal Testimony of John A. Robinett*, pgs. 3 – 6; 13 – 24. After unfairly criticizing the OPC, Mr. Spanos then goes on to attack Staff for interpreting Spire's depreciation study in a manner that resulted in the rates that Spire itself originally requested and then further requested adjustments to accounts 391.95 Enterprise software, 381.1 Smart Meters, and 382.1 Smart Meter installations based on vague statements that "[t]hese assets relate to new technology and we know technology is always changing." *See* Exhibit 35, *Rebuttal Testimony of John J. Spanos*, pgs. 5 – 19.

Spire's decision to completely change the nature of its request mid-case threw everything into confusion (as has already been discussed). The OPC was consequently facing a considerable problem in surrebuttal. The OPC still could not perform its own depreciation study (even if there had been time to do so, which was not the case) and data request responses had now made it clear that there was massive inaccuracies in the depreciation study Spire prepared related to the account 381 Meters. There was also the problem with the plastic mains account discussed above and the fact that Spire was paradoxically agreeing with the OPC's criticism of the rates it had previously proposed and making further adjustments that were aligned with the adjustments the OPC had already made to the cast iron mains account while simultaneously accusing the OPC of not using informed judgement. To cap it all off, the OPC became aware for the first time that Spire appeared to be requesting general pant amortization, which was an issue not addressed before Spire's rebuttal was filed. The OPC thus set out to address **all** of these problems in surrebuttal. *See generally*,

Exhibit 201, *Surrebuttal Testimony of John A. Robinett*. Fortunately, we need not cover this because almost all of the OPC's response has already been addressed.

This brings us to the last piece, which is Spire's surrebuttal.[28] Because Staff did not file rebuttal, Mr. Spanos' surrebuttal responds exclusively to the OPC. First Mr. Spanos responds to the OPC's effort in rebuttal to explain why Spire had not actually filed its depreciation study. Exhibit 36, *Surrebuttal of John J. Spanos*, pgs. 2 – 3. However, Mr. Spanos misconstrues what the OPC said in rebuttal to such an extent that it appears Spanos is under the impression that the OPC was arguing Spire was **not** supposed to file a depreciation study. *Id*. This is so horribly confused that it is almost not worth attempting to explain, but an attempt will still be made. To recap: when the OPC filed rebuttal there was no depreciation study filed in the case so the OPC wrote rebuttal explaining why it **appeared** Spire had not filed a depreciation study to support its case. Exhibit 201, *Rebuttal Testimony of John A. Robinett*, pgs. 1 – 2. It is very important to understand that the OPC was being critical of the fact that Spire had not filed its depreciation study yet. Exhibit 201, *Rebuttal Testimony of John A. Robinett*, pg. 3 lns. 8 – 11 ("Q. Have you received this depreciation study and reviewed its conclusions? A. Yes. **However, my review of the depreciation study is of somewhat limited value given that Spire has not filed the study in this case and has therefore failed to support the depreciation rates it has recommended and is requestin**g."). Spire, meanwhile,

[28] The OPC won't address Staff's surrebuttal which largely just defended its own rates against the criticism raised by Spire and changed the Staff's position on accounts 391.95 Enterprise software, 381.1 Smart Meters, and 382.1 Smart Meter installations. *See generally*, Exhibit 128, *Surrebuttal Testimony of David T. Buttig*.

filed rebuttal that actually **did** have the depreciation study attached. Exhibit 35, *Rebuttal Testimony of John J. Spanos*, Schedule JJS-R2. In surrebuttal, Spire "responds" to the OPC by arguing why it was important to have a new depreciation study and tries to imply that the OPC did **not** want a new depreciation study filed. Exhibit 36, *Surrebuttal of John J. Spanos*, pgs. 2 – 3. This argument is flawed for two reasons. First, the OPC **never** argued that Spire should not file a depreciation study, and, in fact, argued the **exact opposite**. Exhibit 201, *Rebuttal Testimony of John A. Robinett*, pg. 3 lns. 8 – 11. Second, if it was so important for Spire to have a new depreciation study for this case then **why on earth did the Company not file direct testimony to support its rates and include the study**?

The rest of Mr. Spanos' surrebuttal is spent attacking the criticism that the OPC levied at the rates Spire proposed in direct, which, you may recall, were the same rates that Staff adopted in direct and the Company refuted in rebuttal. Some of this has already been addressed such as his response to the OPC regrading cast iron mains. *See* footnote 21 *supra*. Others are just blatant miscommunication. For example, on page 5 a question is posed as to whether using the weighted average rates (which is what Staff has adopted and what Spire *originally* proposed) will result in under-recovery as Mr. Robinett pointed out. Exhibit 36, *Surrebuttal of John J. Spanos*, pg. 5 lns. 17 – 23. Keep in mind that Spanos had literally already testified that they will. Exhibit 35, *Rebuttal Testimony of John J. Spanos*, pg. 18 ln. 12 – pg. 19 ln. 7. Here, though, Spanos basically sidesteps the issue by instead discussing the

"amortized" rate from the depreciation study. Exhibit 36, *Surrebuttal of John J. Spanos*, pg. 6 lns. 1 – 8. The point is that the testimony he is responding to was criticizing a completely different rate; the rate that everyone else **thought** Spire was requesting because that is exactly what Spire said in direct.

To put this in context, consider a single account: 391 Office Furniture. In direct the Company says the rate should be 4.71%. Exhibit 34, *Direct Testimony of Wesley E. Selinger*, Schedule WES-1 H11-Depr Adj (pg. 38 of 45). In rebuttal, the OPC says 4.71% for this account will result in under-recovery. Exhibit 201, *Rebuttal Testimony of John A. Robinett*, pg. 5 lns. 17 – 19. ("To simplify and re-state, Spire's recommendation is setting the Company up for under recovery of all general plant accounts that are amortized."). Spire, in its rebuttal, **also states that 4.71% for this account will result in under-recovery**. Exhibit 35, *Rebuttal Testimony of John J. Spanos*, pg. 18 ln. 12 – pg. 19 ln. 7. Then, in surrebuttal, Mr. Spanos is effectively asked: is John Robinett right that this account will result in under-recovery? And his response is effectively: no, because "new investment in Account 391.00 will be recovered at 5.0% which is consistent with the 20 year amortization period." Exhibit 36, *Surrebuttal of John J. Spanos*, pg. 6 lns. 6 – 8. This frustrating line of questioning is consistent across Mr. Spanos' entire surrebuttal, and the whole testimony should be disregarded by the Commission as a result.

There remains one last major hurdle regarding the depreciation analysis. That is the issue of general plant amortization. We have already seen how the rates proposed by Staff (and Spire's direct) are wrong. The next issue is more nuanced and

difficult to understand. Effectively Spire is seeking the Commission to approve two sets of rates for each account in the general plant bucket. The first is the "amortized" rate, which is applied to plant that is not fully accrued, and the second is a 0.00% rate that will be applied the plant that is fully accrued. *See* Exhibit 35, *Rebuttal Testimony of John J. Spanos*, Schedule JJS-R2, pg. 52 of 396 (note the division of the accounts into two parts "amortized" and "fully accrued"). Based on this, the OPC surmises that Spire is seeking what is known as "general plant amortization" or alternatively "Vintage Year Accounting." Exhibit 202, *Surrebuttal Testimony of John A. Robinett*, pg. 7 lns. 2 – 8; pg. 10 lns. 1 – 2. This type of accounting is not sound, is not in the public interest, and should not be endorsed as explained at length by OPC witness John Robinett. *Id*. at pg. 10 ln. 1 – pg. 12 ln. 7. One might ask, "if that is the case, then what does the OPC recommend?" The answer is quite simple, just order the one rate (the amortized rate) for each account. Thus, for account 391 Office furniture, for example, the Commission should just order a rate of 5.00% for the account and nothing more. If the Commission *does* decide to allow Spire to have the two rates for each account (*i.e.* order general plant amortization), there are several conditions that the OPC proposes:

> If the Commission approves Spire's request for General Plant Amortization, I recommend that the Commission order Spire to continue specifying the original cost and associated retirement units for all additions to the accounts where General Plant Amortization accounting treatment will occur. Additionally, Spire should be placed under a standing order to treat all general plant that exceeds the amortization period as retired for ratemaking purposes

Id. at pg. 12 lns. 10 – 15. These recommendations should largely resolve the issues identified by the OPC's expert witness and are further endorsed by Staff. Exhibit 128, *Surrebuttal of David T. Buttig,* pg. 6 lns. 1 – 7 ("[Q]. If the Commission were to order the depreciation rates as recommended by Mr. Spanos, do you have additional recommendations for the Commission? [A]. Yes. If the Commission orders the amortized depreciation rates of Mr. Spanos, I recommend the Commission order Spire to regularly retire all assets that have reached the end of the amortization period. By ensuring assets are retired at the end of the amortization period, any over-accrual from maintaining assets in rate base past their amortization period will be minimized."). Alternatively, the Commission could just issue the single rate for each account in the general plant category and be done with the issue.

Conclusion

The OPC stands behind its original position that the Commission should order Spire to maintain depreciation rates for Spire East as currently ordered except for accounts 376.2 Mains – Cast Iron, which should be set to 35.87%, and account 376.2 Mains – plastic, which should be changed to 1.87%, and then order these rates applied to Spire West as well.[29] Exhibit 200, *Direct Testimony of John A. Robinett*, pg. 3 lns. 6 – 10; pg. 1 lns. 18 – 19; Exhibit 202, *Surrebuttal Testimony of John A. Robinett*, pg. 6 lns. 16 - 20. Why does the OPC maintain this position? Because the alternatives presented in this case are all based on a depreciation study that has been shown to

[29] The rates for accounts 381.1 and 382.1 ,which were set in case GO-2020-0416, should be included and continued without change as part of this recommendation as well.

have **considerable** problems. Given the massive amounts of irregularities, confusion, and mid-case switches that have occurred, the OPC advocates to maintain the current state of affairs save for the two adjustment just described. Should the Commission decide that a change to depreciation rates is nevertheless necessary, then the OPC recommends the Commission take the following steps.

First start with the Average Service Life and Net Salvage Percentages found in Appendix 3 of Staff's cost of service report. Exhibit 101, *Staff Cost of Service Report*, Appendix 3 (Schedule DTB-d1). Then make the following adjustments:

1. For account 376.2 Mains – Cast Iron, change the Average Service Life to 8 years and the Net Salvage Percentage to -188% to yield a final rate of 35.87%. pg. Exhibit 200, *Direct Testimony of John A. Robinett*,4 ln. 19 – pg. 5 ln. 1.

2. For account 376.2 Mains – Plastic and Copper, change the Average Service Life to 75 years and keep the -40% Net Salvage Percentage the same. Exhibit 202, *Surrebuttal Testimony of John A. Robinett*, pg. 6 lns. 16 - 20.

3. For account 391.95 Enterprise Software, change the Average Service Life to 15 years and the Net Salvage Percentage to -5% to yield a final rate of 7%. Exhibit 128, *Surrebuttal of David T. Buttig*, pg. 7 lns. 1 – 5; GO-2012-0363, *Report and Order*, pg. 10 ¶ 2, pg. 8 ¶ 16.

4. For accounts 381.1 and 382.1, change the Average Service Life to 20 Years and keep the Net Salvage Percentage at 0%. Exhibit 201, *Rebuttal Testimony of John A. Robinett*, pgs. 6 – 7.

Then, once these changes are made, run the calculation found in Staff's cost of service report for all the accounts and use the resulting rate for each account. *See* Exhibit 101, *Staff Cost of Service Report*, pg. 112 lns. 28 – 29.

The Commission should not order a 0.00% rate applied to fully accrued plant in the group labeled "general plant" or otherwise approve general plant amortization accounting or Vintage Year Accounting for General Plant. Exhibit 202, *Surrebuttal Testimony of John A. Robinett*, pg. 10 ln. 1 – pg. 12 ln. 7. If the Commission does decide to order general plant accounting, the Commission should order Spire to continue specifying the original cost and associated retirement units for all additions to the accounts where General Plant Amortization accounting treatment will occur and place Spire under a standing order to treat all general plant that exceeds the amortization period as retired for ratemaking purposes. *Id*. at pg. 12 lns. 10 – 15; Exhibit 128, *Surrebuttal of David T. Buttig,* pg. 6 lns. 1 – 7.

Issue 26. Ultrasonic Meters

Spire should not be permitted to recover the cost of ultrasonic meters installed to replace existing diaphragm meters because Spire cannot prove that its decision to switch to ultrasonic meters was prudent. This is nothing but an attempt to dramatically build out rate-base; an excuse for gold-plating Spire's distribution system. Further, making the transition will create a stranded investment with regard to the existing diaphragm meters that will result in Spire customers having to pay for two or more meters at the same time. If, however, the Commission does permit Spire to recover the cost of ultrasonic meters, it should also order an adjustment to the plant accounts related to Spire's existing diaphragm meters to address the massive reserve deficiency that has already been created and which will grow worse with further diaphragm meter retirements.

Analysis

Spire seeks to recover the cost of new ultrasonic meters put into service to replace existing diaphragm meters. *See* Exhibit 32, *Rebuttal Testimony of James Rieske*, pg. 2 lns. 19 – 21. While the current request seeks recovery of a plant amount that is relatively small, when compared to the total plant-in-service balances for diaphragm meters, the evidence in the record strongly suggests that Spire is on the cusp of a major overhaul of its existing meter infrastructure. *Id.* The present case is thus the first opportunity the Commission has to address an issue that may potentially affect hundreds of millions of dollars of additional plant build-out as well

as hundreds of millions of dollars in stranded investments that will be created if this plant build-out is allowed. Consequently, it is immensely important that the Commission take the time to fully consider the justifications Spire has presented for the switch from diaphragm to ultrasonic meters. Failure to correct the myriad of problems that the OPC is about to elaborate upon now **will** result in those problems returning to this Commission at an ever-increasing scale and severity for both customers and the Company. The OPC thus hopes the Commission uses this opportunity to order corrections to the existing problems with Spire's case and thereby possibly mitigate and diminish the difficulty of future rate cases.

As mentioned, there are numerous problems with Spire's case and its actions undertaken to engineer the switch from diaphragm to ultrasonic meters. Spire failed to present the necessary evidence to support this decision in direct testimony, offered evidence crucial to its argument for the first time in rebuttal testimony, and then changed its position substantially during the hearing. Moreover, Spire has demonstrated a repeated failure to perform the basic due diligence expected of a Company preparing to spend this quantity of capital. Spire has consequently presented a case that is muddled, incomplete, and self-contradictory. All of these issues will be drawn out and discussed through the course of this brief. It is the OPC's intention to show that Spire has not, and at this point cannot, establish the prudency of the meter technology switch it is attempting to recover from its captive customers. However, the OPC will also show how Spire's past and current practices have resulted in, and will further exacerbate, a significant stranded investment issue in its meter

account. The OPC is asking the Commission to address both of these issues, and we shall begin our discussion with the prudency question.

Spire has not proven that it was prudent to replace existing diaphragm meters with new ultrasonic meters

What is a meter? At its most basic level, a meter is the device used to measure the volume of gas used by a customer. As such, the most important aspect of a meter is its ability to accurately determine the volume of gas flowing through it. Diaphragm meters have been proven capable of accomplishing this simple feat in a cost effective manner for decades. Spire now claims it is prudent to switch to a newer, more expensive type of meter: ultrasonic meters. The various rationales the Company puts forward for the prudence of this switch are all fatally flawed, and we will examine each in turn.

Safety

Spire relies heavily on the argument that ultrasonic meters will provide safety benefits to both customers and employees. *See* Exhibit 32, *Rebuttal Testimony of James Rieske*, pg. 4 lns. 16 – 18. In particular, Spire witness Mr. Rieske points to the following safety benefits:

1. Automatic shut-off based on a high flow rate. *See* Exhibit 32, *Rebuttal Testimony of James Rieske*, pg. 5 lns. 5 – 8;

2. Automatic shut-off based on high temperature. *See* Exhibit 32, *Rebuttal Testimony of James Rieske*, pg. 7 lns. 7 – 9;

3. Automatic shut-off based on high pressure. *See* Exhibit 32, *Rebuttal Testimony of James Rieske*, pg. 7 ln. 18 – pg. 8 ln. 2; and

4. "Near-field remote shut-off." *See* Exhibit 32, *Rebuttal Testimony of James Rieske*, pg. 9 lns. 4 – 6.

The simple problem is that none of these safety benefits, **absolutely none of them**, are unique to ultrasonic meters. Exhibit 219, *Honeywell Spec Sheet for AC 250NXS*. This is a point that should be stressed. The difference between a diaphragm and ultrasonic meter lies in the methods used to measure gas flow. A diaphragm meter measures gas through the expansion or contraction of a diaphragm, while ultrasonic meters measures the speed at which sound travels in the gaseous medium within the pipe. The safety features Mr. Rieske is relying on have nothing to do with these measurement systems and instead relate to extraneous safety features that are added by the meter manufacturer. This means that **new** diaphragm meters are being produced that have **all** the same safety features that Mr. Rieske touts as a basis for switching to ultrasonic meters. Exhibit 219, *Honeywell Spec Sheet for AC 250NXS*.

The fact that diaphragm meters with all the same safety features that Spire's witness relies upon can be acquired is proven in OPC exhibit 219. This is a specification sheet for an AC-250 NXS System meter built by Honeywell. Exhibit 219, *Honeywell Spec Sheet for AC 250NXS*. Note at the beginning that the spec sheet states:

> The Honeywell American Meter AC-250NX class meter was designed to be one of the industry's most cost-effective gas meters for residential compact metering, delivering high performance measurement at an economical price. Being one of the smallest and lightest **diaphragm gas**

> **meters in the US market**, AC-250NXS is reliable, accurate, easy to install and fits in tighter spaces, such as meter trees in apartment complexes. More than 90 million meters based on this measurement cartridge design have been sold worldwide. The AC-250NXS is available with built-in temperature conversions for accurate measurements. An integrated CAT-M1 cellular communication module enables automatic meter readings to be updated to utilities multiple times in a day to have real time insights of the gas consumption and meter health.

Exhibit 219, *Honeywell Spec Sheet for AC 250NXS*, pg. 1 (emphasis added). Later on, the spec sheet specifically describes the safety features for this diaphragm meter:

> The AC-250NXS Safety Shutoff Valve employs on-command shutoff to meet storm hardening, non-payment, delinquency, and move-in/move-out requirements. The valve's autonomous shut-off response and alarms are linked to **configurable triggers for high or low pressure, high or low flow and high temperature and fire, and peripheral sensors are provided for methane, seismic activity, corrosion, flooding, and other indicators**. Capabilities are also included to monitor mechanical pressure regulator health.

Exhibit 219, *Honeywell Spec Sheet for AC 250NXS*, pg. 2 (emphasis added). The spec sheet also lists the meters safety features:

- Safety features:
  - Reliable, bubble tight valve
  - **Autonomous shut off based on high pressure, high temperature, tamper and high flow rate**.
  - Safety alert to Head End system during valve closure/open
  - **High flow rate alarm**
  - **Reverse flow detection and alarm**
  - **Remote valve shut off**

- **High response mode (communicates every 15 minutes during emergency situations like High Pressure, High Temperature, High Flow or Valve closure)**

Exhibit 219, *Honeywell Spec Sheet for AC 250NXS*, pg. 1 (emphasis added). In addition, the spec sheet also lists the key features of the shut off valve:

> The key features and benefits of this reliable safety shutoff valve include:
>
> • **Remote disconnection of the gas supply**
>
> • **Automatic gas disconnection on high-pressure/temperature events**
>
> • Single fault-tolerance against unintentional opening of the valve
>
> • Gas re-enabled only once all of the customer's gas appliances are closed
>
> • No energy consumed when valve is open or closed
>
> • Low energy consumption during valve movement
>
> • When valve is closed, it resists at 60 PSI pressure
>
> • Detection of open and closed positions (patent pending solution)
>
> • Configurable valve operation (e.g., valve closure thresholds)
>
> • Located in the meter outlet (robust protection against dust)
>
> • Closes in flow direction (remains tight with increasing pressure)
>
> • Designed for more than 4,000 open/close cycles
>
> • Tamper detection algorithm
>
> • Several million installations in Europe and elsewhere
>
> • Flow check algorithm enables remote opening of the valve in a safe manner

Exhibit 219, *Honeywell Spec Sheet for AC 250NXS*, pg. 2 (emphasis added). It should be pretty obvious that this diaphragm meter has **every single safety feature that**

Spire touts for ultrasonic meters. In fact, this diaphragm meter might even have **more** safety features than the ultrasonic meters Spire seeks to now install. Unfortunately, we will never know because Spire did not perform the basic due diligence necessary to find out.

In response to the OPC's discovery requests, Spire made it clear that it had not performed any cost benefit analysis before it began investing in ultrasonic meter technology. Exhibit 206, *direct Testimony of Geoff Marke*, pg. 2 ln. 17 – pg. 3 ln. 5. Spire claims that it did not perform any such cost benefit analysis because diaphragm meters were "obsolete." *Id*. This claim that diaphragm meters are obsolete is not remotely true, but that will be discussed later on. For now, the point is simply that the Company did not perform **any cost benefit analysis prior to the decision to switch meters**. *Id*. This includes the Honeywell meters discussed above, as explained during the hearing by OPC's witness Dr. Geoff Marke:

> Q. Actually, let me back up. The exhibit that I've handed you, it's a spec sheet for a diaphragm meter produced by Honeywell. Correct?
>
> A. That's correct.
>
> Q. Does this diaphragm meter have a high-flow rate?
>
> A. Yes.
>
> Q. Does it have temperature alarms?
>
> A. Yes.
>
> Q. Does it have almost all of the safety benefits that Mr. Rieske points to with regard to ultrasonic meters?
>
> A. It does.

Q. **Did Spire ever prepare a cost-benefit analysis to compare using this meter or a similar type of meter to this to the ultrasonic meters**?

A. **There's no comparison to any meter**.

[. . .]

Q. I only have a last question regarding that exhibit. Is that a standalone device or is that a whole separate meter?

A. I read this as the entire meter, all of the products and features that are included within it.

Q. **And we don't know what the cost is for this meter**?

A. **That's correct**.

Q. **And we don't know because, again, no cost-benefit analysis**?

A. **No cost-benefit analysis**.

Q. So tying that into the question you received from the judge regarding increased accuracy, is the financial impact of that increased accuracy something you would expect in a cost-benefit analysis?

A. Absolutely.

Q. **What was your initial response from the Company when you asked for a cost-benefit analysis**?

A. **We did not perform one**.

Tr. pg. 297 ln. 21 – pg. 298 ln. 12, pg. 301 lns. 4 – 22. Spire's failure to perform a cost-benefit analysis (and any related due diligence) is an issue that we will return to time and again as we discuss this issue.[30]

[30] In a somewhat confusing turn of events, Spire's witness decide to testify at trial that Spire *had* looked at adding other types of devices to existing diaphragm meters and determined that it was not worth it. *See* Tr. pg. 258 ln. 23 – pg. 259 ln. 19. This naturally contradicts Spire's direct response to the OPC's discovery request that asked for any cost-benefit analysis the company performed to which Spire responded that there was none. Exhibit 206, *direct Testimony of Geoff Marke*, pg. 2 ln. 17 – pg. 3 ln. 5. This came to a head in Spire's cross examination of OPC witness Dr. Geoff Marke:

> Q. And we've had some discussion about some standalone products you identified that could add a shutoff valve to an existing diaphragm meter?

Accuracy

The second rationale that Spire puts forward to justify the switch from diaphragm meters to ultrasonic meters is a claim of increased accuracy. *See* Exhibit 32, *Rebuttal Testimony of James Rieske*, pg. 11 ln. 5 – pg. 12 ln. 3. Specifically, Mr. Rieske claims that "an ultrasonic meter is delivered with accuracy to +/- 0.1% versus the accuracy of +/- 2.0% in diaphragm meter technology." *Id*. at pg. 11 lns. 8 – 9. However there are several problems with this claim. The OPC's witness Dr. Geoff Marke explained the first during the hearing:

> Q. Mr. Rieske in his testimony discussed the increased accuracy of the ultrasonic meter versus the diaphragm meter. And I again reference the plus or minus point-one percent with the ultrasonic versus the plus or minus two percent with diaphragm. Do you have an opinion on what would be the impact of this increased accuracy on the average customer bill?
>
> A. Minimal. It's a difficult question to answer. We actually thought about this very question before we came down here this morning. So if we were to look back to historical gas costs -- I mean, that's the thing. I would need empirical data. And gas, historically, has been a very volatile fuel. It's leveled off in the last five, six years, but gas usage is also going to vary considerably, depending on the weather. So if you were to compare just therms used per company on a per year basis, it's going to vary considerably.

A. Amongst other standalone features.
Q. Okay. Do you know whether Spire investigated any such devices?
A. Based off of my discovery, it does not appear so.
Q. Did you hear Mr. Rieske testify that he did investigate such devices?
A. This was the first I heard of Mr. Rieske saying this.
Q. You don't have any information to dispute that, do you?
A. Again, I would point to my testimony. Based off of my discovery, I could not adequately or competently say that the Company did its due diligence to look at other costs associated with different vendors or different meter technology.

Tr. pg. 275 ln. 12 – pg. 276 ln. 5. To point out the obvious, it is not the OCP's job to "dispute" that Spire performed its due diligence, but rather, it is Spire's job to present the evidence necessary to prove the just and reasonable nature of its rates. RSMo. § 393.150.2.

> The two percent accuracy -- I address this at length in my testimony. I think it's a misleading number. GM-5 in my surrebuttal testimony references the discovery that I asked about it and asked for if the empirical data to substantiate those numbers. Of note, you will -- **what I would like to highlight is that Mr. Rieske is utilizing pre-deployment, out-of-the-box meter data. So rip open the box, let's test it, it's good versus historical assets that have been in the ground for decades**.
>
> There is no comparison -- there is no additional comparison as to what's the out-of-the-box diaphragm. What's the out-of-the-box rotary? What's the out-of-the-box turbine? What's the out-of-the-box thermal mass? There -- what about different vendors? What about Aclara? Honeywell? There's no emphasis on this. We've got a very narrow bit of information that's saying well, the accuracy benefits are profound. I would counter with anything brand-new, out-of-the-box, is going to show a better result.
>
> **If you were to compare ultrasonic meters 20 years from now versus the ultrasonic meters out of the box, I would venture to say the ultrasonic meters out of the box should achieve marginal benefits in terms of accuracy**.
>
> Q. If I could push that question just a bit further. Am I to assume that you -- and likely -- I don't want to ask your opinion on the other witnesses -- are you not discussing the possible increased accuracy with respect to a customer knowing their bill or getting a better, more accurate bill is the reason you're not focusing on that because with whatever inaccuracy you're going to have pluses and minuses?
>
> A. That's right.

Tr. pg. 283 ln. 5 – pg. 285 ln. 3. As Dr. Marke explains, the accuracy analysis that Spire presents is a false comparison. Mr. Rieske is comparing brand-new ultrasonic meters to historical assets that have been in use for decades. *Id*. If one looks at the accuracy provided by new meter diaphragm meters, as shown in the specification sheet for the Honeywell meter provided by the OPC, one can see that the accuracy of these **new** diaphragm meters trends much closer to the +/- 0.1% that Mr. Rieske

trumpets. *Compare* Exhibit 219, *Honeywell Spec Sheet for AC 250NXS*, pg. 4; *and* Exhibit 32, *Rebuttal Testimony of James Rieske*, Schedule JAR-R3 pg. 3 of 4. It should also be noted that the **actual** accuracy of ultrasonic meters is different than the +/- 0.1% that Mr. Rieske claims. Exhibit 32, *Rebuttal Testimony of James Rieske*, Schedule JAR-R3 pg. 3 of 4 ("Intelis will achieve +/- 0.5% at room temperature from 20-300 SCFH.") In fact, the graph included in the specification sheet found in Mr. Rieske's schedule shows that, when not operating at "room temperature," **the accuracy of the ultrasonic meter drifts to +/- 1.0%**. *Id.* Thus, for all the emphasis Spire places on accuracy, in reality these ultrasonic meters may differ from diaphragm meters by as little as 1%.

Besides severely overstating the accuracy benefits that ultrasonic meters have over diaphragm meters, Spire has failed to perform any cost benefit analysis that would show what that increased accuracy was actually worth. Exhibit 206, *direct Testimony of Geoff Marke*, pg. 2 ln. 17 – pg. 3 ln. 5. This was exposed during the OPC's cross-examination of Staff witness J Luebbert:

> Q. You were just asked a question about the increased accuracy and what impact that would have on customer bills and you responded you didn't know. Correct?
>
> A. Correct.
>
> Q. Would you expect that kind of information to be reviewed in a cost-benefit analysis study?
>
> A. Yes, I would.
>
> Q. Did Spire complete any cost-benefit analysis study that you are aware of?

> A. Spire did provide some very high-level cost-benefit analysis in response to data requests that we had sent. And I pointed out in my testimony that a problem with that analysis that they provided was one, that it was high level, but a lot of the numbers were hard coded assumptions without support for those. And, you know, I would expect a more robust cost-benefit analysis if the goal was to replace more than just those meters that needed to be replaced otherwise.

Tr. pg. 269 2 – 19.[31] This lack of proper due diligence was further noted by the OPC's witness:

> Q. So tying that into the question you received from the judge regarding increased accuracy, is the financial impact of that increased accuracy something you would expect in a cost-benefit analysis?
>
> A. Absolutely.
>
> Q. What was your initial response from the Company when you asked for a cost-benefit analysis?
>
> A. We did not perform one.

Tr. pg. 301 lns. 15 – 22. The minuscule difference in accuracy that exists between ultrasonic and diaphragm meters may well only be worth pennies a month to individual Spire customers. There is literally no way to know for sure, because Spire never bothered to engage in the basic due diligence needed to find out. *Id*. This is a problem. The Commission should not simply *assume* that a difference of accuracy that might be as little as +/- 1% would make these ultrasonic meters cost-effective. Spire

[31] Staff counsel asked a follow-up question to determine the meaning of Mr. Luebbert's statement that "a lot of the numbers were hard coded assumptions without support." Tr. pg. 270 lns. 8 – 15 ("Q. Mr. Luebbert, counsel for OPC asked you a question about the assessment of the completeness of their own lists of documents and you referenced getting documents that were hard coded. What does hard coded mean? A. Just a number without a link to support it. So, you know, an assumption without, you know, a way to calculate what that number was or a reason for why that number is reasonable.")

has the burden to **prove** that these are prudent and they have wholly failed to do so. RSMo. § 393.150.2.

Reliability

The third reason Spire offers for why it is prudent to replace diaphragm meters with ultrasonic meters is a claim that ultrasonic meters will be "more reliable" based on an absence of internal moving parts. Exhibit 32, *Rebuttal Testimony of James Rieske*, pg. 11 ln. 11 – pg. 12 ln. 14. This argument is inherently flawed, however, when one considers the respective average service lives of these two types of meters. As currently ordered, ultrasonic meters have an average service life of 20 years. *See* Exhibit 201, *Rebuttal of John A. Robinett*, pg. 7 lns. 8- 10. However, Spire is already requesting the life of these assets be shortened.[32] Exhibit 34, *Direct Testimony of Wesley E. Selinger*, Schedule WES-1 H11-Depr Adj (pg. 38 of 45). This requested change suggests that these new ultrasonic meters are already not lasting as long as Spire had originally expected them to. On the other hand, Spire's expert witness in depreciation has recommended a 35 year average service life for diaphragm meters. *See* Exhibit 35, *Rebuttal Testimony of John J. Spanos*, Schedule JJS-R2, pg. 51 of 396; *see also* Exhibit 202, *Surrebuttal Testimony of John A. Robinett*, pg. 15 lns. 19 – pg. 16 ln. 10. Consequently, no matter what Spire may claim about the benefit of not

[32] As was already discussed during the analysis of the depreciation issue, Spire has recanted this requested change to the average service life for the new ultrasonic meters in its position statement. Spire Missouri, Position Statement, pg.15. At the same time, though, the Company also claims that its "depreciation study supports a depreciation rate change for" the ultrasonic meter accounts and that it is "reserve[ing] the right to request adjustment of the depreciation rate for these accounts in future rate cases." Spire Missouri, Position Statement, pg.15. As such, there is every indication that Spire does believe the ultrasonic meters will end up lasting less than 20 years.

having internal moving parts, the evidence that **the Company itself has presented** shows that diaphragm meters will last **longer** than ultrasonic meters on average.

Now the point just made is immediately thrown into some degree of uncertainty due to the fact that Spire's so-called expert on meters invented a completely different average service life for diaphragm meters at some point during the case. *See* Tr. pg. 230 6 – 10. The issues regarding credibility of witnesses and the impact this change has on the stranded investment problem has already been discussed. For now, all the we need to focus on is this statement by Mr. Rieske offered during the hearing: "[a]t the end of the day, our experience tells us a diaphragm meter last almost exactly what an ultrasonic meter will last, again, 18.8 years, 22.1 years. The ultrasonic meter is 20 years." Tr. pg. 232 ln. 23 – pg. 233 ln. 1. The problem for Spire is that, again, diaphragm meters are lasting as long if not longer than ultrasonic meters. No matter how one chooses to examine it, the claim that ultrasonic meters are somehow "more reliable" is ultimately invalidated by the actual numerical values that Spire itself cites. At the end of the day, this simple, unwavering truth remains: Spire will need to replace ultrasonic meters just as quick, if not even quicker than, diaphragm meters. This renders any claim of increased reliability completely moot.

Obsolescence

The fourth and final argument Spire offers for why it was prudent to switch from diaphragm to ultrasonic meters is the claim that diaphragm meters are obsolete. *See* Exhibit 32, *Rebuttal Testimony of James Rieske*, pg. 12 lns. 16 – 17. Mr. Rieske

openly speculates that other diaphragm meter manufacturers will soon stop selling diaphragm meters and bemoans that Spire will "be forced to continue to try to locate new diaphragm meters from small, unproven manufacturer[s]" if the Commission does not grant recovery. Id. at pg. 12 ln. 22 – pg. 13 ln. 14. **This is simply not true**. Unlike Spire, the OPC actually did the legwork to determine whether other meter manufacturers had or intended to stop production of diaphragm meters and the answer was an unequivocal "no." For example, consider the following from the surrebuttal testimony of OPC witness Dr. Geoff Marke:

> [J]ust because Itron is no longer offering diaphragm meters (despite the website suggesting differently) does not mean other natural gas meter vendors are not offering or making diaphragm meters.
>
> **Q. Do you have any evidence to support that assertion?**
>
> A. I sent an email to Gasco natural gas meter representatives affiliated with Sensus (a Xylem Inc. brand) with the following questions on that very topic. The email questions and response are as follows:
>
> > 1.) Are diaphragm natural gas meters currently in stock and available? If yes, what sizes do you have?
> >
> > 2.) Is there any legitimate fear that diaphragm natural gas meters from Gasco will not be available in the next year? Next five years?
> >
> > 3.) Is there any legitimate fear that diaphragm natural gas meters will not be available from any Company (if Gasco were to stop carrying diaphragm natural gas meters) in the next year? Next five years?
>
> I received the following email response:
>
> > Hi Geoff,
> >
> > Yes, we have ¾", 1", & 1-1/4" in R275's. In the R415's we have 1-1/4" & 1-1/2" connections in-stock. No, there is no fears of these not being available next year or five years even if we did not sell them anymore, they would still be

> available. There are no plans for us to stop selling them within the next five years. Depending on the needed meter we have hundreds in stock and thousands on order with Sensus.
>
> I hope this is helpful. Please don't hesitate to give us a call.
>
> Based on this response I doubt the soundness in Spire's assertion that diaphragm natural gas meter technology is obsolete.

Exhibit 208, *Surrebuttal Testimony of Geoff Marke*, pg. 8 ln. 14 – pg. 9 ln. 17. This evidence was then further supported by screen-captures of 250 series natural gas diaphragm meters currently being advertised for sale by several prominent vendors. *Id*. at pg. 9 ln. 18 – pg. 10 ln. 4.

In addition to the resources identified by Dr. Marke, the existence of the Honeywell AC-250 NXS system further demonstrates that diaphragm meters are not only far from "obsolete" as Spire's witness pretends, but are actually making huge strides forward to be on-par, if not better than, competing alternatives. *See* Exhibit 219, *Honeywell Spec Sheet for AC 250NXS*. This can further be seen in the 2011 news clip from Elster announcing the "launch of a remote shut-off valve for its AC-250 Residential gas meter" included in Dr. Marke's surrebuttal. Exhibit 208, *Surrebuttal Testimony of Geoff Marke*, pg. 11 ln. 14 – pg. 12 ln. 2. Again, the evidence clearly shows that diaphragm meters are not on their way out the door, as Spire would have this Commission believe, but are rather being continuously used and improved by numerous vendors across the country.

There is one other point that needs to be addressed in relation to the obsolescence argument, and that is the termination of Spire East's contract with Landis+Gyr. As explained by Spire witness Mr. Rieske at the hearing, Landis+Gyr is responsible for deploying and maintaining the network that allows Spire to read its meters remotely. Tr. pg. 248 lns. 7 – 13. Spire East currently has a contract with Landis+Gyr that ends April 2025. Tr. pg. 247 lns. 19 – 21. Spire maintains that it will lose meter-reading capabilities after the contract expires and that it is replacing the existing diaphragm meters with ultrasonic meters to account for this. Tr. pg. 248 ln. 14 – pg. 249 ln. 5. The best response to this issue is the one presented in the rebuttal testimony of Staff witness J Luebbert:

> Q. Does a lack of production of a product automatically make it useless and necessary to replace regardless of age?
>
> A. No, it does not. As long as the meters are used, useful, and cost effective they may be worth keeping as an asset. **However, Spire Missouri has not provided cost benefit analyses with supporting documentation that supports abandoning the existing diaphragm meters regardless of the age of the assets in favor of new ultrasonic meters**. Spire stated that "[t]he Company needs to change all meter reading equipment in [Spire] Missouri East by April 2025 because our contract with our current provider (Landis & Gyr) ends at that time." **Spire has not provided documentation that indicates that the existing meter devices will no longer be useable beyond that date**. Information provided by Spire in response to Staff data request No. 0295.3 indicates that **replacing the AMR device with a new "advanced device" on existing diaphragm meters **** ** This cost disparity warrants additional justification for the decision to proceed with replacing existing meters regardless of the age of the meter.

Exhibit 115C, *Rebuttal Testimony of J Luebbert*, pg. 5 ln. 16 – pg. 6 ln. 8 (emphasis added). As can plainly be seen, there is no reason to believe that replacing the existing diaphragm meters with ultrasonic meters is the most prudent option. It may be far, *far* more cost effective to simply upgrade the existing AMR devices on these meters than perform a complete replacement. Moreover, even if Spire **was** to do a complete meter replacement, it may still be far cheaper and more cost efficient to replace with a new diaphragm meter (one that has all the safety benefits of an ultrasonic meter) as opposed to an ultrasonic meter.

In response to the problems identified by Staff witness Mr. Luebbert, Spire's witness Mr. Rieske states the following:

> Under this plan, Spire would install a new module on existing diaphragm meters with the deliberate intent to strand these new assets. This would result in 30,000 to 40,000 meters with new network devices being subsequently replaced with a new meter each year to satisfy the Commission-mandated meter sampling requirements.

Exhibit 33, *Surrebuttal of James Rieske*, pg. 13 lns. 1 – 5. There are several problems with this line of reasoning. First, Mr. Rieske falsely suggests that the attached AMR devices would be stranded if the underlying meter is retired. This is not true, however, because the AMR device is an ancillary piece of equipment attached to the meter. *See* Tr. pg. 243 ln. 24 – pg. 244 ln. 5. This means that the AMR device could almost certainly be salvaged and re-used at minimal cost, and would thus not be stranded. The next problem is that Mr. Rieske suggests that Spire would need to immediately turn-around and replace the meters that the AMR devices were affixed

to, which makes no sense. If the Company comes to replace an AMR device and they find the meter is within the statistical sampling requirement to replace, then they can just replace both the existing diaphragm and AMR device with newer versions at the same time. Spire is creating a false dilemma by offering an illogical and imprudent course of action to solve a simple problem. The third and final problem lies with the fact that Spire has never considered the idea of replacing the existing diaphragm meter with attached AMR device with a new diaphragm meter that includes an AMI component like the Honeywell AC-250 NXS System.

During the evidentiary hearing, the OPC directly questioned Spire's witness whether the Company had performed any cost benefit analysis of the Honeywell AC-250 NXS System. Tr. pg. 220 lns. 22 – 25. Mr. Rieske stated that he had not, and attempted to justify this failure by arguing that any **other** meter would be incompatible with Spire's meter reading network. Tr. pg. 221 lns. 12 – 15 ("Q. So can I say that the answer is no, you did not do a cost comparison analysis? A. I did not compare products that could not fit within the meter reading system that Spire uses."). The problem here should be obvious. On the one hand, Spire is attempting to justify the discontinuation of diaphragm meters in its Spire East territory because the meter reading system it uses (Landis+Gyr) is suspending support. Tr. pg. 248 ln. 23 – pg. 249 ln. 5. On the other hand, Spires says that it did not consider any alternative meter manufacturers because they were not compatible with the meter reading system that Spire uses. Tr. pg. 221 lns. 12 – 15. Clearly if Spire knew that its existing system was going to need to change, Spire should have considered other

possible systems, including the ones offered by Honeywell and other meter manufacturers. Spire's failure to do so should not be rewarded by the Commission turning a blind eye.

Summation

As has been the running theme throughout the course of this discussion, Spire failed to engage in the basic principles of due diligence that one would expect of a Company of this size. Dr. Marke spoke to this point at length on the stand:

> . . . my methodology was, okay, we're replacing ultrasonic meters. Did we look at any other types of meters? Did we compare prices across boards? Did we compare -- was there any analysis conducted? The response was no, we didn't perform a cost-benefit study. They are obsolete.
>
> As I think most people that go through, you know, any formal education will sit there and won't just accept something at face value. There is at least one neuron that says can I prove that? Can I support that? Can I substantiate that? That's where my discovery process came in. In the investigatory process, I apologize. That was me getting on the Honeywell sites. That was me contacting Aclara, you know, as providers, to get a sense of what was the proper due diligence done. In my estimate, sitting here today, I do not believe it was.
>
> Q. In your opinion, would the Company have also been required to do due diligence when deciding -- if they decided now let's keep using the diaphragm?
>
> A. I would've just expected some analysis to provide. Just to show me some evidence where you looked at the cost and the benefits. How much -- how often are we talking about safety-related meter side issues over the past 20 years? Mr. Rieske spoke a lot about, well, we did testing. And none of the empirical -- and Mr. Luebbert's testimony, you know, supported this too. It wasn't at the level that I see other utilities perform. It wasn't at a level that gives me confidence moving forward with supporting it.

Tr. pg. 290 ln. 15 – pg. 291 ln. 5.

Q. When the judge was asking you about some of the criticisms that you had regarding their case, is this what you were referring to that lack for a cost-benefit analysis?

A. This is what I mean by inefficient management. Again, if this was a -- **if this was a private sector, you couldn't just go ahead and start replacing fixed assets for the end of their useful life without some sort of empirical basis to substantiate that**. Otherwise, you run the risk of going bankrupt.

Q. Were you here when Mr. Rieske testified about this document?

A. Yes.

Q. And he made reference to the fact that they wouldn't consider it because it would have other fixed costs associated with it?

A. Yes.

Q. Is there a concern that you see it with the current ultrasonic meters and fixed costs?

A. Yes.

Q. Care to elaborate?

A. You need to look at the totality of this investment. So there are three parts to this. I would say -- I would posit that we're in part number two, which is the meter itself. Part number three is the AMI investment that may or may not come to light. Part one was the platform that Mr. Rieske put forward, at least, on Spire West side, which is Itron. All three of those parts need to be looked at in their totality and their costs. [. . .] [W]hat ends up happening, absent some sort of analysis, just basic analysis, is path-dependant decisions that feed off of each other. **In this case, what you've got is effectively a cheat code to increase your rate base off of each of these investments and make it larger**.

In this case, for example, is Itron that they use the Itron platform in the West. And then Itron says -- and this is an inherent risk -- Itron says well, we're not going to go ahead and use diaphragm meters now. Okay. Now, we're locked into, on the West side, the Itron platform, and that means we need to go ahead and use Itron ultrasonic meters. So it just keeps building out.

The difference, from my vantage point -- and again, what we're trying to do here as economic regulators and why this differs from England and Europe that isn't cost-based regulation; it's performance-based regulation -- **there is a perverse incentive for this company to build out rate base. This is a platform to do it**.

Q. You were asked by the judge what you were referring to when you talk about $100 million investment. Is that tying into what you're describing?

A. It is.

Q. So your fear is that this will just continue? I mean –

A. It's -- it's just -- **it's a construction company at this point**. It just becomes you're getting more and more, you know, earnings based off of just building out stuff, and building out stuff, and building out stuff. And, effectively, if you're a customer, again, let's not lose sight of the big picture here. I just want my monthly reading. I just want to know what my gas usage is at the end of the month.

But now we're into this perverse position where I'm paying one, two, maybe three meters, and all of the ancillary services on top of that, to provide me, again, monthly reading. This is how rates increase larger than they should.

Tr. pg. 298 ln. 13 – pg. 301 ln. 3 (emphasis added). Dr. Marke was not the only witness to this case to describe the incredibly poor job that Spire performed in supporting its case.

Staff's witness Mr. J Luebbert also described in testimony how Spire had failed to follow proper protocols and provide the necessary evidence to support this change to plant:

Q. What testimony did Spire Missouri provide in Direct testimony to support the inclusion of the costs in FERC subaccount 381.1 and 382.22?

A. As I stated in my rebuttal testimony, **the Direct testimony provided by Spire Missouri to support the inclusion of the costs**

to replace existing metering equipment with new advanced metering equipment in this case was limited to . . . two sentences in Mr. Weitzel's Direct testimony[.]

[. . .]

Q. Could Spire Missouri have included the vast majority of what Mr. Rieske included in his rebuttal testimony and in response to Staff's data requests within Direct testimony in this case in order to support its investment in new meters?

A. Yes. Spire Missouri is requesting to recover the costs associated with the replacement of the existing metering infrastructure regardless of the age of the meter replaced. As I stated in my Rebuttal testimony, **Spire Missouri should have provided justification for replacing existing assets with new technology which includes fully supported cost benefit analyses especially in an instance when the existing assets are being replaced regardless of age which increases the possibility of substantial stranded assets**. In fact, **it is the Company's responsibility to provide this information supporting its case at the time of its Direct filing**. However, **neither Mr. Rieske, nor any other Spire Missouri witness, provided the level of detail, support, or justification needed in Direct testimony for Staff to provide the Commission with a reasonable recommendation other than to exclude the costs associated with the ultrasonic meters**. By refusing to provide support for its Direct filed case, Spire has caused unnecessary delays and extra discovery that has hindered the parties in their review of Spire's case.

Exhibit 133, *Surrebuttal Testimony of J Luebbert*, pg. 1 ln. 23 – pg. 2 ln. 4, pg.3 ln. 12 – pg. 4 ln. 6 (emphasis added). This scale of deficiency in Spire's case, when coupled with the degree to which Spire did not perform its basic due diligence, should not be overlooked by the Commission.

Spire has failed to prove the prudency of its ultrasonic meter investments. The evidence in the record shows that the safety benefits that Spire touts, benefits that

are in no way necessary for a meter to function, can be achieved using diaphragm meters. *See* Exhibit 219, *Honeywell Spec Sheet for AC 250NXS*. The accuracy claims Spire has made about ultrasonic meters are overstated and there is no evidence to show what increased accuracy, if any, the ultrasonic meters would actually achieve for ratepayers. Tr. pg. 269 2 – 19, pg. 283 ln. 5 – pg. 285 ln. 3, pg. 301 lns. 15 – 22. Spire's assertion about ultrasonic meters being more reliable and less likely to break-down is undone by the fact that the evidence shows ultrasonic meters will be replaced at least as quickly if not more quickly than diaphragm meters. *See* Tr. pg. 232 ln. 23 – pg. 233 ln. 1. Finally, the allegation that diaphragm meters are obsolete is just false. *See* Exhibit 208, *Surrebuttal Testimony of Geoff Marke*, pg. 8 ln. 14 – pg. 9 ln. 17.; Exhibit 219, *Honeywell Spec Sheet for AC 250NXS*. In the absence of these proffered justifications and the nonexistence of any proper cost-benefit analysis or other forms of due diligence to show that ultrasonic meters are a better, more cost-effective solution, this Commission should disallow cost recovery of the ultrasonic meters placed in service to supplant existing diaphragm meters. Exhibit 206, *direct Testimony of Geoff Marke*, pg. 9 lns. 11 – 13. ("I recommend the Commission disallow the total costs associated with AMI deployment in utility account 381100 that Spire is seeking in this rate case, which is $10,671,837 on a combined Spire East and West basis as of March 31, 2021.").

Stranded investment

The second major issue connected to ultrasonic meters is the problem surrounding the stranded investment that has been created for Spire's diaphragm

meter account (account 381) and associated ERT/AMR accounts (accounts 397.1 and 397.2), which will grow worse if the Commission allows Spire to continue with more diaphragm meter replacements. To fully grasp this problem, one must first wrestle with the difficulty of answering what should be a relatively simple question: when is Spire replacing diaphragm meters?

When is Spire Replacing Diaphragm Meters?

One of the most frustrating aspects of this case has been the fact that Spire has abruptly changed the answer to this simple question through the course of this case. Right now, there are effectively four different possible answers for the age at which Spire expects to replace diaphragm meters with ultrasonic meters moving forward. The first is that Spire is just replacing **any** meter that is over ten years old, as Spire itself originally claimed. *See* Exhibit 32, *Rebuttal Testimony of James Rieske*, pg. 15 ln. 22 – pg. 16 ln. 2 ("In Missouri West, the Company is targeting meters that are already more than ten years old for replacement with an ultrasonic meter."). It appears that this extreme position was taken based on Spire's incorrect interpretation of Commission rule 20 CSR 4240-10.030 (19). *Id*. at pg. 15 lns. 12 – 13, pg. 16 lns. 4 – 5. To be clear, Commission rule 20 CSR 4240-10.030(19) does **not** require meters be replaced every ten years. It instead only requires that they be removed for testing every ten years. 20 CSR 4240-10.030 (19) ("Unless otherwise ordered by the Commission, each gas service meter installed shall be periodically removed, inspected and tested at least once every one hundred twenty (120) months"). Moreover, Spire openly acknowledges that it received a waiver from the Commission

that allowed it to **not** remove and test meters every ten years and instead use a statistical sampling method. *Id*. at pg. 15 lns. 13 – 15. ("Spire was previously granted a waiver to extend the service life of meters beyond ten years by sampling and accuracy testing by vintage and type of meter."). Therefore there is **no** legal mandate to replace meters every ten years as Spire claims.

Given the existence of the waiver from rule 20 CSR 4240-10.030 (19) testing requirements, the OPC was under the impression that Spire's diaphragm meters were lasting as long as the Company's depreciation expert had been consistently claiming they did. Exhibit 202, *Surrebuttal Testimony of John A. Robinett*, pg. 15 lns. 19 – pg. 16 ln. 10. This would mean that Spire's diaphragm meters were lasting, on average, approximately 35 years. *Id*. This 35 year number forms the second possible answer to the question of when exactly Spire is replacing its diaphragm meters. Because Spire had originally told the OPC that it was replacing meters after 10 years and had further told the OPC that these meters would last 35 years (based on depreciation studies), the OPC came to the obvious conclusion that Spire was replacing meters that still had 2/3 of the remaining useful life left. Exhibit 206, *direct Testimony of Geoff Marke*, pg. 1 lns. 19 – 20, pg. 2 lns. 3 – 6. This understanding was, however, thrown into confusion by new evidence developed later in the case.

During the evidentiary hearing, Spire's witness Mr. Rieske offered the third possible answer to the question of how long its diaphragm meters last when he testified they were lasting approximately 18.8 years for Spire East and 22.1 years for Spire West. Tr. pg. 230 lns. 6 – 9. This brief has already discussed how this sudden,

unexpected change in average service life directly contradicts the testimony of Spire's own depreciation expert that was also offered in this case. *See Issue 24: Depreciation supra*. While the OPC does not wish to dwell on the issue too much, the Commission needs to realize that this is a massive problem. It means, at a minimum, that either Mr. Spanos or Mr. Rieske is not credible with regard to the simple question of how long Spire's diaphragm meters last.[33] Moreover, the sudden change in average service life occurred at a time that prevented it from being incorporated into other party's recommendations. Tr. pg. 263 lns. 14 – 19 ("Q. When you made -- when you made that recommendation were you aware of -- let me careful here -- at least Mr. Rieske's position, that diaphragm meters have an average service life of 18.8 or 22.1, I believe were the correct numbers, for East and West respectively? A. I was not." (cross-examination of J Luebbert)).

The fourth and final answer to the question of when Spire may be replacing its meters is unfortunately undefined. All that we know is that Spire certainly believes that it might choose to accelerate the rate of replacement it is currently undertaking:

> Q. So is that at a high level, roughly, when you are going to be doing these replacements, they are going to be [18.8 for the 22 East and 22.1 for the West years] old?
>
> A. So, yes, that would be a good starting point. I think -- you know, **we recognize we need to more aggressively replace our metering populations** because there are a lot of underperforming populations. So **I would expect that to continue to slightly trim downward**, but that is where we're at historically.

[33] The OPC would of course argue that neither witness should be considered credible for all the reasons already laid out in this brief.

Tr. pg. 253 ln. 21 – pg. 254 ln. 7 (emphasis added). Therefore, it is safe to assume that the answer is probably somewhere between 10 and 20 years, which is a rather large gulf relatively speaking. The problem only intensifies if one considers the Landis+Gyr argument that Spire has presented for needing the replacements in the first place. Spire has effectively claimed that it will lose meter-reading capacity in its Spire East territory if the meters are not replaced by April 2025. Tr. pg. 247 lns. 19 – 21, pg. 248 ln. 14 – pg. 249 ln. That would imply that Spire believes these replacements must be carried out in a scant 4 years. This would be a **very** accelerated time frame.

We now have our four different potential answers to what should have been a simple question. When is Spire replacing diaphragm meters? After either 10 years, 35 years, 18.8 or 22.1 years, or some period between 4 and 20 years. The OPC hopes that it is not necessary to point out to the Commission just how bad this situation is. If it is necessary, just consider the following testimony from Staff:

> Spire Missouri also indicated that, "The current sampling program has a significant population of aged meters that can be targeted to accelerate the tempo of replacements. **When a meter is off and customer service needs to be re-stablished, the meter is being replaced regardless of age**. At this point, the change in the frequency of replacements has not been targeted to a level that has warranted an evaluation of the impact to the retirement of the meter plant in service." This response is concerning for several reasons. **First, it is not clear what level of targeting would "warrant an evaluation of the impact of the retirement" according to Spire Missouri. Second, it is concerning that replacement of the meter regardless of age may lead to a significant amount of stranded investment**. Spire Missouri's response to OPC data request No. 2059 indicates that **

_____ ** According to the testimony provided in Case No. GR-2017-0215 the batteries for these types of devices have an effective useful life of approximately 20 years.

Exhibit 115C, *Rebuttal Testimony of J Luebbert*, pg. 5 ln. 16 – pg. 6 ln. 8 (emphasis added). It is this second concern raised by Staff that the OPC wishes to focus on for the remainder of this discussion.[34]

Before we go further, it is probably best we take a moment to define the term "stranded investment." Fortunately, the OPC's witness Dr. Geoff Marke has helpfully provided a definition in his surrebuttal testimony:

> Stranded asset" is a term that has different meanings depending on the context. For example, regulation-based stranded assets differ from market-based stranded assets. The latter simply compares the book value of an asset relative to some future market value of the asset. For example, if an oil reserve has $1 billion book value but sliding demand due to carbon taxes or other environmental regulations reduces its market value to $400 million, the result is $600 million in stranded assets. By contrast, regulation-based assets are assets that are covered by cost of service or other rate-of return regulation. Government regulators at some point have explicitly approved this type of asset in the past to earn a return over a defined period of time—typically in line with the Company's depreciation schedule and subsequent rate cases; however, assets can and should remain useful above and beyond the point they have been paid off. In this case, the stranded assets are the diaphragm meter's remaining book value when Spire decided to "retire" these assets within ten years despite the Company's Commission approved 35-year depreciation schedule the Company has offered and maintained for multiple consecutive rate cases (including this one).

[34] That is not to diminish the importance of the first concern that Staff raises. The fact that Spire does not appear to know or care what the impact to the retirement of the meter plant in service accounts goes a great way toward explaining why the stranded investment problem that we are about to discuss was created.

Exhibit 208, *Surrebuttal Testimony of Geoff Marke*, pg. 2 fn. 1. As Dr. Marke explains, the stranded investment (or stranded asset) at issue in this case comes from the fact that Spire is retiring an asset that should have lasted 35 years (according to its depreciation schedules) much earlier than that. *Id*. This means that the asset is not being fully recovered by the time it is retired and ratepayers will have to continue paying for the asset despite no longer receiving the benefit of having it. The curious point in this case is that, if Mr. Rieske's testimony about diaphragm meters only lasting 18.8 to 22.1 years is taken at face value, the stranded asset problem has already been created.

According to the testimony of Spire's own witnesses, Spire has been stranding its investment in diaphragm meter technology for some time. Exhibit 202, *Surrebuttal Testimony of John A. Robinett*, pg. 14 lns. 5 – 15 (" For some time, there has been a disconnect between the asset depreciation and the practical life of a meter"); Tr. pg. 233 lns. 2 – 4 ("So the disconnect in the depreciation -- this is not a new phenomenon, and I don't understand why it hasn't been recognized until we got into these cases. "); Exhibit 33, *Surrebuttal Testimony of James Rieske*, pg. 11 lns. 18 – 19. ("Stranding assets did not happen much differently than it has for the last 20 years in the expenses in this rate case."). If Spire now accelerates the retirement of diaphragm meters, and the evidence gives every indication that it intends to do so, Spire will only exacerbate the problem. This is because even more meters will be retired before they are fully recovered, and, indeed, are likely to have had even less

of their full cost recovered.[35] This is a problem that the Commission needs to address because the practical effect is that Spire's customer have been, are, and will be paying for multiple meters at the same time.

The Impact on Customers

Customers have already begun paying the price for Spire's decision to strand its meter investments. As OPC witness Dr. Marke explains:

> The Company's unique interpretation of these rules has allowed it to increase its rate base beyond what it should be at great costs to customers. Moreover, Spire's repeated failure to update its meter depreciation schedules to assume a 10-year operational life means that it has been earning a larger return on it meter investments than it should have. Customers are effectively paying for the costs (including profits) of two meters despite only using one at a given time.

Exhibit 208, *Surrebuttal Testimony of Geoff Marke*, pg. 5 ln. 10 – pg. 9 ln. 15. This outcome is unjustifiable in light of all the circumstances, as the OPC's witness Mr. John Robinett explained;

> **Q. Should ratepayers have to pay for Spire's created under recovery for diaphragm meters?**
>
> A. No. First, Spire, in its responses to Staff data request 0443, admits that it has "for years" been retiring meters that met accuracy standards instead of placing them back into inventory and eventually the field. Spire has thus created this problem by how it managed its meters and inventory. Second, in that same data request Spire indicates knowledge

[35] In an ironic twist, Spire's witness Mr. Rieske states the following in surrebuttal testimony: "I agree that going forward Spire and interested parties need to continue to discuss how to handle stranding metering assets **by a more aggressive upgrade program** and Spire is gathering more data to have that discussion." Exhibit 33, *Surrebuttal Testimony of James Rieske*, pg. 11 lns. 19 – 22. It is not clear if Mr. Rieske does not understand that a more aggressive upgrade program will lead to more stranded assets or if he does understand this and is stating that Spire is purposely seeking to strand metering assets.

> of a disconnect between the asset depreciation and practical life of a meter, yet the Company has apparently done nothing to attempt to rectify this problem. For both of these reasons, Spire's customers should not have to pay for the under recovery of diaphragm meters.

Exhibit 202, *Surrebuttal Testimony of John A. Robinett*, pg. 12 lns. 5 – 13. Spire's customers should not have to pay extra to account for Spire's poor handling of its meter inventory and its failure to rectify a problem with its depreciation schedules that has existed for years. The Commission should therefore order an adjustment to correct for this problem. At the moment, there are two such adjustments proposed.

The first adjustment is the one proposed by Staff witness J Luebbert. In his surrebuttal testimony, Mr. Luebbert recommends "the Commission disallow 26% of the costs booked in FERC subaccounts 381.1 and 382.2." Exhibit 133, *Surrebuttal Testimony of J Luebbert*, pg. 4 ln. 22 – pg. 5 ln. 3. This recommendation is based primarily on the failure of Spire to justify its replacements:

> Based on Mr. Rieske's Rebuttal testimony 26% of the meters already replaced with ultrasonic meters were less than ten years old and thus not yet required to be tested in accordance with 20 CSR 4240-10.030(19). None of the cost benefit analyses provided by Spire Missouri to date have justified replacement of existing meters that would not have otherwise needed to be replaced. Staff does not object to Spire Missouri's inclusion of the cost of new ultrasonic meters to the extent that service was already disconnected, the existing meter needed to be replaced, and the alternative replacement option would be to purchase a new diaphragm meter.

Id. at pg. 4 lns. 11 – 18. While the OPC supports this disallowance in principle, the OPC also argues that it is far too small for two reasons. The first, rather obviously, stems from the fact that this disallowance only prevents booking additional costs from

this case and does not address the past stranded investment problem that Spire has knowingly allowed to manifest. The second comes from the fact that, the logic of the argument should be expanded.

During the cross-examination of Mr. Luebbert, he explained that his 26% disallowance recommendation was made **prior** to his learning that Spire considered the average service life of meters to be 18.8 in Spire East and 22.1 in Spire West. Tr. pg. 263 lns. 14 – 19 ("Q. When you made -- when you made that recommendation were you aware of -- let me careful here -- at least Mr. Rieske's position, that diaphragm meters have an average service life of 18.8 or 22.1, I believe were the correct numbers, for East and West respectively? A. I was not."). This lead to the following discussion between Mr. Luebbert and counsel for the OPC:

> Q. Would you agree that it's possible to apply the logic that you applied in making that recommendation to those other numbers, though? Let me break that question down because that might have been a bit confusing. Your recommendation was the idea you were going to disallow everything that was retired before the ten-year period. Right? Was that based off of the assumption that Spire was retiring meters at that ten-year period?
>
> A. So part of my recommendation -- I guess part of the reasoning behind my recommendation is that Spire hasn't provided any justification for retiring those meters that didn't even need to be tested at that point.
>
> Q. So why not disallow the meters what were retired before what Mr. Rieske's considers the average service life?
>
> A. I think an argument could be made to do that as well.
>
> Q. Why not disallow all the meters that are retired before what Spire is claiming in its position statement to be the meter's average service life?
>
> A. I'm not sure.

Tr. pg. 263 ln. 24 – pg. 264 ln. 19. The OPC now proffers the very argument that was alluded to in this discussion: the amount the Commission disallows should be based on the actual average service life of Spire's diaphragm meters.

Spire's current position (it is assumed) is that it intends to retire meters only at the end of their useful life. Based on the logic of Staff's disallowance, Spire should not be permitted to recover the cost of any ultrasonic meter used to replace a diaphragm meter before the end of its useful life. The useful life of a diaphragm meter is either 18.8 in Spire East and 22.1 in Spire West or 35 years depending on which Spire witness one finds credible. Therefore, under the logic of Staff's adjustment, the Commission should either disallow every meter retired that was less than 18.8 years old in Spire East and 22.1 in Spire West or less than 35 years old regardless of service territory, again depending on which Spire witness one finds credible. In the alternative, the OPC offers its own adjustment.

In the course of his surrebuttal, the OPC's witness Mr. John Robinett offered several possible solutions that the Commission could employ to address the stranded investment issue that has been discussed at length in this brief:

> **Q. Do you have any suggestions for the Commission on how to handle the remaining plant balance for the diaphragm meters and the communication equipment ERT and AMI?**
>
> A. Yes, the Commission has several options with how to handle the potentially large reserve shortfall for current meters. First, the Commission could essentially punt the issue to a future rate case, as no parties have really discussed how the stranded asset should be handled and all parties will have a better understanding of the true magnitude of the shortfall in the next rate case. In this scenario, the Commission

would just order a depreciation rate consistent with the current recommendations of all the parties. A second option the Commission could employ is a depreciation rate adjustment to account for the extremely truncated life expectancy of the remaining in-service and inventoried diaphragm meters and electronic reading devices. This adjustment will increase the depreciation expense to be collected over the remaining life period of the existing meter; however, this will greatly increase the depreciation expense from current levels and drive up the revenue requirement in this case. The main issue is that there is currently no set plan for meter replacements with a full conversion date to set new depreciation rates to in order to match the recovery to the period the meters are expected to remain in-service. The next option for the Commission to consider would be to create a regulatory asset for the remaining uncollected balance. In this scenario, the Commission would have multiple decisions it needs to make, the first being to determine whether the regulatory asset should still be in rate base and getting a return on and of the investment. Second, the Commission would need to determine over what period of time the recovery is to take place, which would create the amortization period and define the yearly amortization expense associated with the diaphragm meter regulatory asset. An additional option for the Commission to consider could be a disallowance of a portion of the remaining investment needed to be recovered due to the Company's operation that created a reserve shortfall without making depreciation recommendations to make up for the realized disconnect in depreciation lives to actual experience that Spire has known about "for some time". Finally, the Commission could do a hybrid method of increasing depreciation rates slightly to recover a higher percentage before meters are completely retired and still create a regulatory asset and set up amortization of the allowed asset amount to be recovered over a set period of time.

Exhibit 202, *Surrebuttal Testimony of John A. Robinett*, pg. 16 ln. 16 – pg. 18 ln. 3.

Based on these possible solutions, Mr. Robinett offered the following recommendation:

My first recommendation is to disallow any future realized under recovery of the diaphragm meters and related equipment based on Spire's admitted knowledge and lack of action to alleviate the issue. OPC

> witness Dr. Geoff Marke goes into much greater detail on this issue and I will defer further analysis to him. Should the Commission determine that complete disallowance is not appropriate, I recommend the Commission set up a regulatory asset for the unrecovered portion of diaphragm meters, not grant rate base treatment so Spire gets recovery of the investment but not a return on investment, and set up the amortization period for 20 years to minimize the impact on customers' bills.

Id. at pg. 18 lns. 5 – 12. The OPC requests the Commission adopt Mr. Robinett's first recommendation.

Summation

One point that has not been fully covered thus far is the fact that Spire has indicated a "plan " to facilitate the replacement of its existing diaphragm meters, but has not really shown any cohesive understanding of what that plan actually is. OPC witness Dr. Marke explained this in testimony:

> **Q. Your discovery also asked to provide a copy of the installation strategy. Did Spire provide it?**
>
> A. In part. A three-and-a-half page "Overall Strategy" was provided for ultrasonic/AMI deployment across all of its regulated affiliates (only three pages were Missouri applicable). However, the overall strategy can be summarized as follows: **Plans will be developed**.

Exhibit 208, *Surrebuttal Testimony of Geoff Marke*, pg. 5 ln. 20 – pg. 3 ln. 1 (emphasis added). Dr. Marke elaborated on this point further on the stand:

> Q. Okay. I have one more question. Again, the same question I asked of Mr. Luebbert. I'll, again, ask it both upward ways. In Mr. Rieske's rebuttal testimony, his Schedule Non-OPC JAR-R2. This is the 2020 project timeline question. Did you receive any of those documents, the one that is listed in Mr. Rieske's schedule as titled Program, and it has the AMI strategy completed and the quote, Program management plan

completed? Did you receive that material? And, two, did you receive the materials that that material is talking about, i.e., the actual projects or quote, programs?

A. . . . To your question, that encompasses the second part. In my surrebuttal, under GM-1, I asked this question. I asked to receive this information. In GM-2, I included the document with highlighted sections to emphasize my skepticism of the Company's claims.

On GM-2, I'll read just the highlights, so this won't be long. Under Execution Strategy, I read: A complete implementation will be developed. Under Organizational Readiness, I read: Prior to deployment and organizational readiness, checkness (sic) will be performed. Under Training, I read: A training plan will be created. Under Customer Communication, I read: A customer communication plan will be developed. And so on, and so on. I did not receive any of these documents to support those plans, those strategies. **This document here, this three-page document is the strategy for the $100 million dollar-plus investment the Company is planning on making**.

Tr. pg. 285 lns. 9 – 16, pg. 286 ln. 12 – pg. 287 ln. 3 (emphasis added). This neglect by Spire to fully and properly explain just how its proposed ultrasonic meter conversion was to be accomplished has contributed a great deal to the difficulty of this issue.

Right now, it is not clear what exactly Spire's plans are with regard to ultrasonic meter conversions. Is Spire only intending to retire meters who fall within the statistical sampling parameters and could thus possibly be considered at the end of their useful life? Or is Spire aggressively retiring meters whenever there is an opportunity to do so regardless of the age of the meter? At this point, Spire has stated both. *Compare* Tr. pg. 253 lns. 14 – 18 (" Q. So you're not just replacing the meter because it is ten years old. You are relying on some historical analysis to say this falls under the population that needs to be replaced. Correct? A. Yes.") *and* Exhibit 115C,

Rebuttal Testimony of J Luebbert, pg. 5 lns. 5 – 6 ("When a meter is off and customer service needs to be re-stablished, the meter is being replaced regardless of age."). This is a big deal because the rate at which Spire retires these diaphragm meters will have a direct impact on the scale of stranded investment issue that has been already created. The Commission should not reward Spire with green light to engage in a haphazard replacement program, which is exactly what will be inferred if Spire is permitted full recovery of the ultrasonic meters in this case. Moreover, the Commission should not be forcing Spire's customers to cover the cost of two or potentially more meters because of Spire's poor handling of its meter inventory and its failure to rectify a problem with its depreciation schedules that has potentially existed for years.

Conclusion

Spire has completely failed to present sufficient evidence to support the prudency of its decision to switch from diaphragm to ultrasonic meters. All of the offered reasons for why the switch was necessary (from safety to obsolescence) has been proven false and the Company failed to provide any real evidence to show that this switch was a cost-effective measure. In short, Spire has failed to act as a prudent, non-regulated entity would do and so should not be given the blessing of this Commission to recover costs related to this project. Further, Spire has demonstrated a complete disregard for the proper recovery of its assets by allowing a massive stranded investment problem to develop. This is already forcing Spire's customers to

pay for multiple meters at the same time, with Spire now asking the Commission to allow it to make the situation even worse. Such an outcome should not be permitted.

In many respects, this issue is really just a battle between two simple things: the need to act prudently in accordance with the requirements of proper business and due diligence versus the allure of the new being used as bait to permit rampant gold-plating. Unless the Commission acts now to ensure that utilities are required to provide sufficient evidence to support their requests by denying the unsupported ultrasonic meter replacements, this Commission can be assured that this issue and many more like it will occur in the future. In short, it comes down to this: is this Commission going to act like economic regulators and demand utilities operate as non-regulated business would, or does this Commission endorse this level of mismanaged decisions at the expense of the Missouri public.

Issue 30. Weather Normalization Adjustment Rider

Spire has not put forth sufficient evidence demonstrating the need for the Commission to grant the Company authority to continue employing a Weather Normalization Adjustment Rider ("WNAR") let alone its newly proposed Rate Normalization Adjustment mechanism ("RNA"). The Commission should therefore not approve **any** mechanism to account for fluctuations in revenue due to weather, conservation, or both. If, however, the Commission does allow Spire to employ a weather or conservation mechanism, it should authorize Spire to continue its WNAR with the minor adjustments proposed by the OPC. The Commission should not authorize Spire to institute its proposed RNA because this mechanism is not authorized by statute and is thus beyond the Commission's power to grant. Finally, if the Commission nevertheless does approve Spire's requested RNA, it should do so only with the modifications and conditions proposed by Staff and the OPC.

Analysis:

This case represents the second time in a row that Spire has attempted to use a statute that permits an adjustment mechanism to account for weather and/or conservation to sneak into rates a general decoupling mechanism designed to insulate the Company from **all** changes in revenue. *See*, *e.g.* GR-2017-0215, *Report and Order*, pg. 83; Exhibit 212, *Direct Testimony of Lena M. Mantle*, pg. 14 lns. 8 – 16. Consequently, much of the discussion of this issue will depend upon, and be informed by, the Commission's *Report and Order* from Spire's last general rate case. Before

moving directly to discussing why Spire's proposed RNA is both unsound and unlawful, however, it is important to first discuss Spire's failure to justify even maintaining its existing WNAR.

During Spire's last general rate case, this Commission found that Spire's proposed RSM was "not necessary for the company because the utility is not having any difficulty meeting its revenue requirement and has not been shown to be a good mechanism to incentivize conservation." GR-2017-0215, *Report and Order*, pg. 85. Based on this, the OPC understands the Commission to have set forth two criteria for approving a mechanism for making adjustments to account for weather, conservation, or both: "(1) evidence that Spire needs the mechanism to meet its revenue requirement, and (2) evidence that it is needed to incentivize conservation." Exhibit 214, *Surrebuttal Testimony of Lena M. Mantle*, pg. 5 lns. 9 – 10. In this case, Spire has provided evidence of neither. *Id.* at lns. 11 – 12; Exhibit 214, *Surrebuttal Testimony of Lena M. Mantle*, at pg. 6 lns. 4 – 9. To date, Spire has offered no evidence that **any** mechanism (either a WNAR or RNA) is necessary for the Company to meet its revenue requirement. In fact, the Company's actions strongly suggest that it considers the revenue collected through the WNAR to be immaterial to its revenue requirement as explained by OPC witness Ms. Lena Mantle:

> As Spire prepared a summary file for its most recent request to change its WNAR rates, it discovered in February 2021 that it had failed to change in its billing system the WNAR rate approved by the Commission effective October 1, 2020. Spire, of its own accord, had been giving customers a credit through the WNAR when it should have been collecting additional revenue. **It seems that the revenue that Spire had requested and the Commission approved for collection was**

not great enough for Spire to make sure that the revenues were actually being collected.

Q. Do you recommend the Commission approve any interim rate mechanism to adjust rates to account for fluctuations in revenues due to weather and conservation?

A. No. I recommend the Commission reject Spires' request for such a mechanism. **Spire has not shown a need for the rate mechanism and seems to take for granted this shifting of risk to its customers. This is demonstrated by Spire's lack of testimony providing justification for the Commission to grant it an interim mechanism in this case and not making sure a rate change approved by the Commission was implemented**.

Exhibit 212, *Direct Testimony of Lena M. Mantle*, pg. 4 ln. 24 – pg. 5 ln. 14. As for the issue of incentivizing conservation, the RNA mechanism will not accomplish this feat. On the contrary, because the proposed RNA ensures customers pay **more** if conservation does occur, it would actually **disincentivize** conservation.[36] The WNAR does not include this disincentive. If the weather is normal, the rate does not change regardless of whether customers have conserved or increased their usage.[37] However, while the WNAR does not provide a disincentive to conserve energy, it does not give an incentive either. Given these facts, why should the Commission conclude that

[36] If customers do take measures to purposefully conserve and reduce fuel usage, the result under the RNA is an increase in rates to ensure the Company is made whole. Because customers will have to pay more under the RNA with the more conservation that occurs, it will actually encourage people to conserve **less**. This is a point the Commission **needs to understand**. Any rate stabilization or decoupling mechanism that causes rates to increase if people use less energy will put a pecuniary penalty on ratepayers if less fuel is consumed, and will thus disincentivize conservation.

[37] The weather normalization adjustment formula centers on the difference between normal and actual weather. If the actual weather is the same as normal weather the adjustment is zero meaning there is no weather normalization adjustment.

Spire needs either a WNAR or RNA? The answer: it does not require either mechanism.

After pointing out how Spire had offered literally no evidence or arguments as to why it need to have either a WNAR or RNA in direct testimony,[38] Spire did respond with a half-hearted attempt to justify its request in rebuttal. Exhibit 214, *Surrebuttal Testimony of Lena M. Mantle*, pg. 5 lns. 13 – 19. As explained by OPC witness Ms. Mantle:

> [Spire] provides very little justification for why the Commission should approve a rate adjustment mechanism. [It] gives two reasons why the Commission should approve a rate adjustment mechanism.
>
> > 1. Without a mechanism customers would be [] at risk for higher-than-normal gas bills during cold weather years; and
> >
> > 2. Section 386.266.311 permits a utility to submit tariffs for a rate mechanism.

Exhibit 214, *Surrebuttal Testimony of Lena M. Mantle*, pg. 5 ln. 21 – pg. 6 ln. 3. The first of these reasons "is misleading and [the] second shows Spire's sense of entitlement and disregard for the Commission order in its last rate case." *Id*. at pg. 6 lns. 17 – 18. "None of the mechanisms proposed in this case reduce the risk for higher-than-normal bills due to cold weather." *Id*. at pg. 7 lns. 1 – 2. "Customers would still pay higher-than-normal bills due to weather under all proposed mechanisms." *Id*. at lns. 2 – 3. "In addition, it would be unusual for every month in the winter to be colder

[38] Exhibit 212, *Direct Testimony of Lena M. Mantle*, pg. 2 lns. 18 – 20. ("No witness describes why it is necessary for the Commission to grant Spire either the WNAR or the RNA proposed by Mr. Selinger.")

than normal creating a 'colder than normal' year." *Id.* at lns. 8 – 9. "In all of the mechanisms proposed, the 'off-setting' adjustment for a cold month is netted against adjustments for weather that is warmer than normal in other months mitigating the 'offsetting adjustment' for the colder than normal time period." *Id.* at lns. 9 – 12. Finally, and perhaps most importantly, "[a]ll the mechanisms proposed in this case are two-way mechanisms that, in addition to providing off-sets to customers' bills, can also result in increases being passed on to customers as a result of warmer than normal years." *Id.* at pg. 8 lns. 1 – 3. Thus the first "reason" proposed by the Company can be negated by simply stating the inverse: **With** a mechanism customers would be at risk for higher-than-normal gas bills during **warm** weather years.[39]

With regard to the second reason Spire proffered for why it should be given a rate adjustment mechanism to account for weather, conservation, or both, Ms. Mantle points out the following:

> One of the customer protections in Section 386.266 is that the Commission has the power to modify, extend, or discontinue a rate mechanism once the Commission approves an adjustment mechanism under this section. Spire is asking the Commission to discontinue the current WNAR and approve a completely different mechanism simply because statute allows it to request a mechanism. In doing so, however, the Company is ignoring the part of the statute that gives the Commission the authority to approve, modify, or reject the request.

[39] Given the current increasing trends in global temperatures as determined by the leading consensus of climate scientists, it would appear far more likely that customers will see more warm weather years than cold ones. *See*, *e.g.*, Environmental Protection Agency, *Climate Change Indicators: Seasonal Temperature*, (updated April 2021) https://www.epa.gov/climate-indicators/climate-change-indicators-seasonal-temperature. Therefore, Spire's offered reason for why there should be an adjustment mechanism to account for weather, conservation, or both shows such a mechanism is more likely to harm customers rather than help them.

Exhibit 214, *Surrebuttal Testimony of Lena M. Mantle*, pg. 9 lns. 3 – 9.

> It seems that it is Spire's position that once the Commission grants Spire an interim rate adjustment mechanism under this statute, Spire need not ever again explain to the Commission why it should approve a rate adjustment mechanism to account for fluctuations in revenues due to weather or conservation.

Exhibit 212, *Direct Testimony of Lena M. Mantle*, pg. 2 lns. 20 – 24. Needless to say, Spire's position is clearly wrong. The black-letter statutory law is that **Spire** has "the burden of proof to show that the increased rate or proposed increased rate is just and reasonable." RSMo. § 393.150.2. Simply pointing out that an adjustment mechanism **can** be granted is not sufficient to meet the burden of proving why it should. Spire is clearly just resting on its laurels. As Ms. Mantle points out, Spire's argument that it should get a WNAR just because there is a statute that **permits** the Commission to grant one "shows Spire's sense of entitlement and disregard for the Commission order in its last rate case." *Id*. at pg. 6 lns. 17 – 18.

So far, our discussion has only covered why Spire should not be granted a WNAR given its complete failure to prove the need for such a mechanism. However, the OPC recognizes that Spire's mere failure to meets its burden of proof may not actually prevent it from being granted a mechanism for making adjustments to account for weather, conservation, or both. Therefore, the OPC has presented six modifications that should be made to improve the existing WNAR should the Commission allow Spire to maintain it. First, the interest rate included should be Spire's short-term interest rate, which is necessary to comply with section 386.266.5(2). Exhibit 212, *Direct Testimony of Lena M. Mantle*, pg. 11 lns. 18 – 23;

RSMo. § 386.266.5(2). Second, the ß coefficients measuring response to weather should be updated consistent with the weather normalization of usage in this case. *Id*. pg. 12 lns. 1 – 16. Third, the volumetric rates should be updated consistent with the rates in this case. *Id*. pg. 12 ln. 20 – pg. 13 ln. 11. Fourth, the WNAR should be changed to require an annual filing instead of semi-annual filings. *Id*. pg. 14 lns. 1 – 16. Fifth, Spire's tariff change request filings should be made with a 60-day effective date thereby "giving both the Staff and the Commission a review time of 30 days." Exhibit 214, *Surrebuttal Testimony of Lena M. Mantle*, pg. 14 lns. 1 – 15. Finally, the tariff sheets should be simplified in the manner proposed by Ms. Mantle. Exhibit 212, *Direct Testimony of Lena M. Mantle*, Schedule LMM-D-3. Again, the OPC is not recommending or requesting the Commission approve a WNAR, but rather, has provided these modifications to improve the WNAR in the event that the Commission determines Spire's failure to meet its statutory burden of proof is acceptable [40]

Having discussed the WNAR to completion, let us now turn to the RNA mechanism proposed by Spire and endorsed by Staff. To put the matter bluntly, there is no significant legal difference between this mechanism and the RSM Spire proposed in its last general rate case, which this Commission determined it did not have the statutory authority to approve. Consequently, the Commission should find

[40] No party has opposed these changes proposed by the OPC. *See* Exhibit 123, *Rebuttal Testimony of Michael L. Stahlman*, pg. 5 lns. 5 – 7 ("Q. Ms. Mantle also provided some suggested changes to the WNAR tariff sheets. Do you agree with these changes? A. I do not necessarily oppose the recommended changes.").

it does not have the statutory authority to approve this mechanism as well. Let us now examine the argument in detail.

To begin, we must recall the Commission's conclusions of law made in the last Spire general rate case (GR-2017-0215 and GR-2017-0216):

> A. The Commission's powers are "limited to those conferred by the statutes."[41]
>
> B. A RSM is authorized by Subsection 386.266.3, RSMo, which provides:
>
> > Subject to the requirements of this section, any gas corporation may make an application to the commission to approve rate schedules authorizing periodic rate adjustments outside of general rate proceedings to reflect the non-gas revenue effects of increases or decreases in residential and commercial customer usage due to variations in either weather, conservation, or both.
>
> C. The statue authorizes an RSM that allows adjustments for variations due to weather, conservation, or both. **The Commission cannot approve Spire Missouri's proposed RSM because the RSM would make adjustments for all variations in average usage per customer (such as, fuel switching, rate class switching, new customers with non-average usage, and economic factors) and not just those limited to weather or conservation**.

GR-2017-0215, *Report and Order*, pg. 83. As a result of these legal conclusions, the Commission found "the RSM as proposed is not authorized by the statute." *Id.* at pg. 85. Nothing has changed that would invalidate this conclusion in the roughly three and a half years since the Commission reached it. *State ex. Rel. Utility Consumers Council of Missouri* has not been overturned, and section 386.266.3 has not been

[41] Citing *State ex. Rel. Utility Consumers Council of Missouri v. Public Service Commission*, 585 S.W.2d 41, 49 (Mo. 1979).

modified. Thus, to determine the question of whether the Commission has the statutory authority to approve Spire's requested RNA, we need only ask whether the RNA "would make adjustments for all variations in average usage per customer (such as, fuel switching, rate class switching, new customers with non-average usage, and economic factors) and not just those limited to weather or conservation." *Id*. at 83. The short answer: it does, and is therefore not in compliance with section. 386.266.3.

The fact that the RNA would make adjustments for all variations in customer usage and not just those limited to weather or conservation is effectively uncontroverted. First, there is the design of the RNA itself. As explained in Staff's class cost of service report:

> The RNA accomplishes its designed purpose by insulating the company from fluctuations in the Block 2 portions of its revenue requirement subject to volumetric recovery. **All sales in Block 2 are reconciled to rate case billing determinants**.
>
> [. . .]
>
> An adjustment to the RNA rate would be filed annually by the utility based on changes, if any, in actual volumetric sales compared to the level of volumetric sales, by block, used in establishing rates in the rate case.

Exhibit 104, *Staff Class Cost of Service Report*, pg. 39 lns. 1 – 3, 16 – 18. (emphasis added). As the description by Staff makes clear, the mechanism insulates the company from fluctuations in the amount of sales made **regardless of the reason for those fluctuations**. Any change to the level of sales made will affect the "actual volumetric sales" made and will therefore result in an adjustment to the RNA as Staff describes it. This fact was explained by OPC witness Ms. Lena Mantle:

Q. Would the mechanism proposed by Spire account for changes revenue due to weather and conservation?

A. It accounts for ***all*** changes in revenue in this second block, regardless of the reason for the change including changes in revenues due to weather and conservation. Much like the rate stabilization mechanism proposed by Spire in the last case that the Commission found inconsistent with the statutory requirements, the RNA would account for fuel switching, rate class switching, and economic factors that impact usage in the second block and not just changes due to weather and conservation.

Exhibit 214, *Surrebuttal Testimony of Lena M. Mantle*, pg. 14 lns. 8 – 16. Because the RNA as proposed does not base its adjustment off of **any** factor related to either weather or conservation but instead simply looks at the volume of gas sold compared to the expected volume, it does not – and necessarily cannot – distinguish between reductions due to weather or conservation and those made due to other factors such as, fuel switching, rate class switching, customer growth, and economic factors. *Id.*

The fact that that the RNA would make adjustments for all variations in average usage per customer and not just those limited to weather or conservation is further established in the cross-examination of Spire and Staff witnesses:

Q. If someone changes the amount of usage in the second block, it will affect the RNA?

A. Correct.

Q. Right. So if a customer who is in that second block leaves because, for example, they stopped taking gas service, that will change the RNA. Correct?

A. Correct.

Q. And if a customer who is in that second block leaves because they switched to a different class that's not subject to the RNA, that will affect the RNA. Correct?

A. For the SGS customers more than likely that is a possibility.

Q. If a customer is in that block, they leave because they change class, that will affect the RNA?

A. Sure.

Q. Okay. Sure, that is a yes?

A. Yes, Mr. Clizer.

Q. All right. Thank you. Let's say that we have another lockdown, for example, and we have a bunch of people at home during the winter. Is that going to affect -- if you have a bunch of people at home and they're in that second block, you have more usage, is that going to affect the RNA?

A. Yes.

Q. And then like, if we end the lockdown, people come back out, and we have the less usage in that second block, that is going to affect the RNA?

A. Yes.

Q. And if we go into a recession and people literally can't afford gas and you have less usage in that second block, that's going to affect the RNA?

A. Yes.

Tr. pg. 441 ln. 10 – pg. 442 ln. 17 (Cross-examination of Spire Witness Scott Weitzel).

Q. So for residential usage within the block, would the RNA make adjustments for fuel switching?

A. It could.

Q. Would it normalize for fuel switching?

A. I don't know.

> Q. Would it differentiate between fuel switching and weather or conservation?
>
> A. Could you explain -- can you explain the question please?
>
> Q. If a customer left the block because they made a decision to switch from gas to electric or otherwise stop taking gas services, would that affect the RNA?
>
> A. It could.
>
> Q. For that block, would the RNA make adjustments for rate class switching?
>
> A. I know there is discussion with some -- with Ms. Mantle. She had proposed some for the SGS customers a way to correct for the customers leaving.
>
> Q. Without that correction, though, it would have -- the RNA would be affected by rate class switching. Correct?
>
> A. It could. It depends. That's one of the important things on having the cap for the SGS class as proposed by Staff.

Tr. pg. 455 ln. 14 – pg. 456 ln. 12 (cross-examination of Staff Witness Michael L. Stahlman). Based on these answers, the testimony of OPC witness Ms. Mantle, and the inherent design of the RNA as discussed earlier, we can safely say that the proposed RNA would make adjustments for all variations in average usage per customer (such as fuel switching, rate class switching, customer growth, and economic factors) and not just those limited to weather or conservation. This is the very same factual basis that led the Commission to conclude it did not have the statutory authority to approve the RSM proposed in Spire's last general rate case. GR-2017-0215, *Report and Order*, pg. 83.

With all that has been discussed thus far, it should be very obvious that Spire's proposed RNA exceeds the statutory authority granted by section 386.266.3 in the

exact same manner as the RSM proposed in Spire's last general rate case. GR-2017-0215, *Report and Order*, pg. 83. Unfortunately, Staff is now attempting to confuse this issue by arguing for a completely new and different interpretation of the word "conservation." Specifically, Staff is attempting to argue (in essence) that **all** reduction in usage caused by such things as fuel switching, rate class switching, customer growth, or economic factors would constitute "conservation." *See* Tr. pg. 464 ln. 24 – pg. 465 ln. 25. This is obviously wrong, as the OPC will now demonstrate.

We shall begin with the definition of "conservation." Staff employ's the definition found in Webster's Third New International Dictionary. This dictionary actually contains three separate entries for the definition of "conservation," but only the second entry really addresses the issue at hand:[42]

> **2:** care or keeping and supervision of something by a government authority or by a private association or business: as **a:** planned management of a natural resources to prevent exploitation, destruction, or neglect **b:** the wise utilization of a natural product esp. by a manufacturer so as to prevent waste and insure future use of resources that has been depleted.

Webster's Third New International Dictionary 483 (1976). Staff, for whatever reason, only cited to part (b) of this definition. Exhibit 104, *Staff Class Cost of Service Report*,

[42] For the sake of completeness, the first and third entries for "conservation" are as follows: **1:** deliberate, planned or thoughtful preserving, guarding, or protecting**:** keeping in a safe or entire state; *specif* **:** the repair or preservation of works of art **3:** a field of knowledge concerned with coordination and plans for the practical application of data from ecology, limnology, pedology, and other sciences that are significant to preservation of natural resources. *Webster's Third New International Dictionary* 483 (1976).

pg. 38 fn. 15. When considered in its **entirety**, it becomes obvious that the definition is referring to a *specific* and *intentional* action taken to **preserve** a natural resource. The intent of the party who is undertaking the action is an essential element of the definition. Thus, the definition of "conservation" is not "a fairly broad definition" as Staff's witness claimed. Tr. pg. 465 ln. 5. On the contrary, the definition only refers to the narrow category of actions taken to prevent exploitation, destruction, neglect, or waste of a natural resource. *Webster's Third New International Dictionary* 483 (1976). This would clearly not include actions by a customer taken out of a desire or need to save money.

The customer who decides to switch from natural gas heating to electric heating is not doing so because they are a manufacturer seeking to preserve and insure the further use of some scare natural resource. The storeowner who ceases to heat his premise because of a government mandated lock-down intended to combat a global pandemic is not engaged in the "planned management of a natural resources to prevent exploitation, destruction, or neglect." These are simply not people engaged in the act of conservation. No matter what Staff witnesses may say or think, customers using less natural gas due to "fuel switching, rate class switching, customer growth, and economic factors" does not meet the definition of conservation. Moreover, the Commission should already know this. After all, the definition that Staff is citing has been in place *since 1976*. Yet a mere three years ago, this Commission steadfastly found that fuel switching, rate class switching, customer growth, and economic factors were not compatible with "conservation." GR-2017-

0215, *Report and Order*, pg. 83. To now suddenly deviate from that prior legal conclusion based on a definition that was in effect well before the legal conclusion was rendered would be completely arbitrary. *Oakes v. Mo. Dep't of Mental Health*, 254 S.W.3d 153, 158 (Mo. App. ED 2008) ("The DMH's decision is also arbitrary and capricious as it appears to rely more on the personal whim of its Executive Director rather than on appropriate legal definitions, standards and analysis.").

There is yet a further problem with Staff's new expansive reading of the term "conservation" in that it would violate commonly understood cannons of statutory construction. As explained by the Missouri Supreme Court:

> When ascertaining the legislature's intent in statutory language, it commonly is understood that each word, clause, sentence, and section of a statute should be given meaning. *See Mo. Prop. & Cas. Ins. Guar. Ass'n v. Pott Indus.*, 971 S.W.2d 302, 305 (Mo. banc 1998). The corollary to this rule is that a court should not interpret a statute so as to render some phrases mere surplusage. *See Spradlin v. City of Fulton*, 982 S.W.2d 255, 262 (Mo. banc 1998). Consistent with these principles, a sentence should not be given a meaning that thwarts a section; a clause should not undermine a sentence.

Middleton v. Mo. Dep't of Corr., 278 S.W.3d 193, 196 (Mo. banc 2009). In this case, Staff's expansive reading of "conservation" as used in 386.266.3 would actually thwart and potentially render as mere surplusage the word "weather." After all, if Staff is correct that a storeowner's decision to turn down the heater because nobody is going to the store counts as "conservation,"[43] then why wouldn't a customer's

[43] See Tr. pg. 465 lns. 18 – 25.

decision to turn down the heater because it is not that cold outside be the same? The answer is that they would be the same. In this manner, the word "conservation" would subsume the word "weather" thus rendering the latter mere surplusage in violation of Missouri law. In fact, if one agrees with Staff's expanded definition, quite literally **every action taken by a ratepayer that effects energy use becomes a type of conservation**. This is naturally absurd, which indicates the violation of yet another cannon of statutory construction. *State ex rel. Hawley v. City of St. Louis*, 531 S.W.3d 602, 608 (Mo. App. ED 2017) (When no statutory definitions of terms are provided, the Courts "must interpret those terms according to their plain and ordinary meanings, **with reference to the problem the statute was intended to solve, to the broader statutory context within which the statute applies, and to whether the consequences of any particular interpretation of the statute would be unjust, unreasonable, or absurd**." (emphasis added).

Based on Staff's interpretation of the word "conservation" as a justification for the proposed RNA, Spire would be given a mechanism that would ensure it was made whole for all the following:

1. Loss of sales caused by customers leaving Spire's service territory;
2. Loss of sales caused by customers not having service due to maintenance Spire is performing on its own system;
3. Loss of sales caused by natural disaster including earthquakes, flooding, or major fires that destroys residences or small businesses in Spire's service territory;

4. Loss of sales occasioned by social upheaval including pathological disasters (such as an epidemic or pandemic), armed conflict, or property destruction brought on by riots or looting;

5. Loss of sales caused by customers making the choice to switch energy providers due to cost factors or the abundance of subsidized renewable energy and electrification options at either a federal, state, or utility level; and

6. Lost sales due to failures in interstate natural gas delivery caused by number of potential factors from major judicial or federal-executive decisions to cyber-attacks on pipelines.

Every single one of the items listed here would result in reduced sales to residential and small commercial customers. Because the RNA does not take any actual weather or conservation factors into consideration and instead only considers the "actual volumetric sales compared to the level of volumetric sales, by block, used in establishing rates in the rate case" every single one of these incidents would trigger an adjustment to the RNA. Exhibit 104, *Staff Class Cost of Service Report*, pg. 39 lns. 16 – 18; Exhibit 214, *Surrebuttal Testimony of Lena M. Mantle*, pg. 14 lns. 8 – 16. Thus, Staff's effort to re-write the law would create a truly absurd result where everything from cybercrime to earthquakes would affect the mechanism that is only supposed to address "weather, conservation, or both." RSMo. § 386.266.3.

Given the absurdity of Staff's position, one must question why it was adopted. Here we find, as we have so many times before now, that Staff's position is simply one of inertia. This will of course seem odd, given Staff's radical departed from the Commission's decision in Spire's last general rate case, yet it is nonetheless true. The simple reason that Staff has decided to drastically change its position between rate

cases comes down to the fact that a mechanism that was *similar* to Spire's proposed RNA was adopted for Ameren Missouri. *See*, *e.g.*, Tr. pg. 452 lns. 18 – 21; Exhibit 123, *Rebuttal Testimony of Michael L. Stahlman*, pg. 3 lns. 5 – 10. Because this mechanism was put into place *after* Spire's last general rate case, it has become the last thing the Commission ordered, and thus Staff's position. Incidentally, the Ameren Missouri mechanism effectively forms the *entirety* of Spire's argument for the RNA. It is therefore necessary for us to address this Ameren Missouri mechanism.

The fact that Ameren Missouri has a rate stabilization mechanism similar in nature to what Spire now proposes is irrelevant. This is due simply to the fact that the Ameren Missouri mechanism resulted from a stipulation. Tr. pg. 447 lns. 14 – 25; Exhibit 232, *Attachment A to Order in GR-2019-0077*. The lack of statutory authority to issue the Ameren Missouri mechanism was just as true and relevant, but the OPC choose not to press the issue in exchange for other considerations reached in the settlement of the case. That does not, however, prevent the OPC from now raising the legal argument that Spire's proposed RNA lacks statutory authority. This point was specifically incorporated into the very terms of the stipulation and Commission order that allowed for the Ameren mechanism in the first place. Exhibit 232, *Attachment A to Order in GR-2019-0077*, pg. 9 ("Except as explicitly provided herein, none of the signatories shall be prejudice or bound in any manner by the terms of this agreement in this **or any other proceeding** regardless of whether this agreement is approved" (Emphasis added)); *see also* Tr. pg. 459 ln. 23 – pg. 460 ln. 2.

The existence of the Ameren mechanism does not, and legally cannot, extend the statutory authority of the Commission. Moreover, the language of the stipulation agreement approved by the Commission in GR-2019-0077, by its very terms, prevents the OPC from being judicially estopped from raising the legal issue of statutory authority as it is doing now. As such, the existence of the Ameren Missouri mechanism is perfectly meaningless to this case, and with it falls the last, and frankly only, justification that Spire had for the RNA.

The statutory authority granted to the Commission under section 386.266.3 to create a rate mechanism to account for "weather, conservation, or both" does not grant legal authority to the Commission to approve a rate mechanism that Spire now requests because that mechanism would account for **all** variations in average usage per customer (including fuel switching, rate class switching, customer growth, and economic factors) and not just those limited to weather or conservation. GR-2017-0215, *Report and Order*, pg. 83. Despite what either Staff or Spire may argue, the existence of a similar mechanism in place for Ameren Missouri does not, **and legally cannot**, change this outcome. That mechanism only exists because Ameren was willing to offer agreeable settlement terms to the OPC and other parties, which, is not what occurred in this case.[44] Further, there is no merit to Staff's new and

[44] The importance of these kind of provisions that are included in standard settlement agreements that prevent the issues settled from becoming precedent in other cases should now be quite obvious. The Commission needs to be careful to treat these provisions with the proper respect they require or else it will seriously jeopardize the ability of those parties appearing before it to actually settle cases. For example, if the Commission were to determine that the Ameren stipulation created legal precedent that affected **all** gas companies in spite of the clear language stating the opposite, it would not only be committing legal error but also requiring all future negotiations to be considered in light of all natural gas companies. This could quite easily kill the ability to settle cases.

expansive interpretation of the word "conservation" that is now being offered up as a sort of *post hoc* justification for the Ameren mechanism. Staff's attempt to read "conservation" as meaning "any wise use of energy" is contrary to the actual language of the definition, the clear intent of the statute, and widely adopted cannons of statutory construction. *See State ex rel. Hawley v. City of St. Louis*, 531 S.W.3d 602, 608 (Mo. App. ED 2017). The Commission should thus under no circumstances grant Spire approval of its proposed RNA.

In the event that the Commission disregards all of the legal and factual arguments thus presented and nevertheless approve Spire's RNA, there are several modifications that should be made to the version proposed by Spire. First, the Commission should adopt the "block breaks" proposed by Staff, which are "50 Ccf for the residential class and a beginning block break of [300] and an ending block break of [599] Ccf for the small general service class." Exhibit 213, *Rebuttal Testimony of Lena M. Mantle*, pg. 29 lns. 8 – 9.[45] This would shift less risk onto customers (by guaranteeing Spire less revenue) and would be less likely to result in double recovery due to rate switching. *Id*. at pg. 30 lns. 8 – 19. Further, the RNA rate should modified to only be charged to the second block usage. *Id*. at pg. 17 ln. 23. This will prevent customers with low usage, i.e. non-weather sensitive customers with little room for conservation, being charged more because other customers were more weather-sensitive or conserved energy. *Id*. at lns. 19 – 21. In addition, the normalized Rate

[45] The original Staff recommendation was updated in the rebuttal testimony of Staff witness Ms. Lange. Exhibit No. 114, *Rebuttal Testimony of Sarah L.K. Lange*, pg. 2 lns. 9 – 10. The numbers cited here are the updated numbers.

Case Block Usage used in the calculation of the RNA rate should be adjusted annually for the removal of the usage of any customer that has switched to the LGS class each year. *Id*. at pg. 18 lns. 10 – 12. This will prevent double recovery by the Company from large SGS customers that switch to the LGS class. *Id*. at lns. 1 – 8. Finally, the tariff sheet adopted should be substantially similar to the one included as a schedule to the testimony of Ms. Lena Mantle. LMM-S-1 in order to rectify a number of minor drafting errors.

Conclusion

Spire has utterly failed to demonstrate the need for the Commission to grant the Company authority to continue employing a WNAR. The Commission should therefore order an end to Spire's WNAR. If, however, the Commission does allow Spire to continue its WNAR, it should do so only after ordering the minor adjustments proposed by the OPC. Under no circumstances should the Commission allow Spire to institute its proposed RNA because this mechanism is not authorized by statute and is thus beyond the Commission's power to grant. Finally, if the Commission nevertheless does approve Spire's requested RNA, it should do so only with the modifications and conditions proposed by Staff and the OPC.

Conclusion

Spire has the burden of proving the rates that it seeks are just and reasonable. RSMo. § 393.150.2 ("At any hearing involving a rate sought to be increased, the burden of proof to show that the increased rate or proposed increased rate is just and reasonable shall be upon the gas corporation"). Spire has no regard for this statutory requirement. How else can one explain the behavior displayed in this case? For example, Spire is seeking millions of dollars' worth of plant investment related to the replacement of diaphragm meters with ultrasonic meters (and **clearly** envisions this as the beginning of a full-scale overhaul of its meter infrastructure), yet, Spire's justification for these costs amounted to two sentences in direct testimony. Spire seeks to completely change its depreciation rates, yet failed to file its depreciation study in direct testimony or even correctly state what it was requesting. Spire wants to replace its WNAR with an RNA but offers no justification for either mechanism and instead relies almost exclusively on the argument that, "if Ameren got it, so should we." Finally, Spire's response to the criticism that it is not properly capitalizing overheads by just repeatedly stating that it is following the USOA while offering no evidence in support. To make matters worse, the situation fares no better when you consider what evidence the Company *has* supplied.

For almost every issue where Spire has provided actual evidence to support its position, that evidence has been effectively contradicted in one form or another by other pieces of Spire's own case. Spire's claim that it is not using short-term debt to support its capital is undercut by the schedules its own witness provides that shows

the massive amount of short-term debt that Spire carries in excess of short-term assets (after removing the obviously flawed and blatantly manipulative long-term debt issuance that did not occur until the last two weeks of the true-up period). Spire's proffered benefits of ultrasonic meters is contradicted by the specification sheets for those same meters (written by the meter's manufacturer) and the testimony of Spire's depreciation expert. Spire's return on equity analysis is contradicted by the Company's own internal documentation. The rate at which Spire intends to replace diaphragm meters is contradicted several times across its testimony. Finally, there is the parade of errors and contradictions that is Spire's depreciation request.

Given this plethora of errors, Spire cannot meet its burden of proving that the rates it has requested are just and reasonable. On the contrary, the record now before the Commission shows that Spire has been flagrantly disregarding Commission rules, actively managing its business for the benefit of its non-regulated affiliates, and gold-plating its distribution system in order to artificially inflate its rate base. In short, Spire Missouri is being used to heavily subsidize the numerous other business ventures that Spire Inc. has engaged in, several of which are facing major external threats. Spire Missouri's ratepayers should not have the burden of covering Spire Inc.'s bad business decisions. The OPC looks to this Commission to insulate and protect Spire's customers to ensure that they are only paying for what it costs to continue operating Spire Missouri as a natural gas distributor. In this case, that means balancing the capital investments made against the adjustments needed to

correct for the current subsidization. The result should be that Spire's rates remain static.

WHEREFORE, the Office of the Public Counsel respectfully requests the Commission accept this *Initial Brief* and rule in the Office of the Public Counsel's favor on all matters addressed herein.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that copies of the forgoing have been mailed, emailed, or hand-delivered to all counsel of record this seventh day of September, 2021.

/s/ John Clizer