**BEFORE THE PUBLIC SERVICE COMMISSION**
**OF THE STATE OF MISSOURI**

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| In the Matter of The Empire District<br>Electric Company's Request for Authority<br>to File Tariffs Increasing Rates for Electric<br>Service Provided to Customers in its<br>Missouri Service Area | )<br>)<br>)<br>)<br>) | Case No. ER-2019-0374 |

**MECG STATEMENT OF POSITION**

COMES NOW, the Midwest Energy Consumers Group ("MECG") and for its Statement of Position provides the following. MECG reserves the right to supplement its positions in the context of briefs in this case based upon hearing exhibits that are being filed on this same date.

1. Rate of Return—Return on Equity, Capital Structure, and Cost of Debt:
    a. Return on Common Equity – what return on common equity should be used for determining rate of return?

Position: As reflected in both the testimony of the Commission's Staff as well as Public Counsel, MECG recommends that the Commission authorize a return on equity of 9.25%. Furthermore, as explained in the section addressing Empire's request to implement a weather normalization mechanism, the Commission is tasked to consider the reduction in Empire's business risk as a result of implementing such a mechanism. To the extent that the Commission authorizes such a mechanism, the Commission should consider an explicit reduction in Empire's return on equity..

    b. Capital structure – what capital structure should be used for determining rate of return?

Position: As reflected at page 5 of the direct testimony of David Murray, MECG recommends that the Commission utilize a capital structure consisting of 46% common equity and 54% long term debt. Such a capital structure is consistent with merger conditions agreed to by Empire and its parent company and recognizes a capital structure that allows Empire to earn a reasonable return on equity while also minimizing the cost of capital for ratepayers. Specifically, such a capital structure avoids concerns that Liberty Utilities has manipulated the capital structure of its regulated subsidiaries in order to maximize corporate profits. (Murray Direct, pages 8-14).

c. Cost of debt – what cost of debt should be used for determining rate of return?

Position: Empire's embedded cost of debt is 4.65%. (Murray Direct, pages 14-15).

2. Rate Design, Other Tariff and Data Issues:

r. How should any revenue requirement increase or decrease be allocated to each rate class?

Overview: In the class cost of service studies presented by Staff, Empire and MECG, it is shown that all of the Empire commercial and industrial classes are subsidizing residential rates. This conclusion is consistent with those made by the Commission in each of the last two rate cases. The inclusion of the residential subsidy inflates commercial and industrial rates to the point that they are not competitive with the national average. Thus, as the Commission has previously held, the Empire service area is at a high risk of losing industry and jobs to other parts of the country. In the 2014 rate case, the Commission took steps to eliminate 25% of the residential subsidy. Through its position in this case, MECG asks that the Commission simply eliminate another 25% of the residential subsidy.

Position: Any decision regarding the allocation of any revenue requirement change should be guided primarily by each classes' cost of service as determined by a class cost of service study. "The purpose of a CCOS [class cost of service study] is to allocate a utility's overall cost of service to each rate class in a manner that reflects its underlying cost of service."[1] By allocating each cost in a rational manner to the individual rate classes, one can determine the cost of service for each rate class.

In this case, class cost of service studies were presented by 3 parties: Empire, Staff and MECG. Noticeably, Public Counsel did not conduct a class cost of service study. Rather, in rebuttal testimony, Public Counsel aligned itself with the study conducted by Staff and the conclusions reached by Staff.[2]

The results of the 3 class cost of service studies in this case point to certain undeniable facts. First, consistent with the studies and Commission decisions in previous Empire cases, the residential class is paying rates that are significantly below cost of service. Second, the residential subsidy currently existing in rates is not only detrimental to the industrial rate classes (LP and SC-P), it is also detrimental to the commercial classes (CB, SH, TEB, GP).

[1] Lyons Direct, page 8.
[2] Marke Rate Design Rebuttal, page 5.

**Earned Return by Customer Class**

| | Empire[3] | MECG[4] | Staff[5] |
|---|---|---|---|
| RG – Residential | 2.90% | 2.62% | 5.46% |
| CB – Commercial | 8.23% | 8.16% | 11.31% |
| SH – Small Heating | 7.39% | 7.12% | 11.31% |
| GP – General Power | 11.44% | 12.19% | 11.11% |
| SC-P Praxair | 9.63% | 15.28% | 11.38% |
| Total Electric Bldg | 11.46% | 11.37% | 11.11% |
| PFM - Feed Mill | 10.59% | 10.56% | -36.92% |
| LP - Large Power | 8.34% | 9.52% | 10.88% |
| MS – Miscellaneous | -5.21% | -4.94% | 28.70% |
| SPL – Municipal Ltg. | 1.77% | 1.99% | 28.70% |
| PL – Private Ltg. | 26.95% | 26.48% | 28.70% |
| LS – Special Ltg. | -6.47% | -7.18% | 28.70% |
| Total Company | 6.11% | 6.11% | 6.11% |

These undeniable conclusions are consistent with those from previous cases. Two cases ago, Case No. ER-2014-0351, the Commission also considered the residential subsidy that existed in rates.

> Staff's CCOS recommendation shows that residential rates are 8.06% below costs, while large power ("LP") rates are 8.35% above costs and general power ("GP") rates are 7.9% above costs. All four CCOS studies filed by the parties show that the residential class is contributing below its share of the rate of return.[6]

In that case, the Commission pointed out the importance of competitive industrial rates and concluded that Empire's rates were not competitive with the national average industrial rate.

> Retail rates are pricing signals that drive customer behavior. Empire's average industrial rates are 16% above the national average, while its residential rates are 3.5% below the national average. . . . Competitive industrial rates are important for the retention and expansion of industries within Empire's service area. If businesses leave Empire's service area, Empire's remaining customers bear the burden of covering the utility's fixed costs with a smaller amount of billing determinants. This may result in increased rates for all of Empire's remaining customers.[7]

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[3] Maini Direct, page 31 (based upon Lyons Direct, Schedule TSL-9). Empire subsequently agreed with certain adjustments to "firm up" the revenues for the interruptible SC-P class and to more appropriately allocate the interruptible credits for this class. This has the effect of increasing the earned return for the SC-P class. (See, Lyons Rebuttal, page 10).

[4] Maini Direct, page 31.

[5] Lange Rebuttal, page 17.

[6] Report and Order, Case No. ER-2014-0351, issued June 24, 2015, pages 15-16.

[7] *Id.* at pages 17 and 18.

Given the significant residential subsidy as well as the uncompetitive nature of Empire's industrial rates, the Commission took positive steps to begin eliminating the residential subsidy and help to make Empire's industrial rates more competitive.

> Attempting to completely eradicate the 8.1% residential rate class discrepancy in this rate case would be too punitive to the customers in that class. A revenue neutral adjustment of 25% of the 8.1% needed adjustment would increase the residential rates by approximately 2%. . . . A 2% revenue neutral adjustment for the residential class is not punitive to the residential class and helps to eliminate any residential subsidy in a shorter timeframe.[8]

In the next Empire rate case (ER-2016-0023), the Commission again took steps to eliminate a portion of the residential subsidy. In that case, the Commission approved a unanimous settlement, including Public Counsel, which provided for another shift of costs to the residential class and away from the General Power, Commercial, Large Power and Praxair classes.

> There shall be a $3 million revenue neutral shift to the residential class, allocated as follows: -$2 million to GP; -$525,000 to CB; -$340,000 to LP; and -$135,000 to the Praxair class.[9]

Despite the Commission's actions in the last two cases, a residential subsidy continues to exist. In fact, as previously indicated, each of the class cost of service studies show that the commercial and industrial classes are paying higher rates in order to support the below cost residential rate. Moreover, while the Commission has attempted to take steps to make Empire's industrial rates more competitive, those rates are even more uncompetitive than they were just five years ago. Specifically, while the Commission found that Empire's industrial rates were 16% above the national average just five years ago, Empire's industrial rate is now 16.9% above the national average.[10] In fact, undisputed evidence in this case indicates that Empire's industrial rate is the 12th highest of 95 electric utilities operating in 28 MidAmerican states.[11]

Clearly then, continuing with the logic expressed by the Commission in previous cases, it is incumbent that the Commission again take steps to address the persistent residential subsidy. Each of the parties that submitted a class cost of service study recommended that the Commission take such affirmative steps. In its testimony, MECG again recommended that the Commission seek to eliminate 25% of the existing residential subsidy.[12] Such a movement would lead to a 4.2% increase for the residential class and help to improve the competitiveness of <u>all</u> commercial and industrial classes.

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[8] *Id.* at pages 18 and 19.
[9] Report and Order, Case No. ER-2016-0023, issued August 10, 2016, at Attachment page 9 of 12.
[10] Maini Direct, page 9.
[11] *Id.* at page 9 and Schedule KM-2.
[12] Maini Direct, page 35.

| | Revenue Shift (in thousands) | % Shift |
|---|---|---|
| RG - Residential | +$9,030 | 4.2% |
| CB – Commercial | -$841 | -1.9% |
| SH – Small Heating | -$101 | -1.0% |
| GP – General Power | -$4,310 | -5.1% |
| SC-P – Praxair | -$239 | -5.4% |
| TEB – Total Electric Bldg. | -$1,674 | -4.6% |
| PFM – Feed Mill | -$3 | -4.5% |
| LP – Large Power | -$1,846 | -3.0% |
| MS – Miscellaneous | +$1 | 7.5% |
| SPL – Municipal Ltg. | +$259 | 11.9% |
| PL – Private Ltg. | -$445 | -10.9% |
| LS – Special Ltg. | +$77 | 58.8% |

Such a shift is not punitive. Recognizing that, through the Non-Unanimous Stipulation, Empire has agreed to no rate change. This would only involve a residential increase of 4.2%.[13] In its original filing, Empire sought an increase for the residential class of 5.8%.[14] Thus, even with the partial elimination of the residential subsidy, residential customers will still see a lower increase than they were initially expecting from this case.

In its surrebuttal testimony, Public Counsel seeks to have any revenue reduction ordered in this case be allocated solely to the residential class. In doing so Public Counsel does not dispute that residential rates are currently being subsidized. Rather, Public Counsel simply insinuates that residential customers are being disproportionately harmed by the current Covid-19 pandemic. As reflected in the supplemental surrebuttal testimony of MECG witness Meyer, however, all portions of Empire's customer base is being harmed by the Covid pandemic. As such, there is no basis, other than Public Counsel's emotional appeal, for further inflating the residential subsidy by assigning any revenue reduction to the residential class.

► Rate Design Issues:

e. How should the rates for each customer class be designed?

Position: While the previous issue seeks to correct the significant interclass subsidy that exists in rates, the proposal for the design of rates seeks to address the intraclass subsidy in the rates of certain classes. Specifically, MECG proposes that any rate reduction for the LP and GP rate classes be reflected by reducing both blocks of the class energy charges. In this way, all other charges (customer and demand charges) used for the

[13] In its rebuttal testimony, Empire generally supported the proposal to partially eliminate the residential subsidy. (Lyons Rate Design Rebuttal, pages 10 and 32 ("As mentioned in direct testimony, the Company believes the results of the class cost of service study support a higher rate increase for residential customers since their current rates recover less than the cost of service."). Similarly, Staff also proposes shifts to address the residential subsidy. (Lange Rebuttal, page 18).

[14] Richard Direct, Schedule SDR-9.

collection of fixed costs would remain at current levels.[15] In its rebuttal testimony, Empire agreed with MECG's proposal. "The Company supports MECG's recommendation to apply approved increase for the LP class to the billing demand and facility charges and apply any approved decreases to the energy charge. This approach better aligns recovery of demand-related costs through demand charges and energy-related costs through energy-related charges."[16]

4. WNR and SRLE Adjustment Mechanisms:

a. Should the Commission approve, reject, or approve with modifications Empire's proposed Weather Normalization Rider?

b. Is it lawful for the Commission authorize Empire to implement a Sales Reconciliation to Levelized Expectations ("SRLE") mechanism, such as those Staff and Empire are proposing in this case?

c. Should the Commission adopt Staff's Sales Reconciliation to Levelized Expectations Proposal ("SRLE") or approve the SRLE with modifications as suggested by the Company?

Position: The Commission should approve the WNR / SRLE mechanism set forth in the Non-Unanimous Stipulation. Section 386.266.3 provides statutory authority for the Commission to establish a mechanism authorizing "periodic rate adjustments outside of general rate proceedings to adjust rates of customers in eligible customer classes to account for the impact on utility revenues of increases or decreases in residential and commercial customer usage due to variations in either weather, conservation, or both." The statute continues on to provide that the "eligible customer classes" subject to such a mechanism are "residential and classes that are not demand metered."

The reason for limiting the applicability of such a mechanism to residential and non-demand metered classes are obvious from the evidence in this case. Classes that have demand meters are charged demand rates. For Empire, this includes both a demand charge (used to collect generation and transmission costs) as well as a ratcheted facilities demand charge (used to collect distribution costs). For these classes then, fixed costs are ideally collected through the demand charges and variable costs are collected through the energy charge.

In contrast, the residential and non-demand metered classes are simply charged a customer charge and an energy charge. Given the absence of a demand charge(s) for the collection of fixed costs, a significant amount of the fixed costs for these classes are collected through energy charges. As Mr. Lyons points out, 90.9% of the residential revenue requirement is collected through energy charges.[17] This heavy reliance on energy charges, which are collected on a per kWh basis, means that the utility's recovery of fixed costs from these classes is incredibly susceptible to usage variations due to weather and conservation.

[15] Maini Direct, page 36.
[16] Lyons Class Cost of Service Rebuttal, pages 34-35.
[17] Lyons Direct, page 53.

In an effort to break the linkage between the utility's recovery of fixed costs from these classes' consumption of electricity, the General Assembly authorized the creation of a mechanism that permits changes in rates for these classes to account for increases or decreases in consumption as a result of weather and conservation.

In its direct testimony, Empire sought Commission approval for a weather normalization rider. That mechanism was described in Empire's proposed tariffs as well as the direct testimony of Mr. Lyons. In its testimony, Staff proposed a similar mechanism which it termed a Sales Reconciliation to Levelized Expectations ("SRLE") rider.

In the Non-Unanimous Stipulation, the Signatories proposed a mechanism that is largely consistent with Staff's SRLE mechanism. As indicated, that mechanism is expressly authorized by Section 386.266.3. MECG believes that this mechanism is appropriate and should be approved by the Commission.

It is important to recognize that the creation of a weather normalization / SRLE mechanism results in a significant decrease in the utility's business risk. Specifically, the risk associated with weather and conservation is shifted from the utility to the customers. Section 386.266.8 directs the Commission to consider the change in the utility's business risk resulting from the creation of such a mechanism. Such change in risk should be reflected in the return on equity authorized by the Commission in this case. Given the direction of this statute, MECG urges the Commission to consider the reduction in Empire's business risk resulting from the requested SRLE mechanism and make an explicit reduction in Empire's return on equity to account for the shifting of this risk from the utility to customers.

12. <u>Tax Cut and Jobs Act of 2017 federal income tax rate reduction</u> from 35% to 21% impact for the period January 1 to August 30, 2018:
    a. How should the Commission treat the 2017 TCJA regulatory liability the Commission established in Case No. ER-2018-0366 when setting rates for Empire in this case?

<u>Position</u>: Section 393.137, implemented in 2018, provides two things. First, the statute authorizes the Commission to adjust a utility's rates to prospectively account for the 2017 change in the federal corporate tax rate. Second, the statute required the Commission to defer, as a regulatory liability, the financial impact of the tax reduction for the period from January 1, 2018 through the date on which rates were prospectively changed (the "stub period"). The statute then mandates that the Commission include these stub period benefits in rates in the utility's subsequent general rate proceeding.

In Case No. ER-2018-0366, the Commission held that Empire fell within the scope of Section 393.137. Given this, the Commission prospectively changed Empire's rates to account for the reduction in the federal corporate tax rate. In addition, consistent with the statute, the Commission ordered Empire to create a regulatory liability for the benefits that occurred during the stub period. "Having found that section 393.137.3 applies to Empire, the Commission must comply with that statute by ordering Empire to establish a

regulatory liability to account for its excess earnings during the period of January 1 through August 30, 2018."[18]

In this case, the Signatories to the Non-Unanimous Stipulation have complied with Section 393.137. Specifically, the Signatories have included an amortization of the stub period benefits, as required by the statute, while preserving the vast majority of these benefits in Empire's next rate case when a significant investment with wind is included in rates. The relevant portion of the stipulation provides:

> An amortization of the balance of the stub period amortization of \$11,728,453, in the amount of \$5,000 monthly, is included in the revenue requirement for this case. The amortization balance, and the appropriate amortization period, will be reevaluated in the next general rate case.[19]

Recognizing that this provision is consistent with the statute and has been agreed to by representatives of all of Empire's stakeholder groups, MECG asks that the Commission adopt this provision as a fair and reasonable resolution of this issue that is also consistent with Section 393.137.

13. Asbury:
    a. Is it lawful to require Empire's customers to pay for Asbury costs through new rates?
    b. Is it reasonable to require Empire's customers to pay for Asbury costs through new rates?
    c. If it is unlawful and/or unreasonable to include the costs of the retired Asbury plant in rates, what amount should be removed from Empire's cost of service?

Position: Twice the Commission has indicated that it desired to treat the impacts of the retirement of Asbury through an Accounting Authority Order. It is well established that the Commission may defer the costs / savings associated with an extraordinary event like the retirement of a generating unit through an Accounting Authority Order. In the Non-Unanimous Stipulation the Signatories sought the creation of an Accounting Authority Order for these costs / savings. In addition, that Stipulation provides a baseline of costs by which the Commission may easily quantify savings in Empire's next rate case. Given this, MECG encourages the Commission to approve this provision of the Non-Unanimous Stipulation and Agreement.

25. Asset Retirement Obligations:
    a. Should Asset Retirement Obligations be included in rate base as a regulatory asset and amortized?

Position: In its Direct Testimony, Empire sought to include certain costs in rate base that it classified as an Asset Retirement Obligation ("ARO"). Historically, the Commission

[18] *Report and Order*, Case No. ER-2018-0366, issued August 15, 2018, at page 22.
[19] *Global Stipulation and Agreement*, page 2, provision 3(b).

has not allowed for the recovery of ARO's on the basis that, absent a legal obligation for these costs to be incurred, these future costs were speculative and not known and measureable. During settlement discussions, the parties received a better understanding of the costs in question. In fact, unlike an ARO which addresses future speculative costs, the costs in question had already been incurred and were related to asbestos and ash pond remediation associated with certain Empire generating units. Given this, the Signatories included a provision in the Non-Unanimous Stipulation which provides for the treatment of such costs as a regulatory asset, but not as an Asset Retirement Obligation. Given that these costs have been incurred, and are known and measureable, MECG asserts that they should be included in rates in the manner set forth in the Non-Unanimous Stipulation. (See Meyer Supplemental Surrebuttal, pages 2-4).

Respectfully submitted,

___/s/ David L. Woodsmall________

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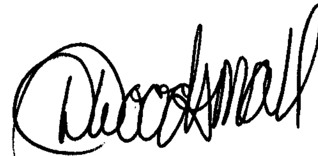
## CERTIFICATE OF SERVICE

I HEREBY CERTIFY that I have this day served the foregoing pleading by email, facsimile or First Class United States Mail to all parties by their attorneys of record as provided by the Secretary of the Commission.



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David L. Woodsmall

Dated: April 17, 2020