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July 31, 1992

via Federal Express

Mr. Brent Stewart
Executive Secretary
Public Service Commission
Truman Building
301 W. High St. - PO Box 360
Jefferson City, MO 65102

RE: In the Matter of the Commission's Rulemaking on Electric Utility Resource Planning - Case No. EX-92-299

Dear Mr. Stewart:

Enclosed for filing is the original and one (1) copy of Comments of the Missouri Industrial Energy Consumers in the above-styled case.

We appreciate your bringing this filing to the attention of the Commission.

Very truly yours,

Diana Schmidt

Diana M. Schmidt

DMS/lal
Enclosures

STL-53872.1

BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of the Commission's Rulemaking on Electric Utility Resource Planning	)))	Case No. EX-92-299

Comments of the Missouri Industrial Energy Consumers

Pursuant to the Commission's Notice of Public Hearing published in the *Missouri Register Volume* 17, *Number* 13, *July 1, 1992*, Ag Processing Inc., Anheuser-Busch Companies, Inc., Archer-Daniels Midland, Barnes Hospital, Chrysler Motors Corporation, Continental Cement Corporation, The Doe Run Company, Emerson Electric Company, Ford Motor Company, General Motors Corporation, Holnam, Inc., MEMC Electronic Materials, Inc., Mallinckrodt Speciality Chemicals Company, McDonnell Douglas Corporation, Mississippi Lime Company, Monsanto Company, Pea Ridge Iron Ore Company, River Cement Company, LaFarge Corporation, and Boehringer Ingelhiem Animal Health ("the Missouri Industrial Energy Consumers" or "MIEC") offer the following comments regarding the Commission's Proposed Rules on Electric Utility Resource Planning, 4 C.S.R. Chapter 22 ("the Proposed Rules"):

The MIEC supports the Commission's development of rules that require cost-effective resource planning by electric utilities. The MIEC commends the Commission's Staff ("the Staff") for its responsiveness to all interested parties in developing very thorough proposed rules. The proposed rules now before the Commission is the result of extensive discussions held in a series of workshops sponsored by the Staff. Partly as a result of these discussions, many important MIEC concerns have been addressed by the Staff and are reflected in the proposed rules. However, there are several areas of the proposed rule that are ambiguous and/or subvert

important purposes of the proposed rules. The MIEC sets forth below the areas where the rule could be improved.

1. The Rules Should Not Provide For Commission Approval or Pre-approval of Resource Plans

An issue of major importance debated at the workshops was whether the rules should provide for Commission approval[1] of resource plans submitted by the utilities, creating a presumption that utility actions taken pursuant to approved plans are prudent. The Staff indicated that the intent of its proposed rules is to provide for Commission review of resource plans only for the limited purpose of determining that utilities have complied with the planning process set forth in the rule. Union Electric and others support a presumption in favor of prudence of utility actions taken pursuant to resource plans that are approved by the Commission.

It is the position or the MIEC that all prudence issues should be considered at the time programs or facilities are presented for rate recovery. The MIEC is opposed to plan approval and any link to automatic cost recovery, and objects to the inclusion of any language calling for approval of specific utility plans and strategies. The Staff's general intent to present the Commission with a proposed rule that does not provide for pre-approval, and the MIEC's strong objection to pre-approval, are consistent with practical considerations and legal principles that should guide the Commission in considering resource planning rules.

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[1]Discussions focused on approval of plans, and also on pre-approval of resource additions contained in the plans leading to automatic cost recovery. The two topics are closely related, and for convenience these Comments will refer to both simply as pre-approval.

Practical considerations against pre-approval are that a formal approval process would necessarily be extended and complicated, would be costly to the parties, and would stretch the Staff's limited resources.

Further, general legal and regulatory principles militate against pre-approval. One of these general principles is that utilities must always retain responsibility and accountability to manage the use of their own system resources, whether demand or supply side. This Commission has observed that "regulation is intended to serve as a surrogate for competition." *Kansas City Power and Light*, 28 Mo. P.S.C. (N.S.) 228, Case Nos. EO-85-185 and EO-85-224 (April 23, 1986). Consistent with this principle, the Commission should to the greatest extent possible allow utilities broad discretion to manage their business affairs. The Commission has acknowledged that it is bound by this principle:

> Although the Commission has the authority to regulate [utilities], it does not have the 'authority to take over the general management of any utility'...'[t]he utility retains the lawful right to manage its own affairs and to conduct its business as it may choose, as long as it performs its legal duty, complies with lawful regulation and does no harm to the public welfare'...
>
> The Commission may review for prudency the management decisions in connection with [the procurement of gas] *as it does other management decisions, in the company's rate cases.*

In the matter of the investigation of developments in the transportation of natural gas and their relevance to the regulation of natural gas corporations in Missouri, 29 Mo. P.S.C. (N.S.) at 137, 143, Case. No. GO-85-264 (March 20, 1987)(emphasis added)(citations omitted) *quoting Laclede Gas Company v. P.S.C.*, 600 S.W.2d 177, 182 (Mo. App. 1969). *See also Laclede Gas Company*, 600 S.W.2d at 228 ("It is obvious that the P.S.C. has no authority to take over the general management of any utility.")

With the privilege to broadly manage its own affairs, comes the risk of, and the responsibility for, management decisions that prove to be imprudent or investments that do not prove to be used and useful to the public. An illustration of this principle is provided by the *Union Electric* case, where the Commission applied the used and useful standard to hold that ratepayers should not bear the cost of cancelled plant, even though that cost was prudently incurred:

> The utility makes the initial decision to build plant. Part of that calculation is the risk of cancellation. The utility seeks investment based upon an analysis of the profit and risk involved in the project. The reasonable investor examines the potential profit and potential risk and acts accordingly. Part of the potential profit to the investor is the reasonable certainty that a completed plant will be placed in rate base and both the investment and a return on investment will be recovered from ratepayers. Part of the potential risk is that the plant might not be completed and therefore all or a portion of the investment may not be recovered through rates.
>
> It can be seen from this analysis that the initial risk of of cancellation is borne by the investor stockholder. If this were not true and a stockholder could be assured a return of his investment whether the plant was cancelled or not, it would make the investment practically risk-free... stockholder and investors have received some compensation for their risk through the rate of return allowed by the Commission.

In the matter of Union Electric Company of St. Louis, Missouri for authority to file tariffs increasing rates for electric service provided to customers in the Missouri service area of the Company, 28 Mo. P.S.C. 189, 200-201. In the *Union Electric* case, the Commission noted that

utility risk is based, in part, on the used and useful principle codified in Mo. Rev. Stat. Section 393.135[2]:

> "[t]he property upon which a rate of return can be earned must be utilized by the utility to provide service to the utility's customers. That is, it must be "used and useful'. The used and useful concept presents a well-defined concept for determining what properties will be allowed into rate base. Once it has been decided that facilities are not necessary for the provision of service to customers, those facilities cannot be included in rate base."

The Commission went on to hold that the risk that property would not prove used and useful was to be borne by utility shareholders:

> "The increased costs of the [Callaway] project and the eventual cancellation of Callaway II were risks take into account by stockholders in investing in UE. Those risks were partially compensated by the rate of return authorized by the Commission."

Union Electric, 28 Mo. P.S.C. at 196.

As recognized in the *Union Electric* case, the Commission has a fundamental obligation to assure that ratepayers pay only for prudently incurred costs associated with utility programs and facilities that are used and useful in providing service. The initiation of a pre-approval process by this rulemaking would seriously compromise this obligation. Pre-approval of utility resource plans would radically alter the standards and procedures for regulatory review of utility investment decisions, to the detriment of ratepayers, because it would shift to ratepayers risks associated with investments such as the implementation of demand side management (DSM)

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[2]This statute provides: "Any charge made or demanded by an electrical corporation which is based on...cost associated with owning, operating, maintaining or financing any property before it is fully operational and used for service is unjust and unreasonable, and is prohibited."

programs and the construction of new electric generating facilities. Pre-approval would also shift to regulators the burden of decisions to initiate expenditures that were previously borne by utility management. Clearly, pre-approval would undermine the prudence and used and useful tests mandated by Missouri law for determining whether investments should be included in rate base.

All utility expenditures, including those associated with DSM measures, should be subject to prudence and to used and useful reviews. DSM measures may not be comparable to supply side resources because their operational characteristics have not yet been defined, and their reliability, availability, and persistence have not yet been demonstrated. Utilities must therefore carefully screen and select from the universe of DSM measures only those that are capable of achieving the intended results. The actual performance of DSM programs is highly variable and uncertain because of ratepayer discretion to modify energy use and purchasing behavior in response to price, technology, or lifestyle changes. Because of these characteristics of DSM programs, ratepayers should not be burdened with the risks of their implementation. The utility expertise places it in a far better position than the Commission to assess the potential of DSM measures. The utility should therefore account for these risks in the resource planning process, and bear the risk of the success or failure of DSM programs.

Under the presumption of prudence supported by utilities, ratepayers would bear the entire risk of construction cancellation, plant abandonment, or failed DSM programs -- risks that are incurred under Missouri's used and useful law, and that this Commission has held should properly be borne by utility shareholders. *See Union Electric*, 28 Mo. P.S.C. at 196. Such a presumption would create reliance on budget estimates to determine the prudence of subsequent,

actually incurred costs. Clearly, utilities' recommendation on pre-approval reflects a serious misunderstanding of the reasons for and the nature of regulatory investigations into the prudence of utility expenditures. As the Commission has noted, review of the prudence of management decisions should be reserved for the time of cost recovery-- in the utility's rate case. *Natural Gas Transportation Order*, 29 Mo. P.S.C. at 137. The regulatory framework presently in place in Missouri appropriately balances the risks to be borne by utility investors and ratepayers. The Commission should not allow utilities to use the resource planning process as an opportunity to fundamentally alter this regulatory framework and improperly shift business risks to ratepayers.

A. *The "Purpose" section introducing 4 CSR 240-22.010 implies pre-approval and should therefore be revised.*

Although the proposed rule submitted for publication does not appear to provide for plan approval, some language in the proposed rule creates uncertainty on this point. The "Purpose" portion of the proposed rule's section on Filing and Scheduling Requirements states:

> The purpose of the compliance review required by this chapter is to determine whether the utility's resource acquisition strategy meets the planning objectives stated in 4 CSR 240-22.010 (2) (A)-(C) ["Policy Objectives"].

Proposed Rule at 4 CSR 240-22.080 ("the objectionable language"). The MIEC suggests that this language simply be deleted from the proposed rules, because it detracts from the purported intent of the rule and is inconsistent with the proposed rule's statement that "[c]ompliance with these rules shall not be construed to result in commission approval of the utility's resource plans, resource acquisition strategies or investment decisions." Proposed Rule at 4 CSR 240-22.010 (1). The "purpose" language of the Filing and Scheduling Requirements section of the rule is

objectionable because it measures the utility's plan against the objectives of the rule, rather than assessing the plan merely for compliance with the rule's technical requirements.

Measuring the utility's plan against the policy objectives of the rule may be construed to result in pre-approval. The Policy Objectives section of the proposed rule states that a goal of the planning process is "to provide the public with energy services that are safe, reliable and efficient, at just and reasonable rates, in a manner that adequately serves the public interest." Proposed Rule at 4 CSR 240-22.010 (2). If, as mandated by the proposed rule, the Commission determined whether a utility plan "meets the planning objectives stated in 4 CSR 240-22.010 (2) (A)-(C)," that determination could be construed as tantamount to a determination that the utility's plan will result in the provision to the public of safe, reliable and efficient energy services at just and reasonable rates. *See* Proposed Rule at 4 CSR 240-22.010 (2). Because the objectionable language expands the Commission's review toward pre-approval, the MIEC proposes that it be deleted.

B. *To ensure that present Missouri law on utility rate proceedings is not altered by resource planning rules, a new paragraph should be added to the rule's Policy Objectives, 4 CSR 240-22.010.*

The MIEC proposes that the following language be added to the rule's Policy Objectives as 4 CSR 240-22.010 (3):

> (3) The determination of just and reasonable rates will continue to be made in accordance with the ratemaking procedures established by Missouri law, and this rule is not intended to alter or vary those procedures. Neither the compliance review process mandated by this rule, nor any cost information developed pursuant to this rule, will be given any extraordinary or predetermined weight in rate proceedings. To the extent that information developed pursuant to the resource planning process is offered in a rate proceeding, both the information and any

conclusions based on the information will be subject to review at that time under Missouri evidentiary law and procedure governing the commission.

Addition of this language to the rule's policy objectives will make clear that the current body of law with respect to rate proceedings will not be changed by the Commission's resource planning rules. As discussed previously, utilities may attempt to use this rule to modify the rate-making process to reduce their risk of not recovering expenditures. The strong possibility that utilities will attempt to use the rule in this manner in their efforts to enhance financial return for their shareholders must be directly addressed by the Commission in the rule. As the MIEC has pointed out, although the rule appears to provide merely for a compliance review of utility plans, utilities may attempt to use that review to avoid responsibility for resource planning decisions, and to shift investment risk to ratepayers. The MIEC's suggested paragraph safeguards against this danger, and helps to ensure that resource planning rules intended simply to facilitate effective utility planning to the benefit of all Missourians do not inadvertently tip the balance in favor of utilities and against ratepayers at the time of cost recovery.

In addition to protecting against utility misuse of the rule in an attempt to alter legally established ratemaking procedures, the MIEC's suggested paragraph ensures that rate structure and rate design are considered only where proper-- in rate cases. The Commission has embraced the principle of cost of service as an important element in determining just and reasonable rates. The planning process as structured by this rule, and the resulting utility plans, will impact utility cost. However, it does not follow that any cost analysis produced by this process will be appropriate for determining just and reasonable cost-based rates. It must be recognized that rate design concepts evolve over time. The MIEC's suggested paragraph

clarifies for parties to future rate proceedings that the rule is not intended to affect rate design, rate structure and evidentiary requirements. Any other approach could bind future Commissions by restricting the presentation and receipt of evidence, and by restricting the Commission's consideration of new approaches to rate design.

To preserve the power and flexibility of the Commission in rate proceedings, the MIEC's proposed paragraph (3) should be included in the rule's section on Policy Objectives, 4 CSR 240-22.010.

2. As a Policy Objective, Minimization of Rates is Equal in Importance to the Objective of Minimizing Utility Costs

The proposed rule should be revised so that the goal of "mitigation of rate increases" is equal in importance to "minimization of long-run utility costs" in the utility's planning process. *See* Proposed Rule at 4 CSR 240-22.010 (B) and (C). In the present draft, mitigation of rate increases is designated as a goal "secondary" in importance to minimizing the present value of revenue requirement (utility cost). The proposed rule's "primary/ secondary" sends a message to utilities to reduce costs above all, which they might do by simply selling less electricity or by reducing load without regard to the effectiveness or rate impact of such actions. This message could result in inefficiencies and increased rates to customers, because it would tend to inhibit economic development, would not recognize the efficiency and average cost reduction benefit associated with off-peak loads, and would lead to a disregard of the economies of scale associated with serving high-load customers. Hence, to set the proper goal for Missouri utilities, the Commission should adopt a policy that minimization of rates is of equal importance to minimization of utility costs in the planning process.

Pursuant to the Commission's Notice of Public Hearing published in the *Missouri Register Volume 17, Number 13, July 1, 1992*, Donald E. Johnstone of the firm of Drazen-Brubaker & Associates, Inc. will appear on behalf of the MIEC to answer questions of the commissioners and the hearing examiner relating to these comments at the public hearing to be held on September 10 and 11, 1992.

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