BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

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

REPLY POSTHEARING BRIEF

OF

THE MIDWEST ENERGY CONSUMERS GROUP

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COMES NOW the Midwest Energy Consumers' Group ("MECG"), pursuant to the Commission's April 28, 2020 *Order Further Modifying the Procedural Schedule*, and provides its Reply Brief in this matter. In this Brief, MECG responds to the arguments raised by Empire, Staff and Public Counsel on the issues of class cost of service / revenue allocation / rate design. In addition, MECG responds to arguments raised by Empire on the issue of return on equity. Finally, MECG addresses certain arguments raised by Public Counsel in opposition to the implementation of a WNR / SRLE mechanism. While MECG has not addressed the issues of cost of debt; capital structure, Tax Cut and Jobs Act Impact; and Asset Retirement Obligation, MECG maintains the positions set forth in its Initial Brief.

TABLE OF CONTENTS

I. INTRODUCTION 4

II. CLASS COST OF SERVICE ISSUES 6

A. RESPONSE TO EMPIRE 6

B. RESPONSE TO STAFF 10

C. CONCLUSION 14

III. REVENUE ALLOCATION 15

IV. LARGE POWER / GENERAL POWER / SC-P RATE DESIGN . . 21

V. RETURN ON EQUITY 23

VI. WNR / SRLE ADJUSTMENT MECHANISMS 25

I. INTRODUCTION

As MECG previously indicated, "MECG is a signatory to the Non-Unanimous Stipulation and Agreement. Pursuant to that agreement, the signatories all agree that no change to Empire's revenue requirement provides for safe and adequate service at just and reasonable rates."[1] It is important to recognize that the non-unanimous stipulation reaches the proposed $0 change in revenue requirement through several specific provisions that are recommended and supported by competent and substantial evidence. For instance, pursuant to Section 393.155.1, the stipulation recommends a phase in of all growth in rate base that occurred between the test year and the true-up in this case. Similarly, the balances of protected and unprotected accumulated deferred income taxes are frozen and will be treated in the next rate case. Additionally, while complying with Section 393.137, the stipulation provides for an amortization of the stub period tax benefits while preserving the majority of those benefits for treatment in the next rate case. MECG asserts that these provisions, in conjunction with all of the other provisions in the stipulation, make the zero revenue requirement change possible as well as a just and reasonable resolution to this case.

Nevertheless, given Public Counsel's opposition to the stipulation, the resolutions contained in that document simply become the joint positions of the parties. Therefore, the Commission is forced to make decisions on each and every one of the disputed issues in this case. For this reason, MECG has briefed several revenue requirement issues. MECG believes, however, that following its individual decisions on each of these issues, the Commission will ultimately reach the same conclusion that a zero revenue requirement change is just and reasonable.

[1] MECG Initial Brief, page 7.

II. CLASS COST OF SERVICE ISSUES

A. RESPONSE TO EMPIRE

As pertains to the class cost of service issues, Empire's position is largely consistent with that of MECG. Specifically, Empire and MECG both: (1) relied upon the A&E approach to allocating fixed production costs; (2) utilized the minimum size method for classifying distribution costs as either demand or customer related; (3) utilized a monthly demand approach to allocating demand related distribution costs; and (4) rejected Staff's energy allocator for allocating general plant costs in favor of allocators that more accurately reflect the manner in which these costs are incurred. With a few variations, Empire and MECG are largely in agreement on the proper approach to conducting a class cost of service issue.

Issue 2(z): How should production-related costs be allocated to each rate class?

Both MECG and Empire agree that the Commission should utilize the Average & Excess ("A&E") methodology for allocating fixed production plant costs.[2] As MECG demonstrated at pages 16-23 of its Initial Brief, the A&E approach has been adopted by all of the Missouri electric utilities as well as virtually every public utility commission in the nation.

That said, however, while Empire believes that the A&E methodology should rely upon monthly peaks for all 12 months (12 NCP method),[3] MECG asserts that the Commission should utilize 6 monthly peaks (6 NCP method), 3 each from the predominant winter and summer peaks.

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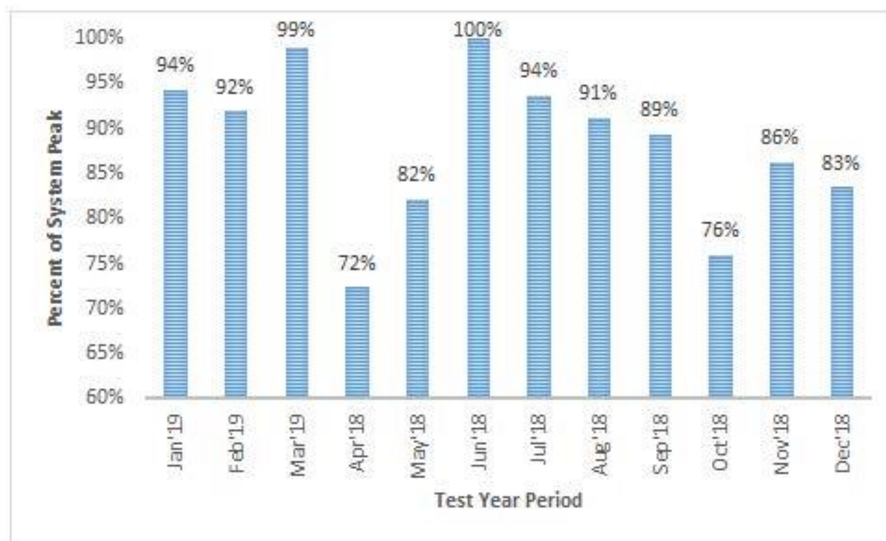
[2] *Id.* at page 20.
[3] *Id.*

As MECG points out, while the class peak demand is a necessary component of the A&E methodology, not all monthly peaks influence the utility's decision to add capacity. Rather, only the largest monthly peaks should be considered. Unlike other utilities which experience simply a summer peak, Empire typically experiences both a winter and a summer peak. Specifically, Empire experiences a winter peak during the months of January through March as well as a summer peak during the months of June through August.

Figure 4: Liberty-Empire Missouri's Monthly Peak Demands As a Percent of Annual Peak



Source: Exhibit 350, Maini Direct, page 17.

Given that Empire experiences two distinct peaks (January through March and June through August), covering a period of six individual months, MECG relied upon these 6 monthly peaks for calculating the excess component of the A&E allocator. As MECG points out:

> Empire constructs generation to meet system peak and I believe that the 6 monthly peaks within 10% of the highest peak would factor into this construction decision. The peaks in the remaining 6 months would be

> secondary to the highest six months and should not be used to calculate the A&E methodology.[4]

In contrast to MECG's assertion that only the highest 6 monthly peaks should be incorporated into the A&E calculation, Empire relied on all 12 monthly peaks.[5] Given this, Empire considers peaks in April and October which represent only 72% and 76% of the annual peak. Therefore, as MECG points out, Empire's approach "dampens cost causation by not recognizing that the primary cost driver for acquiring generation capacity are the highest demands, thereby resulting in an under allocation of costs to the cost causing weather sensitive loads."[6]

The fact that these other months are not critical to Empire's decision to add generation is best highlighted by the fact that Empire, in performing its Integrated Resource Plan, does not rely upon all 12 monthly peaks, but rather only considers two peaks - the highest winter and highest summer peaks.[7] Thus, when Empire decided to add 600 MWs of wind, it was for the purpose of meeting the annual peak. All other peaks would necessarily be subsumed within that annual peak. For this reason, MECG recommends that the Commission rely upon the 6NCP variation of the A&E methodology to allocate fixed production plant-related costs.

Issue 2(aa): How should plant accounts 364, 366 and 368 be classified?

On issue 2(aa), both Empire and MECG agree that distribution plant costs in accounts 364, 366 and 368 should be classified as either customer or demand related based upon the minimum system study.[8] In contrast, while Staff utilized the zero

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[4] Exhibit 351, Maini Rebuttal, page 7.
[5] In all other ways, Empire's A&E calculation mirrors that of MECG.
[6] Exhibit 351, Maini Rebuttal, page 7.
[7] *Id.*
[8] See, Empire Responsive Brief, page 30; MECG Initial Brief, pages 25-27.

intercept approach, it failed to support that methodology in either its Initial or Responsive briefs. Given this, the Commission should utilize the minimum size methodology.

Issue 2(bb): How should primary and secondary distribution plant costs be allocated to each rate class?

Still again, Empire and MECG both largely agree that a monthly peak demand methodology should be used to allocate primary and secondary distribution plant costs to the rate classes. That said, while Empire used 6 monthly peaks to allocate these costs (6 NCP),[9] MECG advocates on behalf of a single monthly peak (1 NCP).[10] As MECG points out, the use of multiple peaks to allocate costs that are incurred to meet each class' single largest peak simply dampens the cost causative factor that drives the sizing of the distribution system.[11]

Furthermore, as MECG further points out, Empire's use of 6 monthly peaks to allocate the demand-related portion of distribution costs represents a radical shift in its approach to allocating these costs. In previous cases, Empire agreed with MECG and allocated such costs based upon the single largest peak.[12] Furthermore, not only has Empire previously allocated such costs based upon a single largest peak, as recommended by MECG, Ameren also allocates the demand related portion of these distribution costs in this manner.[13]

Additionally, Empire's 6 NCP allocation approach contradicts the manner in which distribution costs are collected from demand-metered classes. Specifically, Empire collects its distribution costs from these classes by using a ratcheted facilities

[9] Empire Responsive Brief, page 21.
[10] Exhibit 351, Maini Rebuttal, page 10.
[11] MECG Initial Brief, page 29.
[12] Exhibit 351, Maini Rebuttal, pages 9-10.
[13] Exhibit 351, Maini Rebuttal, page 10.

demand charge.[14] The use of a ratcheted facilities demand charge means that Empire collects its distribution costs from these customers based upon the single largest peak that occurred in the previous 12 months. "[T]he primary reason that the facility demand is ratcheted in LP rates (i.e., based on the maximum customer demand over a twelve month period) is to recognize that the distribution facilities being used, are sized to accommodate the maximum demands, whenever they occur."[15] Recognizing that Empire collects the demand-related portion of distribution plant based upon a customer's single largest peak, it is logical that these costs should be allocated between classes in a similar manner. "Each class' single non-coincident peak demand is therefore a more reasonable indicator to reflect the cost causing characteristic of building the distribution-related infrastructure."[16]

Issue 2(cc): How should general plant facility costs be allocated to each rate class?

On the final class cost of service issue, Empire and MECG are in full agreement on the allocation of general plant costs. Specifically, Empire and MECG both utilize allocators that are logically related to the manner in which Empire incurs these general plant costs.[17] For instance,

> General Plant facilities are generally used by the Company employees. Accordingly the General Plant costs were allocated based on a composite of labor-related O&M expenses. The Company's approach is generally consistent with the allocation method for these costs described in the NARUC manual.[18]

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[14] *Id*. See also, Exhibit 355.
[15] *Id.*
[16] *Id.*
[17] Empire Responsive Brief, page 21; MECG Initial Brief, page 30 ("Empire allocated such costs on a rational basis that reflects the manner in which such costs are incurred.").
[18] *Id.* (citing to NARUC Electric Utility Cost Allocation Manual, page 105).

Similarly, Empire utilized an approach to allocating A&G costs that best reflects how those costs are actually incurred.

> Labor related A&G expenses (such as Accounts 920 through 926) are allocated based on a composite of labor-related O&M expenses, while Plant-related A&G expenses are allocated based on a composite Total Plant allocation. The Company's approach is generally consistent with the allocation method for these costs described in the NARUC manual.[19]

In contrast, Staff simply labeled such costs as "miscellaneous and unassignable" and allocated these costs on the basis of an energy allocator that is punitive to high load factor rate classes. Noticeably, in recent Empire rate cases, Staff used a more logical allocator. For instance, in Empire's last rate case, Staff allocated General Plant on the basis of the gross production, transmission and distribution plant allocator. Similarly, materials and supplies were not allocated in the last case based upon the energy allocator, but instead on the basis of net plant.[20] Again, like the other class cost of service issues, Staff failed to support its methodology in either its Initial or Responsive briefs. As such, the Commission should rely upon the methodology utilized by Empire and MECG.

B. RESPONSE TO STAFF

After receiving significant criticism from Empire and MECG in testimony and briefs, one would expect that Staff would be eager to defend its novel class cost of service study approach. While Staff provided a minimal defense of its Highest Hours fixed production cost allocator, it has failed to provide any defense of the methodology that it used to classify and allocate distribution costs and general plant (issues 2(aa); (bb); and (cc)). Rather, Staff simply suggested that it "does not believe that it is useful or necessary" to justify its methodologies. Therefore, while MECG will address briefly

[19] (citing to NARUC Electric Utility Cost Allocation Manual, pages 106-107).
[20] Exhibit 351, Maini Rebuttal, Schedule KM-2.

Staff's Highest Hours approach, there is nothing in either Staff's Initial or Responsive briefs on these other class cost of service issues for MECG to address.

Issue 2(z): How should production-related costs be allocated to each rate class?

As indicated, Empire and MECG, as well as every other Missouri electric utility, relies upon the A&E method for allocating fixed production plant costs to the various classes. In contrast, Staff utilizes the novel Highest Hours approach.

In their briefs and testimony, Empire and MECG both criticized Staff's approach. For instance, Empire pointed out that, not only is Staff's methodology novel, Staff did not even apply the Highest Hours approach in a manner consistent with the publication in which Staff found it.[21]

In its Initial Brief, page 23, MECG criticized Staff's approach because it represents the latest method in a litany of fixed production plant allocation approaches that Staff has utilized over the past decade.

> [I]t is apparent that Staff's Highest Hours approach is simply its production allocator *du jour*. Specifically, at the beginning of the last decade, Staff argued vehemently on behalf of the Peak & Average approach.[22] Shortly thereafter, Staff advocated for the Base / Intermediate / Peak approach for allocating fixed production costs.[23] Just last year, Staff again changed its approach to what it termed a "functionalized approach."[24] Now, Staff has again changed its approach to an allocator that it read about in a recent publication called the Highest Hour approach.[25]

[21] Exhibit 28, Lyons Rebuttal, page 22.
[22] See, Case No. ER-2010-0036, *Report and Order*, issued May 28, 2010, at pages 85-86.
[23] See, Case No. ER-2016-0285, *Report and Order*, issued May 3, 2017, at page 50.
[24] Exhibit 104, Staff Class Cost of Service Report, page 26.
[25] *Id.*

In response, Staff concedes this point. "This is a fact that Staff will concede."[26] Staff, however, excuses its inability to settle on an approach on the changing electric utility landscape.[27]

Staff fails to recognize that every time that it returns to the laboratory and develops a new methodology it introduces heightened levels of regulatory uncertainty for customers. Specifically, the existence of a residential subsidy and Commission action to address that residential subsidy may be tolerable in the <u>short run</u>. Industrial customers that rely upon a competitive electric rate may take some comfort in knowing that the subsidy will be addressed and rates will be made more competitive. For instance, in recent years the General Assembly has taken steps to address the competitiveness of industrial rates[28] and, while eliminating a portion of a regulatory subsidy, the Commission has expressly noted the importance of competitive industrial rates.[29]

That said, however, a residential subsidy that appears, disappears and then reappears is problematic and introduces regulatory uncertainty not only for the utility, but also for industrial customers. Staff's constantly changing approach, based simply on an approach that sounds appealing in a publication, may cause a previously existing residential subsidy to suddenly disappear or reappear. Furthermore, such an approach may result in volatility in class rates as the Commission addresses a residential subsidy and then suddenly, based simply upon Staff's methodology, an industrial subsidy. For an energy intensive industrial customer that spends hundreds of millions of dollars to build a facility in Missouri, this is an inexplicable risk.

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[26] Staff Responsive Brief, page 11.
[27] *Id.*
[28] See, Section 393.355.
[29] *Report and Order*, Case No. ER-2014-0351, issued June 24, 2015, page 18.

Not only does Staff admit that its approach to allocating fixed production costs has been a constantly changing target over the past decade, it also admits that no other jurisdiction has adopted its approach. While making such an admission, Staff deems this fact "not persuasive."[30]

Labeling such a fact unpersuasive demonstrates that Staff wrongly believes that it is working in a vacuum when it allocates costs and sets rates for a Missouri utility. Over the past decade, MECG and the Commission have worked diligently to try to change Staff's mindset. For instance, throughout several cases, Noranda Aluminum insisted that an uncompetitive Ameren rate made it impossible for it to compete nationally and internationally.[31] More recently, the Commission has also expressed concerns with the competitiveness of Empire rates.[32]

Despite these efforts, Staff still finds it "not persuasive" that the vast majority of public utility commissions have all adopted the Average & Excess approach. In the meantime, because Staff continues to adopt methodologies that are punitive to industrial customers, Missouri industrial rates are becoming increasing more uncompetitive both regionally and nationally. As MECG pointed out, of the 95 investor-owned electric utilities operating in 28 Midwest and Central states, Empire's industrial electric rate is 12th highest.[33]

The problem lies in the fact that when other states are all using the A&E allocator and Staff continues to propose methodologies that are punitive to industrial customers, Missouri's industrial rates will necessarily become more and more uncompetitive relative

[30] Staff Initial Brief, page 11.
[31] See, Case Nos. ER-2010-0036; EC-2014-0224; and ER-2014-0258
[32] See, *Report and Order*, Case No. ER-2014-0351, issued June 24, 2015, page 18.
[33] *Id.* at page 9 and Schedule KM-2.

to these other states. Therefore, while Staff may find such concerns to be "not persuasive", MECG hopes that the Commission will take a broader view and address the concerns with Staff's constantly changing methodology.

C. CONCLUSION

Given Staff's failure to support its methodologies, the Commission should utilize the methodologies utilized by MECG. Specifically, on issue 2(z), the Commission should the Average & Excess (6NCP) approach to allocating fixed production plant costs to the rate classes. On issue 2(aa), the Commission should utilize the minimum size method for classifying account 364, 366, and 368 distribution plant costs as either customer or demand related. On issue 2(bb), the Commission should utilize the single largest monthly peak (1NCP) method for allocating demand related distribution plant costs to the various customer classes. Finally, on issue 2(cc), the Commission should reject Staff's attempt to simply label these costs as "miscellaneous and unassignable" and use the punitive energy allocator for allocating these costs to the customer classes. Instead, the Commission should utilize Empire's logical approach that allocates these costs in a manner that closely related to how these costs are incurred.

III. REVENUE ALLOCATION

Although Staff's class cost of service approach is radically different from the approaches utilized by Empire and MECG, the conclusions reached are similar. As Staff admits, "[t]he three CCOS Studies submitted by Staff, Empire, and MECG in this matter, utilizing different allocation methodologies, still reach similar conclusions regarding the directions of the shifts between and among customer classes."[34]

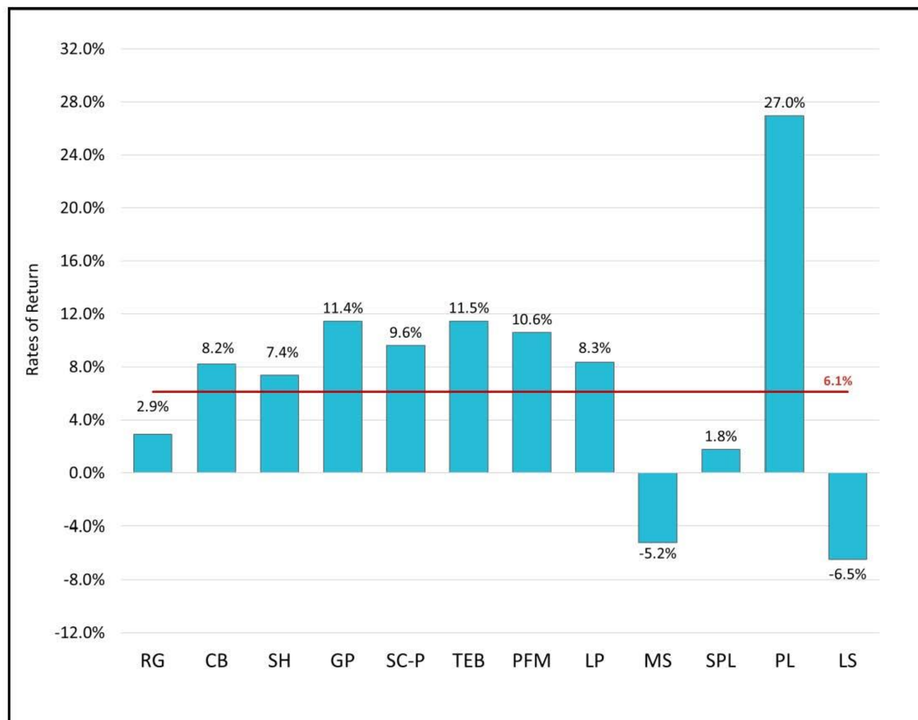
While differing on other class cost of service issues, MECG generally agrees with Staff on this point. That is, while the magnitude of the residential subsidy differs, each study definitely proves that a residential subsidy exists. For instance, while Empire was earning an overall rate of return of 6.11%, it was only earning 2.90%, 2.62% or 5.46% from the residential class under the Empire, MECG and Staff studies respectively.[35]

	Empire[36]	MECG[37]	Staff[38]
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 Svc.	-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%

[34] Staff Responsive Brief, pages 11-12.
[35] See, Table 1.
[36] Exhibit 350, 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, Exhibit 26, Lyons Rebuttal, page 10).
[37] Exhibit 350, Maini Direct, page 31.
[38] Exhibit 121, Lange Rebuttal, page 17.

As Empire states, "[a]n overall goal of rate design is to ensure that the various rates are fair and equitable in that they minimize inter-class subsidies. . . . This is accomplished by assigning a larger increase to classes that produce a lower ROR [rate of return] than the system ROR."[39] Given this, each of the parties that conducted studies recommended revenue neutral shifts to the residential and lighting classes with the commercial and industrial classes being beneficiaries of these shifts. "The Residential, Miscellaneous Service, Municipal Street Lighting, and Special Lighting rate classes require higher increases relative to the system average to achieve the system rate of return."[40] Empire's conclusion is best demonstrated graphically:

Figure 4: Class vs. Overall Rates of Return at Current Base Rates



Source: Exhibit 26, Lyons Direct, page 11. It should be noted that, after making corrections to firm up the load associated with the SC-P class, Empire pointed out that the rate of return for this class increased to 12.78%. (Exhibit 28, Lyons Rebuttal, page 34).

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[39] Empire Responsive Brief, pages 18-19.

[40] *Id.* at page 19.

Given the residential subsidy as well as Empire's increasingly uncompetitive industrial rates, MECG urges the Commission to take steps to reduce the residential subsidy. Specifically, MECG recommends that the Commission eliminate 25% of the residential subsidy.[41] Such a movement would lead to a 4.2% increase for the residential class and improve the competitiveness of all commercial and industrial classes.

	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 Svc.	+$1	7.5%
SPL – Municipal Ltg.	+$259	11.9%
PL – Private Ltg.	-$445	-10.9%
LS – Special Ltg.	+$77	58.8%

Source: Exhibit 350, Maini Direct, page 35.

Consistent with the Commission's finding from a previous Empire case, the recommended 4.2% shift is not punitive to the residential class. Empire has agreed, through the Non-Unanimous Stipulation, to no rate change. Therefore, MECG's proposed revenue neutral shift will only result in an overall residential increase of 4.2%. In its original filing Empire sought an increase for the residential class of 5.8%.[42] Therefore, even after the proposed revenue neutral shift, residential customers would still see a smaller rate increase than they were initially expecting from this case.

While Empire, Staff and MECG all agree that Empire's residential rates are heavily subsidized, Public Counsel disagrees. Instead, Public Counsel simply dismisses

[41] Exhibit 350, Maini Direct, page 35.
[42] Richard Direct, Schedule SDR-9.

all of the studies.[43] "Public Counsel cannot overemphasize enough how the number of estimated billings makes the parties' class cost-of-service studies so unreliable that they are of no use for designing class rates in this case."[44] Interestingly, while claiming that it cannot "overemphasize enough" the unreliability of the class cost of service studies, Public Counsel never bothered to explain in the least how the number of estimated bills has any effect on the aggregate data used in class cost of service studies.[45]

As Empire points out, however, a class cost of service study relies upon "aggregate data" and not the "individual customer data" that would be affected by estimated bills.

> We appreciate Staff's concerns regarding the data quality issues; however, the Company believes that the data quality issues do not result in a material impact on the results of the CCOS nor render them unreliable. The CCOS relies on aggregate customer data rather than individual customer data, and any concerns with individual customer data do not appear to impact the results of the CCOS.[46]

Staff appears to recognize this distinction between individual customer data, which is used for billing, and aggregate data which is used for class cost of service

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[43] Public Counsel schizophrenic approach to this issue is obvious. In rebuttal testimony, Public Counsel indicated that it was "tentatively aligned with Staff's initial recommendations." (Exhibit 208, Marke Rate Design Rebuttal, page 5). Now, after tentatively aligning itself with Staff's methodologies and positions, Public Counsel suggests that "Staff's 'highest hours' methodology is no more of an impractical academic theory than the 'average and excess' approach MECG advocates." (Public Counsel Responsive Brief, page 19). Public Counsel's position is simply that any methodologies that attempt to prove the existence of a residential subsidy is "impractical academic theory."

[44] Public Counsel Responsive Brief, page 17.

[45] Public Counsel points to the number of estimated bills as justification for many of the otherwise unsupportable positions that it takes in this case. As discussed, Public Counsel relies on an increase in estimated bills to justify its position that the Commission should not address the residential subsidy. In addition, Public Counsel suggests that the Commission make an arbitrary 60 basis point reduction in return on equity on the basis that Empire is not providing quality service. (See, Public Counsel Responsive Brief, page 43). Still again, Public Counsel relies on the increase in estimated bills as justification for the Commission rejecting the WNR / SRLE mechanism. (See, Public Counsel Responsive Brief, page 23).

[46] Exhibit 29, Lyons Surrebuttal, page 10.

studies. "[T]he total level of billing determinants for Staff's test period ***will not change based on the number of estimated bills***."[47]

Next, Public Counsel encourages the Commission to increase the residential subsidy to account for the effects of the Covid-19 pandemic.[48] Displaying a cavalier attitude to the fate of commercial and industrial customers, Public Counsel actually suggests that businesses can simply "shut down" to avoid electric rates.[49] In contrast, Public Counsel asserts that a "residential customer cannot 'shut down'."[50]

Unlike Public Counsel, which is clearly apathetic to the fate of commercial and industrial customers, MECG understands that the Covid pandemic will impact all customers. While all customers will be impacted, commercial and industrial customers have virtually no ability to avoid their electric bills. Since 90.9% of the residential revenue requirement is collected through energy charges, residential customers have a large degree of control over their electric bill simply by adjusting consumption or engaging in energy efficiency.[51] In contrast, since the large commercial and industrial classes have both a billing demand and facilities demand charge, these customers have much less control of their electric bill.[52] Therefore, the only option for these customers to avoid their electric bill is to "shut down" as Public Counsel invites.

In the final analysis, the Commission should continue to be cognizant of the significant residential subsidy that exists in Empire's rates. As it has done in each of the

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[47] Exhibit 165, Kliethermes Supplemental Rebuttal, page 3.
[48] Public Counsel Responsive Brief, page 21 ("[B]ecause of the unprecedented turmoil in the economy caused by the COVID-19 national emergency, . . . Public Counsel primarily recommends that, if the Commission finds that Empire's rates should be reduced, it is only the residential customer class' rates that should be reduced.").
[49] Public Counsel Responsive Brief, page 19.
[50] *Id.*
[51] See, MECG Responsive Brief, page 14 (citing to Exhibit 26, Lyons Direct, page 53).
[52] *Id.* at pages 14 and 15.

previous two Empire rate cases, the Commission should take steps to further address this residential subsidy. With this in mind, and as detailed earlier, MECG recommends that the Commission make a revenue neutral shift to eliminate 25% of the residential subsidy.

IV. LARGE POWER / GENERAL POWER / SC-P RATE DESIGN

In its Initial Brief MECG urged the Commission to address the intra-class subsidy existing in the LP, GP and SC-P rates by reducing the energy charges in these rate schedules.[53] Empire agrees. "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."[54]

In its Responsive Brief, Staff raises vague concerns in response to MECG's proposal. Specifically, Staff suggests that MECG's proposal could "potentially decreas[e] the rate paid by some customers for energy below the cost of obtaining that energy from the SPP integrated market."[55] Staff's vague concern is misplaced.

First, the evidence indicates that the load weighted and loss adjusted local marginal price for energy in the SPP integrated market is approximately $0.03 / kWh.[56] As reflected in Exhibit 355, the SC-P energy charges are all well above this threshold. In fact, even a 5% rate reduction for the SC-P class would allow SC-P energy charges to stay above Staff's suggested threshold.

ENERGY CHARGE, per kWh:	Summer Season	Winter Season
On-Peak Period	$ 0.05412	$ 0.03838
Shoulder Period	$ 0.04371	
Off-Peak Period	$ 0.03373	$ 0.03184

[53] MECG Initial Brief, pages 40-43.
[54] Exhibit 28, Lyons CCOS Rebuttal, pages 34-35 (emphasis added).
[55] Staff Initial Brief, page 14.
[56] Exhibit 351, Maini Rebuttal, page 24.

The energy charges for the LP and GP rate classes are even further above the market price of energy. Specifically, the energy charges for the GP class are all above 6.4 cents / kWh. Similarly, the energy charges for the LP class are all above 3.6 cents / kWh.[57] Given this, the Commission could cut the energy charges for the GP class in half and still be above Staff's arbitrary threshold.

Second, the evidence indicates that Empire will be immediately filing another rate case to reflect its capital investment in wind generation. "The addition of this wind generation [in the next case] will have the effect of increasing fixed costs and reducing variable costs. As a result, the demand charges should increase in that case."[58] Given that demand charges will likely increase in the next case to account for these increased fixed costs, MECG questions the logic of reducing demand charges in this case as Staff appears to propose.[59]

Third, the Commission should realize that MECG's proposal is not novel. In the last Ameren and KCPL / GMO rate cases, the Commission took steps to reduce the industrial class energy charges.[60]

Given all of these reasons, MECG suggests that Staff's concern is misplaced and that the Commission should adopt MECG's rate design proposal in which Empire has agreed.

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[57] Exhibit 355.
[58] *Id.*
[59] *Id.* at pages 24-25.
[60] For instance, in the recent Ameren case, the rate reduction for the industrial classes was implemented by reducing the energy charges. See, *Order Approving Stipulation and Agreements*, Case No. ER-2019-0335, issued March 18, 2020, Attachment Corrected Non-Unanimous Stipulation and Agreement Exhibit J. For KCPL and GMO, the recent rate reduction for the industrial classes was also implemented by reducing the industrial class energy charges. See, *Order Approving Stipulations and Agreement*, Case Nos. ER-2018-0145 / 0146, issued October 31, 2018, Attachment Stipulation 4, page 4 ("The LPS and LGS rate design will be an equal percentage decrease applied only to the energy blocks.").

<u>V. RETURN ON EQUITY</u>

In its Initial Brief, MECG pointed out that the Commission had routinely rejected Mr. Hevert's return on equity recommendation on the basis that it was "too high" as a result of using inflated growth rates that exceeded the long-term growth outlook for the economy.

> However, Hevert's estimation of an appropriate ROE is ***<u>too high</u>***. MIEC's witness, Michael Gorman explains that Mr. Hevert relied on long-term sustainable growth rate estimates in his DCF models that are higher than the growth outlook of the economy as a whole. As he explained, it is not rational to expect that utilities can grow faster than the demand of the economies they serve.[61]

Still again,

> Hevert's recommended return on equity is higher than the other recommendations in large part because he over-estimates future long-term growth in his various DCF analyses, making them ***<u>too high</u>*** to be reasonable estimates of long-term sustainable growth. When Hevert's long-term growth rates are adjusted to use more sustainable growth estimates based on published analyst's projections, his multi-stage DCF analysis produces a rate of return more in line with the estimates of LaConte and Gorman.[62]

In addition, MECG pointed out that Mr. Hevert's recommendation is higher than the 9.39% national average authorized return on equity.

> Mr. Hevert's recommended authorized ROE of 9.95% is too high. An authorized ROE of 9.95% is 56 basis points ("bps") higher than the 2019 national average authorized ROE of 9.39%. There were six fully litigated vertically integrated electric cases in the U.S.A. in 2019, of which five utilities were authorized 9.50% or less, and one was authorized 10.00%. Even the one case, involving DTE Electric Co., which was awarded a 10.00% authorized ROE was unique; the utility was authorized a capital structure with a far lower common equity ratio than the other five cases. It

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[61] Case No. ER-2012-0166, *Report and Order*, issued December 12, 2012, at pages 69-70. (emphasis added).
[62] Case No. ER-2011-0028, *Report and Order*, issued July 13, 2011, at page 23. (emphasis added).

> is therefore, implausible for Mr. Hevert to recommend such a high authorized ROE for Empire.[63]

Staff also criticized Empire's return on equity recommendation. "The Commission should reject the bloated and excessive ROE proposed by Company expert Robert Hevert."[64] Staff's criticism mirrors that leveled previously by the Commission and noticed by MECG.

> Mr. Hevert's recommendation is based upon flawed analyses in which the subjective components – the growth rate and the market risk premium – have been grossly inflated in order to produce unreasonably high results.[65]

Noticeably, despite the damning nature of this criticism, Empire never addressed these facts in its Responsive brief.[66] Rather, Empire limited its Responsive brief solely to responding to OPC's ROE recommendation. Given this, the Commission should adopt a 9.25% return on equity as recommended by Staff's witness Chari and supported by MECG.

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[63] Exhibit 108, Chari Rebuttal, pages 6-7. Specifically, while DTE was authorized a return on equity of 10.00%, that return was applied to a capital structure that consisted of only 37.94% common equity. In contrast, the other authorized returns for 2019 were applied to capital structures which included 49.46% to 53.00% common equity. (See, Exhibit 108, Chari Rebuttal, page 7, footnote 6).
[64] Staff Initial Brief, page 6.
[65] *Id.* at pages 6-7.
[66] See, Empire Responsive Brief, pages 7-13.

VI. WNR / SRLE ADJUSTMENT MECHANISMS

In its Responsive Brief, Public Counsel raises three arguments in opposition to the WNR / SRLE mechanism recommended in the non-unanimous Stipulation. First, Public Counsel again relies upon its red-herring argument (increase in estimated bills) in its opposition to the recommended mechanism. Second, Public Counsel argues that the proposed mechanism is not legally compliant. Finally, Public Counsel suggests that Empire is "actually overearning" and, therefore, the recommended mechanism is inappropriate.

As mentioned previously,[67] Public Counsel repeatedly points to the short-term increase in estimated bills as a red-herring justification for virtually all of its positions. For instance, Public Counsel relies on an increase in estimated bills to justify its position that the Commission should not address the residential subsidy.[68] Additionally, Public Counsel suggests that the Commission make an arbitrary 60 basis point reduction in return on equity on the basis that Empire is not providing quality service due to estimated bills.[69] Now here, Public Counsel relies on the increase in estimated bills as justification for the Commission rejecting the WNR / SRLE mechanism.[70]

The short-term increase in estimated bills does not justify rejection of the recommended SRLE mechanism. As mentioned in MECG's Initial Brief, 90.9% of

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[67] See, footnote 45.

[68] Public Counsel Responsive Brief, page 19 ("the Commission should understand that the parties' class cost-of-service studies are unreliable due to the significant amount of estimated billing data.").

[69] Public Counsel Responsive Brief, page 43 ("Empire's customer service in (sic) unacceptable and the Commission should find it so unacceptable that it explicitly reduces the return on equity the Commission would otherwise allow Empire by 60 basis points.").

[70] Public Counsel Responsive Brief, page 23 ("Empire's proposed weather normalization rider should be dismissed out-of-hand and not even be considered before Empire demonstrates with historical empirical data that it can provide consistently accurate bills to customers.").

Empire's recovery of the residential revenue requirement is through energy charges.[71] Given this, Empire's collection of the residential revenue requirement is susceptible to the usage variation caused by weather and conservation. Given this, the General Assembly enacted 386.266.3 to allow electric utilities to break the linkage between residential usage and the recovery of its revenue requirement. The justification for that mechanism (the collection of 90.9% of the residential revenue requirement through energy charges) still remains despite the short-term increase in estimated bills.

Second, Public Counsel's suggestion that the WNR / SRLE mechanism is not "legally compliant" is also misplaced.[72] Specifically, Public Counsel suggests that the proposed mechanism addresses more than simply weather and conservation as permitted by Section 386.266.3.[73] As mentioned in MECG's Initial Brief, the recommended SRLE mechanism attempts to isolate that portion of residential usage that it static from that portion that is susceptible to changes caused by weather and conservation.[74] For the residential class:

> Staff has reviewed Empire's cumulative frequency distribution data to determine the maximum level of usage per customer per month that is more or less constant all year. Usage of approximately 400 kWh per customer per month appears unlikely to be impacted by weather or conservation in the immediate future.[75]

The fact that 400 kWh of residential usage is constant and all other usage is subject to variations caused by weather and conservation was demonstrated graphically.

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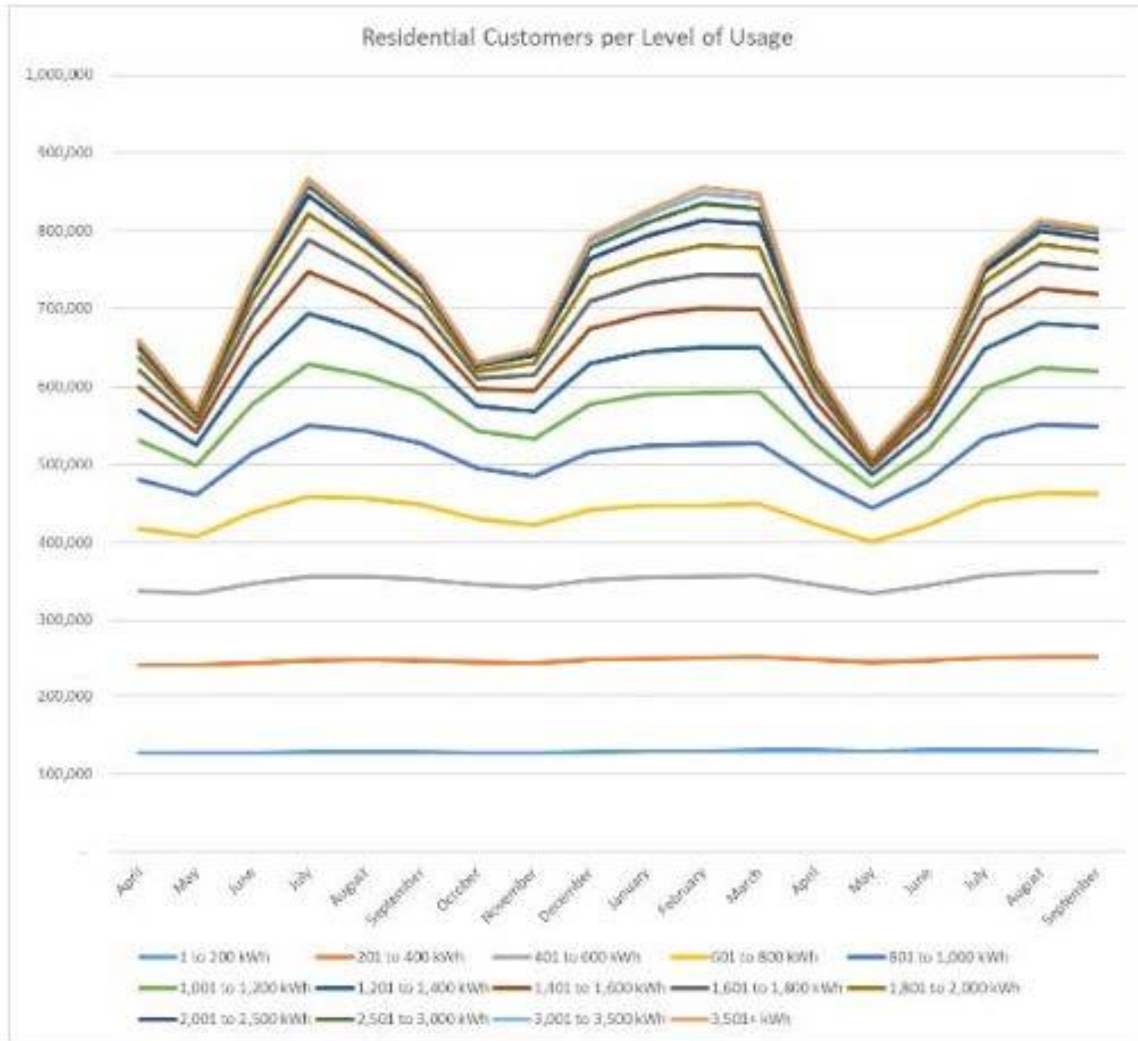
[71] Exhibit 26, Lyons Direct, page 53. Similarly, 89.0% of the Commercial and 92.0% of the Small Heating revenue requirements are collected through energy charges. *Id.*
[72] Public Counsel Responsive Brief, page 21.
[73] *Id.* at page 23.
[74] Exhibit 104, Staff Class Cost of Service Report, pages 3-13.
[75] *Id.* at page 4.



Source: Exhibit 104, Staff Class Cost of Service Report, page 4.

Given this, it is apparent that 400 kWh of usage is relatively constant for all residential customers throughout the year. Usage above that amount fluctuates as a result of weather and conservation. For this reason, the recommended SRLE mechanism addresses usage variation above 400 kWh for the residential class.[76] Staff conducted a similar analysis for the small commercial and small heating classes which showed that usage above 700 kWh

[76] See, Global Settlement, Appendix C, page 3.

was subject to variation caused by weather and conservation.[77] Clearly then, the recommended mechanism complies with Section 386.266.3.

Finally, Public Counsel suggests that the recommended SRLE mechanism is inappropriate because Empire is over-earning. In support of this position, Public Counsel directs the Commission's attention to Staff's "true-up accounting schedules."[78] In its true-up accounting schedules, Staff showed that Empire was over-earning by $6.1 million at a 9.25% return on equity.[79] Public Counsel's assertion that Empire is over-earning assumes that the Commission would agree with Staff on each and every issue. In contrast, Empire asserts that it is under-earning by $21.9 million using a 9.95% return on equity.[80] In reality, the Commission's decision would fall somewhere in between those two points and, perhaps, even justify a rate increase. Clearly then, Public Counsel's position that Empire is over-earning, based upon Staff's "true-up accounting schedules" is simply speculation as to where the Commission will ultimately fall.

Given all of these reasons, MECG urges the Commission to adopt the SRLE mechanism set forth in the non-unanimous stipulation.

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[77] Exhibit 104, Staff Class Cost of Service Report, pages 6-8.
[78] Public Counsel Responsive Brief, page 21.
[79] Exhibit 124, Staff True-Up Accounting Schedules, Accounting Schedule 1.
[80] Exhibit 7, Richard True-Up Direct, page 2.

Respectfully submitted,

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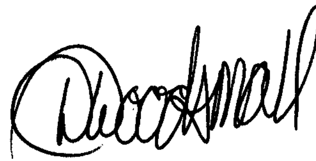
CERTIFICATE OF SERVICE

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.



David L. Woodsmall

Dated: May 18, 2020