BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of the Joint Application of Missouri-American Water Company, St. Louis County Water Company d/b/a Missouri-American Water Company and Jefferson City Water Works Company d/b/a Missouri-American Water Company for an accounting authority order relating to security costs.	)	**Case No. WO-2002-273**

STAFF'S REPLY BRIEF

COMES NOW the Staff of the Missouri Public Service Commission and, for its Reply Brief, states to the Missouri Public Service Commission as follows:

I. INTRODUCTION

The essence of the Company's argument in its Initial Brief amounts to a four-step analysis. The Company contends that: first, it had no choice but to respond to "The Events of September 11" in the way that it did; second, its expenditures were reasonable and prudent; third, the expenditures were extraordinary; and fourth, the Commission should therefore grant the requested accounting authority order.

At the outset, the Staff wants to make it very clear that it believes that it was entirely appropriate for the Company to re-evaluate its security systems in the light of the tragic events that occurred nearly one year ago. The Staff believes, just as the Company does, that it is very important – to the Company and its ratepayers alike – that the Company provide safe and adequate service. And it may well be that the Company had "no choice" but to re-evaluate its security procedures. It does not follow, however, that the Company had no choice but to respond in the way that it did.

In its attempt to justify this AAO request, the Company has tried to present the Commission with a false choice, which might be phrased as follows: "Should the Company have done what it did in response to The Events of September 11, or should the Company have done nothing?" But the choice that the Company had to make was not as simple as answering that question with a "yes" or "no." The Company's options might be likened to those of a driver who approaches an intersection, which is controlled by a stop sign. He is not restricted to the simple decision between going 90 miles per hour straight ahead or remaining stopped at the intersection, but can choose to go left, right, or straight ahead, and he can proceed at different speeds.

Company witness Edward J. Grubb testified that the Company "could not just simply do nothing,"[1] and that the Company argued in its Initial Brief that "there was no choice."[2] This improperly implies that the Company could either do exactly the things that it did, on exactly the timetable that it did them, or it could do nothing. The evidence in the case – and common sense – make it clear that the Company had many more options.

In this regard, this case is different from many previous applications for accounting authority orders, in which the company that sought an AAO had to expend money either in order to comply with a government mandate or to restore service after it was interrupted due to an "act of God" or other catastrophe. The significance of this difference lies in the fact that in those cases – the government mandate and the "act of God" cases – the regulated utility does in fact have "no choice" about what to do and "no choice" about the schedule on which the work is done. As a practical matter, in those cases, the decisions are truly made by others.

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[1] Tr. 305, line 18 – Tr. 306, line 16.
[2] Company's Initial Brief, p. 5.

In the present case, however, there were many different ways that the Company could have responded to the new threats that became apparent after The Events of September 11. This was not a case where there was an interruption of service, in which the Company had an *obligation* to restore the service *immediately*, and had no choice about how to go about it. And it was not a case where a government agency told the Company what it must do and when it must do it. Rather, government agencies warned of the possibility of future attacks, or "strongly recommended" what the Company should do,[3] or published a list of "best practices" for the Company to follow.[4] The ultimate decision as to what to do, exactly how much money to spend on improvements to security, when to do the work, and when (and if) to file for rate relief was in the hands of the Company, however.

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HC--------**[5] Company witness Grubb testified that the Company "had to" beef up its security, but he acknowledged that the Company made a "decision" to do so. He said the Company had to take the "necessary steps," but *the Company decided* what the "necessary steps" were.[6]

To repeat, the Staff does not contend that the Company should have or could have "done nothing." But the Company did have a choice about exactly what to do and when to do it. Furthermore, the Company was able to spread the actual expenditures out over a period of ** HC---------------- ** If the expenditures were of such a magnitude that they caused the Company's rate of return to fall below an acceptable level, there was ample opportunity to file a rate case, in which all relevant factors affecting the Company's return could be considered.

[3] See, *e.g.*, Tr. 144, lines 22-24 and Tr. 188, lines 11-18.
[4] See, *e.g.*, Tr. 146, lines 9-14.
[5] Tr. 178, line 2 – Tr. 180, line 6.
[6] Tr. 306, lines 2-23.

The second contention in the Company's four-step analysis, as it is summarized on page 1 hereof, is that its expenditures for security improvements were "reasonable and prudent."[7] The Staff does not concede the point, but it does not here dispute it, either, and takes no position of this issue, for the question of prudence is simply not relevant to this proceeding. The determination of whether the Company's expenditures were prudent will be left for the next rate case.

The Staff disagrees with the third contention of the Company's four-step analysis, as it is summarized on page 1 hereof. The Company's expenditures should not be classified as extraordinary, for reasons set forth in more detail below, at pages 15-17.

In addition, the Staff urges the Commission to apply four new criteria in determining whether an AAO should be granted, instead of relying strictly upon the single issue of whether the expenditures that the Company has incurred are "extraordinary, unusual, unique and nonrecurring." The four new criteria would require that: (1) the company show that the costs it has incurred are both extraordinary and material; (2) the company's current rates must be inadequate to cover the event; (3) the company's expenditures must result from either an extraordinary capital addition whose costs the company cannot recover through a rate case, or from an extraordinary event that is beyond the control of the utility's management; and (4) there must be a sufficient reason why the company could not file a rate case to recover the costs resulting from the extraordinary event. These new criteria should be applied in this case, and in future cases on a case-by-case adjudication. Adoption of these four new criteria would establish an ascertainable standard, which would enable utilities to know how their application would be judged and would prevent the filing of cases that have little merit and where there is little chance of approval.

[7] Company's Initial Brief, p. 3.

The Staff also disagrees with the final contention of the Company's four-step analysis, as it is summarized on page 1 hereof, that an AAO should be granted in this case. The Company's expenditures in this case do not satisfy the four new criteria that the Staff is asking the Commission to adopt and apply in this case. And even if the Commission does not apply these four new criteria, the Commission should deny the Company's request for an AAO, because it does not meet the Commission's existing criteria, either. This is because The Events of September 11, though extraordinary by themselves, did not have an extraordinary effect on the Company. The Company was not compelled to take a specific immediate action in response to The Events of September 11, but was able to determine what steps to take and when to take them, and could have sought recovery of the expenses it incurred in a rate case, in which all relevant factors would have been considered. If it had done so, there would have been no reason to seek an accounting authority order.

II. ARGUMENT

Issue No. 1: The Commission Should Adopt the Staff's Four Criteria for Evaluating the Company's Application for an AAO.

In the Matter of the Application of Missouri Public Service, 1 M.P.S.C. 3d 200 ("the Sibley Case") is generally regarded as the fount of Commission decision-making in establishing the standard to be applied in determining whether an accounting authority order should be granted. The Company refers to it as the "origin" of the statement that deferral of expenses is appropriate "when events occur during a period which are extraordinary, unusual, unique and not recurring."[8] In the Sibley Case, the Commission cited, and quoted from, the Uniform System of

[8] Company's Initial Brief, p. 12.

Accounts ("USOA") adopted by the Federal Energy Regulatory Commission's predecessor. The role of the USOA in setting the standard for the Commission merits further discussion.

Prior to the Sibley Case, the Commission had, by rule, prescribed the FERC's version of the USOA for use by electric utilities.[9] As the Sibley Case was an electric case, the Commission referred to the FERC version of the USOA. In that case, the Commission set out at length the electric USOA's description of "extraordinary items."[10] After some discussion, the Commission stated that costs might be deferred from one accounting period to another "when events occur during a period which are extraordinary, unusual and unique, and not recurring."[11]

It is interesting to note that, although the USOA's description of "extraordinary items" did talk about "recurring" factors, it did not anywhere use the words "unique" or "unusual." Those words were provided by the Commission itself, not by the USOA. Furthermore, the Commission did not state that it was attempting to follow and apply the USOA's definition of "extraordinary items," and it did not indicate that this definition was binding on the Commission. Indeed, it seems beyond dispute that the USOA's definition is *not* binding on the Commission, for Commission Rule 4 CSR 240-20.030 (4) provides, in part:

> In prescribing this system of accounts, the commission does not commit itself to the approval or acceptance of any item set out in any account for the purpose of fixing rates or in determining other matters before the commission.

It would therefore appear that in the Sibley Case the Commission referred to the USOA provision for guidance, rather than as an absolute rule. The Commission also said in the Sibley Case that the effect of obtaining an AAO is to remove the issue of "whether the item is extraordinary from the next rate case."[12]

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[9] See Rule 4 CSR 240-20.030.
[10] Sibley Case, at p. 203.
[11] Sibley Case, at p. 205.
[12] Sibley Case, at pp. 203-4.

Of course, the instant case is not an electric case, but a water case, so the FERC's USOA may not be directly applicable, in any event. The more germane standard is the USOA for water utilities, which was adopted by the National Association of Regulatory Utility Commissioners ("NARUC"), and which is prescribed by Commission Rule 4 CSR 240-50.030. The provisions of the NARUC USOA for water utilities differ somewhat from the provisions of the FERC's USOA for electric utilities. But the Commission's rules again make clear that the Commission will not be bound by the provisions of the USOA. Rule 4 CSR 240-50.030 (4) reads as follows:

> In prescribing these systems of accounts the commission does not commit itself to the approval or acceptance of any item set out in any account for the purpose of fixing rates or in determining other matters before the commission.

Clearly, the Commission looks to the USOAs for guidance, but not as an absolute rule.

The standard that the Commission has most often applied, in ruling on applications for AAOs, is to ask whether the company's expenditures were "extraordinary, unusual, unique and nonrecurring." There is, no doubt, some redundancy in this terminology. In fact, any event that is *truly* "unique" is probably also "extraordinary, unusual and nonrecurring." The latter three terms may therefore add little, and provide little guidance to a utility that is contemplating filing an application for an AAO. The Company praises this imprecise standard as "flexible."[13]

Furthermore, although the phrase "extraordinary, unusual, unique and nonrecurring" is the one that is most often used to describe the standard for granting an AAO, the Commission has not consistently applied it. In *St. Joseph Light & Power Company,* Case No. EO-2000-845, for example, the Commission decided that going beyond the question of whether a cost is "extraordinary" was required, stating:

> However, *the simple fact that an expense is extraordinary and nonrecurring is not enough* to justify the deferral of that expense. Implicit in the Commission's previous

[13] Company's Initial Brief, p. 7.

> orders regarding requests for AAOs is a requirement that there must be some reason why the expense to be deferred could not be immediately included for recovery in a rate case.

(Emphasis supplied.)

The Staff believes that the Commission and the regulated utilities would both benefit from having a more clear and ascertainable standard. The Staff has proposed such a standard in this case, and urges the Commission to adopt it and apply it in this case and in future cases. The Commission is not bound by the provisions of the USOA, and it is not bound by the decision in the Sibley Case or in other prior cases, but it may look to them for guidance in establishing a new standard.

The electric USOA offers good guidance on the issue of what costs are "material," by providing that: "To be considered as extraordinary under the above guidelines, an item should be more than approximately 5 percent of income, computed before extraordinary items."[14] This is not binding on the Commission, because neither the electric USOA nor the water USOA is binding on the Commission; but it is a useful guideline. The Staff recommends that the Commission adopt this guideline as one of the criteria for deciding AAO cases. The Staff does not, however, suggest that the Commission adopt an ironclad five percent minimum, as the Company suggested in its Initial Brief.[15] Staff witness Fischer testified that the Commission should have some flexibility to go below the five percent minimum in determining whether Proposed Criterion No. 1 is satisfied.[16] The Commission should not reject this proposed standard because of its claimed lack of flexibility.

The Staff knows no reason why the standard for granting an AAO to a water or sewer corporation should be different from the standard for granting an AAO to a gas or electric

[14] Tr. 426, line 7 – Tr. 428, line 2,
[15] See Company's Initial Brief, p. 7, where the Company argues: "It is not good policy for the Commission to eliminate its flexibility in exchange for a rule where 5.00% qualifies for an AAO, but 4.9999% does not.

corporation and the Staff urges the Commission to apply Staff's proposed four criteria to gas, electric, water and sewer utilities alike.

A. The Staff's Proposed Criteria Do Not Constitute a Rulemaking

The Company contends that adoption of the Staff's proposed criteria in this case for general application would constitute an unlawful change in statewide Commission policy, citing § 536.010 (4), RSMo 2000, which defines "rule" as an "agency statement of general applicability that implements, interprets, or prescribes law or policy, or that describes the organization, procedure or practice requirements of any agency."[17]

The Company then argues that the "Staff has announced a *change* in statewide policy and statement of general applicability."[18] Although the Staff is flattered by the influence that the Company has imputed to it, it feels constrained to point out that the Staff is not an *agency*, and is powerless to "announce a change in statewide policy." What the Staff has done, instead, is to announce that it will advocate, on a case-by-case basis, that the Commission apply the Staff's four proposed criteria to the case then at hand. The distinction between an adjudication, as in this case, and a rulemaking is critical. The Missouri Court of Appeals drew this distinction as follows:

> In contrast to a rule, an adjudication is "[a]n agency decision which acts on a specific set of accrued facts and concludes only on them." *Missourians for Separation of Church and State v. Robertson,* 592 S.W.2d 825, 841 (Mo. App. 1979). An adjudication results from a "contested case," which the APA defines as a "proceeding before an agency in which legal rights, duties or privileges of specific parties are required by law to be determined after hearing." § 536.010 (2).[19]

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[16] Tr. 428, line 3 – Tr. 429, line 21.
[17] Company's Initial Brief, p. 9.
[18] Company's Initial Brief, p. 10. (Emphasis in original).
[19] *Branson R-IV Sch. Dist. v. Labor & Indus. RelationsComm'n,* 888 S.W.2d 717, 720-721 (Mo. App. S.D. 1994).

In this case, the Staff is advocating that the Commission use specific criteria when evaluating the Company's AAO application. The Commission will continue to review each case on its own merits. The Staff has not alleged that it would be appropriate to apply these four criteria to every AAO request that may be filed in the future, regardless of the specific circumstances surrounding the AAO application. For example, AAOs issued under the guidelines of the recent amendment to the Cold Weather Rule or other Commission mandates should not be assessed under these four criteria.[20]

The Staff believes that the Commission should continue to apply case-specific standards to AAO applications, but should use the four criteria the Staff has proposed as guidance. Changing or modifying the criteria that the Commission uses when determining whether to grant an AAO is not prohibited, and the criteria should reflect the best applicable standards for the industry and the particular case. In support of this position, the Staff points out that prior decisions of the Commission have no *stare decisis* effect.

The Commission has both the discretion and the authority to modify or discard any test that it has applied in the past to, among other things, refine or improve it, address a new factual situation, or respond to changed circumstances or changed views of the commissioners. The Staff submits that the only circumstance in which it would be inappropriate for the Commission to use the proposed criteria would be when the criteria are beyond application to the facts in the case. The Staff does not suggest that the Commission should arbitrarily or capriciously engage in a sudden change in its approach to the grant of AAOs.

The Company's argument that the Staff's proposed criteria constitute a rulemaking is without merit, and should be rejected.

[20] Tr. 417, line 3 – Tr. 418, line 7.

B. (1) – Staff's Proposed Criterion No. 1: The costs that the Company seeks to defer do not exceed 5% of the Company's income and therefore are not material.

In its Initial Brief, the Company makes the entirely unfounded claim that "the Staff has indicated that it will change the test to ensure that a utility cannot achieve the required threshold."[21]

The Company cites Staff witness Janis E. Fischer's testimony at pages 412 and 413 of the transcript in support of this claim. Interestingly, in its Initial Brief on proposed Criterion No. 1, the Staff also cited the same passage from Ms. Fischer's testimony, but for a different purpose. It is therefore worthwhile to set forth that testimony verbatim, instead of paraphrasing it, so the Commission can see what Ms. Fischer actually said. Ms. Fischer testified as follows:

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Notably, Ms. Fischer did not testify that the Staff would "change the test" to achieve a different result, as the Company charged in its Initial Brief.[22] Nor did she testify "that had she known the Company would meet the materiality test the way she calculated it the first time, she

[21] Company's Initial Brief, p. 11.

would have changed the method," as the Company also charged.[23] The Company's paraphrase of Ms. Fischer's testimony is dead wrong.

It seems obvious from the above excerpt that when Ms. Fischer did her first calculation she did a quick analysis and found that, even after giving the Company the benefit of the doubt on some of her assumptions, the "total net deferral" was only ** HC--------**[24] Because this liberally calculated amount was less than the 5% threshold, there was no need to more carefully examine the data; the Company simply did not satisfy Proposed Criterion No. 1.

But when the Company provided her with updated data, her quick calculation produced a "total net deferral" of ** HC-----------** an amount which exceeded the 5% threshold.[25] It then became necessary to more carefully scrutinize the data. In doing so, she did not "change the test." She merely conducted the test more carefully and determined that some of the "ongoing expenses" should not have been included in the "total net deferral." When those expenses were eliminated, the Company did not satisfy Proposed Criterion No. 1.

As Staff stated in its Initial Brief, ongoing costs associated with capital additions related to security concerns and other security expenses that will be incurred on an ongoing basis should not be included in a deferral under any circumstances, because both categories of costs can be handled through the normal rate case process on a timely basis.[26]

B. (2) -- Staff's Proposed Criterion No. 2: Staff does not contend that the Company's current rates are adequate to cover the event.

Information available to the Staff, through surveillance reports and otherwise, is simply not sufficient to enable the Staff to conclude that the Company's current rates are adequate to

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22 Company's Initial Brief, p. 17.
23 *Id.*
24 Fischer Rebuttal, Ex. 6, HC Schedule JEF -3, p. 1; Tr. 413, lines 1-6.
25 Ex. 14 HC; Tr. 412, lines 21-25.
26 Staff's Initial Brief, p. 14; see also Staff's Initial Brief, p. 15.

cover the costs it has incurred in responding to The Events of September 11.[27] Accordingly, the Staff does not contend that the Company has failed to satisfy Staff's Proposed Criterion No. 2. Under the Staff's proposed criteria, however, the Company must still show that it satisfies each of the other three criteria before it would be appropriate for the Commission to grant an AAO.

B. (3) -- Staff's Proposed Criterion No. 3 (a): There are no unique conditions that prevent the Company from recovering these costs through a rate case filing.

The Company argues that the costs it has incurred in response to The Events of September 11 resulted from "actually a series of projects that are impossible to time with a rate case filing."[28]

This claim is totally untrue, as the Staff pointed out in its Initial Brief.[29] The Company presented testimony that it expected to complete this "series of projects" by the end of August 2002. There is no evidence that it was difficult for the Company to determine when this series of projects might end. And there is no reason to suspect that predicting when the projects would be complete was any more difficult than it would be for the Company to predict when the construction of any other major capital addition, such as a water treatment plant, would be complete. A rate case filing that incorporated the period ending in August 2002 in the test year, update, or true-up period would have allowed timely recovery of these costs, with the only loss to the Company being the normal operation of regulatory lag for a short period of time.

B. (3) -- Staff's Proposed Criterion No. 3 (b): The expenses did not result from an extraordinary event that is beyond the control of the Company's management.

The Company argues that: "the events and the resulting consequences of September 11, 2001, which drove these projects, are certainly "beyond the control of the utility's

[27] That does not mean, however, that the Staff believes the current rates are inadequate.
[28] Company's Initial Brief, p. 19.
[29] Staff's Initial Brief, p. 6.

management."[30] In making this argument, the Company continues to confuse The Events of September 11, and the reaction to them.

The Events of September 11 – *i.e.,* the terrorist attacks, themselves – were clearly "beyond the control of the utility's management." But the decisions about whether and how to respond to the perceived new threat, at what expense, and whether, when and how to seek recovery of the costs were peculiarly within the control of the Company. If the Company had, as it claims, "no choice," it is hard to imagine why no other utility in the State of Missouri was forced to seek recovery of security-related expenses through an accounting authority order.

B. (4) -- Staff's Proposed Criterion No. 4: There is not a sufficient reason why MAWC cannot recover the costs resulting from these expenditures through the normal rate case process.

In its Initial Brief, MAWC states, without supporting argument, that the Staff's Proposed Criterion No. 4 is new.[31] That is, however, not the case. In *In Re St. Joseph Light and Power Company,* Case No. EO-2000-845, the Commission applied virtually the very same test that the Staff now proposes that the Commission should adopt as Criterion No. 4.

In the *St. Joseph Light and Power Company* case, the Commission said: "Implicit in the Commission's previous orders regarding requests for AAOs is a requirement that there must be some reason why the expense to be deferred could not be immediately included for recovery in a rate case."

The Staff's formulation of this test is found in the first sentence of the proposed Criterion No. 4, reading as follows: "There must be a sufficient reason why the Company could not file a rate case to recover the costs resulting from the extraordinary event."

[30] Company's Initial Brief, p. 19.
[31] Company's Initial Brief, p. 15.

The Staff contends that the Commission should apply this standard strictly. That is, if there is not a good reason why a rate case could not have been filed, the company's request for an AAO should be summarily rejected.

On the other hand (or "alternatively," as stated in the Staff's proposed Criterion No. 4), if the Commission decides *not* to apply the foregoing standard strictly, and grants an AAO even when there is not a good reason why a rate case could not have been filed instead, the Commission should order that a rate case be filed within 90 days, or it should order an immediate amortization.

The Company's acceptance of the immediate amortization option in this case makes the 90-day filing requirement moot, but not the main criterion – that is, the one stated in the *St. Joseph Light and Power Company* case. There is not a good reason why MAWC could not file a rate case to recover its security costs, so this AAO should be denied.

In its Initial Brief, the Company said: "[T]he Company has provided the reasons it cannot recover these expenditures though (*sic*) the normal rate case process … Whether the expenses are found in a test year or not, none of the amounts that MAWC seeks to defer will be recovered in a future rate case."[32] This amounts to a statement that the Company filed the application for an AAO in order to avoid the effects of regulatory lag, because the Company does not want to file its next rate case until June 2003.

But a desire to avoid the effects of regulatory lag is not a sufficient reason for issuing an accounting authority order. As the Commission stated in *In Re Missouri Public Service Co.*:

> Avoidance of rate case expense is a beneficial goal since it reduces the cost of doing business, but delaying rate cases just to avoid rate case expense should not be used as an excuse to defer costs which are attributable to normal operations of a company. The benefit gained will not necessarily outweigh the increased rates caused by the deferral.

[32] Company's Initial Brief, p. 23.

> Lessening the effect of regulatory lag by deferring costs is beneficial to a company but not particularly beneficial to ratepayers. Companies do not propose to defer profits to subsequent rate cases to lessen the effects of regulatory lag, but insist it is a benefit to defer costs. Regulatory lag is a part of the regulatory process and can be a benefit as well as a detriment. Lessening regulatory lag by deferring costs is not a reasonable goal unless the costs are associated with an extraordinary event.[33]

C. Even if the Commission does not Adopt the Staff's Proposed Criteria, it Should Still not Grant an AAO, Because the Costs the Company has Incurred are not "Extraordinary, Unusual, Unique and Nonrecurring."

The Company correctly notes, at pages 24-26 of its Initial Brief, that the American public is much more concerned about the possibility of a terrorist attack of some sort now than it was prior to The Events of September 11. Government entities and others have properly encouraged Americans in general, and the owners of utility plants in particular, to take a new look at security and to beef up their security systems if necessary. The Staff supports the Company's efforts to re-evaluate the security of its plant.

The events that gave rise to the Company's expenditures in this case, however, are different in kind from the events for which the Commission has typically granted accounting authority orders in the past. In this case, there was no damage to the Company's plant that required repair. There was no interruption of service to the Company's customers. And there has been no government mandate requiring the Company to take any specific action.

The Company has always had an obligation to secure its facilities, and that obligation continues today. Security costs are a typical, ongoing cost of doing business for the Company and other utilities, as well as other industries.

The Events of September 11 involved a suicide attack by commercial airplane. The Company makes no pretense that its recent expenditures will provide any protection against a similar attack in the future. The Company's beefed-up security measures were designed, instead,

[33] 1 M.P.S.C. 3d 200, 207.

primarily to protect against the poisoning of the public water supply, an event that, to the best of Staff's knowledge, has never occurred in the United States.

It therefore appears that the Company's expenditures were not required by any government mandate, or to restore service to customers, or even to protect against another attack similar to The Events of September 11, but rather to protect against the possibility of a different kind of attack that has never been experienced. The Company did not make its expenditures because it had to do so, but because of what it perceives as a new kind of risk.

The Staff applauds the Company's vigilance, but submits that a change in the Company's perception of a risk does not rise to the level of an "extraordinary, unusual, unique and nonrecurring" event for which an accounting authority order is justified.

The Company also points out, at page 27 of its Initial Brief, that the Commission has in the past issued AAOs for gas safety costs and for costs associated with FAS 106 / OPEBs.

The AAOs for the gas safety costs were granted because the Commission ordered Missouri gas utilities to replace all service lines and mains over a specified period of time. The Commission granted these AAOs because it mandated the safety plant replacement program. There is no comparable mandate in the present case.

The AAOs that were granted in connection with FAS 106 / OPEBs are also not analogous to MAWC's security costs. Those AAOs were intended to allow deferrals of the excess of FAS 106 expense amounts over the traditional PAYGO (actual cash payment to retirees) treatment. These AAOs reconciled the difference between the accounting treatment for OPEBs required for financial accounting purposes and the accounting treatment then prescribed by the Commission for regulatory accounting purposes. Due to changes in financial reporting standards and

Missouri law, those AAOs were never actually used by the utilities that received them to defer FAS 106 costs.

<u>Issue No. 2:</u> The Commission Should not Grant the Company an AAO to Defer Recognition of the Costs that it has Incurred and Attributed to The Events of September 11.

For reasons that are adequately set forth in the Staff's Initial Brief, and in other portions of this Reply Brief, the Commission should not grant the accounting authority order that the Company has requested.

<u>Issue No. 3. A:</u> If the Commission does Grant an AAO, as the Company Requests, it Should Order the Company to Begin Amortization of the Deferred Amounts Immediately, but Should not Make a Decision about the Length of the Amortization Period.

The Staff agrees with the Company that if the Commission does grant an accounting authority order, it should direct the Company to begin to amortize the deferred amounts immediately.

The Commission should not, however, make a ratemaking decision about the length of the amortization period, which should properly be decided in a rate case. If the Commission does establish an amortization period for accounting / bookkeeping purposes, the Staff recommends that it be only 10 years, instead of 20 years as the Company has requested. In addition to the reasons previously mentioned in Staff's Initial Brief, the shorter amortization period would provide an additional incentive to the Company to more promptly file a new rate case.

<u>Issue No. 3. B:</u> If the Commission does Grant an AAO, it Should not Make any Indication Regarding Future Ratemaking Treatment of the Deferred Expenditures in the Commission's Order.

The Staff's position on this issue is now the same as the Company's position on this issue.

III. CONCLUSION

The Commission should adopt the new four-part test that the Staff has proposed for judging applications for AAOs, and should reject the Company's Application in this case, because it does not satisfy the requirements of this new test. The Events of September 11 did not have an extraordinary effect on MAWC, and the company should not be authorized to defer its security-related costs.

Respectfully submitted,

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I hereby certify that copies of the foregoing have been mailed, hand-delivered, transmitted by facsimile or e-mailed to all counsel of record this 4th day of September 2002.

/s/ Keith R. Krueger