BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of the Tariffs of Aquila, Inc., d/b/a Aquila Networks-MPS and Aquila Networks-L&P Increasing Electric Rates for the Service Provided to Customers in the Aquila Networks MPS and Aquila Networks-L&P Service Areas.	))))))	**Case No. ER-2007-0004**

APPLICATION FOR REHEARING

COMES NOW, AG Processing, Inc. ("AGP") and Sedalia Industrial Energy Users' Association ("SIEUA"), pursuant to Section 386.500 RSMo., and applies for rehearing of the Commission's May 17, 2007 Report and Order ("Order") on the following grounds:

1. The Order is unlawful, unjust and unreasonable in that the Commission has once again failed to provide adequate findings of fact related to the record as required by law thereby making it impossible for these Intervenors to specify with particularity the factual errors that are contained in such Order. Labeling recitations of evidence and testimony as findings of fact when they are nothing more than descriptions of what one or the other parties contended do not substitute for findings of fact and has repeatedly been ruled as insufficient by Missouri courts. Accordingly, the Order violates these Intervenors' rights to due process as guaranteed by the United State and Missouri Constitutions by attempting to deny them access to the courts and should be set aside as unlawful and unconstitutional forthwith.

2. The Order is unlawful, unjust, unreasonable and unconstitutional in that it completely fails to specify conclusions of law that are drawn from the findings of fact.

3. The Order is unlawful, unjust, unreasonable and unconstitutional in that it is not supported by competent and substantial evidence upon the whole record, and is contrary to the substantial and competent evidence of record. Moreover, it is apparent from the Commission's citations to "evidence" that the Commission has improperly relied upon extra-record information.[1] Of particular concern, is one Commissioner's explicit acknowledgement of information provided in an ex-parte communication that is not part of the record.

Many of the errors identified in this Application for Rehearing result from the agency's failure to either consider the evidence in the record or attempts to try to make that evidence fit preconceived notions on certain issues under the guise of "balancing interests." A specific example is found in the agency's admission, in connection with the Return on Equity issue, that "the experts have managed to create a thicket of conflicting opinions. If the Commission were to attempt to force its way through the tangle it could easily lose its way or even become ensnared."[2] Agency failure to consider the evidence, for fear of becoming ensnared in the thicket, or forcing such evidence to fit predetermined views inevitably results in contradictions, inconsistencies, misstatements and mischaracterization of the evidence, reliance upon extra-record evidence, and ignoring the overwhelming weight of the evidence that does exist.

I. FUEL ADJUSTMENT CLAUSE

4. The Order is unlawful in that the Commission has authorized a fuel adjustment clause which, contrary to the express provisions of Section 386.266 provides for the pass through of increases and decreases in fuel and purchased power costs that

[1] See, Report and Order, footnotes 74 and 80 in which the Commission references testimony from the pending AmerenUE proceeding.
[2] *Id*. at page 58.

result from imprudent utility decisions. Section 386.266.1 provides the Commission with the authority to implement rate adjustments outside of general rate proceedings "to reflect increases and decreases in its ***prudently incurred*** fuel and purchased power costs, including transportation." (emphasis added). Despite its clear understanding that only prudent costs should be passed through the adjustment mechanism,[3] the adjustment mechanism authorized by the Commission clearly contemplates that the prudence review will occur after the costs have already passed through the adjustment clause. By relying upon after-the-fact prudence reviews, the Commission cannot ensure, contrary to the express provisions of Section 386.266.1, that imprudent costs are not passed through the adjustment mechanism. Indeed, the Commission even acknowledged the deficiencies of its post-recovery approach.[4]

5. The Order is unlawful, unjust and unreasonable, is based on inadequate findings of fact, is not supported by competent and substantial evidence on the whole record and is contrary to the competent and substantial evidence that is on record, is arbitrary and capricious and is an abuse of discretion in that the Commission failed to address the issue denoted in SIEUA / AGP's Posthearing brief as "length of fuel adjustment clause." As reflected in that brief, this issue was raised in the testimony of both SIEUA / AGP and Staff.

6. The Order is unlawful, unjust and unreasonable, is based on inadequate findings of fact, is not supported by competent and substantial evidence on the whole record and is contrary to the competent and substantial evidence that is on record, is arbitrary and capricious and is an abuse of discretion in that the Commission granted

[3] *Id.* at page 20 in which the Commission notes that the adjustment mechanism should only reflect increases and decreases in "prudently incurred fuel and purchased-power costs."
[4] *Id.* at page 53.

Aquila a waiver of 4 CSR 240-20.090(9) without providing the parties a hearing on the issue. 4 CSR 240-20.090(15) provides that "[p]rovisions of this rule may be waived by the commission for good cause shown ***after an opportunity for a hearing***." While the Commission did hold a hearing in this case, the parties were never apprised that the Commission was considering granting such a waiver and would use such hearing to receive evidence necessary for the Commission to consider the appropriateness of such a waiver. Without such notice of the issues to be decided, the parties' right to a hearing was undermined. This action constitutes a violation of the most fundamental due process rights of these parties, *i.e.,* the right to have notice of the nature of the proceeding. Holding a hearing, then later determining what the hearing was about, constitutes arbitrary and capricious agency action.

7. The Order is unlawful, unjust and unreasonable, is based on inadequate findings of fact, is not supported by competent and substantial evidence on the whole record and is contrary to the competent and substantial evidence that is on record, is arbitrary and capricious and is an abuse of discretion in that the Commission found that no party would be prejudiced by the Commission granting a waiver from 4 CSR 240-20.090(9).[5] There is no evidence in the record to support such a finding. Indeed, SIEUA / AGP note the simple fact that the Commission rule requires a ***timely*** "jurisdictional system loss study" is an implicit understanding that parties will be prejudiced by such an outdated analysis.

8. The Order is unlawful, unjust and unreasonable, is based on inadequate findings of fact, is not supported by competent and substantial evidence on the whole record and is contrary to the competent and substantial evidence that is on record, is

[5] *Id.* at page 25.

arbitrary and capricious and is an abuse of discretion in that the Commission erroneously bases its decision on the mistaken belief that any fuel adjustment mechanism "must be reasonably designed ***to help*** the company earn its allowed return on equity."[6] A fuel clause should be limited to recovery of prudent fuel expense and limit rate changes to only an amount that increases the utility's earnings to its authorized return. The language purportedly quoted by the agency does not appear in the statute.

9. The Order is unlawful, unjust and unreasonable, is based on inadequate findings of fact, is not supported by competent and substantial evidence on the whole record and is contrary to the competent and substantial evidence that is on record, is arbitrary and capricious and is an abuse of discretion in that the Commission obviously based its decision regarding fuel adjustment clause on the belief fuel and purchased power costs have increased between 13% and 20% for the last 3 years. Moreover, the Commission notes that "[b]ased upon evidence presented to the Commission in this case, there is strong reason to believe this trend will continue."[7] Similarly, the Commission finds that "the evidence in this case supports a conclusion Aquila will likely under recover tens of millions of dollars without a RAM."[8] A review of the evidence cited by the Commission clearly fails to support these Commission findings. In fact, in at least one citation explicitly referenced by the Commission, the transcript clearly demonstrates that the discussion was in the nature of an "illustration" of the mechanics of the proposed fuel adjustment clause (which relied upon an "assumption" of a 15% annual increase in fuel costs) and **not** evidence of the likelihood that fuel and purchased power costs would increase.

[6] *Id.* at page 11. (emphasis added).
[7] *Id.* at page 24.
[8] *Id.* at page 32.

10. The Order is unlawful, unjust and unreasonable, is based on inadequate findings of fact, is not supported by competent and substantial evidence on the whole record and is contrary to the competent and substantial evidence that is on record, is arbitrary and capricious and is an abuse of discretion in that the Commission seeks to deny Intervenors' their due process rights in regards to their participation in the development of future heat rate testing. The Commission's action, as found at pages 29 and 46 of the Report and Order, substantially changes an agreement that was presented at the hearing without providing the parties with the opportunity to present evidence, cross-examine or brief on the Commission's modified position. The Commission bases its action on nothing more than the speculative belief that parties may attempt to use such heat rate testing to "block adjustments" to an approved RAM. Obviously, there is no competent and substantial evidence to support such a finding or conclusion. In fact, the Commission's express finding of fact is later contradicted by the Commission. Specifically Ordered Paragraph 5 notes that:

> Aquila, Inc. shall complete the proposed heat rate and / or efficiency schedule and testing plan with written procedures, as described in 4 CSR 240-3.161(2)(P) ***that is either agreed to by all parties to this case*** or has been approved by the Commission no later than sixty (60) days before the effective date listed on the tariff for its initial fuel adjustment clause filing for the purpose of adjusting a fuel adjustment clause rate pursuant to 4 CSR 240-3.161(7) and 4 CSR 240-20.090(4).

11. The Order is unlawful, unjust and unreasonable, is based on inadequate findings of fact, is not supported by competent and substantial evidence on the whole record and is contrary to the competent and substantial evidence that is on record, is arbitrary and capricious and is an abuse of discretion in that the Commission finds that

Exhibit 242 alleviated Mr. Taylor's concerns without any competent and substantial evidence to support such finding.

12. The Order is unlawful, unjust and unreasonable, is based on inadequate findings of fact, is not supported by competent and substantial evidence on the whole record and is contrary to the competent and substantial evidence that is on record, is arbitrary and capricious and is an abuse of discretion in that the Commission fails to adequately address the issue of performance standards to be used in conjunction with a fuel adjustment mechanism. In its Report and Order, the Commission erroneously asserts that the performance standards are designed only to address the situation in which "Aquila might imprudently shut down one of its base load generating facilities."[9] In so stating, the agency displays its utter misunderstanding of the purpose of a performance standard. Section 386.266 was not enacted by the General Assembly in order to make the ratepayers involuntary insurers of the utility's operations. The testimony clearly indicates that performance standards are designed to address involuntary and negligent actions in which a base load generating station is no longer capable of generating electricity. In its brief, SIEUA / AGP reference the destruction of the Lake Road and Taum Sauk facilities (neither of which was a voluntary action on the part of the utility). An additional reference could be made to the Hawthorne explosion that occurred several years ago to Kansas City Power & Light Co. As the Commission notes, "after-the-fact prudence reviews alone are insufficient to assure Aquila will continue to take reasonable steps to keep its fuel and purchased power costs down."[10] Moreover, in order to reject these parties evidence, the agency had to "assume Aquila would imprudently shut down one of

[9] *Id.* at page 50.
[10] *Id.* at page 53.

its base load generating facilities."[11] This "finding" is not supported by competent and substantial evidence on the whole record and is contrary to the competent and substantial evidence that is of record. There is no factual basis in this record for the agency's assumption. Given the acknowledged insufficiency of the prudence review and its admitted misunderstanding of the purpose of the performance standards, it is incumbent that the Commission rehear this issue or correct its Order.

13. The Order is unlawful, unjust and reasonable, is based on inadequate findings of fact, is not supported by competent and substantial evidence on the whole record and is contrary to the competent and substantial evidence that is on record, is arbitrary and capricious in that it fails to take into account that the Commission has previously approved performance standards for Aquila in connection with its steam system operations.

14. The Order is unlawful, unjust and unreasonable, is based on inadequate findings of fact, is not supported by competent and substantial evidence on the whole record and is contrary to the competent and substantial evidence that is on record, is arbitrary and capricious and is an abuse of discretion in that the Commission, after setting forth a three-part test for the authorization of a fuel adjustment mechanism, finds that Aquila "meets all three criteria."[12] Notably, the Commission finds that a fuel adjustment mechanism is appropriate in situations in which costs "fluctuate significantly."[13] American Heritage Dictionary defines fluctuate as "to rise and fall like waves; undulate." The record does not support a Commission finding that fuel costs fluctuate significantly. Moreover, the witness did not so testify.

[11] *Id.* at page 50.
[12] *Id.* at page 37.
[13] *Id.* at page 34.

15. The Order is unlawful, unjust and unreasonable, is based on inadequate findings of fact, is not supported by competent and substantial evidence on the whole record and is contrary to the competent and substantial evidence that is on record, is arbitrary and capricious and is an abuse of discretion in that the Commission, misconstrued and mischaracterized the proposal regarding an "acute" financial need because such proposal focused upon the sharp and sudden fly-up of fuel costs which would protect the interest of customers. In so doing the Commission failed to provide an order that is supported by competent and substantial evidence upon the whole record and its decision is, instead, contrary to the competent and substantial evidence that is of record.

16 The Order is unlawful, unjust and unreasonable, is based on inadequate findings of fact, is not supported by competent and substantial evidence on the whole record and is contrary to the competent and substantial evidence that is on record, is arbitrary and capricious and is an abuse of discretion in that the Commission, in support of its finding that 27 of 29 states have fuel adjustment clauses, has relied upon the mere recitation of evidence out of another case. A careful review of the transcript fails to provide any independent, first hand testimony regarding the acceptance of fuel adjustment clauses throughout the nation.

17. The Order is unlawful, unjust and unreasonable, is based on inadequate findings of fact, is not supported by competent and substantial evidence on the whole record and is contrary to the competent and substantial evidence that is on record, is arbitrary and capricious and is an abuse of discretion in that the Commission implemented a sharing percentage (95% ratepayers and 5% shareholders) in the fuel

adjustment clause that is completely unsubstantiated by the record. In fact, when queried at the Commission's agenda session, the Commissioner that suggested this sharing level noted that "you won't find that in the record" and that he "pulled it out of thin air."[14]

Moreover, such a sharing level is insufficient to create a meaningful incentive for Aquila to control its fuel and purchased power costs, which in turn seems to be based upon the agency's misunderstanding of cost projections and the effect that meaningful incentives would have on the incurrence of costs. Meaningful incentives are intended to prevent high fuel costs, yet the Commission perversely inverts the logic of the evidence to attempt to argue that fictitious increasing fuel costs **minimize the need for incentives**. This conclusion is not drawn from facts that are supported by competent and substantial evidence in this record. Even using the worst-case scenario adopted by the Commission (15% annual increases), Aquila shareholders will only share to the level of $1.5M. Importantly, this does not account for the tax deductible nature of fuel and purchased power as an operating expense. Accounting for the tax-deductible nature of these expenses, Aquila shareholders will only actually share to the level of $900,000. Based upon the reconciliations provided by the parties, this equates to a paltry 11 basis points. Moreover, this fails to account for savings that the Company has already realized (salary and benefits of Keith Stamm, refinancing of long-term debt costs, etc.) that have already occurred, but went unrealized in the ratemaking process because they were outside of the test year. Certainly, given all of these considerations, it is ludicrous to believe that the Commission has actually maintained any meaningful incentive for Aquila to procure fuel and purchased power in a least cost manner, thereby demonstrating the dangers of

[14] Commission agenda session dated May 10, 2007.

resorting to numbers that were grasped out of "thin air" in lieu of the record evidence and proving the much-touted "consumer protections" of Senate Bill 179 to be a sham.

18. The Order is unlawful, unjust and unreasonable, is based on inadequate findings of fact, is not supported by competent and substantial evidence on the whole record and is contrary to the competent and substantial evidence that is on record, is arbitrary and capricious and is an abuse of discretion in that it appears that, among the majority that voted in favor of the Report and Order, there was no meeting of the minds on a common position or findings of fact. Specifically, in its Report and Order, the Commission implemented a 95% / 5% sharing mechanism to be included in the fuel adjustment mechanism. That said, however, in his concurrence, Chairman Davis indicates that based upon a $30 million annual increase in fuel and purchased power expense, shareholders would absorb losses of $3 million. This clearly equates to a sharing mechanism of 90% / 10%. Therefore, the Report and Order is "a nullity because it lacked a showing that a majority of the Commission adequately concurred therein."[15] The agency is not a court and, unlike courts, must demonstrate that the facts purportedly found by the agency to support its conclusions were so found by a majority of the members of the agency.

19. The Order is unlawful, unjust and unreasonable, is based on inadequate findings of fact, is not supported by competent and substantial evidence on the whole record and is contrary to the competent and substantial evidence that is on record, is arbitrary and capricious and is an abuse of discretion in that the Commission fails to account for the overwhelming evidence which indicates the complete ineffectiveness of after-the-fact prudence reviews.

[15] *State ex rel. County of St. Louis v. Public Service Commission*, 228 S.W.2d 1 (1950).

II. RETURN ON EQUITY

20 The Order is unlawful, unjust and unreasonable, is based on inadequate findings of fact, is not supported by competent and substantial evidence on the whole record and is contrary to the competent and substantial evidence that is on record, is arbitrary and capricious and is an abuse of discretion in that the Commission failed to address several issue denoted in the Issue List. The Commission's failure to address these issues makes it impossible for a reviewing court to determine how the Commission reached its authorized return on equity. For instance, there is no identification of the comparable company group on which the Commission ultimately relied; no identification of the return on equity model utilized; and no identification of the appropriate inputs to be used in that model.

21. The Order is unlawful, unjust and unreasonable, is based on inadequate findings of fact, is not supported by competent and substantial evidence on the whole record and is contrary to the competent and substantial evidence that is on record, is arbitrary and capricious and is an abuse of discretion in that the Commission failed to provide adequate findings of fact. Specifically, the Commission claims that the return on equity should be adjusted upwards by 10 to 15 basis points[16] to arrive at a final return on equity of 10.25%.[17] Therefore, prior to any upward adjustments, the Commission apparently started at a return on equity of 10.1% to 10.15%.[18] Noticeably, the Commission never provides any findings of fact for a party to determine how it arrived at the 10.1% to 10.15% starting point. In fact, the Commission's own findings indicate that it relied upon the analysis of SIEUA / AGP witness Gorman who provided a

[16] Report and Order at page 62.
[17] *Id.* at page 63.
[18] 10.25% less 10 to 15 basis points.

recommended return on equity of 10.0%. Apparently, the ultimate return on equity was inflated by 10 to 15 basis points without any explanation, finding of fact or conclusion.

22. The Order is unlawful, unjust and unreasonable, is based on inadequate findings of fact, is not supported by competent and substantial evidence on the whole record and is contrary to the competent and substantial evidence that is on record, is arbitrary and capricious and is an abuse of discretion in that the Commission failed to account for the reduced risk resulting from its authorization of a fuel adjustment clause. Specifically, while explicitly adopting the analysis provided by Gorman, the Commission inexplicably failed to provide for his 30 basis point reduction that should accompany the implementation of a fuel adjustment clause. As Gorman explains, the business risk profile for Aquila is based upon **no** fuel adjustment clause. The comparable company groups consist of companies that display a comparable risk profile. The Commission's implementation of a fuel adjustment mechanism would cause a reduction in Aquila's risk profile that is ***not*** reflected in the comparable company group. Therefore, the Commission has failed to account for this change in risk through adequate findings and conclusions drawn therefrom.

23. The Order is unlawful, unjust and unreasonable, is based on inadequate findings of fact, is not supported by competent and substantial evidence on the whole record and is contrary to the competent and substantial evidence that is on record, is arbitrary and capricious and is an abuse of discretion in that the Commission, on May 22, 2007, issued its Report and Order in which it authorized a return on equity for AmerenUE (a comparable company of Aquila) of 10.2%. It is inexplicable that the Commission

could give Aquila, despite the lower risk that results from the implementation of its fuel adjustment mechanism, a higher authorized return on equity than AmerenUE.

24. The Order is unlawful, unjust and unreasonable, is based on inadequate findings of fact, is not supported by competent and substantial evidence on the whole record and is contrary to the competent and substantial evidence that is on record, is arbitrary and capricious and is an abuse of discretion in that the Commission failed to account for Aquila's reduced risk as a result of its lack of nuclear operations, operations in deregulated states, non-regulated affiliates and hurricane risk. Specifically, the Commission, in rejecting the Hadaway analysis, noted that it was inappropriate to provide an increase in return on equity as a result of increased construction risk while simultaneous ignoring other aspects that caused return on equity to be lower (nuclear operations, operations in deregulated states, non-regulated affiliates and hurricane risk). Despite its explicit rejection of Hadaway's construction risk adjustment ("the construction risk upward adjustment proposed by Dr. Hadaway appears to be a transparent effort to inflate the company's proposed return on equity."), the Commission inexplicably claims that "Aquila's return on equity should be adjusted upwards by 10 to 15 basis points to reflect [Aquila's] increased construction risk compared to the comparable companies." No explanation is provided and no finding of fact supports this conclusion. It is, in fact, not supported by competent and substantial evidence on the whole record.

25. The Order is unjust and unreasonable, is based on inadequate findings of fact, is not supported by competent and substantial evidence on the whole record and is contrary to the competent and substantial evidence that is on record, is arbitrary and

capricious and is an abuse of discretion in that the Commission finds that "the decreased risk associated with having a cost recovery mechanism is already accounted for in Mr. Gorman's return on equity calculation and no additional adjustment is necessary."[19] As the Commission recognized in its Report and Order, the decreased risk of a fuel adjustment clause is ***not*** reflected in Gorman's analysis.[20]

WHEREFORE, prior to the implementation of new rates that would necessarily result in the denial of the issues detailed in this Application, the Commission should order rehearing of its Report and Order and a new Order consistent with governing law, commission precedent and based exclusively upon the evidence herein should be issued.

Respectfully submitted,

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ATTORNEYS FOR AG PROCESSING, INC. AND SEDALIA INDUSTRIAL ENERGY USERS' ASSOCIATION

[19] *Id.* at pages 62-63.
[20] *Id.* at page 57 ("Aquila, Staff, SIEUA, AG-P, and FEA sponsored financial analysts who recommended a return on equity in this case. Their recommended ROEs are: Aquila – 10.25%, plus a 50 basis point adder; Staff – 9.0 – 10.25%; SIEUA, AG-P and FEA – 10%, ***with a 30 basis point reduction if a fuel adjustment clause is authorized***." (emphasis added).

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 23, 2007