

BEFORE THE PUBLIC SERVICE COMMISSION

OF THE STATE OF MISSOURI

In the matter of a special contract filed by Kansas City)
Power & Light Company.) Case No. EO-95-181
)

REPORT AND ORDER

Issue Date: November 22, 1995

Effective Date: December 6, 1995

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In the matter of a special contract filed by Kansas City)
Power & Light Company.) Case No. EO-95-181
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APPEARANCES

William G. Riggins and Susan B. Cunningham, Staff Attorneys, Kansas City Power & Light Company, 1201 Walnut Street, Kansas City, Missouri 64106, for Kansas City Power & Light Company.

Richard W. French, French & Stewart Law Offices, 1001 East Cherry Street, Suite 302, Columbia, Missouri 65201, for Trigen-Kansas City Energy Corporation.

Gary W. Duffy, Brydon, Swearingen & England, P.C., 312 East Capitol Avenue, Post Office Box 456, Jefferson City, Missouri 65102, for Missouri Gas Energy, a division of Southern Union Company.

Lewis R. Mills, Jr., Deputy Public Counsel, Office of the Public Counsel, Post Office Box 7800, Jefferson City, Missouri 65102, for the Office of the Public Counsel and the public.

Steven Dottheim, Deputy General Counsel, Missouri Public Service Commission, Post Office Box 7800, Jefferson City, Missouri 65102, for the staff of the Missouri Public Service Commission.

ADMINISTRATIVE
LAW JUDGE:

Cecil I. Wright, Chief.

REPORT AND ORDER

Kansas City Power & Light Company (KCPL) on December 7, 1994, filed a motion for a protective order to protect certain information it considers confidential associated with a special contract between KCPL and one of its customers. KCPL also filed a proposed tariff sheet with the contract. The Missouri Public Service Commission (Commission) established this docket to consider the motion and the special contract and the proposed tariff sheet. The proposed tariff sheet contains other changes to the existing sheet No. 37. On

December 23, 1994, KCPL filed a substitute proposed tariff sheet No. 37 which extended the effective date from January 6, 1995, to February 5, 1995.

The Commission, by order issued December 9, 1994, adopted a Protective Order for this case. By order issued January 3, 1995, the Commission granted intervention to Trigen-Kansas City Energy Corporation (Trigen) and Missouri Gas Energy, a division of Southern Union Company, (MGE) and set a date for a prehearing conference. The Commission also suspended the proposed tariff sheet 120 days from its initial effective date to May 6, 1995.

On April 4, 1995, KCPL filed a motion requesting the Commission approve the special contract on an interim basis pending a Commission final decision on the special contract and the proposed tariff sheet. The Commission granted KCPL's motion and approved an interim tariff sheet which allowed the special contract to be implemented during the pendency of this proceeding. The Commission found that KCPL would hold the other ratepayers harmless if the special contract was not ultimately approved.

The Commission, by order issued April 28, 1995, adopted a proposed procedural schedule for this case and suspended the proposed tariff sheet six months beyond May 6, 1995, to November 6, 1995. A hearing was held as scheduled in this matter on September 11 and 12, 1995. Briefs were filed by the parties which addressed the issues involving the special contract and the more generic issues raised by the Commission. On October 31, 1995, the Commission suspended the proposed tariff sheet an additional thirty days to allow for further deliberation of the issues.

Findings of Fact

The Missouri Public Service Commission, having considered all of the competent and substantial evidence upon the whole record, makes the following findings of fact.

The issues in this case involve two inquiries which, although related, will be decided separately. The first inquiry involves the specific special contract and the associated proposed tariff which initiated this case. The second inquiry involves the Commission's questions concerning the lawfulness of: (1) special contracts; (2) flexible rates; and (3) protecting the terms of the special contracts from public disclosure. The Commission will first address the generic issues and then the special contract and proposed tariff sheet which initiated this case.

Generic Issues

Based upon the conclusions reached by the Commission in the conclusions of law below, the Commission finds that special contracts are lawful and are an appropriate way to establish rates as long as the statutory requirements are met. The Commission also finds, based upon the conclusions, that the protection of certain information with respect to special contracts from public inspection is reasonable and lawful and does not violate the provisions of Chapters 386, 393, or 610, R.S.Mo. 1994. Again, the protection of the information is appropriate as long as other statutory provisions are satisfied.

The Commission has considered these matters and finds that the tariffing of many if not all of the terms and conditions associated with special contracts is not only reasonable and in the public interest but is required by law. Section 392.140(11), R.S.Mo. 1994, requires that all rates and charges be set out in a schedule for public review. Sections 393.130 and 393.140 require that rates not be discriminatory. The Commission finds that these sections of the statutes require a company to have a published tariff for each service that it offers and to offer that tariffed service to all similarly situated customers.

KCPL and Staff have proposed generic tariff language for the offering of electric service under special contracts in certain circumstances. KCPL

witness Giles supports service pursuant to generic tariff provisions under which customers who meet certain criteria can take service at rates less than those available under the Primary Large Service (PLS) tariff. This proposed service contains different language than the proposed tariff which initiated this case. This generic service would allow KCPL to flex down from the rates in the PLS tariff in order to meet a competitive threat. The service would only be available to customers or potential customers which: (1) have demands of 1,000 KW or greater; (2) are faced with competition from other energy suppliers; and, (3) in KCPL's determination, it is necessary to retain service to the existing customer or to acquire a new customer.

The proposed service would be at a rate not less than the greater of 1.3¢/kwh on an average annual basis or at a rate above KCPL's annualized incremental cost per kwh. The proposed tariff contains additional language which requires nondiscriminatory treatment of customers, and the contracts would be furnished to Staff and OPC. The proposed tariff language also states that the tariff does not bind the Commission for ratemaking purposes.

Staff witness Proctor contends that KCPL's proposed tariff would allow KCPL too much flexibility since it allows KCPL to flex down anytime it perceives there is some form of competitive threat. Proctor testifies that, in his opinion, KCPL will not face a general threat of competition until retail customers are given open access to KCPL's system. In addition, Proctor proposes a third provision to the tariff proposed by Giles. This provision would be "(3) the special contract is not a prohibited promotional practice as set out in Commission rule 4 CSR 240-14." Proctor also proposes that the incremental price floor for each component of service be specified and that the 1.3¢/kwh be eliminated. Staff witness Straub proposes that the Commission add language to the proposed tariff which requires that multiple-location customers must take a total of 3,000 KW with no single location taking less than 1,000 KW. Straub also

proposes additional language placing the burden on KCPL to show the prudence of the contract.

Proctor proposes that the generic tariffed service for special contracts would specify the conditions of applicability, a description of the form of the special pricing, and a price ceiling and price floor for each service component. Proctor recommends that the fixed price be set but that the service be offered as an unbundled service with separately identified components including distribution facilities, transmission services, production firm capacity service, production energy service, and customer services. Proctor then describes how he would set the price floor and ceiling for each component.

The Commission has considered these two proposed generic service tariffs for special contracts and finds that the establishment of a generic tariff for special contracts entered into based upon competition should be addressed in KCPL's rate design case, Case No. EO-94-199. The Commission finds that the type of competition now faced by KCPL may require a bundled service which is based upon the covering of incremental costs in the aggregate. If there is any retail competitive threat to KCPL at this time, it is from other service providers offering full electric service on an aggregated basis. The tariffed service proposed by KCPL witness Giles may be appropriate for meeting this type of competition. The Commission finds that the parties in EO-94-199 should look at the proposed modifications of Staff witnesses Straub and Proctor to the tariff proposed by Giles.

The Commission, though, finds that in preparation for the potential of the full range of competition within KCPL's service territory, KCPL may need unbundled, tariffed services as proposed by Staff witness Proctor. This service may be within a range, as proposed by Proctor, or with just a floor for each service. The Commission finds that these matters would be better addressed in the rate design case where parties can more fully evaluate which parts of service

should be unbundled and what the proper pricing floor and/or ceiling for each part should be.

Specific Special Contract

In Case No. EO-95-67 the Commission issued an order approving a tariff sheet which was associated with a special contract between KCPL and one of its customers. The Commission also approved the special contract in its order. The special contract contained rates which were specifically designed to meet the needs of the particular customer. Those rates and the provisions of the contract were considered highly confidential (HC) under the terms of a Commission-approved Protective Order and so were not made public. In December, when KCPL requested approval of the special contract in this case, the Commission suspended the proposed tariff sheet associated with the special contract and determined that the issues raised by the use of special contracts by regulated utilities should be addressed at the same time the issues involving this particular special contract were addressed.

The positions of the parties on both the specific issues of the special contract and proposed tariff sheet and the more generic issues have provided the Commission with a good basis for addressing the issues involving the special contract. Although there is a substantial amount of evidence which has been classified as HC that addresses the specific contract involved in this case, the Commission believes it can issue a Report And Order which adequately addresses the issues without discussing the HC evidence. The Commission will address the special contract without reference to HC information unless it finds that the information to be used is not HC or is necessary for the decision to be understood.

The special contract in this case is patterned closely to the one approved in Case No. EO-95-67. The terms allow the customer pricing flexibility

which corresponds to the customer's production needs and better enables the customer to reduce its cost of electricity while maintaining or even increasing its production. As stated in KCPL's cover letter filed with the proposed tariff sheet, the special contract establishes KCPL as the exclusive provider of electricity to the customer for a ten-year period and guarantees KCPL a margin on all energy sold to the customer, utilizing hourly price signals, with the result that KCPL is able to manage its resources and reduce its peak load. The evidence in this case supports this statement.

The production of the customer in this case is linked directly to the production of the customer for which the special contract was approved in Case No. EO-95-67. The terms of this special contract would allow the customer in this case to adjust its production in conjunction with the production requirements of the customer in EO-95-67. Innovative rate design and pricing provisions allow these two customers to operate their systems more effectively to reduce energy costs, and KCPL benefits by the curtailment provisions of the special contract. These peak curtailment provisions allow KCPL to remove a certain amount of interruptible load from its system planning forecasts and to then defer peak generation purchases.

In addition, KCPL's Primary Large Service (PLS) tariff, with optional Primary Service Rider No. 1, does not meet the production needs of the customer. The current PLS rate limits customers to time-of-day pricing, which is not flexible enough to meet the day-to-day changes in variable electric production costs of the customer. The PLS tariff does not meet the needs of this customer while the special contract terms approved for the customer in EO-95-67 do. The special contract provisions also have the potential of allowing KCPL to increase its sales because of the possible expansion of the customer's operations in KCPL's service territory.

Trigen and the Office of the Public Counsel (OPC) generally oppose the special contract because they assert that there is no threat that the customer will switch its production to another energy source or to another location, and without that immediate threat, no special contract pricing is warranted. Trigen argues, additionally, that the special contract's effect, if not intention, is to preempt competition of KCPL's service. OPC proposes a three-prong test for a special contract to be in the public interest. First, the customer must be making a significant contribution to the utility's fixed costs; second, electrical energy is a primary input to the customer's production processes or operations; and third, the customer has a real and verifiable option to move operations out of the utility's territory or off of the utility's system.

The Commission finds that the focuses of OPC and Trigen regarding the special contract are too narrow and do not address the unique situation involved in this customer's operations and the potential for additional benefits to KCPL and other ratepayers if the customer expands its production. Additionally, under the current monopoly structure, special contracts and KCPL's attempt to ensure a stable energy market for its product are benefits to KCPL and ratepayers, rather than reasons for denying this special contract as suggested by OPC and Trigen. A stable energy market for KCPL allows it to minimize the risks of its business operations over a number of years and thus keep costs and rates lower. The Commission's primary concerns in this area are to ensure that other ratepayers do not pay for costs for which the customers receiving the special rates should pay, and that KCPL does not discriminate among its own customers in providing the special contracts.

In addition, under the analysis performed by Staff witness Proctor, the rates established in the special contract will recover incremental costs plus a contribution to KCPL's fixed costs. This standard for setting rates is reasonable when added to the benefits of a stable customer and the curtailment

provisions of the contract. The witnesses for OPC and Trigen challenged Proctor's incremental cost analysis, but the Commission finds that the calculation of avoided costs made by Proctor is a reasonable basis for determining whether proposed rates will recover incremental costs plus provide a contribution to fixed costs. Trigen witness Thompson proposed an embedded allocation method for determining if the special contract was recovering its costs. During cross-examination Thompson admitted this method was more difficult to calculate than the avoided cost method utilized by Staff witness Proctor. The Commission finds that the avoided cost calculation performed by Proctor is a reasonable method of determining whether the rates set in this contract are reasonable.

Based upon the unique characteristics of their energy patterns, the Commission finds that the customer in EO-95-67 and the customer in this case compose a special class of customer. This separate class of customer has unique characteristics which allow for rates to be set for this particular class different from the rates for the PLS class of customer. The Commission finds, additionally, that those special contract rates are just and reasonable since they recover KCPL's incremental cost plus provide a contribution to fixed costs. The question of whether an embedded cost rate would have to be developed if many additional customers qualify for this rate is not being addressed. If this situation occurs, the issue may be brought back to the Commission for decision.

Although the Commission is approving the special contract in this case, the Commission cannot approve the proposed tariff sheet. The evidence indicates that the provisions of the proposed tariff would not allow for the approval of the special contract. The two conditions of the proposed tariff sheet which would have to be met are: (1) that KC faces existing or future competition from other energy suppliers for the customer; and (2) that KCPL determines that a

contract is necessary to retain service to an existing customer or to acquire a new customer.

The evidence does not support a finding that KCPL faces existing or future competition for the energy needs of the customer in this case. There is some evidence that the customer might move production out of Missouri. This evidence, though, is not probative and other evidence, see Exhibit 7HC, indicates the customer will more than likely stay and expand its operations.

Based upon the Commission's review of the proposed tariff sheet in this case, it will reject the proposed sheet and order KCPL to file a tariff sheet which reflects the unique service being offered by KCPL to the customer in this case and the customer in EO-95-67. The tariffed service should contain the three requirements recommended by Staff witness Proctor. Those conditions are that: (1) contract demand exceeds 1,000 KW; (2) be interruptible for at least 80 percent of contract demand; and (3) be subject to hourly change in energy prices. The tariff language for this service should contain language that rates, in the aggregate, shall exceed KCPL's incremental costs plus make a contribution to fixed costs, and that it will be offered on a nondiscriminatory basis. The contracts entered into under this tariff shall be furnished to Staff and OPC and shall be listed on the tariff sheet. These provisions, when tariffed, will allow any customer of KCPL which can meet the conditions for the service to take electric service at the rates established using the incremental costs of providing the service.

Although the Commission is approving the special contract in this case and has approved the special contract in EO-95-67, the Commission is concerned with the length of the contracts. Approval of these two contracts should not be seen as acceptance by the Commission that contracts of this length are to be the standard. The Commission finds that shorter term contracts are preferable in light of the changing conditions in the electric market.

Conclusions of Law

The Missouri Public Service Commission has arrived at the following conclusions of law.

The Commission has jurisdiction over the rates proposed by KCPL to be charged a specific customer in this case pursuant to the provisions of Sections 392.130, 392.140, 392.150 and 392.270, R.S.Mo. 1994. In pertinent part, these statutes: (1) prohibit a utility from charging a particular customer a different rate than a rate charged other customers for like and similar service unless the service is provided under different circumstances or conditions: (2) require a utility to file and keep open for public inspection schedules showing all rates and charges, and prohibit a utility from collecting a greater or lesser charge than the rates appearing on the filed schedules unless those rates are extended to all customers in similar circumstances; and (3) authorize the Commission to fix just and reasonable rates after hearing. The special contract and tariff and the proposed generic tariff for which KCPL seeks approval in this case must meet the conditions of these statutory provisions to be approved.

First the Commission must determine whether special contracts are a lawful mechanism for a public utility to set rates or charges for customers. The parties have briefed this issue and only OPC raises the possibility that special contracts are not lawful. The Commission concludes, based upon the analyses of the parties and its own review of the statutes and case law, that special contracts are recognized both historically and in the statutes and are a lawful method of providing service to customers of regulated utilities.

Section 392.140(11) specifically refers to the authority of the Commission to require the filing of all forms of contracts or agreements, and that any contract or agreement must be available to similarly situated customers. In addition, contracts were in existence when the PSC law was first enacted and

the Missouri Supreme Court recognized that the Commission could review these contracts and approve them for service under the new law if they were found to be reasonable. *May Department Stores Co. v. UE Light and Power Co., et al.*, 107 S.W.2d 41, 49 (Mo. 1937).

The Commission, as cited by Staff, has approved special contracts for KCPL in the past as well as for other utilities under its jurisdiction, including Trigen-KC. The approval of these contracts may not be determinative, but it does indicate a history of recognizing the need for flexible pricing provisions where exigent circumstances exist. The Commission concludes that where a unique class of customer takes service under a tariff which allows rates to be set by special contract, the contract and tariff are lawful where the terms and conditions of the contract are offered to similarly situated customers.

The Commission concludes further that flexible rates are lawful where, as here, the floor for each contract is established and all customers are subject to the same calculation of the rates to be charged under the special contract. The specific rate paid by the customer will not be set in the tariff since each customer will have different costs and therefore pay a different rate or combination of rates. This does not make the rates unduly discriminatory where the conditions of taking service are the same. This flexibility is essential in the modern environment for providing electric service where customers have unique production needs for energy. As stated by Staff witness Proctor, as long as the incremental costs of providing the service are covered by the pricing in the special contract and provide some contribution to fixed costs, the utility's customers benefit from the customer remaining on the system. Pricing flexibility for customers who meet the conditions of the tariff will allow KCPL to retain these customers.

In addition to the legal questions raised concerning special contracts, the Commission is also being asked to approve the terms of the special contract

without determining the ratemaking treatment for the rates which will be charged. The Commission interprets this request to mean that even though it finds the rates in the contract are just and reasonable, KCPL may have additional revenue imputed to it in a rate case if KCPL can be shown to be imprudent in entering into the contract.

The Commission does not believe it can lawfully approve tariffs as just and reasonable and then reserve a full prudence review before determining the ratemaking treatment of the revenues generated by the contracts. The questions which the Commission concludes can be reserved are whether the rates, in the aggregate, recover incremental costs of providing the service plus make a contribution to fixed costs, and whether the customer qualifies for the service. This is the determination of whether KCPL has met the conditions of the tariff. This review is the same review the Commission will undertake under the recently approved flexible tariff for United Cities Gas Company, Case No. GR-95-160.

The other question that the Commission must address is whether the terms and conditions of each contract and the rates in each contract may be kept under seal and therefore not open to the public. Missouri courts recognize that certain information can be treated as a "trade secret" and thus kept from public view. *Ultra Life Laboratories v. Eames*, 221 S.W.2d 224 (Mo. App. 1949). Section 386.480, R.S.Mo. 1994, prevents disclosure of information provided to the Commission by a utility except by Commission order or by the Commission during a hearing. In addition, the Commission has adopted a Protective Order in this case, as well as in many other cases, which recognizes the need for confidentiality of some information about a customer and about the terms of the contract. This approach is consistent with the rules of civil procedure and the law in other jurisdictions.

The problem with keeping certain information about rates and charges under seal is that such treatment of the information concerning the rates and

charges seems to contravene the provisions of Sections 393.140(11) and 393.150(1), which require the rates, charges, and form of contracts or agreements be open for public inspection. There is case law, though, that suggests that the Commission's Protective Order and in camera review procedures offer sufficient protection of the public interest to overcome this concern. **Utility Consumers Council of Missouri v. P.S.C.**, 562 S.W.2d 688 (Mo. App. 1979). The Commission concludes, based upon this case law, that the requirements in the statutes are met when the general terms and conditions under which service is taken are set forth in the tariff, as is the standard for pricing the service, and parties have access to the actual contracts under the terms of a Protective Order. The only additional requirement the statute requires is that these contracts and rates be filed with the Commission for review. The Commission concludes that where these contracts are required to be provided for review by OPC and Staff, the statutory requirement for open inspection is satisfied. A customer seeking to take service under the proposed tariff could determine whether it meets the requirements and whether it might be economical for it to take the service. Review by Staff and OPC, and potentially intervenors, under a Protective Order would ensure there was no undue discrimination among customers.

Even though the terms of the contract and specific rate may be under seal, the Commission concludes that Section 393.140(11) requires that each contract be filed with the Commission. This requires that each special contract entered into by KCPL must be listed on the tariff sheet and a copy of the contract filed with the revised tariff sheet. The contents may be filed under seal and the listing on the tariff sheet may only be a tariff file number or other designation. The tariff sheet and filing of the contract are for notice purposes, and the Commission does not intend to enter into a prudence review of future contracts in order to approve the tariff sheet. KCPL retains the risk that the contract will not meet the conditions in the tariff. In addition, the

Commission concludes that a revised tariff sheet should be filed when a contract expires which removes the special contract from the list.

The Commission concludes further that the specific special contract in this case is lawful since the Commission has found that the customer in this case and the customer in Case No. EO-95-67 are a separate class of customer and therefore, as a separate class, they may be charged rates different from those charged customers on the general PLS tariff. The statutes also authorize the Commission to set rates by either rate or contract as long as similarly situated customers are charged the same rates. By ordering KCPL to file a tariff which contains the general conditions for taking the service, the Commission concludes the statutory requirements have been satisfied,

Based upon the findings in this case, the Commission will approve the specific special contract but reject the tariff filed by KCPL. The specific contract, as discussed earlier, has been found to be reasonable and lawful. The proposed tariff sheet, though, was not found to be reasonable and so it will be rejected. KCPL shall be ordered to file a tariff sheet with language in compliance with this Report And Order for this special contract and the one approved in Case No. EO-95-67.

IT IS THEREFORE ORDERED:

1. That the proposed tariff sheet submitted by Kansas City Power & Light Company (File No. 9500403) is hereby rejected and Kansas City Power & Light Company shall file, in lieu thereof, a tariff sheet with language in compliance with this Report And Order. The tariff sheet shall be for service on and after December 6, 1995.

2. That the special contract filed by Kansas City Power & Light Company in this case is hereby approved for service on and after December 6, 1995.

3. That the interim tariff sheet approved by the Commission on April 20, 1995, is hereby canceled.

4. That this Report And Order shall become effective on the 6th day of December, 1995.

BY THE COMMISSION



David L. Rauch
Executive Secretary

(S E A L)

Mueller, Chm., McClure, Kincheloe,
Crompton and Drainer, CC., concur
and certify compliance with the
provisions of Section 536.080,
R.S.Mo. 1994.

Dated at Jefferson City, Missouri,
on this 22nd day of November, 1995.